





Dear Shareholder,

Go right ahead – break out the noisemakers, blow up the balloons, toss the confetti.  It's time to celebrate.

It's Herman Miller's 75th birthday – a time to glance back and to look forward. And it's time to celebrate another great year. We're celebrating our third straight year of record sales (\$1.7 billion), cash flow from operations  (\$268.7 million), profits (\$128.3 million), and EVA (\$78.4 million).

 We also are celebrating who we are – the company we've become over the past 75 years. We've built our business on insight, inventiveness, integrity, and sincerity. We've always believed in empowering people to succeed, both the people we serve and  the people within our corporate community. We're honored that *Fortune* magazine named us as one of the 100 best companies to





work for in America, and as the country's most socially responsible corporation.



At Herman Miller, there is still a spirited vitality – a creative, will-do attitude – permeating our company from Bath, England, to Zeeland, Michigan.

Our goal is straightforward: We intend to lead our industry in providing healthy, safe, and productive work environments.

Our plan is powerful: Build on a foundation of knowledge and thought leadership.

Connect with our customers in new and different ways, including the use of emerging technologies like electronic commerce.



Deliver to our customers the knowledge we've acquired, both in our products and services – with unparalleled speed, convenience, and reliability. Tie it all together with the best network of service providers in the world.





Bold goals are nothing new at Herman Miller. Through the visionary leadership of our founders, the DePree family, and others, our company has responded to change many times over the past 75 years. Our ability to meet the challenges of change has brought us to this birthday celebration – and to the best year in the history of our company.

Happy 75th birthday, with best wishes for many, many more.



Michael A. Volkema

Michael A. Volkema
President and Chief Executive Officer

David L. Nelson

David L. Nelson
Chairman of the Board



Management's Discussion and Analysis

The issues discussed in management's discussion and analysis should be read in conjunction with the company's consolidated financial statements and the notes to the consolidated financial statements.

Forward-Looking Statements

This discussion and analysis of financial condition and results of operations, as well as other sections of our Annual Report, contain forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act, as amended, that are based on management's beliefs, assumptions, current expectations, estimates, and projections about the office-furniture industry, the economy, and about the company itself. Words such as "anticipates," "believes," "confident," "estimates," "expects," "forecasts," "likely," "plans," "projects," "should," variations of such words, and similar expressions are intended to identify such forward-looking statements. These statements are not guarantees of future performance and involve certain risks, uncertainties, and assumptions that are difficult to predict with likelihood, and degree of occurrence. Therefore, actual results may materially differ from what may be expressed or forecasted in such statements. Furthermore, Herman Miller, Inc., undertakes no obligation to update, amend, or clarify forward-looking statements, whether as a result of new information, future events, or otherwise.

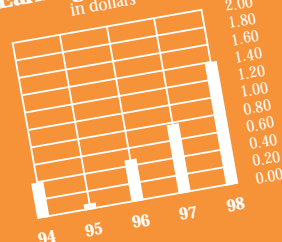
Overview

Let us begin our overview by stating that we had another record-setting year at Herman Miller, Inc. We set records in "Economic Value Added" (EVA), net sales, new orders, net income, earnings per share, cash flow from operating activities, and cash returned to shareholders.

If you have been following our company for the past few years, you will remember that two years ago we adopted EVA as our measurement tool to determine whether or not we had created value for both our external shareholders and our employee-owners. Extensive independent research has shown that EVA more closely correlates than any other performance measure.

Simply put, EVA is what remains of profits after tax once a charge for the capital employed in the business is deducted. As an operating discipline, the main advantage of EVA is that it focuses management's attention on the balance sheet as well as on the income statement. Our company is, in effect, competing for scarce capital resources. Management's task is to put this scarce resource to work and earn the best possible return for our shareholders. This means investing in projects that earn a return greater than the cost of the funds sourced from our investors. As long as we are making investments that earn a return higher than the cost of capital, then our investors should earn a return in excess of their expectations.

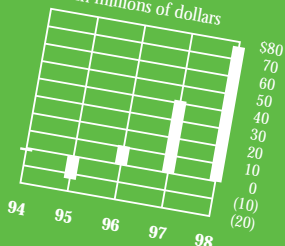
Earnings Per Share
in dollars



market
with shareholder value

EVA

in millions of dollars



We took EVA a step further by linking our incentive-based compensation to it. All of our executive incentive compensation plans as well as all of our employee gain-sharing programs at each of the business units have been linked to this measure. Using EVA-based plans shifts the focus from budget performance to long-term continuous improvements in shareholder value. The EVA target is raised each year by an improvement factor, so that increasingly higher EVA targets must be attained in order to earn the same level of incentive pay. Our Board of Directors has set the EVA improvement factor for a period of three years.

This year, we decided to present our results to you by discussing what changes in our business have driven our EVA improvement. We believe this is important because EVA is utilized not only to measure our results, but also to evaluate potential business opportunities. In addition, we hope you will get a clearer picture of what will drive future improvements in both net income and in EVA and ultimately the value of your investment in our company. Let's begin by reviewing our EVA results.

Calculation of Economic Value Added

(In Thousands)	1998	1997	1996
Operating income	\$208,295	\$130,683	\$ 74,935
Adjust for:			
Divestiture/patent litigation	—	14,500	16,535
Interest expense on noncapitalized leases ⁽¹⁾	4,166	4,509	4,316
Goodwill amortization	6,161	4,725	4,115
Other	13,765	5,093	3,071
Increase in reserves	1,290	18,649	6,548
Capitalized design and research	2,101	2,819	1,984
Adjusted operating profit	235,778	180,978	111,504
Cash taxes ⁽²⁾	(90,703)	(72,091)	(34,561)
Net operating profit after taxes (NOPAT)	145,075	108,887	76,943
Weighted-average capital employed ⁽³⁾	606,018	617,727	605,438
Weighted-average cost of capital ⁽⁴⁾	11%	11%	11%
Cost of capital	66,662	67,950	66,598
Economic value added	\$ 78,413	\$ 40,937	\$ 10,345

(1) Imputed interest as if the total noncancelable lease payments were capitalized.

(2) The reported current tax provision is adjusted for the statutory tax impact of interest expense.

(3) Total assets less noninterest bearing liabilities plus the LIFO, doubtful accounts and notes receivable reserves, warranty reserve, amortized goodwill, loss on sale of the German manufacturing operation, patent litigation settlement costs, deferred taxes, restructuring costs, and capitalized design and research expense. Design and research is capitalized and amortized over 5 years.

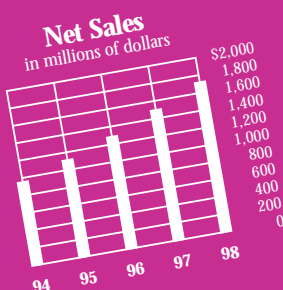
(4) Management's estimate of the weighted average of the minimum equity and debt returns required by the providers of capital.

As you can see, we generated \$78.4 million of EVA this year, compared to \$40.9 million last year, and just \$10.3 million in 1996. In 1998, our EVA increased 91.5 percent after increasing nearly 300 percent in 1997. Let's take a look at the drivers behind this improvement.

Key Drivers

Net Sales One of our key goals is know that we will not achieve this strategies which, in the long run, goal. In the current year, we very small margin. In 1998, net percent to a record the goal years with 18.5 percent,

to increase net sales by 15 percent per annum. We goal in each and every year. But we intend to develop are designed to enable us to meet or to exceed this missed that goal by a sales increased 14.9 \$1.72 billion. We exceeded in both of the prior two increases of 16.5 percent and respectively. Of course, growth is



only good if it is profitable growth. As you will read later in this document, not only did we increase our top line, we improved our operating margin on every dollar of sales. In 1998, the increase in net sales of \$222.7 million contributed approximately \$16.3 million to EVA and net income, which represents approximately 44 percent of the increase in EVA from 1997.

Domestic Operations The United States office furniture industry has experienced very strong demand over the past two years. The Business and Institutional Furniture Manufacturers Association (BIFMA) reported that United States sales grew approximately 12.5 percent in the twelve months ended May 1998, after increasing 10.7 percent in 1997, and 4.8 percent in 1996. As we explained last year, we believe that the strong demand has been driven by secular changes affecting work environments. The primary drivers were new and emerging work styles, the rapid deployment of technology, and the fast-growing population of knowledge workers. Because of these drivers, companies have been completely rethinking their approach to providing work environments for their employees. In addition, the favorable economic climate and healthy corporate profits in the U.S. have enabled companies to reinvest in their infrastructure.

We believe these secular changes will continue to drive industry dynamics for the foreseeable future. This should enable the industry to grow at a higher rate than the general economy. However, industry growth rates are expected to decline from the very fast pace of the past two years. BIFMA is currently estimating that industry sales will increase 8 percent in calendar 1998 and 6 percent for calendar 1999, or approximately 7 percent for our fiscal year 1999. This is somewhat less than had been previously predicted. While our domestic sales continued to grow at a very rapid rate during our fourth quarter of 1998, industry growth rates for the same period were significantly less than those experienced during the previous two years. Our ability to continue to grow at a multiple of the industry will depend on a variety of factors.

In 1998, our domestic sales increased by 16.7 percent, compared to 19.2 percent in 1997, and 16.7 percent in 1996. Given that our growth has exceeded the industry's growth, we believe we have gained market share in each of the past three fiscal years. Our domestic growth has been primarily driven by unit volume increases during the past three years. We have not materially changed list prices during the past three years and discounts have remained relatively stable during the past two years, after a slight increase in 1996. Individually, none of our acquisitions were material. Excluding acquisitions, our domestic sales increased 15.9 percent in 1998, 16.4 percent in 1997, and 13.7 percent in 1996.

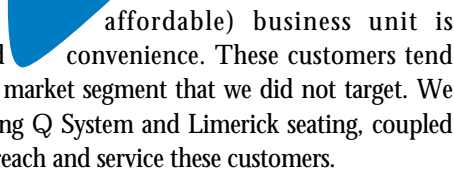
These growth statistics are nice, but what has enabled us to grow faster than our competition? The five key factors that have enabled us (and should continue to allow us to increase our share of the domestic market) are an industry trend of consolidation, our capability to serve two focused customer segments, development of a service business, an expanded product offering, and new channels created to reach out to customers not previously served by us.

Over the past 11 years, the combined market share of the five largest domestic manufacturers increased from 41 percent to 59 percent. This trend has been the result both of acquisitions and internal growth. We have benefited from this trend as our market share has increased significantly over this time period. We believe the trend reflects our customers' desire to do business with companies that can supply a broad range of value-creating products and services.

We understand that the key to our success with customers who have more complex needs lies in our ability to develop and maintain effective, long-term relationships with them. Such customers typically ask us to provide bundled solutions – products and services – that are both comprehensive and tailored to their needs. In response, our standard product offering is being expanded, as is our ability to cost-effectively design, specify, and manufacture custom products. Design and installation services traditionally provided by dealerships continue to be a mainstay; to these we are adding speciality



innovation and it still does. Our strategy to expand our product line is unquestionably winning. Aeron and its internal resources



affordable) business unit is convenience. These customers tend to be in the mass segment that we did not target. We have a 100% system and Limerick seating, coupled with a 100% service these customers.

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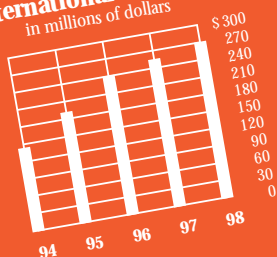
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Asian economy with softening demand for our products in that region. The weakness in Asia, combined with the absence of large projects in other regions, resulted in a decrease of 6.7 percent in international sales in the fourth quarter of 1998. Keep in mind that our international business is very sensitive to large projects. In the fourth quarter of 1997, we had two very large projects which made the comparison unusually difficult.

The sales growth in 1998 and the prior year (4.6 percent) reflect increased unit volume growth. Fiscal 1996 sales growth (27.3 percent) was partially attributable to unit volume growth, but was impacted by acquisitions. Excluding the acquisitions, unit volume growth was 9.2 percent in that year.

More importantly, our international operations continued to show improvements in earnings. Earnings have increased from a loss in 1996 of \$8.0 million, to income of \$1.3 million (excluding the sale of our German manufacturing operation) in 1997, to income of \$11.2 million in 1998. Starting with the fourth quarter of fiscal 1997, we have had five consecutive quarters of operating profits in our international business. While we are not generating positive EVA in our international operations, we are pleased with the progress we have made over the past two years. The improvement in 1998 reflects the higher sales volume levels in Canada and the United Kingdom and the sale of the German manufacturing operation. This followed a year of substantial improvements in our Mexican operation.

International Net Sales
in millions of dollars



resulted in a share after tax).

In 1996, our loss from international operations included pretax charges for the discontinuation of two product lines in Europe (\$1.6 million) and provisions for unrealizable barter receivables in Mexico (\$2.5 million). In addition, a charge of approximately \$1.0 million was recorded to reserve for deferred tax assets associated with our Mexican operations.

Gross Margin During 1998, we achieved our second consecutive year of improved gross margin. Gross margin, as a percent of sales, increased to 37.2 percent for the year, compared to 35.7 percent in the prior year, and 33.9 percent in 1996. This improvement contributed approximately \$13.5 million to EVA and net income in the current year.

Historically, one of our weaknesses was manufacturing operations, not due to lack of good people, but due to lack of focus. This began to change in 1995, when we performed an assessment of our manufacturing and distribution capacity and processes. This assessment led to the decision to reengineer certain manufacturing processes, to change our logistics operations, and to close nonvalue-adding facilities. These efforts resulted in increased throughput, decreased fixed and semifixed manufacturing costs, and, ultimately, increased levels of gross margin.

Additionally, the gross margin improvements in both 1998 and 1997 were attributable to a more favorable product mix, value enhancement engineering projects in our domestic activities, and, to a lesser extent, improvements in Mexico and Germany. Gross margins in 1996 were comparable to

the second half of
were offset by

1995. Cost benefits from the manufacturing and logistics changes additional price discounts given to customers. The manufacturing improvements were also a primary driver of a reduction in our days sales outstanding in the sum of accounts receivable and inventory.

At the end of 1998, this statistic had improved to 56.2 days, compared to 63.3 days and 75.6 days at the end of 1997 and 1996, respectively.

During the past three years, we have begun to introduce lean manufacturing techniques into our operations. These techniques are a process of continuous improvement that focuses on the elimination of waste in all aspects of our business. We are in the very early stages of this work. Therefore, the benefits derived to date have not been significant. We are also in the process of implementing a new Enterprise Resource Planning most of our U.S. operations. Internally, we refer to this as we will spend over \$80 million on this project. As part of this most of our operating processes. In the long run, we believe the implementation of Project Renaissance, coupled with the implementation of lean manufacturing techniques, will improve our quality, reduce lead-times and the cost of producing product, and improve our usage of both fixed assets and working capital. We are very confident of the long-term benefits we expect from both of these initiatives. However, we need to be realistic about the risks. Many companies are negatively impacted by disruptions during the implementation phase of projects like Renaissance. We are taking reasonable precautions to avoid disruptions, but it is important to consider the risks. In the end, assuming no significant change in competitive pricing, we believe that gross margins should remain at approximately the same level as we have experienced over the

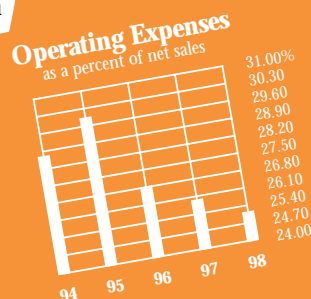
(ERP) system in Project Renaissance. In total, project, we are reengineering the implementation of Project Renaissance, coupled with the implementation of lean manufacturing techniques, will improve our quality, reduce lead-times and the cost of producing product, and improve our usage of both fixed assets and working capital. We are very confident of the long-term benefits we expect from both of these initiatives. However, we need to be realistic about the risks. Many companies are negatively impacted by disruptions during the implementation phase of projects like Renaissance. We are taking reasonable precautions to avoid disruptions, but it is important to consider the risks. In the end, assuming no significant change in competitive pricing, we believe that gross margins should remain at approximately the same level as we have experienced over the past two years.

Operating Expenses At the beginning of 1996, we set a goal to expenses as a percent of net sales to 25.0 percent by the end of 1998. Our operating expenses was selling, general, administrative, and research expenses. This goal may not sound aggressive today, but we had just a year in which these costs had ballooned to 30.0 percent. We are proud to state that we reached our goal in the fourth quarter of 1998 with operating expenses of 24.3 percent of net sales and narrowly missed the target for the whole year with annual operating expenses of 25.1 percent. This compares to 26.0 percent and 26.7 percent in 1997 and 1996, respectively. Over the next three years, our goal is to further reduce operating expenses as a percent of sales to 23.0 percent.

Much of the improvement in 1998 stems from our ability to contain costs while redeploying resources, both people and dollars, to our strategic priorities. The improvement in operating expenses contributed approximately \$8.1 million to EVA and net income in the current year.

Selling, general, and administrative expenses, including design

reduce operating
definition of
and design
completed



and research expenses, primarily due to invest-

ments in and maintenance of information systems, an average 4.0 percent year-over-year increase in compensation and benefits, increases in compensation plans that vary with sales and EVA, and acquisitions.

Research and development costs, excluding royalty payments, were \$29.0 million in 1998, compared to \$25.7 million in 1997 and \$24.5 million in 1996.

Royalty payments made to designers of the company's products as the products are sold are not included in research and development costs, since they are considered to be a variable cost of the product. As a percentage of net sales, research and development costs were 1.7 percent in 1998, 1.7 percent in 1997, and 1.9 percent in 1996. As discussed earlier, new product design and development has been, and continues to be, a key business strategy. The increased expenditures in 1998 are directly related to the increased number of new products introduced in June of 1998.

Operating Income The combination of improved gross margins and lower operating expenses has resulted in significant improvements in operating income. As a percent of sales, operating income improved to 12.1 percent in 1998, after improving to 9.7 percent in 1997, and 7.1 percent in 1996. The amounts exclude the charges for the sale of our German manufacturing operation and the patent litigation settlement, respectively. The 12.1 percent recorded in 1998 was the highest reported for a fiscal year in over five years.

Income Taxes The effective tax rate was 38.8 percent in 1998, compared to 40.9 percent and 34.5 percent in 1997 and 1996, respectively. The higher tax rates in 1998 and 1997 reflect the tax-law change effective in 1997 that reduced the benefit of the Corporate Owned Life Insurance Program. Provisions were recorded in 1997 and 1998 for the potential cost of unwinding this program.

The 1997 tax rate was also negatively impacted by the loss on the sale of the German manufacturing operation, which provided a tax benefit that was lower than our statutory rate.

The 1996 effective tax rate was lowered by the completion of a sale and leaseback of our Roswell, Georgia, facility and by the sale of excess land to our captive insurance company. The completion of these transactions resulted in the recognition of certain deferred tax assets that were reserved for in previous periods.

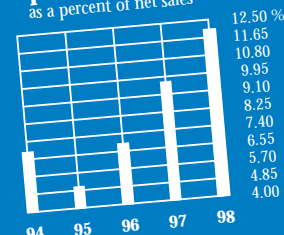
Management expects its effective tax rate for 1999 to be in the range of 37.0 to 39.0 percent.

Liquidity and Capital Resources The table below shows certain key cash flow and capital highlights:

(In Thousands)	1998	1997	1996
Cash and cash equivalents	\$115,316	\$106,161	\$ 57,053
Cash from operating activities	\$268,723	\$218,170	\$124,458
Days sales in accounts receivable and inventory	56.2	63.3	75.6
Capital expenditures	\$ 73,561	\$ 54,470	\$ 54,429
Interest-bearing debt to total capital	36.1%	30.7%	29.9%
EVA capital	\$543,789	\$615,120	\$605,438
NOPAT to EVA capital	26.7%	17.7%	12.7%

In 1998, we continued to improve the cash flow generated from operating activities. This was primarily due to increased profitability and our ability to better leverage working capital. As previously discussed, working capital from accounts receivable and inventory improved 7.1 days in 1998. This improvement translates to a reduction of capital of approximately \$26.0 million or a

Operating Income
as a percent of net sales



percent in

1997 and 1996

operation and the

patent litigation settlement, respectively.

The 12.1 percent recorded in 1998 was the highest reported

for a fiscal year in over five years.

reduction in our capital charge, for EVA purposes, of approximately \$2.9 million. We believe that the lean initiatives, combined with Project Renaissance, should allow us to gain further improvements in working capital.

The 1998 capital expenditures were primarily for investments in Project Renaissance, the development of our electronic selling platform, new products, and machinery and equipment to improve operational performance and expand capacity. At the end of the fiscal year, \$10.3 million of capital was committed for future expenditures.

We expect capital expenditures, net of redeployments, to increase to \$125-\$150 million in 1999. The largest expenditures planned in 1999 will be for the continued implementation of Project Renaissance, our electronic selling platform, and new products.

During 1996, we began to redeploy cash invested in nonproductive or nonessential assets. We are currently in the process of selling the facilities and land at our Grandville, Michigan, and Roswell, Georgia, sites. The net book value of these sites is approximately \$12.9 million, and we anticipate a selling price in excess of current net book value. The Grandville site is no longer needed and will not be replaced. The Georgia facility will be replaced by a new facility. The facility will enable us to consolidate the operations currently performed on our owned site with operations performed at two leased locations, thus lowering our operating costs at this location.

In 1998, we acquired three privately owned North American dealers as part of our service strategy. These local service organizations were acquired for approximately \$4.1 million. We expect to invest between \$15 million and \$25 million in acquiring additional local and regional service operations in 1999.

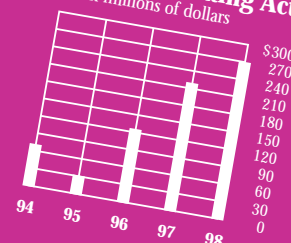
At the end of 1998, we continued to have a high level of cash and cash equivalents. Frankly, we had more nonoperating cash than we would like. The high level of cash was the result of better-than-expected improvements in working capital, coupled with a reduced level of investment in capital expenditures and acquisitions. We intend to utilize the cash to repurchase shares of the company's stock, to fund acquisitions related to the service strategy, and to fund future capital expenditures. If necessary, we have \$100 million in available committed credit facility and \$50 million in informal credit lines.

We have established a target debt-to-capital structure with a debt-to-total-capital ratio of 30 to 35 percent. Cash in excess of requirements for capital expenditures, acquisitions, and dividends will be used to fund the purchase of the company's common stock subject to market conditions. Due to the large amount of company stock repurchased during 1998, our debt-to-capital ratio exceeded our target and was 36.1 percent at May 1998. In the future, we expect to remain at the upper end of our target range.

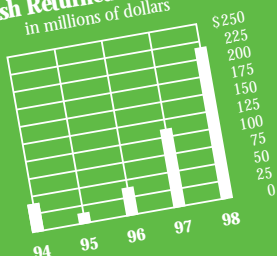
Common Stock Transactions

(In Thousands, Except Per Share Data)	1998	1997	1996
Shares acquired	5,222,361	2,765,984	860,395
Cost of shares acquired	\$ 201,982	\$ 97,962	\$ 25,101
Cost per share acquired	\$ 38.68	\$ 35.42	\$ 29.17
Shares issued	1,347,483	470,082	731,773
Cost per share issued	\$ 21.23	\$ 28.13	\$ 24.95
Cash dividends	\$ 13,361	\$ 12,593	\$ 12,999
Dividends per share	\$.15	\$.13	\$.13

Cash Flow from Operating Activities
in millions of dollars



Total Cash Returned to Shareholders
in millions of dollars



to reflect the split.

Year 2000

Many currently installed computer systems and software products are coded to accept only two-digit entries in the date code field. Beginning in the year 2000, or in some cases even earlier, these date code fields will need to accept four-digit entries to distinguish 21st century dates from 20th century dates. As a result, in less than two years, computer systems and/or software used by many companies may need to be upgraded to comply with such "Year 2000" requirements.

We understand the risk that this problem poses not only to our internal operations, but also to our suppliers and dealers. Management has developed and implemented an action plan to address internal Year 2000 issues and to ensure that any key suppliers and dealers are also addressing the problem on a timely basis. Through the end of 1998, \$3.1 million has been spent on these issues. We do not expect significant costs in fiscal 1999 related to Year 2000 compliance.

As discussed earlier, most of the domestic operations are implementing a new ERP system. While this system would have corrected many Year 2000 issues, management was not comfortable with its dependence on the implementation of this system to correct the Year 2000 issues. Instead, we have insisted that existing internal systems be modified for Year 2000 issues no later than early 1999. We know this may result in some additional costs which have a very short life-cycle, but we believe the risk of not taking prompt action is much higher than any duplicate costs.

While we believe the modifications will be made on a timely basis and will not have a material effect on the company's operating results, there is no guarantee that the company, its suppliers, or dealers will be able to make all of the modifications on a timely basis. This could have a material adverse effect on the company's business, financial condition, and results of operations.

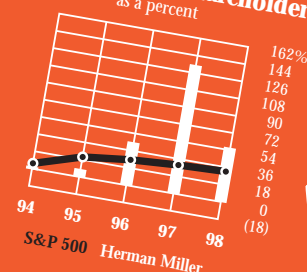
Patent Litigation Settlement and Other Contingencies

In 1992, Haworth, Inc., (Haworth) filed a lawsuit against the company, alleging that the electrical systems used in creation of the company's products infringed one or more of Haworth's patents. In 1996, the company and Haworth agreed to terms of a settlement. We continue to believe, based upon written opinion of counsel, that our products did not infringe Haworth's patents and we would, more likely than not, have prevailed on the merits. However, based on the mounting legal costs, distraction

The Board of Directors first authorized the company to repurchase its common stock in 1984 and has periodically renewed its authorization. Management and the Board of Directors believe the share repurchase program is an excellent means of returning value to our shareholders and preventing dilution from employee-ownership programs. During 1998, we repurchased 5,222,361 shares of common stock for \$202.0 million.

On January 20, 1998, the Board of Directors approved a 2-for-1 stock split effected in the form of a 100 percent dividend to shareholders of record on February 27, 1998, payable on March 16, 1998. The distribution increased the number of shares outstanding from 44,831,103 to 89,662,206. All appropriate share and per share data, including stock plan information, are restated

Total Return to Shareholders
as a percent





of management focus, and the uncertainty present in any litigation, we concluded that settlement was in the best interest of our shareholders. The settlement included a one-time cash payment of \$44.0 million in exchange for a complete release. The companies also exchanged limited covenants not to sue with respect to certain existing and potential patent designs. We simultaneously reached a settlement with one of our suppliers, who agreed to pay the company \$11.0 million and, over the next seven years, to rebate a percentage of its sales to Herman Miller that are in excess of then current levels. These rebates are recorded when earned. Accordingly, we recorded a net litigation settlement expense of \$16.5 million after applying previously recorded reserves and the settlement with the supplier.

The company for a number of years has sold various products to the United States Government under General Services Administration (GSA) multiple award schedule contracts. The GSA is permitted to audit the company's compliance with the GSA contracts. As a result of its audits, the GSA has asserted a refund claim under the 1982 contract for approximately \$2.7 million and has other contracts under audit review. Management has been notified that the GSA has referred the 1988 contract to the Justice Department for consideration of a potential civil False Claims Act case. Management disputes the audit result for the 1982 contract and does not expect resolution of the matter to have a material adverse effect on the company's consolidated financial statements. Management does not have information that would indicate a substantive basis for a civil False Claims Act case under the 1988 contract.

We are not aware of any other litigation or threatened litigation that would have a material impact on the company's consolidated financial statements.

Conclusion

In conclusion, we have shared with you the key elements of our strategy, including how we intend to increase our market opportunity and improve our operational performance. Each of these elements played a key role in our EVA and net income improvement over the past three years and, we believe, will continue to enable us to improve EVA and net income and provide superior returns to our shareholders in the future. We also hope you have gained some insight into the risks and challenges we face.



Review of Operations

(In Thousands, Except Per Share Data)

1998 1997 1996 1995

Operating Results

Net Sales	\$1,718,595	\$1,495,885	\$1,283,931	\$1,083,050
Gross Margin	638,839	533,924	434,946	378,269
Selling, General, and Administrative	396,698	359,601	316,024	303,621
Design and Research Expense	33,846	29,140	27,472	33,682
Operating Income	208,295	130,683	74,935	9,066
Income (Loss) Before Income Taxes	209,531	125,883	70,096	4,039
Net Income (Loss)	128,331	74,398	45,946	4,339
Cash Flow from Operating Activities	268,723	218,170	124,458	29,861
Depreciation and Amortization	50,748	47,985	45,009	39,732
Capital Expenditures	73,561	54,470	54,429	63,359
Common Stock Repurchased plus Cash Dividends Paid	215,498	110,425	38,116	13,600

Key Ratios

Sales Growth	14.9	16.5	18.5	13.6
Gross Margin ⁽¹⁾	37.2	35.7	33.9	34.9
Selling, General, and Administrative ⁽¹⁾	23.1	24.0	24.6	28.0
Design and Research Expense ⁽¹⁾	2.0	1.9	2.1	3.1
Operating Income ⁽¹⁾	12.1	8.7	5.8	0.8
Net Income Growth	72.5	61.9	958.9	(89.3)
After-Tax Return on Net Sales	7.5	5.0	3.6	0.4
After-Tax Return on Average Assets	16.7	10.3	6.8	0.7
After-Tax Return on Average Equity	49.5	25.0	15.4	1.5

Share and Per Share Data⁽²⁾

Earnings per Share – Diluted	\$1.39	\$0.77	\$0.46	\$0.04
Cash Dividends Declared per Share	0.15	0.13	0.13	0.13
Book Value per Share at Year End	2.51	2.99	3.07	2.89
Market Price per Share at Year End	27.69	17.88	7.72	5.42
Weighted-Average Shares Outstanding – Diluted	92,039	96,124	100,515	99,168

Financial Condition

Total Assets	\$784,346	\$755,587	\$694,911	\$659,012
Working Capital	21,803	100,253	115,878	39,575
Current Ratio	1.06	1.35	1.53	1.15
Interest-Bearing Debt	130,655	127,369	131,710	144,188
Shareholders' Equity	231,002	287,062	308,145	286,915
Total Capital	361,657	414,431	439,855	431,103
Interest-Bearing Debt to Total Capital	36.1	30.7	29.9	33.4

(1) Shown as a percent of net sales.

(2) Retroactively adjusted to reflect two-for-one stock splits occurring in 1998 and 1997.



1994	1993	1992	1991	1990	1989	1988
\$953,200	\$855,673	\$804,675	\$878,732	\$865,016	\$828,981	\$742,884
337,138	298,501	277,076	314,159	313,171	294,721	269,102
245,189	230,219	229,392	233,126	209,683	193,403	169,643
30,151	24,513	20,725	23,212	20,784	21,650	18,138
61,798	43,769	1,989	39,206	82,704	72,349	75,864
63,473	42,354	(988)	33,159	74,996	67,902	72,008
40,373	22,054	(14,145)	14,059	46,596	45,702	46,408
69,764	82,588	77,000	86,393	81,706	61,150	61,496
33,207	31,600	30,473	32,761	28,005	25,412	23,034
40,347	43,387	32,024	32,609	34,978	60,765	55,417
38,461	21,157	23,558	18,016	14,782	24,062	14,823

11.4	6.3	(8.4)	1.6	4.3	11.6	25.5
35.4	34.9	34.4	35.8	36.2	35.6	36.2
25.7	26.9	28.5	26.5	24.2	23.3	22.8
3.2	2.9	2.6	2.6	2.4	2.6	2.4
6.5	5.1	0.2	4.5	9.6	8.7	10.2
83.1	255.9	(200.6)	(69.8)	2.0	(1.5)	35.0
4.2	2.6	(1.8)	1.6	5.4	5.5	6.2
7.9	4.6	(2.9)	2.7	8.8	9.3	11.3
13.9	7.8	(4.8)	4.5	15.7	17.1	19.6

\$0.40	\$0.22	\$ (0.14)	\$0.14	\$0.45	\$0.44	\$0.45
0.13	0.13	0.13	0.13	0.13	0.13	0.11
2.93	2.84	2.78	3.08	3.07	2.73	2.48
6.22	6.41	4.75	5.03	5.13	5.25	5.16
101,020	99,972	100,652	102,740	102,572	102,840	103,748

\$533,746	\$484,342	\$471,268	\$492,947	\$533,982	\$520,806	\$460,878
50,943	62,711	66,545	113,980	127,003	106,321	108,909
1.29	1.43	1.48	2.06	2.09	1.83	2.00
70,017	39,877	53,975	75,693	109,997	140,268	105,875
296,325	283,942	280,082	314,782	314,315	278,534	255,912
366,342	323,819	334,057	390,475	424,312	418,802	361,787
19.1	12.3	16.2	19.4	25.9	33.5	29.3





Share Price, Earnings, and Dividends Summary

Herman Miller, Inc., common stock is quoted in the NASDAQ-National Market System (NASDAQ-NMS Symbol: MLHR). As of August 3, 1998, there were approximately 29,000 shareholders of record of the company's common stock.

Per Share and Unaudited	Market Price High	Market Price Low	Market Price Close	Earnings Per Share-Diluted	Dividends Per Share
Year Ended May 30, 1998					
First quarter	25.875	17.344	25.875	.30	.03625
Second quarter	28.406	22.000	25.375	.33	.03625
Third quarter	31.750	23.250	30.625	.36	.03625
Fourth quarter	35.563	26.030	27.688	.40	.03625
Year	35.563	17.344	27.688	1.39	.14500
Year Ended May 31, 1997					
First quarter	9.563	7.469	9.381	.16	.03250
Second quarter	11.875	9.250	11.750	.18	.03250
Third quarter	17.000	11.265	16.437	.14	.03250
Fourth quarter	18.657	14.437	17.875	.29	.03625
Year	18.657	7.469	17.875	.77	.13375

Quarterly Financial Data

Summary of the quarterly operating results on a consolidated basis:

	May 30, 1998; May 31, 1997; June 1, 1996 (In Thousands, Except Per Share Data)			
	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
1998 Net sales	\$ 401,545	\$ 415,086	\$ 436,708	\$ 465,256
Gross margin	147,001	151,643	164,896	175,299
Net income ⁽¹⁾	27,807	30,446	32,639	37,439
Earnings per share – diluted ⁽¹⁾	\$.30	\$.33	\$.36	\$.40
1997 Net sales	\$ 342,484	\$ 377,137	\$ 365,060	\$ 411,204
Gross margin	118,272	134,300	131,933	149,419
Net income	15,586	17,852	13,535	27,425
Earnings per share – diluted	\$.16	\$.18	\$.14	\$.29
1996 Net sales	\$ 301,088	\$ 328,393	\$ 312,915	\$ 341,535
Gross margin	102,879	112,653	103,415	115,999
Net income	12,014	4,955	11,900	17,077
Earnings per share – diluted	\$.12	\$.05	\$.12	\$.17

(1) Amounts have been restated for the adoption of Statement of Position 98-1, "Accounting for the Costs of Computer Software Developed or Obtained for Internal Use."



Consolidated Statements of Income

May 30, 1998; May 31, 1997; June 1, 1996	1998	1997	
1996 (In Thousands, Except Per Share Data)			
Net Sales	\$1,718,595	\$1,495,885	\$
1,283,931			
Cost of Sales	1,079,756	961,961	
848,985			
Gross Margin	638,839	533,924	
434,946			
Operating Expenses:			
Selling, general, and administrative	396,698	359,601	
316,024			
Design and research	33,846	29,140	
27,472			
Patent litigation settlement	—	—	
16,515			
Loss on divestiture	—	14,500	
—			
Total Operating Expenses	430,544	403,241	
360,011			
Operating Income	208,295	130,683	
74,935			
Other Expenses:			
Interest expense	8,300	8,843	
7,910			
Interest income	(11,262)	(8,926)	
(6,804)			
Loss on foreign exchange	270	1,687	
1,614			
Other, net	1,456	3,196	
2,119			
Net Other Expenses	(1,236)	4,800	
4,839			
Income Before Income Taxes	209,531	125,883	
70,096			
Income Taxes	81,200	51,485	
24,150			
Net Income	\$ 128,331	\$ 74,398	\$
45,946			
Earnings Per Share – Basic	\$ 1.42	\$.79	\$
.46			
Earnings Per Share – Diluted	\$ 1.39	\$.77	\$
.46			

The accompanying notes are an integral part of these statements.

Consolidated Balance Sheets

May 30, 1998, and May 31, 1997
(In Thousands, Except Share and Per Share Data)

1998 1997

Assets

Current Assets:

Cash and cash equivalents	\$ 115,316	\$ 106,161
Accounts receivable, less allowances of \$13,792 in 1998 and \$12,943 in 1997	192,384	179,242
Inventories	47,657	53,877
Prepaid expenses and other	44,778	46,584
Total Current Assets	400,135	385,864

Property and Equipment:

Land and improvements	27,279	26,936
Buildings and improvements	156,605	156,002
Machinery and equipment	364,817	346,653
Construction in progress	47,171	25,991
	595,872	555,582

Less accumulated depreciation	305,208	290,355
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Net Property and Equipment	290,664	265,227
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Notes Receivable, less allowances of \$8,430 in 1998 and \$8,489 in 1997	27,522	47,431
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Other Assets	66,025	57,065
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Total Assets	\$ 784,346	\$ 755,587
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Liabilities and Shareholders' Equity

Current Liabilities:

Unfunded checks	\$ 35,241	\$ 25,730
Current portion of long-term debt	10,203	173
Notes payable	19,542	17,109
Accounts payable	92,241	76,975
Accrued liabilities	221,105	165,624

Total Current Liabilities	378,332	285,611
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Long-Term Debt, less current portion above	100,910	110,087
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Other Liabilities	74,102	72,827
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Total Liabilities	553,344	468,525
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Shareholders' Equity:

Preferred stock, no par value (10,000,000 shares authorized, none issued)	—	—
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Common stock, \$.20 par value (120,000,000 shares authorized, 86,986,957 and 46,030,822 shares issued and outstanding in 1998 and 1997)	17,397	9,207
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Additional paid-in capital	—	—
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Retained earnings	227,464	292,237
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Cumulative translation adjustment	(9,360)	(10,863)
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Key executive stock programs	(4,499)	(3,519)
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Total Shareholders' Equity	231,002	287,062
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Total Liabilities and Shareholders' Equity	\$ 784,346	\$ 755,587
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The accompanying notes are an integral part of these balance sheets.

Consolidated Statements of Shareholders' Equity

(In Thousands, Except Share and Per Share Data)	Common Stock	Additional Paid-In Capital	Retained Earnings	Cumulative Translation Adjustment	Key Executive Stock Programs	Total Shareholders' Equity
Balance June 3, 1995	\$ 4,967	\$ 21,564	\$270,631	\$ (6,985)	\$ (3,262)	\$286,915
Net income	—	—	45,946	—	—	45,946
Cash dividends (\$.130 per share)	—	—	(12,999)	—	—	(12,999)
Exercise of stock options	79	9,817	—	—	31	9,927
Employee stock purchase plan	18	2,258	—	—	—	2,276
Repurchase and retirement of 860,395 shares of common stock	(172)	(26,006)	—	—	1,077	(25,101)
Stock issued for acquisitions	43	6,425	—	—	—	6,468
Stock grants earned (forfeited)	(8)	(639)	—	—	931	284
Stock grants issued	7	1,049	—	—	(1,467)	(411)
Stock purchase assistance plan	—	—	—	—	(512)	(512)
Current year translation adjustment	—	—	—	(4,648)	—	(4,648)
Balance June 1, 1996	\$ 4,934	\$ 14,468	\$303,578	\$(11,633)	\$ (3,202)	\$308,145
Net income	—	—	74,398	—	—	74,398
Cash dividends (\$.134 per share)	—	—	(12,593)	—	—	(12,593)
Exercise of stock options	63	9,049	—	—	—	9,112
Employee stock purchase plan	14	2,637	—	—	—	2,651
Repurchase and retirement of 2,765,984 shares of common stock	(553)	(29,374)	(68,414)	—	379	(97,962)
Stock dividend	4,732	—	(4,732)	—	—	—
Directors' fees	1	225	—	—	—	226
Stock grants earned	—	—	—	—	387	387
Stock grants issued	16	2,995	—	—	(1,776)	1,235
Stock purchase assistance plan	—	—	—	—	693	693
Current year translation adjustment	—	—	—	770	—	770
Balance May 31, 1997	\$ 9,207	\$ —	\$292,237	\$(10,863)	\$ (3,519)	\$287,062
Net income	—	—	128,331	—	—	128,331
Cash dividends (\$.145 per share)	—	—	(13,361)	—	—	(13,361)
Exercise of stock options	246	14,105	—	—	—	14,351
Employee stock purchase plan	21	3,831	—	—	—	3,852
Tax benefit relating to employee stock plans	—	10,074	—	—	—	10,074
Repurchase and retirement of 5,222,361 shares of common stock	(1,044)	(30,161)	(170,777)	—	—	(201,982)
Stock dividend	8,966	—	(8,966)	—	—	—
Directors' fees	1	325	—	—	—	326
Stock grants earned	—	—	—	—	718	718
Deferred compensation plan	—	1,826	—	—	(1,826)	—
Stock purchase assistance plan	—	—	—	—	128	128
Current year translation adjustment	—	—	—	1,503	—	1,503
Balance May 30, 1998	\$ 17,397	\$ —	\$227,464	\$ (9,360)	\$ (4,499)	\$231,002

The accompanying notes are an integral part of these statements.

Consolidated Statements of Cash Flows

May 30, 1998; May 31, 1997; and June 1, 1996 (In Thousands)	1998	1997	1996
Cash Flows from Operating Activities:			
Net Income	\$ 128,331	\$ 74,398	\$ 45,946
Adjustments to reconcile net income to net cash provided by operating activities	140,392	143,772	78,512
Net Cash Provided by Operating Activities	268,723	218,170	124,458
Cash Flows from Investing Activities:			
Notes receivable repayments	561,923	449,405	455,973
Notes receivable issued	(544,182)	(460,956)	(454,261)
Property and equipment additions	(73,561)	(54,470)	(54,429)
Proceeds from sales of property and equipment	870	5,336	13,486
Net cash paid for acquisitions	(4,076)	(9,743)	(5,101)
Other, net	(7,102)	1,548	(212)
Net Cash Used for Investing Activities	(66,128)	(68,880)	(44,544)
Cash Flows from Financing Activities:			
Short-term debt borrowings	192,808	236,627	517,862
Short-term debt repayments	(189,619)	(239,417)	(579,613)
Long-term debt borrowings	—	—	270,985
Long-term debt repayments	(7)	(186)	(222,772)
Dividends paid	(13,516)	(12,463)	(13,015)
Common stock issued	18,529	11,989	12,203
Common stock repurchased and retired	(201,982)	(97,962)	(25,101)
Capital lease obligation repayments	(172)	(116)	(250)
Net Cash Used for Financing Activities	(193,959)	(101,528)	(39,701)
Effect of Exchange Rate Changes on Cash and Cash Equivalents	519	1,346	352
Net Increase in Cash and Cash Equivalents	9,155	49,108	40,565
Cash and Cash Equivalents, Beginning of Year	106,161	57,053	16,488
Cash and Cash Equivalents, End of Year	\$ 115,316	\$ 106,161	\$ 57,053

The accompanying notes are an integral part of these statements.

Notes to Consolidated Financial Statements

Significant Accounting and Reporting Policies

The following is a summary of significant accounting and reporting policies not reflected elsewhere in the accompanying financial statements.

Principles of Consolidation The consolidated financial statements include the accounts of Herman Miller, Inc., and its wholly owned domestic and foreign subsidiaries (the company). All significant intercompany accounts and transactions have been eliminated.

Description of Business The company is engaged in the design, manufacture, and sale of office systems, products, and services principally for offices, and to a lesser extent, for healthcare facilities and other uses. The company's products are sold primarily to or through independent contract office furniture dealers. Accordingly, accounts and notes receivable in the accompanying balance sheets principally are amounts due from the dealers.

Fiscal Year The company's fiscal year ends on the Saturday closest to May 31. The years ended May 30, 1998, May 31, 1997, and June 1, 1996, each contained 52 weeks.

Foreign Currency Translation The functional currency for most foreign subsidiaries is the local currency. The cumulative effects of translating the balance sheet accounts from the functional currency into the United States dollar at current exchange rates and revenue and expense accounts using average exchange rates for the period are included as a separate component of shareholders' equity. The United States dollar is used as the functional currency for subsidiaries in highly inflationary foreign economies, and the financial results are translated using a combination of current and historical exchange rates, and the resulting translation adjustments are included along with gains or losses arising from remeasuring all foreign currency transactions into the appropriate functional currency when determining net income.

Cash Equivalents The company invests in certain debt and equity securities as part of its cash management function. Due to the relative short-term maturities and high liquidity of these securities (consisting primarily of Euro overnight investments), they are included in the accompanying consolidated balance sheets as cash equivalents at market value and totaled \$67.3 million and \$85.1 million as of May 30, 1998, and May 31, 1997, respectively. The company's cash equivalents are considered "available for sale." As of May 30, 1998, the market value approximated the securities' cost. All cash and cash equivalents are high-credit quality financial instruments, and the amount of credit exposure to any one financial institution or instrument is limited.

Property, Equipment, and Depreciation Property and equipment are stated at cost. The cost is depreciated over the estimated useful lives of the assets, using the straight-line method. The average useful lives of the assets are 32 years for buildings and 7 years for all other property and equipment.

Notes Receivable The notes receivable are primarily from certain independent contract office furniture dealers. The notes are collateralized by the assets of the dealers and bear interest based on the prevailing prime rate. Interest income relating to these notes was \$4.3, \$4.8, and \$3.9 million in 1998, 1997, and 1996, respectively.

Long-Lived Assets The company assesses the recoverability of its long-lived assets whenever events or circumstances such as current and projected future operating losses or changes in the business climate indicate that the carrying amount may not be recoverable. Assets are grouped and evaluated at the lowest level for which there are independent and identifiable cash flows. The company considers historical performance and future estimated results in its evaluation of potential impairment and then compares the carrying amount of the asset to the estimated future cash flows (undiscounted and without interest charges) expected to result from the use of the asset. If the carrying amount of the asset exceeds the expected future cash flows, the company measures and records an impairment loss for the excess of

the carrying value of the asset over its fair value. The estimation of fair value is made by discounting the expected future cash flows at the rate the company uses to evaluate similar potential investments based on the best information available at that time. If the assets being tested for recoverability were acquired in a purchase business combination, the goodwill that arose in that transaction is included in the asset group's carrying values on a pro-rata basis using the relative fair values.

In situations where goodwill and intangible balances remain after applying the impairment measurements to business unit asset groupings under Statement of Financial Accounting Standards (SFAS) No. 121, the company assesses the recoverability of the remaining balances at the enterprise level under the provisions of APB Opinion 17. Applying these provisions, when the estimated undiscounted future operating income (before interest and amortization) for individual business units is not sufficient to recover the remaining carrying value over the remaining amortization period, the company recognizes an impairment loss for the excess.

Excluding the impairment incurred in connection with the divestiture of the company's German manufacturing operation in 1997 (see Acquisitions and Divestitures note), such provisions were not significant in 1998, 1997, or 1996.

Intangible assets included in other assets consist mainly of goodwill, patents, and other acquired intangibles, and are carried at cost, less applicable amortization of \$16.0 and \$12.1 million in 1998 and 1997, respectively. These assets are amortized using the straight-line method over periods of five to 15 years.

Unfunded Checks As a result of maintaining a consolidated cash management system, the company utilizes controlled disbursement bank accounts. These accounts are funded as checks are presented for payment, not when checks are issued. The resulting book overdraft position is included in current liabilities as unfunded checks.

Self-Insurance The company is partially self-insured for general liability, workers' compensation, and certain employee health benefits. The general and workers' compensation liabilities are managed through a wholly owned insurance captive; the related liabilities are included in the accompanying financial statements. The company's policy is to accrue amounts equal to the actuarially determined liabilities. The actuarial valuations are based on historical information along with certain assumptions about future events. Changes in assumptions for such matters as legal actions, medical costs, and changes in actual experience could cause these estimates to change in the near term.

Research, Development, Advertising, and Other Related Costs Research, development, advertising materials, preproduction, and start-up costs are expensed as incurred. Research and development costs consist of expenditures incurred during the course of planned search and investigation aimed at discovery of new knowledge that will be useful in developing new products or processes, or significantly enhancing existing products or production processes, and the implementation of such through design, testing of product alternatives, or construction of prototypes. Royalty payments made to designers of the company's products as the products are sold are not included in research and development costs, as they are considered to be a variable cost of the product. Research and development costs, included in design and research expense in the accompanying statements of income, were \$29.0, \$25.7, and \$24.5 million in 1998, 1997, and 1996, respectively.

Income Taxes Deferred tax assets and liabilities are recognized for the expected future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities, and their respective tax bases. Deferred tax assets and liabilities are measured using the enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to reverse.

Revenue Recognition Revenues are recorded when product is shipped and invoiced or performance of services is complete.



Use of Estimates in the Preparation of Financial Statements The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

New Accounting Standards In March 1998, the American Institute of Certified Public Accountants issued Statement of Position (SOP) 98-1, "Accounting for the Costs of Computer Software Developed or Obtained for Internal Use." The company adopted this SOP during the third quarter of fiscal 1998, retroactive to the beginning of the fiscal year. The adoption of this SOP did not have a material effect on the financial statements. The company is also in compliance with Emerging Issues Task Force (EITF) Issue 97-13, "Accounting for Costs Incurred in Connection with a Consulting Contract that Combines Business Process Reengineering and Information Technology Transformation."

Beginning in the third quarter of fiscal 1998, the company adopted Statement of Financial Accounting Standards No. 128, "Earnings per Share." This statement establishes standards for computing and presenting "basic" and "diluted" earnings per share (EPS). Basic EPS excludes the dilutive effect of common shares that could potentially be issued (i.e., primarily stock options in the case of Herman Miller) and is computed by dividing net income by the weighted-average number of common shares outstanding for the period. Diluted EPS is computed by dividing net income by the weighted-average number of shares outstanding plus all shares that could potentially be issued. All prior period EPS data has been restated to conform to this statement.

In fiscal 1998, the company adopted Statement of Financial Accounting Standards No. 132, "Employers' Disclosures about Pensions and Other Postretirement Benefits." All information in the Employee Benefit Plans note has been presented accordingly.

In June 1998, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 133, "Accounting for Derivative Instruments and Hedging Activities." The Statement establishes accounting and reporting standards requiring that every derivative instrument (including certain derivative instruments embedded in other contracts) be recorded in the balance sheet as either an asset or liability measured at its fair value. The Statement requires that changes in the derivative's fair value be recognized currently in earnings unless specific hedge accounting criteria are met. Statement 133 is effective in fiscal year 2000. The company has not yet determined the timing or method of adoption of Statement 133; however, the Statement is not expected to have a material impact on the company's consolidated financial statements.

Acquisitions and Divestitures

During 1998, 1997, and 1996, the company made several acquisitions, all of which were recorded using the purchase method of accounting. Accordingly, the purchase price of these acquisitions has been allocated to the assets acquired and liabilities assumed, based on the estimated fair values at the date of the acquisition. The cost of the acquisitions in excess of net identifiable assets acquired has been recorded as goodwill.

During 1998, 1997, and 1996, the company purchased various privately owned North American dealers. These companies were acquired for approximately \$25.5 million. The consideration included 212,662 shares of Herman Miller common stock and approximately \$19.0 million in cash, which resulted in approximately \$16.0 million of goodwill. The results of the acquisitions were not material to the company's consolidated operating results.

During the second quarter of fiscal 1997, declining sales and continuing losses at the company's German subsidiary led the company, in accordance with its accounting policies, to assess the realizability of



the subsidiary's long-lived assets. At that time, estimates of expected future cash flows under various options to improve the company's operating results in Germany were evaluated to determine if any potential impairment existed. Although none of the options was developed to the extent required to enable the company to reach a decision and plan for implementation, based on the results of its various evaluations of potential impairment, the company determined at the enterprise level the goodwill and intangibles associated with the acquisition were no longer recoverable. As a result, a pretax charge of \$5.5 million (\$4.5 million, or \$.05 per share after tax) was recorded for the write-off of the goodwill and brand-name assets of the subsidiary.

During the third quarter of fiscal 1997, management authorized and committed the company to a plan to restructure the manufacturing component of its German operation. Based on the most current information available at that time, management believed that closing the facility was the most viable option. As a result, the company recorded a pretax restructuring charge of \$13.7 million (\$5.4 million, or \$.06 per share after tax).

During the fourth quarter of fiscal 1997, the company sold the German manufacturing operation. The sale had the effect of reducing both the pretax restructuring costs recorded in the third quarter by \$4.7 million and the anticipated tax benefit by \$5.2 million.

In summary, after adjusting for the effects of the sale, the divestiture of the company's investments in its German manufacturing operation resulted in a pretax loss of \$14.5 million (\$10.4 million, or \$.11 per share after tax) for fiscal 1997.

Inventories

(In Thousands)	1998	1997
Finished products	\$ 19,807	\$ 23,552
Work in process	8,844	8,074
Raw materials	19,006	22,251
	<u>\$ 47,657</u>	<u>\$ 53,877</u>

Inventories are valued at the lower of cost or market and include material, labor, and overhead. The inventories of Herman Miller, Inc., are valued using the last-in, first-out (LIFO) method. The inventories of the company's subsidiaries are valued using the first-in, first-out method. Inventories valued using the LIFO method amounted to \$25.2 and \$27.5 million at May 30, 1998, and May 31, 1997, respectively.

If all inventories had been valued using the first-in, first-out method, inventories would have been \$13.6 and \$15.6 million higher than reported at May 30, 1998, and May 31, 1997, respectively.

Prepaid Expenses and Other

(In Thousands)	1998	1997
Current deferred income taxes	\$ 27,154	\$ 26,382
Other	17,624	20,202
	<u>\$ 44,778</u>	<u>\$ 46,584</u>

Accrued Liabilities

(In Thousands)	1998	1997
Compensation and employee benefits	\$ 110,684	\$ 80,778
Income taxes	22,809	15,802
Other	87,612	69,044
	<u>\$ 221,105</u>	<u>\$ 165,624</u>



Other Liabilities

(In Thousands)	1998	1997
Pension benefits	\$ 41,898	\$ 25,319
Postretirement benefits	9,618	23,089
Other	22,586	24,419
	<u>\$ 74,102</u>	<u>\$ 72,827</u>

Notes Payable

(In Thousands)	1998	1997
Non-U.S. dollar currencies	\$ 19,542	\$ 17,109

The following information relates to short-term borrowings in 1998:

(In Thousands)	Domestic	Foreign
Weighted-average interest rate at May 30, 1998	—	4.8%
Weighted-average interest rate at May 31, 1997	—	6.4%
Weighted-average interest rate during 1998	—	4.6%
Unused short-term credit lines	\$ 6,000	\$ 44,824

In addition to the company's formal short-term credit lines shown above, the company has available informal lines of credit totaling \$50.0 million.

Long-Term Debt

(In Thousands)	1998	1997
Series A senior notes, 6.37%, due March 5, 2006	\$ 70,000	\$ 70,000
Series B senior notes, 6.08%, due March 5, 2001	15,000	15,000
Series C senior notes, 6.52%, due March 5, 2008	15,000	15,000
Finance lease obligation	10,000	10,000
Other	1,113	260
	<u>\$ 111,113</u>	<u>\$ 110,260</u>
Less current portion	10,203	173
	<u>\$ 100,910</u>	<u>\$ 110,087</u>

During the third quarter of 1996, the company entered into a private placement of \$100.0 million of senior notes with seven insurance companies. The Series A, B, and C notes have interest-only payments until March 5, 2000, March 5, 2001, and March 5, 2004, respectively.

The company has available an unsecured revolving credit loan that provides for a \$100.0 million line of credit. The loan permits borrowings in multi-currencies and matures on February 28, 2002. Outstanding borrowings bear interest, at the option of the company, at rates based on the prime rate, certificates of deposit, LIBOR, or negotiated rates. Interest is payable periodically throughout the period a borrowing is outstanding. During 1998, the company borrowed at the LIBOR contractual rate or other negotiated rates. During 1997, the company had no borrowings.

Provisions of the senior notes and the unsecured senior revolving credit loan restrict, without prior consent, the company's borrowings, long-term leases, and sale of certain assets. In addition, the company has agreed to maintain certain financial performance ratios. At May 30, 1998, the company was in compliance with all of these provisions.



During May 1996, the company entered into an agreement for the sale and leaseback of its Roswell, Georgia, facility. The company has an early buyout option at the end of one-and-one-half years at an amount equal to approximately 103.03 percent of the lessor's cost. The company also has a purchase option at the end of five years at an amount equal to the facility's then fair market value. If the purchase option is not exercised, the lease automatically renews for an additional 30 months. The company has guaranteed a residual value of 59.0 percent of the lessor's cost. The lease has been accounted for as a financing lease in accordance with SFAS No. 98. The company is currently negotiating an earlier buyout option with the lessor; therefore, the lease has been classified as current. The book value and accumulated depreciation of the facility are approximately \$19.4 million and \$11.8 million, respectively.

Annual maturities of long-term debt for the five years subsequent to May 30, 1998, (in millions) are as follows: 1999 – \$10.2; 2000 – \$10.1; 2001 – \$25.1; 2002 – \$10.1; 2003 – \$10.1; thereafter – \$45.5.

Operating Leases

The company leases real property and equipment under agreements that expire on various dates. Certain leases contain renewal provisions and generally require the company to pay utilities, insurance, taxes, and other operating expenses.

Future minimum rental payments (in millions) required under operating leases that have initial or remaining noncancellable lease terms in excess of one year as of May 30, 1998, are as follows: 1999 – \$14.7; 2000 – \$12.7; 2001 – \$9.9; 2002 – \$7.7; 2003 – \$5.9; thereafter – \$10.2.

Total rental expense charged to operations was \$20.4, \$20.9, and \$23.9 million in 1998, 1997, and 1996, respectively. Substantially all such rental expense represented the minimum rental payments under operating leases.

Employee Benefit Plans

The company maintains plans which provide retirement benefits for substantially all employees.

Pension Plans The principal domestic plan is a noncontributory defined-benefit pension plan. Benefits under this plan are based upon an employee's years of service and the average earnings for the five highest consecutive years of service during the 10 years immediately preceding retirement. Domestically, the company's policy is to fund its plan to the maximum amount currently deductible for federal income-tax purposes, which equals or exceeds the minimum amount required by the Employee Retirement Income Security Act.

In 1998, the Board of Directors approved the redesign of the company's domestic benefit plans. The redesign will result in the conversion of the defined-benefit pension plan from the existing benefit calculation to a cash-balance calculation. As part of the redesign, the company will buy out the postretirement healthcare obligation for active employees through a one-time lump-sum transfer contribution to the cash-balance plan.

The amendment converting the plan to the cash-balance formula was the primary reason for the \$43.9 million change in the projected benefit obligation.

In addition to the domestic pension plan and the retiree healthcare and life insurance plan, one of Herman Miller, Inc.'s wholly owned foreign subsidiaries has a defined-benefit pension plan which is similar to the principal domestic plan. This plan has not been amended and is included in the following information.

	Pension Benefits		Postretirement Benefits	
	1998	1997	1998	1997
Change in benefit obligations				
Benefit obligations at beginning of year	\$ 188,743	\$ 158,125	\$ 24,467	\$ 22,237
Service cost	11,722	9,620	1,168	1,132
Interest cost	14,678	12,683	1,713	1,653
Transfer of obligations	15,822	—	(15,822)	—
Actuarial effects of plan redesign	(43,878)	—	—	—
Actuarial (gain) loss	10,018	12,509	(480)	213
Benefits paid	(4,387)	(4,194)	(721)	(768)
Other	1,005	—	62	—
Benefit obligations at end of year	193,723	188,743	10,387	24,467
Change in plan assets				
Fair value of plan assets at beginning of year	184,178	145,678	—	—
Actual return on plan assets	47,692	40,365	—	—
Employer contribution	9,085	2,329	721	768
Benefits paid	(4,387)	(4,194)	(721)	(768)
Fair value of plan assets at end of year	236,568	184,178	—	—
Funded status	42,845	(4,565)	(10,387)	(24,467)
Unrecognized transition amount	(1,975)	(2,506)	—	—
Unrecognized net actuarial (gain) loss	(38,651)	(18,019)	769	2,359
Unrecognized prior service cost	(44,117)	(229)	—	(981)
Prepaid (accrued) benefit cost	(41,898)	(25,319)	(9,618)	(23,089)

Weighted-average assumptions

Discount rate	7.25%	7.50%	7.25%	7.50%
Expected return on plan assets	9.00%	7.50%	N/A	N/A
Rate of compensation increase	5.00%	5.00%	N/A	N/A

For measurement purposes, a 7.5 percent annual rate of increase in the per-capita cost of covered healthcare benefits was assumed for 1999. The rate was assumed to decrease gradually to 6.0 percent for 2001 and remain at that level thereafter.

	Pension Benefits			Postretirement Benefits		
	1998	1997	1996	1998	1997	1996
Components of net periodic benefit cost						
Service cost	\$ 11,722	\$ 9,620	\$ 8,688	\$ 1,168	\$ 1,132	\$ 1,140
Interest cost	14,678	12,683	10,588	1,713	1,653	1,496
Expected return on plan assets	(16,913)	(11,008)	(8,886)	—	—	—
Net amortization	(523)	(514)	(224)	(50)	(44)	(39)
Cost of early retirement incentive program	—	—	479	—	—	—
Net periodic benefit cost	\$ 8,964	\$ 10,781	\$ 10,645	\$ 2,831	\$ 2,741	\$ 2,597

Assumed healthcare cost trend rates have a significant effect on the amounts reported for the healthcare plans. A one-percentage-point change in assumed healthcare cost trend rates would have the following effects:

	1-Percentage-Point Increase	1-Percentage-Point Decrease
Effect on total of service and interest cost components	\$ 68	\$ (85)
Effect on postretirement benefit obligation	306	(367)

Plan assets consist primarily of listed common stocks, mutual funds, and corporate obligations. Plan assets at May 30, 1998, and May 31, 1997, respectively, included 888,346 and 1,310,688 shares of Herman Miller, Inc., common stock.

Profit Sharing Plan Herman Miller, Inc., and three of its subsidiaries have a trustee profit sharing plan that covers substantially all employees who have completed one year of employment. The plan provides for discretionary contributions (payable in the company's common stock) of not more than 6.0 percent of pretax income of the participating companies, or such other lesser amounts as may be established by the Board of Directors. The cost of the plan charged against operations was \$8.1, \$6.6, and \$4.5 million in 1998, 1997, and 1996, respectively.

As part of the plan redesign, the profit sharing plan's discretionary contributions were converted to an EVA-based calculation computed using the company's consolidated results. In addition, participants will now be eligible to begin participating at the beginning of the quarter following the date of hire.

Common Stock and Per Share Information

On January 20, 1998, the Board of Directors approved a 2-for-1 stock split effected in the form of a 100 percent dividend to shareholders of record on February 27, 1998, payable on March 16, 1998. The distribution increased the number of shares outstanding from 44,831,103 to 89,662,206. All share and per share data, including stock plan information, are restated to reflect the split. The Board of Directors also approved an increase in the cash dividend from \$.03250 to \$.03625 per share for shareholders of record on May 31, 1997.

The following table reconciles the numerators and denominators used in the calculations of basic and diluted EPS for each of the last three years:

(Dollars In Thousands)	1998	1997	1996
Numerators:			
Numerator for both basic and diluted EPS, net income	\$ 128,331	\$ 74,398	\$ 45,946
Denominators:			
Denominator for basic EPS, weighted-average common shares outstanding	90,240,102	94,627,772	100,006,240
Potentially dilutive shares resulting from stock option plans	1,799,067	1,496,428	508,700
Denominator for diluted EPS	92,039,169	96,124,200	100,514,940

The following exercisable stock options were not included in the computation of diluted EPS because the option prices were greater than average quarterly market prices.

Exercise Price	1998	1997	1996
\$32.50	132,368	—	—

Stock Plans

Under the terms of the company's 1987 Employee Stock Purchase Plan, 4.1 million shares of authorized common stock were reserved for purchase by plan participants at 85.0 percent of the market price. At May 30, 1998, 3,610,056 shares remained available for purchase through the plan, and there

were 7,305 employees eligible to participate in the plan, of which 2,143, or 29.3 percent, were participants. During 1998, 1997, and 1996, employees purchased 107,182, 71,213, and 89,222 shares, respectively.

The company has stock option plans under which options are granted to employees and nonemployee officers and directors at a price not less than the market price of the company's common stock on the date of grant. All options become exercisable one year from the date of grant and expire 10 years from the date of grant. At May 30, 1998, there were 170 employees and 11 nonemployee officers and directors eligible, all of whom were participants in the plans. At May 30, 1998, there were 1,549,391 shares available for future options.

The company's Long Term Incentive Plan, along with the Nonemployee Officer and Director Stock Option Plan, authorize reload options. Reload options provide for the purchase of shares equal to the number of shares delivered upon exercise of the original options plus the number of shares delivered to satisfy the tax liability incurred in the exercise. The reload options retain the expiration date of the original option, however, the exercise price must equal the fair market value on the date the reload options are granted. During fiscal 1998, 435,266 reload options were automatically granted.

A summary of shares subject to options follows:

	1998		1997		1996	
	Shares	Weighted-Average Exercise Prices	Shares	Weighted-Average Exercise Prices	Shares	Weighted-Average Exercise Prices
Outstanding at beginning of year:	4,028,196	\$ 7.27	4,863,840	\$ 6.48	5,157,400	\$ 5.99
Granted	1,599,152	\$ 22.12	338,000	\$ 15.92	1,615,600	\$ 7.57
Exercised	(2,081,834)	\$ 6.90	(1,102,644)	\$ 5.78	(1,572,680)	\$ 5.89
Terminated	(81,700)	\$ 17.60	(71,000)	\$ 7.74	(336,480)	\$ 6.39
Outstanding at end of year:	3,463,814	\$ 14.19	4,028,196	\$ 7.27	4,863,840	\$ 6.48
Exercisable at end of year:	1,921,162	\$ 7.58	3,770,196	\$ 6.68	3,361,440	\$ 5.98
Weighted-average fair-market value of options granted		\$ 6.54		\$ 4.42		\$ 2.08

A summary of stock options outstanding at May 30, 1998, follows:

Range of Exercise Price	Outstanding Stock Options			Exercisable Stock Options	
	Shares (In Thousands)	Weighted-Average Remaining Contractual Life	Weighted-Average Exercise Price	Shares (In Thousands)	Weighted-Average Exercise Price
\$4.66-\$7.28	1,266	4.99 years	\$ 6.20	1,266	\$ 6.20
\$7.56-\$19.88	1,692	8.67 years	\$ 16.14	655	\$ 10.23
\$24.44-\$32.50	506	7.89 years	\$ 27.63	—	\$ —
Total	3,464	7.21 years	\$ 14.19	1,921	\$ 7.58

The company accounts for its employee stock purchase plan and its stock option plans under APB Opinion 25; therefore, no compensation costs are recognized when employees purchase stock or when stock options are authorized, granted, or exercised. If compensation costs had been computed under

SFAS No. 123, "Accounting for Stock-Based Compensation," the company's net income and earnings per share would have been reduced by approximately \$10.4 million, or \$.08 per share in 1998, \$1.1 million, or \$.01 per share in 1997, and \$2.4 million, or \$.02 per share in 1996.

For purposes of computing compensation costs of stock options granted, the fair value of each stock option grant was estimated on the date of grant using the Black-Scholes option pricing model with the following weighted-average assumptions: 5.39% to 6.26% (in 1998) and 5.93% to 6.35% (in 1997) and 5.70% to 6.19% (in 1996) risk-free interest rates; three-year expected lives in 1998, 1997, and 1996; 34% (in 1998) and 31% (in 1997 and 1996) expected volatility; and .5% expected dividend yields in 1998, 1997, and 1996. Black-Scholes is a widely accepted stock option pricing model; however, the ultimate value of stock options granted will be determined by the actual lives of options granted and future price levels of the company's common stock.

Key Executive and Director Stock Programs

Restricted Stock Grants The company has granted restricted common shares to certain key employees. Shares were awarded in the name of the employee, who has all rights of a shareholder, subject to certain restrictions on transferability and a risk of forfeiture. The forfeiture provisions on the awards expire annually, over a period not to exceed six years, as certain financial goals are achieved. During fiscal 1998, no shares were granted under the company's long-term incentive plan, no shares were forfeited, and the forfeiture provisions expired on 52,917 shares. As of May 30, 1998, 176,154 shares remained subject to forfeiture provisions and restrictions on transferability.

The remaining shares subject to forfeiture provisions have been recorded as unearned stock grant compensation and are included as a separate component of shareholders' equity under the caption Key Executive Stock Programs. The unearned compensation is being charged to selling, general, and administrative expense over the five-year vesting period and was \$.7, \$.4, and \$.3 million in 1998, 1997, and 1996, respectively.

Key Executive Deferred Compensation Plan During fiscal 1997, the company established the Herman Miller, Inc., Key Executive Deferred Compensation Plan, which allows certain executives to defer receipt of all or a portion of their EVA cash incentive. The company may make a matching contribution of 30% of the executive's contribution up to 50% of the deferred EVA cash incentive. The company matching contribution vests at the rate of 33 $\frac{1}{3}$ % annually. In accordance with the terms of the plan, the executive deferral and company matching contribution have been placed in a "Rabbi" trust, which invests solely in the company's common stock. These Rabbi trust arrangements offer the executive a degree of assurance for ultimate payment of benefits without causing constructive receipt for income tax purposes. Distributions to the executive from the Rabbi trust can only be made in the form of the company's common stock. The assets in the Rabbi trust remain subject to the claims of creditors of the company and are not the property of the executive, and are therefore included as a separate component of shareholders' equity.

Key Executive Stock Purchase Assistance Plan In October 1994, the company adopted a key executive stock purchase assistance plan whereby the company may extend credit to officers and key executives to purchase the company's stock through the exercise of options or on the open market. These loans are secured by the shares acquired and are repayable under full recourse promissory notes. The sale or transfer of shares is restricted for five years after the loan is fully paid. The plan provides for



the key executives to earn repayment of a portion of the notes, including interest, based on meeting annual performance objectives as set forth by the Executive Compensation Committee of the Board of Directors. The notes bear interest at 7.0 percent per annum. Interest is payable annually and principal is due on various dates through September 1, 2007. As of May 30, 1998, the notes outstanding relating to the exercise of options were \$.4 million and are included as a separate component of shareholders' equity under the caption Key Executive Stock Programs. Notes outstanding related to open-market purchases were \$.8 million and are recorded in other assets. Compensation expense related to earned repayment was \$2.5 million in 1998, \$3.9 million in 1997, and \$1.7 million in 1996.

Director Fees During fiscal 1997, the Board of Directors approved a plan that allows the Board members to elect to receive their director fees in the form of unrestricted company stock at the then fair-market value rather than in cash. Under this plan, the Board members received 7,510 and 4,968 shares of the company's stock in fiscal 1998 and 1997, respectively.

Income Taxes

Pretax income consisted of the following:

(In Thousands)	1998	1997	1996
Domestic	\$ 186,266	\$ 141,742	\$ 77,169
Foreign	23,265	(15,859)	(7,073)
	<u>\$ 209,531</u>	<u>\$ 125,883</u>	<u>\$ 70,096</u>

The provision for income taxes consisted of the following:

(In Thousands)	1998	1997	1996
Current: Domestic – Federal	\$ 77,161	\$ 66,003	\$ 15,725
Domestic – State	4,430	4,957	1,615
Foreign	6,184	(2,287)	(527)
	<u>\$ 87,775</u>	<u>\$ 68,673</u>	<u>\$ 16,813</u>
Deferred: Domestic – Federal	(7,019)	(15,938)	6,115
Domestic – State	321	(677)	50
Foreign	123	(573)	1,172
	<u>(6,575)</u>	<u>(17,188)</u>	<u>7,337</u>
Total income-tax provision	<u>\$ 81,200</u>	<u>\$ 51,485</u>	<u>\$ 24,150</u>

The following table represents a reconciliation of income taxes at the United States statutory rate with the effective tax rate as follows:

(In Thousands)	1998	1997	1996
Income taxes computed at the United States statutory rate of 35%	\$ 73,336	\$ 44,059	\$ 24,534
Increase (decrease) in taxes resulting from:			
Corporate-owned life insurance	3,915	1,854	(3,302)
Changes in valuation allowance, net	—	—	(2,762)
Additional reserves provided	—	—	2,834
State taxes, net	3,088	2,782	1,082
Other	861	2,790	1,764
	<u>\$ 81,200</u>	<u>\$ 51,485</u>	<u>\$ 24,150</u>

The tax effects and types of temporary differences that give rise to significant components of the deferred tax assets and liabilities at May 30, 1998, and May 31, 1997, are presented below:

(In Thousands)	1998	1997
Deferred tax assets:		
Foreign net operating loss carryforwards	\$ 8,114	\$ 10,791
Book over tax loss on sale of fixed assets	5,845	6,045
Compensation-related accruals	9,475	4,186
Accrued pension and postretirement benefit obligations	21,743	17,671
Reserves for inventory	4,317	5,295
Reserve for uncollectible accounts and notes receivable	5,756	5,212
Other	31,703	27,208
Valuation allowance	(8,114)	(10,791)
	<u>\$ 78,839</u>	<u>\$ 65,617</u>
Deferred tax liabilities:		
Book basis of property in excess of tax basis	\$ (19,828)	\$ (19,429)
Capitalized software costs	(5,340)	—
Prepaid employee benefits	(2,665)	(2,239)
Other	(9,386)	(8,904)
	<u>\$ (37,219)</u>	<u>\$ (30,572)</u>

The company has foreign net operating loss carryforwards, the tax benefit of which is \$8.1 million, of which \$6.1 million expires at various dates through 2008, and of which \$2.0 million has unlimited expiration. For financial statement purposes, the tax benefit of the foreign net operating loss carryforward has been recognized as a deferred tax asset, subject to a valuation allowance.

Changes in the valuation allowance during 1996 reflect the utilization of the company's capital loss carryforwards which served to offset capital gains recognized on the sale and leaseback of the Roswell, Georgia, facility (see the Long-Term Debt note for a description of the lease) and on certain excess land sold to the company's captive insurance company. In addition, in each of the years presented, the allowance reflects changes in the net operating loss carryforwards at the company's foreign subsidiaries, which in 1997 primarily reflects the divestiture of the German manufacturing operations.

The company has not provided for United States income taxes on undistributed earnings of foreign subsidiaries totaling \$50.3 million. Recording of deferred income taxes on these undistributed earnings is not required, since these earnings have been permanently reinvested. These amounts would be subject to possible U.S. taxation only if remitted as dividends. The determination of the hypothetical amount of unrecognized deferred U.S. taxes on undistributed earnings of foreign entities is not practicable.

Fair Value of Financial Instruments

The carrying amount of the company's financial instruments included in current assets and current liabilities approximates their fair value due to their short-term nature. The fair value of the notes receivable is estimated by discounting expected future cash flows using current interest rates at which

similar loans would be made to borrowers with similar credit ratings and remaining maturities. As of May 30, 1998, and May 31, 1997, the fair value of the notes receivable approximated the carrying value. The company intends to hold these notes to maturity and has recorded allowances to reflect the terms negotiated for carrying value purposes. As of May 30, 1998, and May 31, 1997, the carrying value approximated the fair value of the company's long-term debt.

Financial Instruments with Off-Balance-Sheet Risk

The company utilizes derivative financial instruments to manage its exposure to foreign currency volatility at the transactional level. The majority of these contracts relate to major currencies such as the Japanese yen, the Australian dollar, and the British pound. The exposure to credit risk is minimal, since the counterparties are major financial institutions. The market risk exposure is essentially limited to currency rate movements. The gains or losses arising from these financial instruments are applied to offset exchange gains or losses on related hedged exposures. Realized gains or losses in 1998, 1997, and 1996 were not material to the company's results of operations. At May 30, 1998, and May 31, 1997, the company had no outstanding derivative financial instruments.

Supplemental Disclosures of Cash Flow Information

The following table presents a reconciliation of net income to net cash provided by operating activities:

(In Thousands)	1998	1997	1996
Depreciation and amortization	\$ 50,748	\$ 47,985	\$ 45,009
Loss on divestiture	—	14,500	—
Provision for losses on accounts and notes receivable	5,245	7,302	4,635
Loss on sales of property and equipment	2,243	1,575	120
Deferred taxes	(6,575)	(17,188)	7,337
Other liabilities	2,815	17,070	1,468
Stock grants earned	718	387	284
Changes in current assets and liabilities:			
Decrease (increase) in assets:			
Accounts receivable	(12,706)	(11,735)	4,295
Inventories	5,237	11,130	11,042
Prepaid expenses and other	3,715	(4,096)	(5,009)
Increase in liabilities:			
Accounts payable	13,691	15,296	627
Accrued liabilities	75,261	61,546	8,704
Total changes in current assets and liabilities	85,198	72,141	19,659
Total adjustments	\$140,392	\$143,772	\$ 78,512

Cash payments for interest and income taxes were as follows:


(In Thousands)	1998	1997	1996
Interest paid	\$ 7,709	\$ 8,759	\$ 7,458
Income taxes paid	\$ 66,023	\$ 53,185	\$ 13,883






Contingencies

In fiscal 1992, Haworth, Inc., (Haworth) filed a lawsuit against the company, alleging that the electrical systems used in creation of the company's products infringed one or more of Haworth's patents. In fiscal 1996, the company and Haworth agreed to terms of a settlement. The company continues to believe, based upon written opinion of counsel, that its products did not infringe Haworth's patents and that it would, more likely than not, have prevailed on the merits. However, based on the mounting legal costs, distraction of management focus, and the uncertainty present in any litigation, the company concluded that settlement was in the best interest of its shareholders. The settlement included a one-time cash payment of \$44.0 million in exchange for a complete release. The companies also exchanged limited covenants not to sue with respect to certain existing and potential patent designs. Herman Miller simultaneously reached a settlement with one of its suppliers, who agreed to pay the company \$11.0 million and, over the next seven years, to rebate a percentage of its sales to Herman Miller that are in excess of then current levels. The \$11.0 million, plus interest, will be paid in annual installments over seven years and the rebates will be recorded when earned. Accordingly, the company recorded a net litigation settlement expense of \$16.5 million after applying previously recorded reserves and the settlement with the supplier.



The company, for a number of years, has sold various products to the United States Government under General Services Administration (GSA) multiple award schedule contracts. The GSA is permitted to audit the company's compliance with the GSA contracts. As a result of its audits, the GSA has asserted a refund claim under the 1982 contract for approximately \$2.7 million and has other contracts under audit review. Management has been notified that the GSA has referred the 1988 contract to the Justice Department for consideration of a potential civil False Claims Act case. Management disputes the audit result for the 1982 contract and does not expect resolution of the matter to have a material adverse effect on the company's consolidated financial statements. Management does not have information that would indicate a substantive basis for a civil False Claims Act case under the 1988 contract.

The company is also involved in legal proceedings and litigation arising in the ordinary course of business. In the opinion of management, the outcome of such proceedings and litigation currently pending will not materially affect the company's consolidated financial statements.



Segment Information

The company operates on a worldwide basis in a single industry consisting of the design, manufacture, and sale of office furniture systems, products, and related services. The following information is presented with respect to the company's operations in different geographic areas for the fiscal years ended May 30, 1998, May 31, 1997, and June 1, 1996. Transfers between geographic areas represent the selling price of sales to affiliates, which is generally based on cost plus a markup. Net income of foreign operations and exports includes royalty income from licensee sales and reflects the gain or loss on foreign currency exchange. The cash and cash equivalents accounts of the company are considered to be corporate assets. All other assets have been identified with domestic or foreign operations. No single customer accounted for more than 10.0 percent of consolidated net sales.

(In Thousands)	United States	Foreign Operations and Exports	Adjustments and Eliminations	Consolidated
1998				
Sales to unaffiliated customers	\$1,451,885	\$ 266,710	\$ —	\$1,718,595
Transfers between geographic areas	20,765	20,255	(41,020)	—
Net sales	\$1,472,650	\$ 286,965	\$ (41,020)	\$1,718,595
Net income	\$ 117,091	\$ 11,240	\$ —	\$ 128,331
Identifiable assets	\$ 599,810	\$ 69,220	\$ —	\$ 669,030
Corporate assets				115,316
Total assets				\$ 784,346
1997				
Sales to unaffiliated customers	\$1,244,645	\$ 251,240	\$ —	\$1,495,885
Transfers between geographic areas	23,723	15,732	(39,455)	—
Net sales	\$1,268,368	\$ 266,972	\$ (39,455)	\$1,495,885
Net income (loss)	\$ 83,497	\$ (9,099)	\$ —	\$ 74,398
Identifiable assets	\$ 554,044	\$ 95,382	\$ —	\$ 649,426
Corporate assets				106,161
Total assets				\$ 755,587
1996				
Sales to unaffiliated customers	\$1,043,850	\$ 240,081	\$ —	\$1,283,931
Transfers between geographic areas	34,667	13,176	(47,843)	—
Net sales	\$1,078,517	\$ 253,257	\$ (47,843)	\$1,283,931
Net income (loss)	\$ 53,977	\$ (8,031)	\$ —	\$ 45,946
Identifiable assets	\$ 532,371	\$ 105,487	\$ —	\$ 637,858
Corporate assets				57,053
Total assets				\$ 694,911

Report of Independent Public Accountants

To the Shareholders and Board of Directors of Herman Miller, Inc.:

We have audited the accompanying consolidated balance sheets of Herman Miller, Inc., (a Michigan corporation) and subsidiaries as of May 30, 1998, and May 31, 1997, and the related consolidated statements of income, shareholders' equity, and cash flows for each of the three years in the period ended May 30, 1998. These financial statements are the responsibility of the company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Herman Miller, Inc., and subsidiaries as of May 30, 1998, and May 31, 1997, and the results of their operations and their cash flows for each of the three years in the period ended May 30, 1998, in conformity with generally accepted accounting principles.

Arthur Andersen LLP
Grand Rapids, Michigan
June 25, 1998



Management's Report on Financial Statements

The consolidated financial statements of Herman Miller, Inc., and subsidiaries were prepared by, and are the responsibility of, management. The statements have been prepared in conformity with generally accepted accounting principles appropriate in the circumstances and include amounts that are based on management's best estimates and judgments.

The company maintains systems of internal accounting controls designed to provide reasonable assurance that all transactions are properly recorded in the company's books and records, that policies and procedures are adhered to, and that assets are protected from unauthorized use. The systems of internal accounting controls are supported by written policies and guidelines and are complemented by a staff of internal auditors and by the selection, training, and development of professional financial managers.

The consolidated financial statements have been audited by the independent public accounting firm Arthur Andersen LLP, whose appointment is ratified annually by shareholders at the annual shareholders' meeting. The independent public accountants conduct a review of internal accounting controls to the extent required by generally accepted auditing standards and perform such tests and related procedures as they deem necessary to arrive at an opinion on the fairness of the financial statements.

The Financial Audit Committee of the Board of Directors, composed solely of directors from outside the company, regularly meets with the independent public accountants, management, and the internal auditors to satisfy itself that they are properly discharging their responsibilities. The independent public accountants have unrestricted access to the Financial Audit Committee, without management present, to discuss the results of their audit and the quality of financial reporting and internal accounting control.

Michael A. Volkema, President and Chief Executive Officer

Brian C. Walker, Executive Vice President, Financial Services, and Chief Financial Officer

June 25, 1998

Board of Directors

Bill Brehm	<i>Chairman of the Board, SRA International, Inc.</i> Systems integrator and information technology consulting Member of Executive and Nominating Committees
Jim Carreker	<i>Chairman of the Board and Chief Executive Officer, Aspect Telecommunications Corporation</i> Telecommunications systems company Member of Executive Compensation Committee
Harold Chandler	<i>Chairman, President, and Chief Executive Officer, Provident Companies, Inc.</i> Insurance company Member of Executive Compensation Committee
Dave Crockett	<i>General Partner, Aspen Ventures</i> High-technology venture-capital firm Member of Financial Audit Committee
 Brian Griffiths	<i>International Advisor, Goldman Sachs International Limited</i> <i>Lord Griffiths of Fforestfach</i> International investment banking firm and House of Lords, United Kingdom
Dave Nelson	<i>Chairman of the Board, Herman Miller, Inc.</i> Member of Executive Committee
Bill Pollard	<i>Chairman of the Board, The ServiceMaster Company</i> Management and consumer services for healthcare, industrial, and educational facilities Member of Executive and Nominating Committees
Ruth Alkema Reister	<i>Private Investments and Civic and Charitable Activities</i>
Dick Ruch	<i>Former Chairman, President, and Chief Executive Officer, Herman Miller, Inc.</i> Member of Executive and Financial Audit Committees
Dorothy Terrell	<i>President, Services Group, and Senior Vice President, Corporate Operations, Natural MicroSystems Corporation</i> Telecommunications technology company Member of Executive Compensation Committee
Mike Volkema	<i>President and Chief Executive Officer, Herman Miller, Inc.</i> Member of Executive Committee
Jim DeBoer, Jr.	<i>Secretary of the Board</i> Partner, Varnum, Riddering, Schmidt & Howlett LLP Attorneys at Law

Leverage and Focus Team

Mike Volkema	<i>President and Chief Executive Officer</i>
Jim Christenson	<i>Executive Vice President, Legal Services, and Secretary</i>
Bob Frey	<i>Executive Vice President, President, Herman Miller International</i>
Dave Knibbe	<i>Executive Vice President, Sales and Distribution</i>
Rod McCowan	<i>Executive Vice President, Human Resources and Corporate Communication</i>
Andrew McGregor	<i>Executive Vice President, President, Herman Miller Choices</i>
Gary Miller	<i>Executive Vice President, Product Services</i>
Gene Miyamoto	<i>Executive Vice President, President, Coro</i>
Bix Norman	<i>Executive Vice President, Chief Information Officer</i>
Vicki TenHaken	<i>Executive Vice President, Strategic Planning</i>
Gary Van Spronsen	<i>Executive Vice President, President, Miller SQA</i>
Brian Walker	<i>Executive Vice President, Financial Services, and Chief Financial Officer</i>

Herman Miller, Inc. Zeeland, Michigan



Corporate Offices

Herman Miller, Inc. *Zeeland, Michigan*

Milsure Insurance Limited *Bridgetown, Barbados*

United States Operations

Coro, Inc. *Zeeland, Michigan*

Herman Miller North America *Zeeland, Michigan*

Integrated Metal Technology, Inc. *Spring Lake, Michigan*

Meridian Incorporated *Spring Lake, Michigan*

Milcare, Inc. *Grandville, Michigan*

Miller SQA, Inc. *Holland, Michigan*

Powder Coat Technology, Inc. *Spring Lake, Michigan*

International Operations

Herman Miller Asia (Pte), Ltd. *Singapore*

Herman Miller (Australia) Pty., Ltd. *Sydney, Australia*

Herman Miller Canada, Inc. *Toronto, Ontario*

Herman Miller Et Cie *Paris, France*

Herman Miller Hong Kong, Ltd. *Hong Kong, China*

Herman Miller Italia S.p.A. *Milan, Italy*

Herman Miller Japan, Ltd. *Tokyo, Japan*

Herman Miller Latin America/Caribbean *Miami, Florida*

Herman Miller Ltd. Niederlassung Deutschland *Ratingen, Germany*

Herman Miller Limited *Bath, United Kingdom*

Herman Miller Mexico S.A. de C.V. *Mexico City, Mexico*

The Resource Alliance, Inc. *Toronto, Ontario*

Licensees

B.I.I. *Barbados*

Colección S.A. *Buenos Aires, Argentina*

CWC Group *Philippines*

Decodibo S.A. *Caracas, Venezuela*

Fernando Mayer *Santiago, Chile*

Interiores Cía. Ltda. *Quito, Ecuador*

Modusistemas C.A. *Caracas, Venezuela*

Móveis Teperman, S.A. *São Paulo, Brazil*

Multiproyectos Ltda. *Bogotá, Colombia*

Onir S.A. *Montevideo, Uruguay*



Manufacturing/Distribution Facilities

Bath and Chippenham, United Kingdom

Holland, Spring Lake, and Zeeland, Michigan

Mexico City, Mexico

Roswell and Stone Mountain, Georgia

Rocklin, California

Shareholder Reference Information

Line of Business

Herman Miller, Inc., is engaged primarily in the design, manufacture, and sale of office systems, products, and services principally for offices, and to a lesser extent, for healthcare facilities and other uses. Through research and design, the company has developed innovative solutions to operational problems in the office, institutional, healthcare, material-handling, and other environments.

Investor Relations and Form 10-K

Any shareholder may obtain a copy (without charge) of the Form 10-K (1997 Annual Report filed with the Securities and Exchange Commission) by writing Brian Walker or Bob Dentzman:

Brian Walker, Executive Vice President, Financial Services, and Chief Financial Officer

Email: investor@hermanmiller.com

Telephone: 616 654 8589

Bob Dentzman, Vice President Treasury, Investor Relations

Email: investor@hermanmiller.com

Telephone: 616 654 5044

Herman Miller, Inc., 855 East Main Avenue, PO Box 302, Zeeland, MI 49464-0302

Transfer Agent and Registrar

First Chicago Trust Company of New York, PO Box 2500, Jersey City, NJ 07303-2500

Attention: Herman Miller, Inc., Shareholder Relations

Telephone: 800 446 2617

Common Stock

Herman Miller, Inc., common stock is quoted on the NASDAQ-National Market System (NASDAQ-NMS Symbol: MLHR). As of August 3, 1998, there were approximately 29,000 shareholders of the company's common stock.

Independent Public Accountants

Arthur Andersen LLP, Grand Rapids, Michigan

Affirmative Action

Herman Miller, Inc., is an equal opportunity employer and supports affirmative action programs for minorities and women, including the recruitment, education and training, and economic development of businesses.

Internet Address

www.hermanmiller.com