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TAITRON COMPONENTS INC
Form 10-Q
November 14, 2001

UNITED STATES
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 September 30, 2001

TRANSITION REPORT PURSUANT TO SECTION 13 or 15(d) OF THE
SECURITIES EXCHANGE ACT OF 1934

Commission File Number 0-25844

TAITRON COMPONENTS INCORPORATED
(Name of Registrant as specified in its charter)

California
(State or Other Jurisdiction of
Incorporation or Organization)

95-4249240
(I.R.S. Employer
Identification No.)

28040 West Harrison Parkway
Valencia, California 91355-4162
(Address Of Principal Executive Offices)

(661) 257-6060
(Registrant's Telephone Number, Including Area Code)

NONE
(Former Name, Address and Fiscal Year, if Changed Since Last Report)

Check 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 (X) NO ()

Indicate the number of shares outstanding of each of the registrant's classes of common stock, as of the latest practicable date:

| Class | Outstanding on October 15, 2001 |
|--|---------------------------------|
| Class A Common Stock, \$.001 par value | 4,890,037 |
| Class B Common Stock, \$.001 par value | 762,612 |

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

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TAITRON COMPONENTS INCORPORATED

Condensed Consolidated Balance Sheets (Dollars in Thousands)

| | | September 30, 2001 |
|---|----|-----------------------|
| Assets | | ----- (Unaudited) |
| Current assets: | | |
| Cash and cash equivalents | \$ | 125 |
| Trade accounts receivable, net | | 2,748 |
| Inventory, net | | 28,933 |
| Prepaid expenses | | 277 |
| Deferred income taxes | | 602 |
| Other current assets | | 127 |
| | | ----- |
| Total current assets | | 32,812 |
| Property and equipment, net | | 6,882 |
| Other assets | | 296 |
| | | ----- |
| Total assets | \$ | 39,990 ===== |
| Liabilities and Shareholders' Equity | | |
| Current liabilities: | | |
| Revolving line of credit | \$ | 12,430 |
| Current portion of long term debt | | 23 |
| Trade accounts payable | | 1,307 |
| Accrued liabilities and other | | 189 |
| | | ----- |
| Total current liabilities | | 13,949 |
| Long-term debt, less current portion | | 394 |
| | | ----- |
| Total liabilities | | 14,343 ----- |
| Commitments | | -- |
| Shareholders' equity: | | |
| Preferred stock, \$.001 par value. Authorized 5,000,000 shares. None issued or outstanding. | | -- |
| Class A common stock, \$.001 par value. Authorized 20,000,000 shares; issued and outstanding 4,891,837 and 4,983,975 shares as of September 30, 2001 and December 31, 2000, respectively. | | 5 |
| Class B common stock, \$.001 par value. Authorized, issued and outstanding 762,612, shares as of September 30, 2001 and December 31, 2000. | | 1 |
| Additional paid-in capital | | 10,823 |
| Accumulated comprehensive income | | (53) |
| Retained earnings | | 14,871 |
| | | ----- |
| Total shareholders' equity | | 25,647 ----- |

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Total liabilities and shareholders' equity \$ 39,990
=====

See accompanying notes to condensed consolidated financial statements.

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TAITRON COMPONENTS INCORPORATED

Condensed Consolidated Statements of Operations
(Dollars in thousands, except per share amounts)

| | Three months ended September 30, 2001 ----- (Unaudited) | 2000 ----- (Unaudited) | Nine months e 2001 ----- (Unaudited) |
|--|--|------------------------------|---|
| Net sales | \$ 3,726 | \$ 8,663 | \$ 13,402 |
| Cost of goods sold | 2,621 ----- | 5,915 ----- | 9,394 ----- |
| Gross profit | 1,105 | 2,748 | 4,008 |
| Selling, general and administrative expenses | 1,263 ----- | 1,711 ----- | 4,280 ----- |
| Operating earnings (loss) | (158) | 1,037 | (272) |
| Interest expense, net | 188 | 243 | 634 |
| Other expense (income), net | 24 ----- | (26) ----- | (29) ----- |
| Earnings (loss) before income taxes | (370) | 820 | (877) |
| Income tax provision (benefit) | (63) ----- | 297 ----- | (132) ----- |
| Net earnings (loss) | \$ (307) ===== | \$ 523 ===== | \$ (745) ===== |
| Earnings (loss) per share | | | |
| Basic | \$ (.05) ===== | \$.09 ===== | \$ (.13) ===== |
| Diluted | \$ (.05) ===== | \$.09 ===== | \$ (.13) ===== |
| Weighted average shares outstanding | | | |
| Basic | 5,664,460 ===== | 5,781,310 ===== | 5,690,161 ===== |
| Diluted | 5,664,460 ===== | 6,069,675 ===== | 5,690,161 ===== |

See accompanying notes to condensed consolidated financial statements.

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TAITRON COMPONENTS INCORPORATED
 Condensed Consolidated Statements of Cash Flows
 (Dollars in thousands)

| | Nine months ended |
|---|---------------------------------------|
| | ----- 2001 ----- (Unaudited) |
| Cash flows from operating activities: | |
| Net earnings (loss) | \$ (745) |
| | ----- |
| Adjustments to reconcile net earnings (loss) to net cash provided by operating activities: | |
| Depreciation and amortization | 421 |
| Gain on sale of assets | (7) |
| Deferred income taxes | 92 |
| Changes in Assets and Liabilities: | |
| Trade accounts receivable | 2,061 |
| Inventory | 1,676 |
| Prepaid expenses | 78 |
| Other current assets | 124 |
| Other assets | (9) |
| Trade accounts payable | (1,188) |
| Accrued and other liabilities | (713) |
| | ----- |
| Total adjustments | 2,535 |
| | ----- |
| Net cash provided by operating activities | 1,790 |
| | ----- |
| Cash flows from investing activities: | |
| Acquisitions of property and equipment | (98) |
| Proceeds from sale of assets | 7 |
| | ----- |
| Net cash used in investing activities | (91) |
| | ----- |
| Cash flows from financing activities: | |
| Borrowings on long term debt | 3,955 |
| Payments on long term debt | (5,472) |
| Repurchase of Class A Common Stock | (294) |
| Exercise of stock options | 55 |
| | ----- |
| Net cash used in financing activities | (1,756) |
| | ----- |
| Impact of changes in exchange rates on cash | (8) |
| | ----- |
| Net decrease in cash and cash equivalents | (65) |
| Cash and cash equivalents, beginning of period | 190 |
| | ----- |

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| | | |
|--|----|-------|
| Cash and cash equivalents, end of period | \$ | 125 |
| | | ===== |
| Supplemental disclosure of cash flow information: | | |
| Cash paid for interest (net of capitalized interest of none and \$31 in 2001 and 2000, respectively) | \$ | 682 |
| | | ===== |
| Cash paid for income taxes | \$ | 309 |
| | | ===== |

See accompanying notes to condensed consolidated financial statements.

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Notes to Condensed Consolidated Financial Statements

As of and for the quarterly period ending September 30, 2001

(All amounts are unaudited, except for the balance sheet as of December 31, 2000)

(1) Basis of Presentation

The condensed consolidated financial information furnished herein is unaudited and, in the opinion of management, includes all adjustments (consisting of normal recurring adjustments and accruals) in conformity with the accounting principles reflected in the financial statements included in the Annual Report on Form 10-K filed with the Securities and Exchange Commission for the year ended December 31, 2000. The results of operations for interim periods are not necessarily indicative of results to be achieved for full fiscal years.

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with the instructions to Form 10-Q and, therefore, do not include all information and footnotes necessary for a fair presentation of financial position, results of operations and cash flows in conformity with generally accepted accounting principles. The unaudited condensed consolidated financial statements and notes should, therefore, be read in conjunction with the financial statements and notes thereto in the Annual Report on Form 10-K for the year ended December 31, 2000.

(2) Summary of Significant Accounting Policies

Principles of Consolidation

The unaudited condensed consolidated financial statements include the accounts of the Company and its majority-owned subsidiary. All significant intercompany transactions have been eliminated in consolidation.

Revenue Recognition

Revenue is recognized upon shipment of the merchandise. Reserves for sales allowances and customer returns are established based upon historical experience and management's estimates as shipments are made. Sales returns for the quarters ended September 30, 2001 and 2000 aggregated to \$89,000 and \$175,000, respectively and for the nine months ended September 30, 2001 and 2000 aggregated to \$280,000 and \$421,000, respectively.

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Allowance for Sales Returns and Doubtful Accounts

The allowance for sales returns and doubtful accounts at September 30, 2001 and December 31, 2000 aggregated \$102,000 and \$120,000, respectively.

Inventory

Inventory, consisting principally of products for resale, is stated at the lower of cost or market, using the first-in, first-out method. The value presented is net of valuation allowances of \$1,436,000 and \$1,326,000 at September 30, 2001 and December 31, 2000, respectively.

Net Earnings (Loss) Per Share

Common equivalent shares are excluded from the computation of diluted earnings (loss) per share for the three month period ended September 30, 2001 and for the nine month period ended September 30, 2001, as their effect is anti-dilutive.

Reclassification

Certain amounts in the 2000 financial statements have been reclassified to conform with the current 2001 financial statement presentation.

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(3) Revolving Line of Credit

During the quarter ended September 30, 2001, the Company renewed its revolving line of credit facility which provides up to \$16 million for operating purposes and up to an additional \$4 million for business acquisition purposes, extending the maturity date to May 18, 2003. The agreement governing this credit facility contains covenants that require the Company to be in compliance with certain financial ratios. Borrowings on the line of credit are secured by substantially all of the Company's assets.

Item 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Results of Operations

The following table sets forth, for the periods indicated, certain operating amounts and ratios as a percentage of net sales.

| | Three Month Period Ended September 30, | | Nine Month Period Ended Septe | |
|-----------|---|-------------|----------------------------------|----|
| | 2001 | 2000 | 2001 | |
| | (Unaudited) | (Unaudited) | (Unaudited) | (|
| | (Dollars in thousands) | | (Dollars in tho | |
| Net sales | \$ 3,726 | \$ 8,663 | \$ 13,402 | \$ |

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| | | | |
|--|----------|--------|----------|
| Cost of goods sold | 2,621 | 5,915 | 9,394 |
| Gross profit | 1,105 | 2,748 | 4,008 |
| % of net sales | 29.7% | 31.7% | 29.9% |
| Selling, general and administrative expenses | 1,263 | 1,711 | 4,280 |
| % of net sales | 33.9% | 19.8% | 31.9% |
| Operating earnings (loss) | (158) | 1,037 | (272) |
| % of net sales | (4.2)% | 12.0% | (2.0)% |
| Interest expense, net | 188 | 243 | 634 |
| % of net sales | 5.0% | 2.8% | 4.7% |
| Net earnings (loss) | \$ (307) | \$ 523 | \$ (745) |
| % of net sales | (8.2)% | 6.0% | (5.6)% |

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Three month Period Ended September 30, 2001 Compared To The Three month Period Ended September 30, 2000.

Net sales for the three months ended September 30, 2001 were \$3,726,000, compared with net sales for the three months ended September 30, 2000 of \$8,663,000, a decrease of \$4,937,000 or 57%. The decrease is primarily due to an industry wide decrease in demand for discrete semiconductors. Passive component sales decreased by \$1,255,000 during the quarter ended September 30, 2001 and export sales decreased to \$441,000 from \$847,000, comparing the same periods. The average unit selling price increased to 2.2 cents for the current period from 1.6 cents during the same period last year.

Cost of goods sold for the quarter ended September 30, 2001 decreased to \$2,621,000 from \$5,915,000 for the same period last year, a decrease of 55.7% or \$3,294,000. Consistent with the decrease in net sales, cost of goods sold decreased, however at a slower rate, resulting in gross profits decreasing as a percentage of net sales to 29.7% for the quarter ended September 30, 2001 from 31.7% for the same period last year. Gross profits decreased by \$1,643,000 to \$1,105,000 for the quarter ended September 30, 2001 from \$2,748,000 for the same period in 2000.

Selling, general and administrative ("SG&A") expenses decreased by \$448,000 or 26.2% for the quarter period ended September 30, 2001 compared to the same period of 2000. The decrease is primarily attributable to reducing personnel-related expenses and commissions paid to independent sales representatives resulting from lower net sales. These costs, as a percentage of net sales, increased to 33.9% for the three months ended September 30, 2001 as compared to 19.8% for the three months ended September 30, 2000, which was primarily attributable to the overall decrease in net sales.

Operating loss was \$158,000 for the quarter ended September 30, 2001 as compared to operating earnings of \$1,037,000 for the same period ended September 30, 2000. Operating earnings decreased primarily due to the decrease in net sales, as discussed above.

Interest expense, net of interest income for the quarter ended September 30, 2001 decreased by \$55,000 compared to the same period last year. The decrease is primarily due to lower effective average borrowing rates incurred during the current quarter at 5.6%, when compared to 8.0% for the same period

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last year.

Income tax benefit was \$63,000 during the quarter ended September 30, 2001, as compared to income tax expense of \$297,000 for the same period in 2000. The change is a direct result of the Company recording operating losses during the quarter ended September 30, 2001 as compared to operating earnings during the same period last year.

Net loss was \$307,000 for the quarter ended September 30, 2001 as compared with net earnings of \$523,000 for the same period last year, resulting from the reasons discussed above.

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Nine month Period Ended September 30, 2001 Compared To The Nine month Period Ended September 30, 2000.

Net sales for the nine months ended September 30, 2001 were \$13,402,000 compared with net sales for the nine months ended September 30, 2000 of \$25,837,000, a decrease of \$12,435,000 or 48.1%. The decrease is primarily due to an industry wide decrease in demand for discrete semiconductors. Passive component sales decreased by \$1,951,000 during the nine months ended September 30, 2001 and export sales decreased to \$1,493,000 from \$2,270,000, comparing the same periods. The average unit selling price increased to 2.2 cents for the current nine month period from 1.8 cents during the same period last year.

Cost of goods sold decreased by \$8,305,000 to \$9,394,000 for the nine months ended September 30, 2001, a decrease of 46.9% from the same period in 2000. Consistent with the decrease in net sales, cost of goods sold decreased, however at a slower rate, resulting in gross profits decreasing as a percentage of net sales to 29.9% for the first nine months of this year from 31.5% for the same period last year. Gross profits decreased by \$4,130,000 to \$4,008,000 for the nine months ended September 30, 2001 from \$8,138,000 for the same period in 2000.

SG&A expenses decreased by \$767,000 or 15.2% for the nine months ended September 30, 2001 compared to the same period in 2000. The decrease is primarily attributable to reducing personnel-related expenses and commissions paid to independent sales representatives resulting from lower net sales. SG&A expenses, as a percentage of net sales, increased to 31.9% for the nine months ended September 30, 2001 from 19.5% for the same period in 2000, due from the overall decrease in net sales.

Operating loss was \$272,000 for the nine months ended September 30, 2001 as compared to operating earnings of \$3,091,000 for the same period ended September 30, 2000. Operating earnings decreased primarily due to the decrease in net sales, as discussed above.

Interest expense, net of interest income for the nine months ended September 30, 2001 decreased by \$25,000 compared to the nine months ended Sept 30, 2000. The decrease is due to a decrease in borrowing levels as compared to the same period last year and lower effective average borrowing interest rates incurred during the nine month period of 6.2%, compared to 7.8% for the same period last year.

Income tax benefit was \$132,000 in the current nine month period ended September 30, 2001, as compared to income tax expense of \$981,000 for the same period in 2000. The change is a direct result of the Company recording operating losses during the nine months ended September 30, 2001 as compared to operating earnings during the same period last year.

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Net loss was \$745,000 for the nine months ended September 30, 2001 compared to net earnings of \$1,509,000 for the same period in 2000, a decrease of \$2,254,000 resulting from the same reasons discussed above.

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Supply and Demand Issues

The demand for discrete semiconductors in the U.S. market decreased from 1996 through the middle of 1999. Since then until late 2000, demand had increased as a result of industry wide shortages creating significant price increases. However, the industry wide shortage began to diminish towards the end of 2000 with economic conditions worsening resulting in weaker demand in 2001.

The Company's core strategy is to maintain a substantial inventory of discrete semiconductors purchased at prices generally lower than those commonly available to its competitors. This strategy allows the Company to fill customer orders immediately from stock held in inventory. During 2000, the Company took advantage of the strong demand in the discrete semiconductor market, as such, inventory levels increased throughout the year to \$30,609,000 at December 31, 2000. Since demand started to weaken towards the end of 2000 and continued to be weak through the end of September 30, 2001, the Company expects to continue lowering inventory balances throughout 2001. There are no assurances that demand in the discrete semiconductor market will increase and that market conditions will improve in 2001.

Readers are cautioned that the foregoing statements are forward looking and are necessarily speculative. There can be no guarantee that a recovery in the discrete semiconductor market will take place. Also, if prices of components held in our inventory decline or if new technology is developed that displaces products distributed by us and held in inventory, our business could be materially adversely affected. See "-Cautionary Statement Regarding Forward Looking Information".

Liquidity and Capital Resources

We have satisfied our liquidity requirements principally through cash generated from operations and short-term commercial loans. A summary of our cash flows resulting from our operating, investing and financing activities for the nine months ended September 30, 2001 and 2000 are as follows:

| (Dollars in thousands) | Nine months ended September 30, | |
|---------------------------|---------------------------------|-------------|
| | 2001 | 2000 |
| | (Unaudited) | (Unaudited) |
| Operating activities..... | \$ 1,790 | \$ 1,258 |
| Investing activities..... | (91) | (1,230) |
| Financing activities..... | (1,756) | (91) |

Cash flows provided by operating activities increased to \$1,790,000 during the nine months ended September 30, 2001, as compared to \$1,258,000 during the nine months ended September 30, 2000. The change is primarily due to the overall decline in business and net sales which caused a decrease in net income by \$2,254,000 to a net loss of \$745,000. Also contributing to the increase in operating cash flow was a decrease in accounts receivable and inventory of

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\$2,061,000 and \$1,676,000, respectively, during the first nine months of 2001, as compared to an increase of \$1,073,000 and \$1,181,000, respectively, during the same period last year. Conversely, the overall increase in operating cash flow was partially offset by a decrease in accounts payable and accrued and other liabilities of \$1,188,000 and \$713,000, respectively, during the first nine months of 2001, as compared to an increase of \$1,008,000 and \$785,000, respectively, during the same period last year.

Cash flows used in investing activities was \$91,000 during the nine months ended September 30, 2001 compared to \$1,230,000 during the nine months ended September 30, 2000. The decrease is primarily due to the completion of construction in December 2000 of interior improvements to our new 55,000 square foot warehouse and headquarters.

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Cash flows used in financing activities increased to \$1,756,000 from \$91,000 during the nine months ended September 30, 2001, as compared to the same period in 2000, primarily due to increased net re-payments to our bank revolving line of credit during the current period in 2001, as compared to the same period in 2000.

During the quarter ended September 30, 2001, the Company renewed its revolving line of credit facility which provides up to \$16 million for operating purposes and up to an additional \$4 million for business acquisition purposes, extending the maturity date to May 18, 2003. The agreement governing this credit facility contains covenants that require the Company to be in compliance with certain financial ratios. Borrowings on the line of credit are secured by substantially all of the Company's assets.

We believe that funds generated from operations and our bank revolving lines of credit should be sufficient to finance our working capital and capital expenditure requirements for the foreseeable future.

As of the date of this Report, we had no commitments for other equity or debt financing or other capital expenditures.

Cautionary Statement Regarding Forward Looking Information

Several of the matters discussed in this document contain forward looking statements that involve risks and uncertainties. Such forward looking statements are usually denoted by words or phrases such as "believes," "expects," "projects," "estimates," "anticipates," "will likely result," or similar expressions. We wish to caution readers that all forward looking statements are necessarily speculative and not to place undue reliance on such forward looking statements, which speak only as of the date made, and to advise readers that actual results could vary due to a variety of risks and uncertainties. Factors associated with the forward looking statements that could cause the forward looking statements to be inaccurate and could otherwise impact our future results are set forth in detail in our most recent annual report on Form 10-K. In addition to the other information contained in this document, readers should carefully consider the information contained in our Form 10-K for the year ended December 31, 2000 under the heading "Cautionary Statements and Risk Factors."

Year 2000

In 1999, we completed our remediation and testing of our systems. Because of those planning and implementation efforts, we experienced no significant disruptions in critical information technology and non-information technology systems and those systems have successfully responded to the Year 2000 date

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change. We did not incur any significant expenses during 1999 in connection with remediating our systems. We are not aware of any material problems resulting from Year 2000 issues, either with our products, internal systems, or the products and services of our third parties. We will continue to monitor our critical computer applications and those of our suppliers and vendors throughout the year 2001 to ensure any latent Year 2000 matters arising are addressed promptly.

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PART II. OTHER INFORMATION

Item 1. through Item 5.

Not applicable

Item 6. Exhibits and Reports on Form 8-K

(a) Exhibits:

10.18 Amendment to Business Loan Agreement and Master Revolving Note, dated May 18, 2001, between the Registrant and Comerica Bank - California.

(b) Reports on Form 8-K:

None

SIGNATURES

In accordance with the requirements of the Securities Exchange Act of 1934, the registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

TAITRON COMPONENTS INCORPORATED

Date: November 08, 2001

By: /s/ Stewart Wang

Stewart Wang
Chief Executive Officer
and Director

Date: November 08, 2001

By: /s/ Steven H. Dong

Steven H. Dong
Chief Financial Officer
(Principal Accounting Officer)

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