Gulf & Western Industries, Inc.

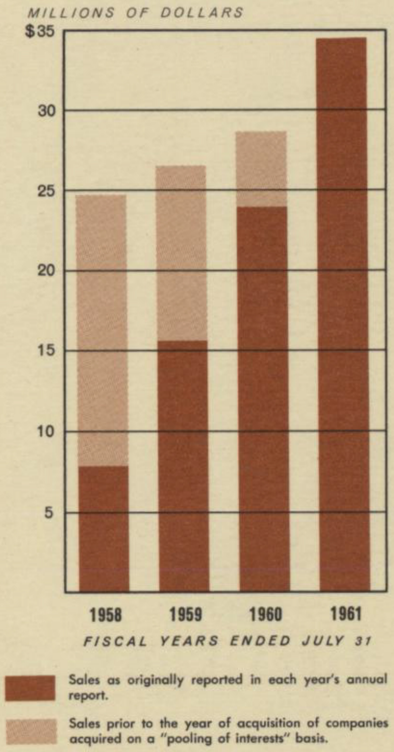
ANNUAL REPORT

1961

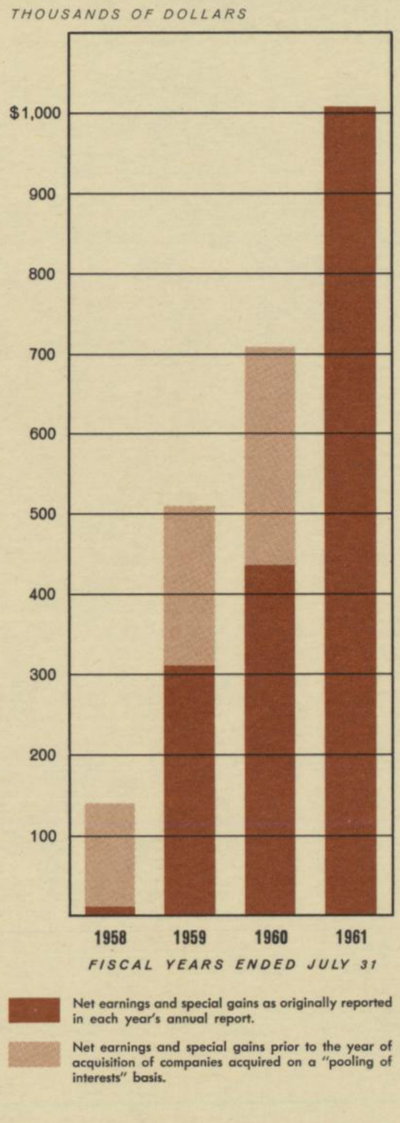
C O N T E N T S

Expanding our wholesale automotive parts system to meet the needs of a growing industry

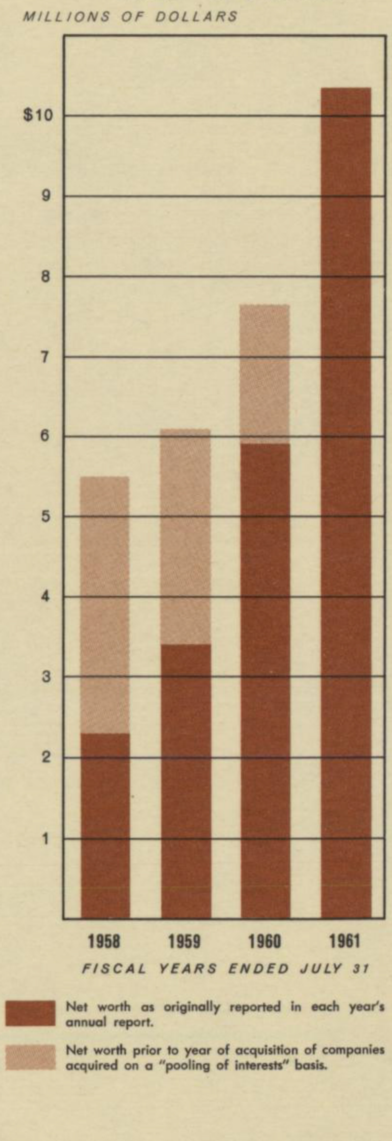
ANNUAL SALES



NET EARNINGS AND SPECIAL GAINS



NET WORTH



This report and the financial statements it contains are submitted for general information of the stockholders of Gulf & Western Industries, Inc., and are not intended to induce, or to be used in connection with, any sale or purchase of securities.

COMPARATIVE HIGHLIGHTS

Fiscal Years Ended July 31, 1961, and July 31, 1960 (Adjusted)

	1961	1960	*Increase*
Net sales	$33,835,000	$28,759,000	17.6%
Net earnings after taxes:			
After special gains	$ 1,002,000	$ 706,000	41.9%
Before special gains	$ 850,000	$ 561,000	51.4%
Average shares outstanding	915,000(A)	832,000(B)	9.9%
Per share earnings:			
After special gains	$ 1.10	$ .85	29.4%
Before special gains	$ .93	$ .67	38.8%
Current assets	$17,044,000	$11,332,000	50.4%
Current liabilities	$ 6,779,000	$ 4,217,000	60.7%
Working capital	$10,264,000	$ 7,114,000	44.3%
Total assets	$22,571,000	$13,936,000	62.0%
Long-term debt	$ 5,004,000	$ 1,798,000	178.2%
Stockholders' equity	$10,381,000	$ 7,882,000	31.7%
Book value per share of common stock (Based on 1,046,154 shares outstanding at end of period, compared with 829,605 shares outstanding for the prior period)	$ 9.92	$ 9.50	4.4%
Employees (end of period)	1,822	1,072	70.0%
Number of units (end of period)	99	51	94.1%

(A) Average number of shares outstanding during the period.

(B) Current equivalent of shares outstanding during the period — adjusted for a five per cent stock dividend issued during the year ended July 31, 1961, and for the shares applicable to companies acquired during the current year on a "pooling" basis.

Letter to Our Stockholders:

Your company has continued to move forward during the past year, recording a new high in sales and earnings.

Consolidated sales and net earnings for our fiscal year ended July 31, 1961, reflected substantial increases over sales and net earnings for the previous year. Our sales increased to $33.8 million as compared to $28.7 million*. After provision for federal income taxes, earnings for this year amounted to $1 million, or $1.10 per share, as compared to $706 thousand, or $.85* per share last year.

Of particular significance is the fact that during the past fiscal year, your company has doubled in size. The sales of our subsidiaries are now going at the annual rate of $50 million as compared to an annual rate of only $25 million for the subsidiaries owned a year ago. Assets have been increased to $22 million in comparison with only $11 million reported a year earlier. It is highly noteworthy that while experiencing this explosive acquisition growth, your company maintained an upward trend in earnings. Furthermore, we expect important contributions to future earnings as the newly acquired companies are streamlined and integrated into our organization.

For the past three and one-half years, your company has been engaged in an organized program to acquire well established regional automotive parts wholesalers and, in this relatively short period of time, has established itself as one of the nation's leading distributors in the field. Although the costs of acquiring and integrating new companies have placed a substantial initial burden on income, our acquisition program has generated additional benefits realized through the sale of automotive parts acquired at costs well below replacement value. The profit from these sales has increased our gross income by approximately $750 thousand this past year, as compared with only $120 thousand in the previous year. It is expected that this trend will continue as our acquisition program grows in both size and scope.

Since our last annual report, considerable progress

Charles G. Bluhdorn
Chairman of the Board

John H. Duncan
President

has been made in our program to centralize such functions as purchasing, statistical control, and accounting. The results thus far have been invaluable in initiating a number of sales and merchandising techniques at the subsidiary level.

Automotive parts outlets now owned by your company total 92, compared with 37 the previous year. In broadening the company's distribution pattern, your management has paid particular heed to expanding into areas which have been experiencing greater than normal growth, both in population and in economic development.

For the third successive year, your company paid a five per cent stock dividend. This dividend was paid October 1, 1961. Similar dividends were paid in September 1960 and in October 1959. During the past year, the number of stockholders has increased to 1743, or by 22 per cent.

Your company's favorable progress during this fiscal year, as in the past, has been a product of careful planning, aggressive action, and teamwork among the men and women making up the Gulf & Western organization. With this coordinated effort and continued confidence of our stockholders, we look for even greater progress in the years ahead.

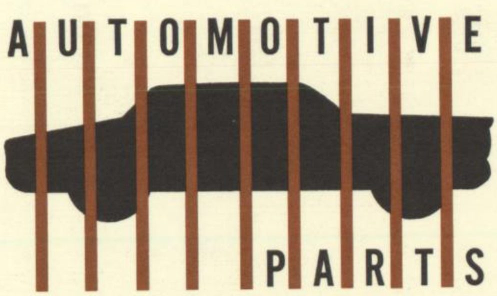
Charles G. Bluhdorn
Chairman of the Board

John H. Duncan
President

October 7, 1961

**Sales and earnings per share have been adjusted from the previously reported amounts of $24 million and $.63 to reflect the accounting concept of "pooling of interests" with respect to two subsidiaries acquired during the current year. Under this concept, the consolidation of the businesses of the parent and the "pooled" subsidiaries is presumed to have been in effect throughout their corporate lives, and the parent's historical earnings have been adjusted accordingly.*

Expansion and Growth Keynote Gulf & Western's Progress



PARTS DISTRIBUTION EXPANDED

During the past fiscal year, Gulf & Western has made its most progressive strides in meeting its primary goal — that of establishing a national network of automotive parts outlets strategically located to serve a vast, growing parts market.

The accelerated program of expansion carried out by the management of American Parts Company division has been primarily responsible for this favorable progress made in enlarging the distribution pattern.

Five automotive parts companies have been acquired since our last annual report. Four of these — The Scheufler Supply Company, Inc., The Motor Supply Company, Patten Sales Company of Jacksonville, Inc., and Hendrie & Bolthoff Company, Inc. — are located in the Midwest, Southeast and Rocky Mountain region and have combined annual sales of over $24 million. The fifth, Overseas, S. A., represents the company's first automotive parts acquisition outside the United States.

Gulf & Western's entry into the automotive parts distribution field was in December 1957, with the acquisition of Beard & Stone Electric Company, Inc., a Texas-based distributor. Subsequently, 17 operations were acquired, 13 of which were in the wholesale automotive parts distribution field.

Currently operating under the American Parts Company division are nine subsidiaries comprising 92 wholesale automotive parts outlets. This number represents an increase of 55 in the number of outlets since our last annual report.

Gulf & Western's remanufactured line of electrical and mechanical automotive parts, which was introduced in March 1960, has been very well received. In an up-trend market for remanufactured parts, the company is taking full advantage of the acceptance of its quality parts by rapidly expanding the line into new sales territories.

*Hendrie & Bolthoff Company, Inc.,
a 31-store system with headquarters in Denver, Colorado,
serves 10,000 active accounts from Canada to the Mexican border
from a working inventory of more than 250,000 different items
in the automotive, industrial, electrical and hardware fields.
Shown above is the new outlet in Colorado Springs, Colorado.*

*From one central facility in Mexico City, Overseas, S. A.,
serves all the Republic of Mexico,
from Tijuana in lower California to
Matamoros and to Merida on the Yucatan peninsula.
In addition to stocking a complete inventory
of parts and accessories, the company provides
a specialized personal sales and service for the automotive trade.
Pictured here is the sales counter at the office and warehouse.*

*The new IBM-7070 high-speed
electronic data processing machine
is used for rapid processing
of vital company sales
and accounting data.*

FRANCHISE PROGRAM READIED

In connection with American Parts Company's internal development program to increase sales and improve earnings, a plan is being readied to establish a franchise wholesaler program for selected independent automotive parts concerns throughout our marketing area. The basic program includes the merchandising of certain American Parts brands and can be easily expanded into new areas as additional subsidiaries are acquired. Initial research and study have proved most encouraging, and it is anticipated that a market test of the plan will take place shortly after the first of the year.

One of the advanced methods used by The Klock Corporation in the thermal processing of metals for spacecraft is the nitriding of stainless steels. This process permits the engineer to select and harden a specific area of the metal surface.

NON-AUTOMOTIVE SUBSIDIARIES

In manufacturing and other fields of distribution, Gulf & Western operates six subsidiaries. The sales and earnings of these companies contributed materially to over-all progress.

Michigan Plating and Stamping Company, Grand Rapids, Michigan, is a manufacturer of bumpers and bumper parts for passenger cars and trucks since the early 1920's. This year the company completed a $1.5 million expansion and modernization program which has doubled the production capacity of the plant.

Unicord Incorporated, of New York City, is a nationwide distributor of the "Pianorgan" electric chord organ. The company has recently completed an advertising program to increase its share of the ever-expanding leisure market.

Unicord International is a non-domestic subsidiary and is engaged in sales and distribution of foreign products outside the United States.

J. A. Walsh & Co., Inc., of Houston, Texas, is a regional distributor for RCA Victor and RCA Whirlpool products. During the year, Walsh improved its market penetration in the Houston-Gulf Coast area.

Mal Tool & Engineering Corporation, of Manchester, Connecticut, manufactures precision parts and assemblies required in jet engines, rockets, and other space-

The final step in Michigan Plating and Stamping Company's five-year expansion program was the installation of a 1000-ton bumper press. This installation, together with the installation of other large presses, nickel tanks, the streamlining of plant layout and enlarging the shipping area enabled the company to double its production capacity.

craft. Production was recently accelerated at the plant to satisfy a record backlog of orders. In order to better serve its customers in Florida, Mal Tool opened a new installation at Palm Beach which is now operating at full capacity.

The Klock Corporation, of Manchester, Connecticut, is a thermal processor of space age metals and also does sub-assemblies of aircraft and missile components. This company, which was acquired in May 1961, strengthened Gulf & Western's position in this field of great potential. Klock's sales and earnings during 1960-61 were at record highs.

INTERNAL PROGRESS

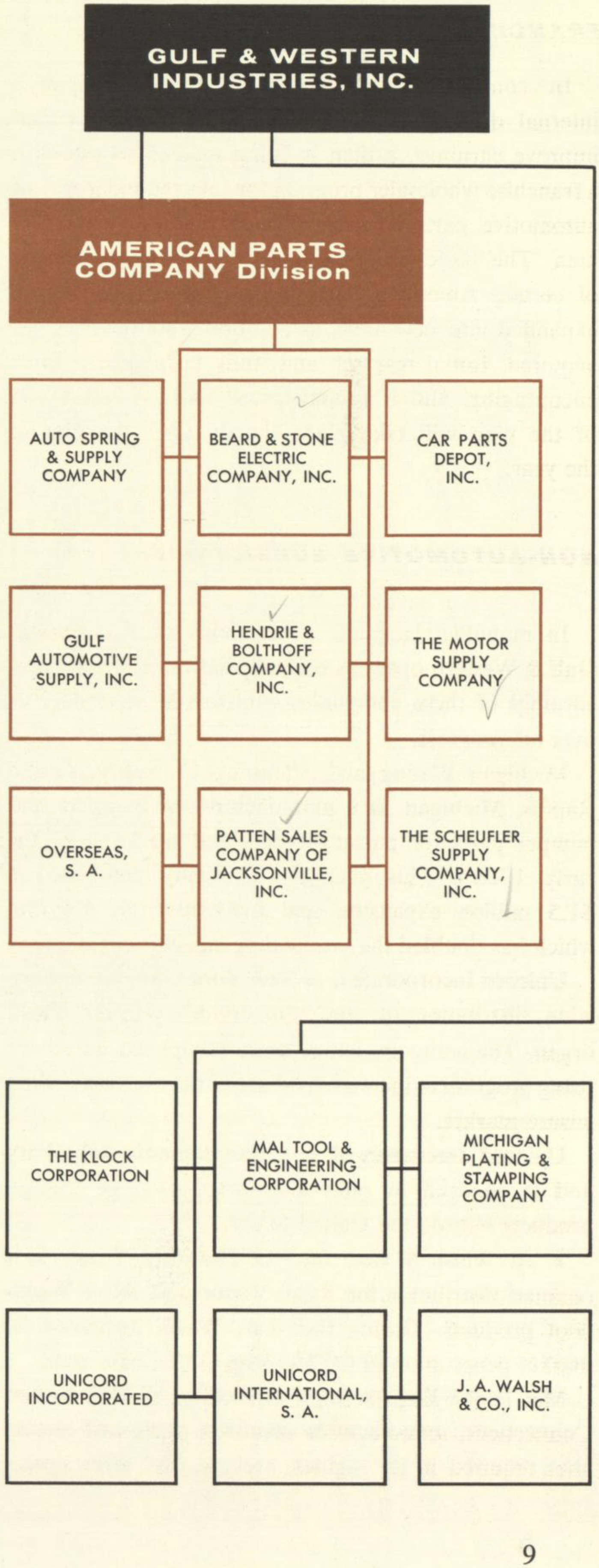
Gulf & Western's 1822 employees, now located over a broad geographical area, have increased by 70 per cent over the number at July 31 last year. The company instituted this year an employees' Stock Purchase Plan which is being well received. The Stock Purchase Plan, together with the employees' Group Insurance Plan, are contributing effectively to the development of a sound, long-range employees' benefit program.

Substantial progress also has been made in effecting economies and improving efficiency of operation through the use of electronic data processing equipment for sales analysis, billing, and inventory control. This system of processing data is rapidly being effected throughout the American Parts Company division.

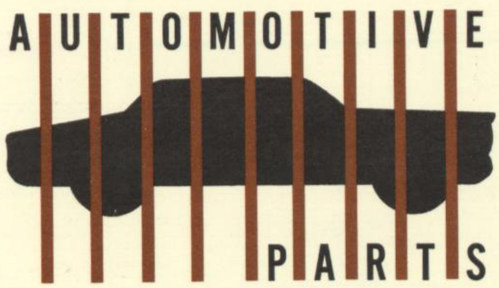
FINANCIAL PROGRESS

Since Gulf & Western launched its expansion program in December 1957, it has grown from a single product company with annual sales of $6.5 million and a net worth of $2.3 million on July 31, 1957, to a distributing and manufacturing organization which as of July 31, 1961, had annual sales of $33.8 million and a net worth of $10.4 million.

Total assets of the company have been increased from $3.6 million to $22.6 million during this four-year period, while working capital was increased from $752 thousand to $10.3 million.



AUTOMOTIVE PARTS D



LEGEND

- ■ Auto Spring & Supply Company
- ▲ Beard & Stone Electric Company, Inc.
- ● Car Parts Depot, Inc.
- ★ Gulf Automotive Supply, Inc.
- † Hendrie & Bolthoff Company, Inc.
- □ The Motor Supply Company
- ○ Overseas, S. A.
- ♦ Patten Sales Company of Jacksonville, Inc.
- ♣ The Scheufler Supply Company, Inc.

STRIBUTION EXPANDED

Through nine subsidiaries comprised of 92 outlets, American Parts Company division is increasing its sales and service over a broad geographical area.

AUTO SPRING & SUPPLY COMPANY

Abilene, Texas
Nocona, Texas
Stamford, Texas
Vernon, Texas
Wichita Falls, Texas (2 outlets)

BEARD & STONE ELECTRIC COMPANY, INC.

Northern Division

Amarillo, Texas
Dallas, Texas
Fort Worth, Texas

Southern Division

Houston, Texas

CAR PARTS DEPOT, INC.

Alamogordo, New Mexico
Artesia, New Mexico
Carlsbad, New Mexico
Hobbs, New Mexico
Las Cruces, New Mexico
Roswell, New Mexico
Silver City, New Mexico
Alpine, Texas
Clint, Texas
El Paso, Texas (4 outlets)
Kermit, Texas
Marfa, Texas
Pecos, Texas

GULF AUTOMOTIVE SUPPLY, INC.

Northern Division

Dallas, Texas
Littlefield, Texas
Lubbock, Texas
Waco, Texas

Southern Division

Beaumont, Texas
Conroe, Texas
Galveston, Texas
Houston, Texas
Huntsville, Texas
Navasota, Texas
Orange, Texas
Palestine, Texas

HENDRIE & BOLTHOFF COMPANY, INC.

Aurora, Colorado
Boulder, Colorado
Colorado Springs, Colorado
Denver, Colorado (2 outlets)
Durango, Colorado
Fort Collins, Colorado
Fort Morgan, Colorado
Grand Junction, Colorado
Greeley, Colorado
La Junta, Colorado
Lakewood, Colorado
Lamar, Colorado
Longmont, Colorado
Pueblo, Colorado
Sterling, Colorado
Billings, Montana
Scottsbluff, Nebraska
Albuquerque, New Mexico
Santa Fe, New Mexico
Deadwood, South Dakota

Casper Supply Company, Inc.

Chadron, Nebraska
Rapid City, South Dakota
Casper, Wyoming (2 outlets)
Cheyenne, Wyoming
Lander, Wyoming
Laramie, Wyoming
Riverton, Wyoming
Sheridan, Wyoming
Worland, Wyoming

THE MOTOR SUPPLY COMPANY

Augusta, Georgia (2 outlets)
Brunswick, Georgia
Savannah, Georgia (4 outlets)
Waycross, Georgia
Aiken, South Carolina
Beaufort, South Carolina

OVERSEAS, S. A.

Mexico City, Mexico

PATTEN SALES COMPANY OF JACKSONVILLE, INC.

Jacksonville, Florida
Tampa, Florida

THE SCHEUFLER SUPPLY COMPANY, INC.

Dodge City, Kansas
Garden City, Kansas
Goodland, Kansas
Great Bend, Kansas (2 outlets)
Hays, Kansas
Hutchinson, Kansas
Larned, Kansas
Lyons, Kansas
Russell, Kansas

Profile of a Growing Industry

As one of the nation's leading wholesale automotive parts distributors, Gulf & Western is an integral part of the multi-billion dollar U. S. automotive industry — an industry which employs one out of every seven wage-earners in the United States. The automotive industry, further, represents more than 17 per cent of all businesses in the U. S. and accounts for about 18 per cent of the total dollar volume of all U. S. retail, wholesale and service firms.

The distribution and sales of automotive parts is vitally important to the stability of the automotive industry as a whole. Last year a total of $4.5 billion was spent at the national level for automotive merchandise to maintain in operating condition the vast number of cars, trucks, and off-the-highway equipment. Gulf & Western is expanding its distribution system to meet the needs of this growing industry.

VEHICLE REGISTRATIONS CLIMB

The market for automotive parts is based upon the number of registered vehicles. This number is a figure which has increased steadily year after year. In 1960, total registration reached 73.6 million, compared to 62.8 million only five years ago. Vehicle registration is expected to climb to over 89 million by 1966, and ten years from now, in 1971, should reach more than 101.2 million. As each model year passes, the future market for parts is assured by the tremendous numbers of new cars and trucks coming off the production lines.

PARTS SALES INCREASE

Sales of parts and accessories have steadily increased over the past five years until in 1960 the average sales to each motor vehicle reached $58.50. Next only to food and housing which take 27 per cent and 13 per cent, respectively, out of the average family budget, transportation requirements take the largest slice. During the year, the average car owner uses approximately 12 per cent of his total expenditures for transportation, while he spends about 10 per cent for clothing and 6 per cent for medical care. The automobile has, undoubtedly, become one of the necessities of life.

Industry surveys indicate that parts sales this year will rise 8 to 10 per cent. Based on past performance, it is estimated that over the next ten years, sales in the automotive parts replacement industry will increase by 100 per cent.

U. S. MOTOR VEHICLE REGISTRATIONS

YEAR	TOTAL REGISTRATIONS
1960	73,564,000
1959	71,212,000
1958	68,299,000
1957	67,131,000
1956	65,154,000
1955	62,760,000
1954	58,590,000

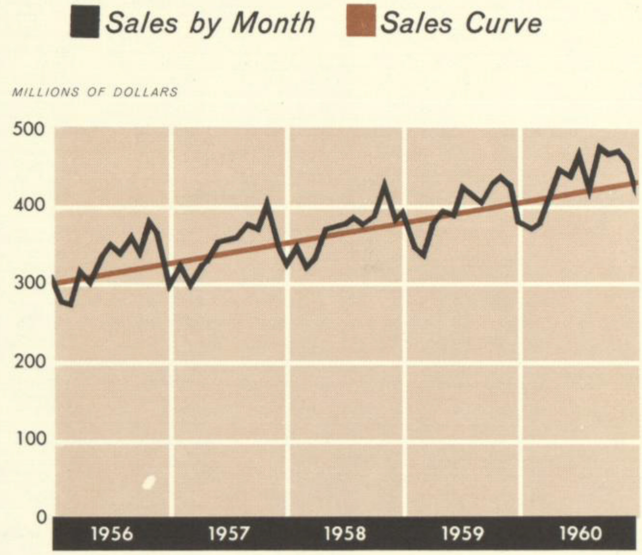
MARKET FOR PARTS ASSURED

The solidity of the parts aftermarket is confirmed by the sales growth that has been established over the years. However, there are other noteworthy evidences of its stability. One may be seen in its relative position during fluctuations in the economy. In years of recession, motorists tend to drive their cars even longer than they would normally, depending upon replacement parts to keep their cars in operating condition. It has been proved many times that the purchase of a new car is postponable, whereas the purchase of a replacement part is not. On the other hand, in years of business upswing, records indicate that the number of two- and three-car families greatly increases. At the same time, while a rise in the economy is normally typified by additional new car sales, motorists in general spend more for maintenance of their cars.

With the increasing numbers of families moving to the suburbs and commuting to the cities over high-speed, multiple-lane highway systems, more people are driving more cars more miles than ever before. In 1960 the number of vehicle miles traveled reached an all-time high of 720 billion miles. A rising standard of living and the application of modern production methods have kept the United States ahead in producing vehicles for transportation. This nation continues to lead all countries, accounting for 52 per cent of the world's production of passenger cars. In 1960, 77 per cent of all families in the U. S. owned one or more cars. This figure is up from 60 per cent in 1950. It has reached a point where last year there was one car for every three Americans.

PARTS AND ACCESSORIES

Sales in Millions of Dollars by Month



ANNUAL MILES OF TRAVEL IN U. S.

(IN THOUSANDS)

YEAR	TOTAL MILES OF VEHICLE TRAVEL
1960	720,000,000
1959	700,478,000
1958	664,653,000
1957	647,004,000
1956	627,843,000
1955	603,434,000
1954	560,857,000

GULF & WESTERN'S EXPANSION SOUND

Based on industry's statistics and Gulf & Western's own market surveys, the soundness of the company's parts distribution program continues to be confirmed. With these facts in mind and the experience that has been gained from three years of successful operation, management is confident of achieving its goal — to establish a nation-wide system of wholesale automotive parts outlets.

Gulf & Western Industries, Inc.

AND SUBSIDIARIES

CONSOLIDATED BALAN

ASSETS	**1961**	**1960**
CURRENT ASSETS		
Cash	$ 1,161,349	$ 1,055,618
Marketable securities — at cost	63,135	182,364
Trade accounts and notes receivable, less allowances of $86,621 in 1961 and $62,295 in 1960	6,052,531	3,192,694
Inventories:		
At last-in, first-out cost — (current prices were higher by $890,494 in 1961 and $607,946 in 1960) — merchandise	$ 2,335,745	$ 1,516,882
At lower of first-in, first-out cost or market:		
Merchandise	6,463,840	4,385,867
Manufacturing	707,987	863,441
	$ 9,507,572	$ 6,766,190
Prepaid insurance, taxes, and other expenses	259,982	135,213
TOTAL CURRENT ASSETS	$17,044,569	$11,332,079
PROPERTY, PLANT, AND EQUIPMENT — at cost	$ 6,387,427	$ 3,603,568
Less allowances for depreciation and amortization	2,265,785	1,651,774
	$ 4,121,642	$ 1,951,794
OTHER ASSETS		
Investment in capital stock of subsidiary not consolidated (72% interest), at cost (underlying net book value $43,271)	$ 44,350	$ 44,350
Note receivable — Note K	450,000	—
Unamortized debenture expense	—	143,125
Deferred acquisition and expansion program costs, less amortization — Note B	217,208	81,731
Excess of cost of subsidiaries purchased over net book value of underlying assets at date of acquisition, less amortization	546,101	275,449
Cash value of life insurance and other	147,275	108,127
	$ 1,404,934	$ 652,782
	$22,571,145	$13,936,655

CE SHEET *JULY 31, 1961, AND JULY 31, 1960 (ADJUSTED — NOTE A)*

LIABILITIES	**1961**	**1960**
CURRENT LIABILITIES		
Notes payable:		
To banks, secured by:		
Accounts receivable or equipment	$ 188,819	$ 295,207
Note receivable and stock under purchase option — Note K	450,000	—
Unsecured	854,567	948,692
To others, partly secured	199,090	131,160
Trade accounts payable	3,389,666	1,777,600
Accrued salaries, taxes, and other expenses	671,025	511,976
Federal taxes on income — estimated	339,000	392,654
Current maturities of long-term debt	687,636	160,645
TOTAL CURRENT LIABILITIES	$ 6,779,803	$ 4,217,934
LONG-TERM DEBT, less current maturities — Note C	5,004,673	1,798,915
DEFERRED FEDERAL INCOME TAXES — Notes B and H	293,000	37,500
MINORITY INTEREST IN CONSOLIDATED SUBSIDIARY	112,509	—
STOCKHOLDERS' EQUITY		
Common stock, par value $1.00 a share:		
Authorized 2,000,000 shares; issued and outstanding 1,046,154 in 1961 and 829,605 in 1960 — Notes E and F	$ 1,046,154	$ 829,605
Paid-in surplus	4,010,192	2,344,014
Retained earnings	5,324,814	4,708,687
	$10,381,160	$ 7,882,306
	$22,571,145	$13,936,655

See notes to consolidated financial statements.

Consolidated Statement of Earnings

Years ended July 31, 1961, and July 31, 1960 (Adjusted — Note A)

	1961	1960
Net sales	$33,835,385	$28,759,469
Cost of goods sold — Note H	25,092,953	21,662,859
GROSS PROFIT	$ 8,742,432	$ 7,096,610
Selling, administrative, and general expenses	6,995,987	5,855,230
	$ 1,746,445	$ 1,241,380
Other charges:		
Amortization of intangibles — Note A	$ 27,545	$ —
Minority interest in earnings of a consolidated subsidiary	3,490	—
Interest expense	189,393	133,811
Others — net	4,332	50,569
	$ 224,760	$ 184,380
EARNINGS BEFORE SPECIAL GAINS AND FEDERAL INCOME TAXES	$ 1,521,685	$ 1,057,000
Federal income taxes — estimated — Notes B, D, and H	671,642	495,454
NET EARNINGS BEFORE SPECIAL GAINS	$ 850,043	$ 561,546
Special gains:		
Gain upon the sale of a subsidiary's business and assets — Note A	$ 141,080	$ —
Proceeds of life insurance policies	11,174	144,672
	$ 152,254	$ 144,672
NET EARNINGS AND SPECIAL GAINS	$ 1,002,297	$ 706,218

Note — Depreciation and amortization amounted to $453,062 in 1961 and $300,525 in 1960.

Consolidated Statements of Retained Earnings and Paid-In Surplus

Years ended July 31, 1961, and July 31, 1960 (Adjusted — Note A)

	1961	1960
RETAINED EARNINGS		
Amount at beginning of year	$ 4,708,687	$ 3,954,696
Add:		
Net earnings and special gains for the year	1,002,297	706,218
Retained earnings of a wholly-owned subsidiary (accumulated prior to acquisition) applicable to issuance of 105,000 shares of common stock on debentures convertible under warrants	—	275,953
	$ 5,710,984	$ 4,936,867
Deduct dividends:		
Fair value of common stock issued as 5% stock dividends (35,375 shares at $10.00 in 1961 and 19,693 at $9.75 in 1960) — Note G	$ 353,750	$ 192,007
Cash payments in lieu of fractional shares on stock dividends	6,975	5,728
Cash dividends paid by a "pooled" subsidiary prior to acquisition	25,445	30,445
	$ 386,170	$ 228,180
AMOUNT AT END OF YEAR	$ 5,324,814	$ 4,708,687
PAID-IN SURPLUS		
Amount at beginning of year	$ 2,344,014	$ 1,542,314
Add:		
Sale of capital stock by a "pooled" subsidiary prior to acquisition	3,600	—
Proceeds from sale of warrants on 50,000 shares of common stock — Note F	500	—
Amounts, in excess of par value, recorded in respect to common shares issued in connection with acquisition of companies, stock dividends, exercise of stock options, and conversion of debentures — Note E	1,977,441	815,950
	$ 4,325,555	$ 2,358,264
Deduct:		
Costs incurred on acquisition of "pooled" subsidiaries	$ 10,379	$ 14,250
Unamortized debenture expense applicable to debentures converted to common stock	132,784	—
Purchase of treasury stock by a "pooled" subsidiary prior to acquisition	172,200	—
	$ 315,363	$ 14,250
AMOUNT AT END OF YEAR	$ 4,010,192	$ 2,344,014

See notes to consolidated financial statements.

Notes to Consolidated Financial Statements

YEAR ENDED JULY 31, 1961

NOTE A — Principles of consolidation and acquisitions of businesses

The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries and one of its two partly-owned subsidiaries. All inter-company investments, accounts, and transactions have been eliminated upon consolidation. The operations, assets, and liabilities of the subsidiary not consolidated are minor in amount.

Five subsidiaries were acquired during the year, two in transactions treated as "pooling of interests" and three in transactions treated as purchases.

The two "pooled" subsidiaries' assets, liabilities, paid-in surplus, and retained earnings have been combined with the corresponding accounts of the Company upon consolidation at the amounts shown by the subsidiaries' books, and the operations of the subsidiaries for periods prior to acquisition have been combined with the operations of the Company for corresponding periods as though the combination of the businesses had been in effect throughout the period of two years ended July 31, 1961.

The three "purchased" subsidiaries' accounts have been taken into consolidation on the basis of purchase cost to the Company or to its other subsidiaries, and their operations (excepting those of The J. W. M. Corporation, doing business as The Motor Supply Company) have been included in consolidation beginning with the date of acquisition. When controlling interest of J. W. M. was purchased by the Company, it was operating a business not compatible with that of the Company or any of its other subsidiaries. J. W. M. therefore subsequently sold this business and the assets pertaining to it (at a gain of $141,080 over the purchase cost) and concurrently purchased an automotive parts business, and J. W. M.'s operations have been included in consolidation beginning with the operation of the automotive parts business.

In addition to the five subsidiaries acquired during the year, the Company during the year purchased five other businesses and their related assets (including the aforementioned automotive parts business purchased by J. W. M.), and the income statements include the operations of these businesses beginning with the date of purchase.

The differences between cost to the Company of "purchased" subsidiaries and net book value of underlying assets of the subsidiaries at date of purchase are allocated upon consolidation to the underlying net assets, including intangibles not shown by the books of the subsidiaries, by methods appropriate to the terms and conditions of the purchase and are charged, commencing August 1, 1960, to consolidated income by periodic amortization.

NOTE B — Deferred acquisition and expansion program costs and related income taxes

The Company incurred expenses of $168,843 in 1961 and $81,731 in 1960 in connection with its corporate acquisition and expansion program. These expenses are deferred and amortized over a period of five years. This amortization amounted to $33,366 in 1961 and $ —o— in 1960. In computing taxable income, these expenses are deducted in the year incurred. As income of future years will be reduced by amortization of these expenses without corresponding tax benefits, provision has been made in the consolidated financial statements for applicable estimated deferred federal income taxes of $75,500 in 1961 and $37,500 in 1960.

NOTE C — Long-term debt

Long-term debt includes the following:

	1961	1960
Notes payable to banks:		
5% and 5½% notes with annual maturities of $93,148	$ 308,960	$ —
6% note, maturing $8,606 monthly, secured by chattel mortgage on certain equipment	100,000	—
Notes payable arising from acquisition of subsidiaries:		
6% note secured by chattel mortgage on equipment, and conditional sales contracts	27,156	74,483
5% and 6% unsecured notes with annual maturities of $61,231	361,851	67,557
Unsecured, non-interest bearing notes with annual maturities of $136,894	837,045	—
Unsecured, non-interest bearing notes, payable over a five-year period, with payment contingent on the net earnings before taxes of a subsidiary	420,909	—
Amount due on purchase of assets of Hendrie & Bolthoff Company, Inc. (see paragraph below)	3,353,023	—
Other:		
5% unsecured note, maturing $12,500 monthly	175,000	300,000
6% convertible subordinated debentures	—	1,500,000
8% note secured by mortgage on building, maturing $500 monthly	35,447	—
Conditional sales contract, notes on equipment, and other	72,918	17,520
	$5,692,309	$1,959,560
Less amounts due within one year classified as current liabilities	687,636	160,645
	$5,004,673	$1,798,915

The amount due on the purchase of assets of Hendrie & Bolthoff Company, Inc., was paid on August 31, 1961, from the proceeds of $3,600,000 of 5½% notes issued to a group of banks. The Company intends to retire these notes from the proceeds of other long-term financing. Should an event occur, which would preclude the completion of such other financing, certain of the banks have indicated a willingness to amend the notes from a five-month to a five-year term loan. Accordingly, the liability for the asset purchase has been classified herein as long-term debt.

NOTE D — Federal income taxes

For the year ended July 31, 1961, a consolidated federal income tax return will be filed by the Company and all of its domestic subsidiaries which qualify for such consolidation. The consolidated federal income tax is approximately

$103,000 less than it otherwise would be because the sale of the assets of a subsidiary resulted in a loss for federal income tax purposes, but resulted in a gain for financial statement purposes (see Note A). For the prior tax year, the Company and its subsidiaries filed separate federal income tax returns.

NOTE E — Capital stock

Additional shares of the Company's capital stock were issued during the year:

	Shares Issued	Related Amounts In Excess of Par Value Credited to Paid-In Surplus
In connection with acquisition of net assets and business of three corporations	27,116	$ 244,044
Exercise of options under executives' stock option plan	23,979	67,644
Issued to stockholders as a stock dividend	35,375	318,375
Conversion of 6% convertible subordinated debentures	130,079	1,347,378
	216,549	$1,977,441

NOTE F — Stock options and reservations

Options granted and exercised during the year ended July 31, 1961, and the status of unexercised options granted pursuant to the Company's Stock Option Incentive Plan (option prices are not less than 95% of the quoted value of the Company's stock at the time the options were granted) are summarized as follows:

	No. of Shares	Option Prices
Options granted during the year	44,334	$545,045
Options rescinded during the year	5,512	19,998
Options exercised during the year	23,979	91,623
Shares reserved at July 31, 1961:		
For options granted and exercisable	1,654	$ 14,965
For options granted but not yet exercisable	83,973	863,845
	85,627	$878,810
For additional options, not yet granted	40,394	
	126,021	

On August 5, 1960, the Company entered into an agreement with a financial consultant pursuant to which the financial consultant purchased from the Company warrants entitling the holder to subscribe for 25,000 shares of the Company's common stock at $11.00 per share and 25,000 shares of the Company's common stock at $12.50 per share. On August 16, 1961, the Company repurchased from said financial consultant, at the original price, all of such warrants other than warrants to purchase 12,500 shares of the Company's common stock at $12.50 per share. On September 14, 1961, 11,250 shares were purchased under these warrants.

During the year, the Company established an employees' Stock Purchase Plan, and reserved 100,000 shares of the unissued common stock for possible sale thereto, none of which reserved shares had been sold at July 31, 1961 (however, 1,213 shares of the Company's common stock were purchased by the Plan in open market transactions during the five months the Plan has been in operation).

On January 30, 1961, the Company entered into an agreement with one of its Directors, who is an Officer of one of its Divisions, confirming a previous agreement pursuant to which the Company agreed to sell and the Director agreed to purchase 11,000 shares of the Company's common stock at $10.00 per share. The purchase price for the aforesaid shares is equal to the closing price of the Company's common stock on the American Stock Exchange on the day prior to the effective date of the original agreement.

NOTE G — Events subsequent to July 31, 1961

On August 17, 1961, the Board of Directors authorized a 5% stock dividend payable October 1, 1961, to shareholders of record at September 1, 1961 (fractional shares being payable in cash). Such stock dividend requires the reservation of additional 6,260, 550, and 63 shares, respectively, under "anti-dilution" provisions of the stock option plan, the stock reserved for sale to an officer of the Company, and for warrants set forth in Note F. Of the 6,260 shares reserved for the stock option plan, 4,281 apply to options that have been granted but not exercised.

NOTE H — Effect of business acquisitions on consolidated income

See letter to stockholders, page four, concerning effect of business acquisitions on consolidated gross income. Due to certain differences between the Company's financial statement reporting and income tax reporting of this income, $49,000 of the $60,000 related income tax provision in 1960 and $131,000 of the $385,000 related income tax provision in 1961 will not become due and payable, for all practical purposes, until the assets of the purchased businesses are sold or liquidated by the Company, and the "deferred" portions of tax provisions therefore are classified as deferred income taxes.

NOTE I — Long-term leases

The Company and all except three of its consolidated subsidiaries lease all office and warehouse facilities from various lessors on terms ranging from monthly to twenty years. The leases in effect at July 31, 1961, require annual rental payments of approximately $603,000 and, in most instances, the companies are liable for payment of property taxes, insurance, and repairs.

NOTE J — Pension, retirement, and profit-sharing plans

Amounts contributed by three of the Company's subsidiaries under various pension, retirement, and profit-sharing plans were $70,806 in 1961 and $140,097 in 1960. With respect to a retirement plan, consulting actuaries estimate that amounts required to fund past service costs were $333,000 at July 31, 1961, and $270,000 at July 31, 1960.

NOTE K — Note receivable and related purchase option

A note receivable for $450,000 at July 31, 1961, is secured by pledge of corporate stock optioned to the Company at a price of $1,392,222. Subject to certain conditions occurring not later than March 1964, the Company is obligated to exercise such purchase option.

AUTOMOTIVE PARTS

REPORT *of*

Certified Public Accountants

ERNST & ERNST
CERTIFIED PUBLIC ACCOUNTANTS
2600 GULF BUILDING
HOUSTON 2, TEXAS

BOARD OF DIRECTORS,
GULF & WESTERN INDUSTRIES, INC.,
HOUSTON, TEXAS.

We have examined the consolidated financial statements of Gulf & Western Industries, Inc. and its consolidated subsidiaries for the year ended July 31, 1961. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

Included in long-term debt in the accompanying balance sheet is an obligation of $3,353,023 which was a current liability at July 31, 1961 but which the Company has classified as long-term debt for the reasons described in Note C.

In our opinion, the accompanying balance sheet and statements of earnings, retained earnings, and paid-in surplus present fairly the consolidated financial position of Gulf & Western Industries, Inc. and its consolidated subsidiaries at July 31, 1961, and the consolidated results of their operations for the year then ended, in conformity with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

Ernst & Ernst

Houston, Texas
September 20, 1961

Directors

Joel Dolkart
Partner
Strasser, Spiegelberg, Fried & Frank
New York, New York

From left to right:

John H. Duncan
President
Gulf & Western Industries, Inc.
Houston, Texas

Charles G. Bluhdorn
Chairman of the Board
Gulf & Western Industries, Inc.
New York, New York

Thos. F. Plant
Chairman of the Executive Committee
Gulf & Western Industries, Inc.
Houston, Texas

Siegel W. Judd
Partner
Warner, Norcross & Judd
Grand Rapids, Michigan

David N. Judelson
President
Oscar I. Judelshon
New York, New York

Lewis M. Krohn
Member
Ira Haupt & Co.
New York, New York

Basil E. Ryan
Chairman of the Board
Car Parts Depot, Inc.
El Paso, Texas

Irwin Schloss
President
Irwin Schloss & Co., Inc.
New York, New York

EXECUTIVE COMMITTEE

Thos. F. Plant, *Chairman* · Charles G. Bluhdorn · John H. Duncan · David N. Judelson · Joel Dolkart

OFFICERS

Charles G. Bluhdorn, *Chairman of the Board*
John H. Duncan, *President*
Basil E. Ryan, *Vice President*
William W. Brown, *Vice President*
David N. Judelson, *Vice President*
T. H. Neyland, *Treasurer, Controller, Assistant Secretary*
Joel Dolkart, *Secretary*
Siegel W. Judd, *Assistant Secretary*
Daniel C. Arnold, *Assistant Secretary*

TRANSFER AGENT

Gulf & Western Industries, Inc.
Grand Rapids, Michigan

REGISTRAR

The Old Kent Bank and Trust Co.
Grand Rapids, Michigan

ANNUAL MEETING

November 21, 1961
Houston, Texas

SUBSIDIARIES

Auto Spring & Supply Company
Beard & Stone Electric Company, Inc.
Car Parts Depot, Inc.
Gulf Automotive Supply, Inc.
Hendrie & Bolthoff Company, Inc.
The Motor Supply Company
Overseas, S. A.
Patten Sales Company of Jacksonville, Inc.
The Scheufler Supply Company, Inc.
The Klock Corporation
Mal Tool & Engineering Corporation
Michigan Plating and Stamping Company
Unicord Incorporated
Unicord International, S. A.
J. A. Walsh & Co., Inc.

Gulf & Western
Industries, Inc.
OFFICES:
HOUSTON, TEXAS, 2903 RICHMOND AVE.
GRAND RAPIDS, MICH., 740 ANN STREET, N. W.
NEW YORK, N. Y., 4615 EMPIRE STATE BUILDING