NITCHES INC
Form 10-Q
April 12, 2001

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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: FEBRUARY 28, 2001

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 [X] No [ ]

As of April 12, 2001, 1,064,680 shares of the Registrant's common stock were outstanding.

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INDEPENDENT ACCOUNTANT'S REPORT

Board of Directors and Shareholders
Nitches, Inc.

We have reviewed the accompanying condensed consolidated balance sheets of Nitches, Inc. and Subsidiaries as of February 28, 2001, and the related condensed consolidated statements of income for three and six months ended and cash flows for the six months ended February 28, 2001. These financial statements are the responsibility of management of Nitches, Inc.

We conducted our review in accordance with standards established by the American Institute of Certified Public Accountants. A review of interim financial information consists principally of applying analytical procedures to financial data and making inquiries of persons responsible for financial and accounting matters. It is substantially less in scope than an audit conducted in accordance with generally accepted auditing standards, the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, we do not express such an opinion.

Based on our review, we are not aware of any material modifications that should be made to the condensed consolidated financial statements referred to above for them to be in conformity with generally accepted accounting principles.

We have previously audited, in accordance with generally accepted auditing standards, the consolidated balance sheet of Nitches, Inc. and Subsidiaries as of August 31, 2000, and the related consolidated statements of income, shareholders' equity and cash flows for the year then ended not presented herein; and in our report dated October 13, 2000, we expressed an unqualified opinion on those consolidated financial statements. In our opinion, the information set forth in the accompanying condensed consolidated balance sheet as of August 31, 2000, is fairly presented, in all material respects, in relation to the consolidated balance sheet from which it has been derived.

Moss Adams, LLP

Los Angeles, California
April 5, 2001

PART I - FINANCIAL INFORMATION

Item 1. Financial Statements

NITCHES, INC. AND SUBSIDIARIES
Condensed Consolidated Balance Sheets

	February 28, 2001	August 31, 2000
	(Unaudited)	
ASSETS		

Current assets:		
Cash and cash equivalents	$ 174,000	$ 314,000
Receivables:		
Trade accounts, less allowances	3,848,000	4,224,000
Due from affiliates and employees	92,000	38,000
	3,940,000	4,262,000
Inventories, net	4,527,000	5,055,000
Deferred income taxes	150,000	150,000
Other current assets	46,000	76,000
Total current assets	8,837,000	9,857,000
Furniture, fixtures and equipment, net	95,000	109,000
Deferred income taxes	28,000	28,000
Other assets	19,000	17,000
	$ 8,979,000	$10,011,000

LIABILITIES AND SHAREHOLDERS' EQUITY

Current liabilities:		
Accounts payable	$ 1,952,000	$ 2,534,000
Accrued expenses	136,000	417,000
Income tax payable	93,000	98,000
Total current liabilities	2,181,000	3,049,000
Shareholders' equity:		
Common stock, no par value, 50,000,000 shares authorized; 1,064,680 shares issued and outstanding	805,000	805,000
Retained earnings	5,993,000	6,157,000
Total shareholders' equity	6,798,000	6,962,000
	$ 8,979,000	$10,011,000

The accompanying notes are an integral part of these financial statements

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

	Three months ended		
	February 28, 2001	February 29, 2000	February 2001

Net sales	$7,073,000	$9,664,000	$18,066
Cost of goods sold	5,132,000	7,365,000	13,254
Gross profit	1,941,000	2,299,000	4,812
Expenses:			
Selling, general and administrative	1,771,000	1,706,000	3,735
Income from operations	167,000	593,000	1,077
Interest and other income (expense), net	22,000	(20,000)	(31
Income before income taxes	189,000	573,000	1,046
Provision (benefit) for income taxes	70,000	225,000	408
Net income	$ 119,000	$ 348,000	$ 638
Earnings per share	$ .11	$ .33	$
Shares outstanding	1,064,680	1,064,680	1,064

The accompanying notes are an integral part of these financial statements

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

	Six months ended	
	February 28, 2001	February 29, 2000
Net cash provided (used) by operating activities	$(238,000)	$ 582,000
Cash flows from investing activities:		
Capital expenditures	(2,000)	(42,000)
Cash flows from financing activities:		
Advances from factor	898,000	300,000
Dividends paid	(798,000)	(798,000)
Net cash provided (used) by financing activities	100,000	(498,000)
Net increase (decrease) in cash and cash equivalents	(140,000)	42,000
Cash and cash equivalents at beginning of period	314,000	201,000

Cash and cash equivalents at end of period	$ 174,000	$ 243,000
	=========	=========
Supplemental disclosures of cash flow information:		
Cash paid during the period:		
Interest	$ 108,000	$ 64,000
Income taxes	$ 300,000	$ 32,000

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 primarily of women's clothing manufactured to its specifications and distributed in the United States under Company brand labels and private retailer labels.

2. CONDENSED FINANCIAL STATEMENTS:

The accompanying unaudited consolidated financial statements have been prepared in accordance with the instructions to Form 10-Q. These have been reviewed by the Company's independent auditors in accordance with the professional standards and procedures as set forth in Statement of Auditing Standards No. 71 (SAS 71). SAS 71 procedures for conducting a review of interim financial information generally are limited to inquiries and analytical procedures concerning significant accounting matters relating to the financial information to be reported. 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. 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, 2000. In the opinion of Management, all adjustments considered necessary for a fair representation have been included in the interim period. Operating results for the six months ended February 28, 2001 are not necessarily indicative of the results that may be expected for the year ending August 31, 2001.

3. EARNINGS PER SHARE:

At February 28, 2001, there were no stock options or similar instruments outstanding and therefore no dilutive effect to the weighted average number of shares outstanding.

4. INVENTORIES:

	February 28, 2001	August 31, 2000
Fabric and Trims	$ 148,000	$ 126,000

Finished Goods	4,379,000	4,929,000
	$4,527,000	$5,055,000

5. TRADE ACCOUNTS:

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 Company may request advances in anticipation of customer collections and open letters of credit through the factor, all of which are collateralized by all of the Company's assets. Outstanding advances are charged interest at the factor's prime rate less one half percent. Advances and contingent liabilities for irrevocable letters of credit outstanding are as follows:

NITCHES, INC. AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statement (continued)

5. TRADE ACCOUNTS (CONTINUED):

	February 28, 2001	August 31, 2000
Receivables assigned to factor:		
Non-recourse	$ 5,676,000	$ 4,986,000
Recourse	278,000	239,000
Advances from factor	(1,894,000)	(996,000)
Due from factor	4,060,000	4,229,000
Non-factored accounts receivable	173,000	220,000
Allowance for customer credits and doubtful accounts	(385,000)	(225,000)
	$ 3,848,000	$ 4,224,000
Contingent liabilities for irrevocable letters of credit	$ 3,139,000	$ 4,510,000

The factoring agreement allows the Company to borrow up to $15,000,000, limited by certain percentages of outstanding accounts receivable and finished goods inventory owned by the Company. The Company's President has provided a $1,000,000 personal guarantee in connection with the factoring arrangement.

6. SPECIAL DIVIDENDS AND RELATED PARTY TRANSACTIONS:

The Company paid a special dividend of $.25 (twenty-five cents) per share on November 30, 2000, for a total of approximately $266,000, to the shareholders of record as of November 6, 2000. Furthermore, on February 23, 2001, the Company paid a special dividend of $.50 (fifty cents) per share, for a total of approximately $532,000, to the shareholders of record as of February 6,

2001. During fiscal 2000, the Company declared and paid special dividends of $1.65 per share.

The Company purchases labor and administrative services as needed, at fair market rates, from Kuma Sport, Inc., a company that was 40% owned by a director of Nitches until December 2000. At that time, the director transferred his ownership in Kuma Sport to an unrelated party. The Company purchased labor and administrative services from Kuma Sport for $305,000 through December 2000.

7. SIGNIFICANT CUSTOMERS:

Sales to three separate customers (Mervyn's, Sears, and Kohl's) accounted for 30.6%, 24.7%, and 14.5% respectively, of the Company's net sales in the three months ended February 28, 2001. Three customers accounted for 27.5%, 20.9%, and 15.0% of the Company's net sales in the three months ended February 29, 2000.

These same customers accounted for 28.5%, 30.3%, and 11.7%, respectively, of the Company's trade receivable balance at February 28, 2001. Three customers accounted for 35.6%, 23.6%, and 15.2% of the Company's trade receivable balance at February 29, 2000.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

RESULTS OF OPERATIONS

SIX MONTHS ENDED FEBRUARY 28, 2001 COMPARED TO THE SIX MONTHS ENDED FEBRUARY 29, 2000

Net sales for the six months ended February 28, 2001 decreased approximately $3.1 million (14.7%) as compared to the six months ended February 29, 2000. This decline was primarily attributable to a decrease in unit sales in the Company's sleepwear product line, including the lack of orders from a major customer which accounted for sales of $1.5 million in fiscal 2000 (see BACKLOG from 10-Q for period ended May 31, 2000) and the delay of shipments into the third quarter by customers due to the slowing of retail sales.

Gross margin increased from 24.4% for the six months ended February 29, 2000 to 26.6% for the current six-month period. The increase was the result of the Company's product mix shifting to higher gross margin western wear product during the current quarter. The Company's product mix constantly changes to reflect customer mix, fashion trends and changing seasons. Consequently, gross margins are likely to vary on a quarter-to-quarter basis and in comparison to gross margins generated in the same period of prior fiscal years.

Selling, general and administrative expenses for the first six months of fiscal 2001 were equal to the $3.6 million from last year, and increased as a percent of net sales from 17.1% last year to 20.7% for the current period. The primary reason for the increase as a percentage of sales was due to the decrease in net sales from the earlier period. However, in the second quarter of fiscal 2001 the Company incurred reorganization expenses of approximately $150,000 related primarily to the closing of an overseas buying office in favor of an agency relationship.

THREE MONTHS ENDED FEBRUARY 28, 2001 COMPARED TO THE THREE MONTHS ENDED FEBRUARY 29, 2000

Net sales for the three months ended February 28, 2001 decreased approximately $2.6 million (26.8%) as compared to the three months ended February 29, 2000. This decline was primarily attributable to a decrease in unit sales in the Company's sleepwear product line, including the lack of orders from a major customer which accounted for sales of $1.5 million in fiscal 2000 (see BACKLOG, 10-Q for period ended May 31,2000) and the delay of shipments into the third quarter by customers due to the slowing of retail sales.

Gross margin increased from 23.8% for the three months ended February 29, 2000 to 27.4% for the current three-month period. The increase was the result of the Company's product mix shifting to higher gross margin western wear product during this period. The Company's product mix constantly changes to reflect customer mix, fashion trends and changing seasons. Consequently, gross margin is likely to vary on a quarter-to-quarter basis and in comparison to gross margins generated in the same period of prior fiscal years.

Selling, general and administrative expenses for the second quarter of fiscal 2001 were slightly higher at $1.8 million as compared to $1.7 million a year ago, and increased as a percent of net sales from 17.7% last year to 25.1% for the current period. The primary reason for the increase as a percentage of sales was due to the decrease in net sales from the earlier period. However, in the second quarter of fiscal 2001 the Company incurred reorganization expenses of approximately $150,000 related primarily to the closing of an overseas buying office in favor of an agency relationship.

LIQUIDITY AND CAPITAL RESOURCES

Working capital declined slightly to $6.7 million at February 28, 2001 as compared to $6.8 at August 31, 2000, and the current ratio increased to 4.05:1 at February 28, 2001 from 3.23:1 at August 31, 2000.

The Company paid a special dividend of $.25 (twenty-five cents) per share on November 30, 2000, for a total of approximately $266,000, to the shareholders of record as of November 6, 2000. Furthermore, on February 23, 2001, the Company paid a special dividend of $.50 (fifty cents) per share, for a total of approximately $532,000, to the shareholders of record as of February 6, 2001.

The Company sells substantially all of its trade receivables to a factor (CIT) on a pre-approved, non-recourse basis. The Company attempts to make any recourse shipments on a COD basis or ensure that the customer's payments are backed by a commercial or standby letter of credit issued by the customers' bank. The amount of the Company's receivables which were recourse and were not made on a COD basis or supported by commercial or standby letters of credit at February 28,2001 was approximately $451,000 of which approximately $142,000 had been collected through March 31, 2001.

Payment for non-recourse factored receivables is made at the time customers make payment to CIT or, if a customer is financially unable to make payment, within approximately 180 days of the invoice due date. Under the Discount Factoring Agreement, the Company can request advances in anticipation of customer collections at CIT's prime rate (currently 9.0%) less one-half percent, and open letters of credit through CIT. The amount of borrowings by the Company, including a portion of outstanding letters of credit, are limited to certain percentages of outstanding accounts receivable and finished goods inventory owned by the Company. Borrowings are collateralized by all of the assets of the Company as well as a $1 million guaranty of the Company's president, Mr. Wyandt. At February 28, 2001, the Company had outstanding letters of credit of approximately $3.1 million for the purchase of finished goods, which had been opened through CIT. Under the Discount Factoring Agreement, the Company is required to maintain $5 million of net worth and $5 million of working capital. The Discount Factoring Agreement can be terminated by CIT on 60-days written notice.

INVENTORY

In its ordinary course of operations, the Company generally makes some sales below its normal selling prices or below cost. Based on prior experience, management believes this will be true for some inventory held or acquired after February 28, 2001. The amount of such sales depends on several factors, including general economic conditions, market conditions within the apparel industry, the desirability of the styles held in inventory and competitive pressures from other garment suppliers.

The Company's inventory decreased from $5.1 million at August 31, 2000 to $4.5 million at February 28, 2001. The Company has established an inventory markdown reserve as of February 28, 2001, which management believes will be sufficient for current inventory that is expected to be sold below cost in the future. There can be no assurance that the Company will realize its expected selling prices, or that the inventory markdown reserve will be adequate, for items in inventory as of February 28, 2001 for which customer sales orders have not yet been received. The inventory markdown reserve is calculated based on specific identification of aged goods and styles that are slow-moving or selling off-price.

BACKLOG

The Company had unfilled customer orders of $13.6 million at February 28, 2001 compared to $14.0 million at February 29, 2000, with such orders generally scheduled for delivery by August 2001 and August 2000, respectively. The decrease in the backlog of $0.4 million is primarily the result of a decrease in new private label sleepwear sales for the third quarter, offset by the shifting of some orders from the second quarter due to the slowing of retail sales. These amounts include both confirmed orders and unconfirmed orders that the Company believes, based on industry practice and past experience, will be confirmed. While cancellations, rejections and returns have generally not been material in the past, there can be no assurance that cancellations, rejections and returns will not reduce the amount of sales realized from the backlog of orders at February 28, 2001.

IMPACT OF EXCHANGE RATES

While the Company purchases over 90% of its products from foreign manufacturers, all of its purchases are denominated in United States dollars. Because the Company's products are sold primarily in the United States, in dollar denominated transactions, the Company does not engage in hedging or other arbitrage to reduce currency risk. An increase in the value of the dollar versus foreign currencies could enhance the Company's purchasing power for new purchase orders and reduce its cost of goods sold. Conversely, a decrease in the value of the dollar relative to foreign currencies could result in an increase in the Company's cost of manufacturing for new purchase orders and costs of goods sold.

IMPACT OF INFLATION AND DEFLATION

Management does not believe that inflation has had any material impact upon the Company's revenues or income from operations to date. However, continued deflation in women's clothing prices may put pressure on gross margins for the balance of fiscal 2001. The strong resistance on the part of the consumer to increases in price and increasing fabric and labor costs lead to an increased cost of goods on a percentage basis.

CAUTIONARY STATEMENT UNDER THE PRIVATE SECURITIES LITIGATION REFORM ACT OF 1995

Statements in the annual report on Form 10K under the caption "Management's Discussion and Analysis of Financial Condition and Results of Operations", as well as oral statements that may be made by the Company or by officers, directors or employees of the Company acting on the Company's behalf, that are not historical fact constitute "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 of 1934, as amended. Forward-looking statements involve known and unknown risks and uncertainties that may cause the Company's actual results in future periods to differ materially from forecasted results. Those risks include a softening of retailer or consumer acceptance of the Company's products, pricing pressures and other competitive forces, or unanticipated loss of a major customer. In addition, the Company's business, operations and financial condition are subject to reports and statements filed from time to time with the Securities and Exchange Commission.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

There were no material legal proceedings to which the Company or any of its subsidiaries was a party in the six months ended February 28, 2001.

Item 4. Submission of Matters to a Vote of Security Holders

An annual meeting of shareholders of the Company was held on December 5, 2000. At the meeting, the shareholders approved the following:

(1) the appointment of Moss Adams LLP as the Company's independent certified public accountants for the fiscal year ending August 31, 2001 by votes of 980,665 for, 500 against, and 102 abstentions, and

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(2) the election of directors as follows:

Name	Votes For	Withheld
Arjun C. Waney	980,567	700
Steven P. Wyandt	980,767	500
Luther A. Henderson	980,167	1,100
Eugene B. Price II	980,767	500
William L. Hoese	980,767	500

Item 6. Exhibits and Reports on Form 8-K

There were no reports on Form 8-K during the quarter ended February 28, 2001.

SIGNATURES

Pursuant to the requirement of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned there unto duly authorized.

NITCHES, INC.

Registrant

April 12, 2001

By:
/s/ Steven P. Wyandt

Steven P. Wyandt
As Principal Financial Officer and
on behalf of the Registrant