

NITCHES INC
Form 10-Q
July 15, 2004

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

Form 10-Q

**QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE
SECURITIES EXCHANGE ACT OF 1934**

For the quarterly period ended: May 31, 2004

Commission File Number 0-13851

NITCHES, INC.

(Exact name of registrant as specified in its charter)

California **95-2848021**
(State of Incorporation) (I.R.S. Employer Identification No.)
10280 Camino Santa Fe, San Diego, California 92121
(Address of principal executive offices)

Registrant's telephone number: (858) 625-2633

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
Common Stock, no par value	NASDAQ SmallCap Market

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes No

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act).

Yes No

As of May 31, 2004 the Registrant had 1,171,169 shares of common stock outstanding.

PART I - FINANCIAL INFORMATION

Item 1. Financial Statements

NITCHES, INC. AND SUBSIDIARIES
Condensed Consolidated Balance Sheets

	<u>May 31,</u> <u>2004</u>	<u>August 31,</u> <u>2003</u>
	(Unaudited)	
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 239,000	\$ 110,000
Receivables:		
Trade accounts, less allowances	5,117,000	894,000
Due from affiliates and employees	1,000	28,000
	<u>5,118,000</u>	<u>922,000</u>
Total receivables		922,000
Refundable income taxes		466,000
Inventories, less allowances	3,011,000	4,974,000
Deferred income taxes	192,000	192,000
Other current assets	42,000	57,000
	<u>8,602,000</u>	<u>6,721,000</u>
Total current assets		6,721,000
Investment in Designer Intimates, Inc.	2,000	
Furniture, fixtures and equipment, net	44,000	56,000
Deferred income taxes	53,000	53,000
Other assets	17,000	17,000
	<u>\$ 8,718,000</u>	<u>\$ 6,847,000</u>
LIABILITIES AND SHAREHOLDERS EQUITY		
Current liabilities:		
Accounts payable	\$ 1,866,000	\$ 1,525,000
Accrued expenses	714,000	182,000
Income taxes payable	371,000	
	<u>2,951,000</u>	<u>1,707,000</u>
Total current liabilities		1,707,000
Long term liabilities:		
Loss on investment in Designer Intimates, Inc.		236,000
Shareholders' equity:		
Preferred stock, no par value; 25,000,000 shares authorized, no shares issued or outstanding		
Common stock, no par value; 50,000,000 shares authorized; 1,171,169 shares issued and outstanding	1,495,000	1,495,000
Retained earnings	4,272,000	3,409,000
	<u>5,767,000</u>	<u>4,904,000</u>
Total shareholders' equity		4,904,000
	<u>\$ 8,718,000</u>	<u>\$ 6,847,000</u>

The accompanying notes are an integral part of these financial statements.

NITCHES, INC. AND SUBSIDIARIES
 Consolidated Statements of Income
 (Unaudited)

	Three Months Ended May 31,		Nine Months Ended May 31,	
	2004	2003	2004	2003
Net sales	\$ 9,024,000	\$ 7,028,000	\$ 25,503,000	\$ 24,185,000
Cost of goods sold	6,305,000	4,884,000	17,991,000	18,370,000
Gross profit	2,719,000	2,144,000	7,512,000	5,815,000
Selling, general and administrative expenses	2,264,000	2,009,000	6,404,000	5,670,000
Income/(loss) from operations	455,000	135,000	1,108,000	145,000
Interest and other income				3,000
Interest expense	(40,000)	(11,000)	(83,000)	(74,000)
Income/(loss) from unconsolidated subsidiary	(172,000)	(159,000)	238,000	73,000
Income/(loss) before income taxes	243,000	(35,000)	1,263,000	147,000
Provision/(benefit) for income taxes	160,000	49,000	400,000	(80,000)
Net income/(loss)	\$ 83,000	\$ (84,000)	\$ 863,000	\$ 227,000
Earnings per share	\$ 0.07	\$ (0.07)	\$ 0.74	\$ 0.19
Shares outstanding	1,171,169	1,171,169	1,171,169	1,171,169
Dividends per share	\$	\$ 0.05	\$	\$ 0.25

The accompanying notes are an integral part of these financial statements.

NITCHES, INC. AND SUBSIDIARIES
Condensed Consolidated Statements of Cash Flows
(Unaudited)

	Nine Months Ended May 31,	
	2004	2003
Net income	\$ 863,000	\$ 227,000
Cash flows from operating activities:		
Depreciation and amortization	20,000	26,000
(Increase) decrease in accounts receivable	(4,196,000)	1,292,000
Decrease in inventories and other current assets	2,444,000	1,316,000
Increase (decrease) in payables and accrued expenses	1,244,000	(2,397,000)
Non-cash income from unconsolidated subsidiary	(238,000)	(73,000)
Net cash provided by operating activities	\$ 137,000	\$ 391,000
Cash flows from investing activities:		
Capital expenditures	(8,000)	(5,000)
Cash flows from financing activities:		
Dividends paid		(293,000)
Net increase (decrease) in cash and cash equivalents	129,000	93,000
Cash and cash equivalents at beginning of period	110,000	182,000
Cash and cash equivalents at end of period	\$ 239,000	\$ 275,000
Supplemental disclosures of cash flow information:		
Cash paid during the period:		
Interest	\$ 83,000	\$ 74,000
Non-cash investing activity:		
Accrued earnings of unconsolidated subsidiary	\$ (238,000)	\$ 73,000

The accompanying notes are an integral part of these financial statements.

NITCHES, INC. AND SUBSIDIARIES
Notes to Condensed Consolidated Financial Statements

1. Description of Business

Nitches, Inc. (the Company) is a wholesale importer and distributor of clothing manufactured to its specifications and distributed in the United States under Company brand labels and private retailer labels. The Company's product lines include women's sleepwear and western wear and men's casual wear. During the recent quarter the Company discontinued the manufacture and distribution of performance apparel, however this did not have a material effect on the results for the current period, nor is it expected to materially impact future operating results.

2. Condensed Financial Statements:

The accompanying unaudited consolidated financial statements have been prepared in accordance with the instructions to Form 10-Q. They do not include all information and footnotes necessary for a fair presentation of financial position and results of operations and cash flows in conformity with generally accepted accounting principles in the United States of America. These consolidated financial statements should be read in conjunction with the consolidated financial statements and related notes contained in the Company's Annual Report on Form 10-K for the year ended August 31, 2003. In the opinion of Management, all adjustments considered necessary for a fair presentation have been included in the interim period. Operating results for the nine months ended May 31, 2004 are not necessarily indicative of the results that may be expected for the year ending August 31, 2004.

3. Earnings Per share:

At May 31, 2004, there were no stock options or similar instruments outstanding and therefore no dilutive effect to the number of shares outstanding.

4. Inventories:

	May 31, 2004	August 31, 2003
Fabric and trim	\$ 9,000	\$ 320,000
Work in progress	1,164,000	1,254,000
Finished goods	1,838,000	3,400,000
	<u>\$ 3,011,000</u>	<u>\$ 4,974,000</u>

5. Trade accounts receivable:

Pursuant to the terms of an agreement between Nitches and a factor, Nitches sells a majority of its trade accounts receivable to the factor on a pre-approved, non-recourse basis. The price at which the accounts are sold is the invoice amount reduced by the factor commission (.3% of the invoice amount) and all selling discounts. For accounts sold to the factor without recourse, the factor is responsible for collection, assumes all credit risk, and obtains all of the rights and remedies against the company's customers. For such accounts, payment is due from the factor upon the earlier of the payment of the receivable to the factor by the customer, or the maturity of the receivable (generally 180 days from the date of shipment to the customer). As of May 31, 2004, non-recourse receivables totaled \$6,669,000.

Trade accounts receivable not sold to the factor remain in the custody and control of the Company and the Company maintains all credit risk on those accounts as well as accounts which are sold to the factor with recourse. The combined credit risk for non-factored and recourse receivables as of May 31, 2004, totaled \$364,000.

The Company may request payment from the factor in advance of the collection date or maturity. Any such advance payments are assessed an interest charge through the collection date or maturity at the factor's prime rate less 1.5% (one and one half percent) per annum. The company's obligations with respect to advances from the factor are limited to the interest charges thereon. Advance payments are limited to a maximum of 85% (eighty-five percent) of eligible accounts receivable. The factoring agreement also provides for the issuance of irrevocable letters of credit for the Company's purchase of inventory in the normal course of its business. Letters of credit are subject to a \$6 million

NITCHES, INC. AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statement (continued)

limit. All assets of the company collateralize the advances and letters of credit. The Company's Chairman has also provided a personal guaranty in connection with the factoring arrangement.

5 Trade accounts receivable (continued):

The status of the Company's trade accounts receivable and letters of credit are as follows:

	<u>May 31,</u> <u>2004</u>	<u>August 31,</u> <u>2003</u>
Receivables assigned to factor:		
Non-recourse	\$ 6,669,000	\$ 2,599,000
Recourse	137,000	16,000
Advance payments from factor	(1,417,000)	(1,542,000)
	<u>5,389,000</u>	<u>1,073,000</u>
Due from factor	5,389,000	1,073,000
Non-factored accounts receivable	227,000	370,000
Allowance for customer credits and doubtful accounts	(499,000)	(549,000)
	<u>\$ 5,117,000</u>	<u>\$ 894,000</u>
Contingent liabilities for irrevocable letters of credit	<u>\$ 1,668,000</u>	<u>\$ 2,401,000</u>

6 Dividends:

The Company did not pay any dividends during the current period. During fiscal 2003 the Company declared and paid dividends of \$.30 per share.

7 Significant Customers:

Sales to two separate customers, Wal-Mart (Sam's Club) and Kohl's, accounted for 38.6% and 23.5% respectively of the Company's net sales in the three months ended May 31, 2004. Two customers, Kohl's and Mervyn's, accounted for 23.7% and 12.3% of the Company's net sales in the three months ended May 31, 2003. Two customers, Wal-Mart (Sam's Club) and Kohl's, accounted for 30.9% and 30.2% of the Company's net sales for the nine months ended May 31, 2004. Three customers, Kohl's, Mervyn's and Sears, accounted for 31.5%, 21.3% and 14.4% of the Company's net sales for the nine months ended May 31, 2003.

Two customers, Wal-Mart (Sam's Club) & Kohl's, accounted for 46.1% and 14.6% respectively of the Company's trade receivable balance as of May 31, 2004. Two customers, Kohl's and Mervyn's, accounted for 19.0% and 16.3% respectively of the Company's trade receivable balance at May 31, 2003.

8 Minority Interest:

In October 2002 the Company acquired a 28% interest in Designer Intimates, Inc., which owns 100% of NAP, Inc., a New York-based intimate apparel company. Designer Intimates had acquired NAP from its founders and obtained a credit line of approximately \$12 million from HSBC, secured by the inventory and accounts receivable of NAP and the guarantees of shareholders of Designer Intimates. Nitches guarantees \$3 million of this credit line and this guarantee formed the consideration from Nitches for its 28% ownership interest in Designer Intimates. Nitches reports any income or loss from the ongoing operation of Designer Intimates using the equity method of accounting, whereby Nitches 28% interest in Designer Intimates is reported as a single line item on the Consolidated Statement of Income.

For the nine months ended May 31, 2004, the Company recognized \$238,000 in income from the unconsolidated subsidiary. This income is reported net of tax and is not taxable to the Company. For that same period, Designer Intimates earned net income of \$851,000 on sales of \$61.3 million. For the nine months ended May 31, 2003, the

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Company recognized \$73,000 in income from Designer Intimates on net income of \$262,000 and sales of \$57.3 million. For the three months ended May 31, 2004, the Company recognized a \$172,000 loss from the unconsolidated subsidiary. For that same period Designer Intimates lost \$614,000 on sales of \$12.1 million. For the three months ended May 31, 2003, the Company lost \$159,000 from Designer Intimates on a loss of \$568,000 and sales of \$11.8 million for the unconsolidated subsidiary.

Following are the unaudited condensed financial statements of Designer Intimates, Inc. as of May 31, 2004 for the 3 and 9 month periods then ended:

Designer Intimates, Inc.
Consolidated Balance Sheet
(Unaudited)

May 31,	August 31,
2004	2003