PACIFICHEALTH LABORATORIES INC
Form 10QSB
August 14, 2003

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-QSB

(Mark One)
[X] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended June 30, 2003

-OR-

[_] TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from ____________ to _____________

Commission File No. 333-36379

PACIFICHEALTH LABORATORIES, INC.
(Exact name of issuer as specified in its charter)

DELAWARE	22-3367588
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)
100 Matawan Road, Suite 420 Matawan, NJ	07747
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code: (732) 739-2900

Check whether the issuer (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 [_]

At August 14, 2003, there were 6,115,703 shares of common stock, par value $.0025 per share, of the registrant outstanding.

Transitional small business disclosure format: Yes [ ] No [X]

PACIFICHEALTH LABORATORIES, INC.

TABLE OF CONTENTS

PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

Balance Sheets as of June 30, 2003 (Unaudited) and December 31, 2002...................

Statements of Operations (Unaudited) for the three and six months ended
June 30, 2003 and June 30, 2002...

Statements of Cash Flows (Unaudited) for the six months ended
June 30, 2003 and June 30, 2002...

Notes to Financial Statements...

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

ITEM 3. CONTROLS AND PROCEDURES...

PART II. OTHER INFORMATION

ITEM 1. Legal Proceedings...

ITEM 2. Changes in Securities and Use of Proceeds.................................

ITEM 3. Defaults Upon Senior Securities...

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

ITEM 5. Other Information...

ITEM 6. Exhibits and Reports..

SIGNATURES..

PACIFICHEALTH LABORATORIES, INC.
BALANCE SHEETS

ASSETS

	June 30, 2003 (Unaudited)	December 31, 2002 (Audited)
Current assets:		
Cash and cash equivalents	$ 210,616	$ 628,436
Accounts receivable, net	768,968	335,219
Inventories	1,209,272	1,537,784
Prepaid expenses	271,196	142,865
Total current assets	2,460,052	2,644,304
Property and equipment, net	59,156	66,835
Other assets:		
Deposits	17,378	3,991
Total assets	$2,536,586	$2,715,130

LIABILITIES AND STOCKHOLDERS' EQUITY

	June 30, 2003 (Unaudited)	December 31, 2002 (Audited)
Current liabilities:		
Notes payable	$ 259,287	$ 64,212
Accounts payable and accrued expenses	693,496	280,384
Other	31,734	100,000
Total current liabilities	984,517	444,596
Stockholders' equity:		
Common stock, $.0025 par value; authorized 50,000,000 shares; issued and outstanding: 6,115,703 shares at June 30, 2003 and 6,114,703 shares at December 31, 2002	15,289	15,287
Additional paid-in capital	13,848,583	13,839,973
Accumulated deficit	(12,311,803)	(11,584,726)
	1,552,069	2,270,534
Total liabilities and stockholders' equity	$2,536,586	$2,715,130

3

PACIFICHEALTH LABORATORIES, INC.
STATEMENTS OF OPERATIONS
FOR THE THREE MONTHS AND SIX MONTHS ENDED JUNE 30,2003 AND 2002
(UNAUDITED)

	Three Months Ended June 30,		Six Ended
	2003	2002	2003
Revenues			
Net product sales	$1,520,552	$1,818,096	$2,918,33
Cost of goods sold	737,272	807,185	1,456,99
Gross Profit	783,280	1,010,911	1,461,33
Selling, general and administrative expenses	1,029,219	1,024,723	2,026,92
Research & development	43,248	24,523	130,53
Depreciation expense	13,356	9,359	27,47
	1,085,823	1,058,605	2,184,93
Net operating income (loss)	(302,543)	(47,694)	(723,59
Other income (expense):			
Interest income	522	4,086	1,46
Interest expense	(8,952)	(918)	(9,94
Other	5,000	-	5,00
	(3,430	3,168	(3,48
Income (loss) before income taxes	(305,973)	(44,526)	(727,07
Provision for income taxes	-	-	
Net income (loss)	$ (305,973)	$ (44,526)	$ (727,07
Basic income (loss) per share	$ (0.05)	$ (0.01)	$ (0.1
Diluted income (loss) per share	$ (0.05)	$ (0.01)	$ (0.1
Weighted average common shares:			
Basic	6,115,703	6,061,302	6,115,43
Diluted	6,448,220	7,313,680	6,684,59

PACIFICHEALTH LABORATORIES, INC.
STATEMENTS OF CASH FLOWS
FOR THE SIX MONTHS ENDED JUNE 30, 2003 AND 2002
(UNAUDITED)

	2003	2002
Cash flows from operating activities:		
Net income (loss)	$ (727,076)	$ (295,850)
Adjustments to reconcile net income (loss) to net cash used in operating activities:		
Depreciation	27,473	18,574
Intrinsic value of stock options granted	7,552	15,950
Changes in assets and liabilities:		
Decrease (Increase) in accounts receivable	(433,749)	(605,489)
Decrease (Increase) in inventories	328,512	(223,737)
Decrease (Increase) in prepaid expenses	(128,331)	(105,701)
Decrease (Increase) in deposits	(13,387)	--
Increase (Decrease) in accounts payable/accrued expenses	413,112	345,524
Increase (Decrease) in other current liabilities	(68,266)	--
Net cash used in operating activities	(594,160)	(850,729)
Cash flows from investing activity:		
Purchase of fixed assets	(19,794)	(14,946)
Net cash used in investing activities	(19,794)	(14,946)
Cash flows from financing activities:		
Issuance of notes payable	254,491	52,700
Repayments of notes payable	(59,417)	(41,113)
Common stock options/warrants exercised	1,060	126,750
Net cash provided by financing activities	196,134	138,337
Net increase (decrease) in cash	(417,820)	(727,338)
Cash, beginning balance	628,436	1,848,847
Cash, ending balance	$ 210,616	$1,121,509

PACIFICHEALTH LABORATORIES, INC.
NOTES TO FINANCIAL STATEMENTS
FOR THE THREE AND SIX MONTHS ENDED JUNE 30, 2003 AND 2002
(UNAUDITED)

1. Basis of Presentation:

The accompanying unaudited financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and with the instructions for Form 10-QSB and Item 310 of Regulation S-B. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for the three and six months ended June 30, 2003 are not necessarily indicative of the results that may be expected for the year ending December 31, 2003. The unaudited financial statements should be read in conjunction with the financial statements and footnotes thereto included in the Company's annual report on Form 10-KSB for the year ended December 31, 2002.

2. Inventories

As of June 30, 2003 and December 31, 2002, inventories consist of the following:

	06/30/03	12/31/02
Raw Materials	$ 9,431	$ 3,228
Packaging supplies	41,016	39,341
Work in Process	48,605	-
Finished goods	1,110,220	1,495,215
	$1,209,272	$1,537,784

3. Stock Based Compensation

The Company granted 21,000 Incentive Stock Options (ISOs) to employees during the first six months of 2003 with exercise prices ranging from $0.80 per share to $1.92 per share. 11,000 of these options vest during the first quarter of 2004 and 10,000 of these options vest during the first quarter of 2005. The exercise price for all 21,000 options was equal to the fair market value of the common stock on the date of grant. Since the Company accounts for its options under APB No. 25, no compensation expense was recognized.

The Company also granted 4,500 stock options to consultants during the first six months of 2003. All 4,500 options vested upon grant with exercise prices ranging from $0.89 per share to $2.15 per share. These options were determined to have a value of $4,873 for the six months ended June 30, 2003 and this amount was charged to operations and added to paid-in capital in accordance with SFAS 123. In addition, 45,000 options issued to consultants expired during the first six months of 2003.

The following table illustrates the effect on net (loss) income and earnings per share if the fair value based method had been applied to all awards:

Six Months Ended June 30,	2003	2002
Reported net (loss) income	$ (727,076)	$ (295,850)
Stock-based employee compensation expense included in reported net loss, net of related tax effects	-0-	-0-
Stock-based employee compensation determined under the fair value based method, net of related tax effects	(130,271)	(82,757)
Pro forma net (loss) income	$ (857,347)	$ (378,607)
Basic and diluted (loss) per share:		
As reported	($0.12)	($0.05)
Pro forma	($0.14)	($0.06)

4. Income Taxes

The Company has approximately $11,588,000 in Federal net operating loss carryovers that were generated through June 30, 2003 and are available to offset future taxable income in calendar years 2003 through 2023.

The components of the Company's deferred tax assets as of June 30, 2003 and December 31, 2002 are as follows:

	2003	2002
Net operating loss carry forwards	$ 4,270,000	$ 4,066,000
Deferred charges	45,000	45,000
Valuation allowance	(4,315,000)	(4,111,000)
Deferred tax asset	$ -	$ -

5. Notes Payable

Included in notes payable, the Company, during the second quarter of 2003, secured a $750,000 asset-based credit facility from USA Funding of Dallas, TX. The amount of available credit is based on the value of the Company's eligible receivables from time to time. This credit facility bears interest at a rate of prime plus 2% as well as a 0.75% discount rate on all advances.

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

This quarterly report on Form 10-QSB contains statements relating to future results of the Company (including certain projections and business trends) that are "forward-looking statements" as defined in the Private Securities Litigation Reform Act of 1995. These statements can be identified by introductory words such as "expects", "plans", "intends", "believes", "will", "estimates", "forecasts", "projects" or words of similar meaning, and by the fact that they do not relate strictly to historical or current facts. Actual outcomes and results may differ materially from what is expressed or implied in our forward-looking statements. Among the factors that affect future results are changes in political and economic conditions; demand for and market acceptance of new and existing products, as well as other risks and uncertainties detailed from time to time in the filings of the Company with the Securities and Exchange Commission.

(a) Introduction

The Company was incorporated in April 1995 as a nutrition technology company that researches, develops, and commercializes functionally unique proprietary products for sports performance, weight loss and Type 2 diabetes.

Sports Performance

Our first sports performance product, ENDUROX(R), was introduced in March 1996 with commercial sales beginning in May 1996. In March 1997, we extended the ENDUROX line of products with ENDUROX EXCEL(R). In February 1999, we introduced ENDUROX(R) R4(R) Performance/Recovery Drink to be taken following exercise. In clinical studies performed or funded by the Company, ENDUROX R4 has demonstrated a number of exercise-related benefits including enhanced performance, extended endurance, and decreased post-exercise muscle damage. In June 2001, we introduced ACCELERADE(R) Sports Drink, to be taken during exercise using the same patented technology as ENDUROX R4. Research studies funded by the Company have shown that ACCELERADE is significantly better than conventional sports drinks in improving endurance during exercise. In the first two quarters of 2003, we commenced test marketing of our ready-to-drink form of ACCELERADE in the San Diego and Colorado Springs areas. The test market is expected to continue through the 3rd quarter of 2003 in Colorado Springs.

Weight Loss

In weight loss, the Company has focused its research and development efforts on development of novel nutritional compositions that stimulate the body's major satiety peptide, or cholecystokinin (CCK). In April 2000, we introduced our first weight loss product, SATIETROL(R), a natural appetite control product based on this research. Clinical studies performed or funded by the Company have shown that Satietrol, a pre meal beverage, can reduce hunger up to 43% 3 1/2 hours after eating. In January 2001, we extended our weight loss product line with the introduction of SATIETROL COMPLETE(R), a 220-calorie meal replacement product that incorporates the patented SATIETROL technology. In June 2001, the Company signed an exclusive worldwide Licensing Agreement with GlaxoSmithKline ("GSK") for its SATIETROL technology. Under the Agreement, the Company received an initial payment of $1,000,000 and received a subsequent milestone payment of $250,000. GSK subsequently canceled the Licensing Agreement in September 2002 with all rights reverting to the Company. In the third quarter of 2002, the Company funded clinical studies that confirmed an improvement in the efficacy of SATIETROL. The Company is conducting further studies on SATIETROL in 2003.

Type 2 Diabetes

Type 2 diabetes has become the fastest growing chronic condition in the United States. Obesity and poor glucose regulation appear to be primary characteristics of this condition. Research has suggested that cholecystokinin (CCK) may play a role in insulin release and glucose regulation. The Company's research in this area is to develop a nutritional product that can help Type 2 diabetics lose weight by controlling appetite while improving glucose regulation. The Company expects to initiate clinical trials on a product for use by Type 2 diabetics in the future.

(b) Results of Operations - Six Months Ended June 30, 2003 vs. June 30, 2002

We recorded a net loss of ($305,973), or ($0.05) per share, for the second quarter ended June 30, 2003 compared to a net loss of ($44,526), or ($0.01) per share, for the second quarter ended June 30, 2002. We recorded a net loss of ($727,076), or ($0.12) per share, for the six-month period ended June 30, 2003, compared to a net loss of ($295,850), or ($0.05) per share, for the six-month period ended June 30, 2002. The increase in the net loss for the three-month period ended June 30, 2003 vs. the same period in 2002 is due primarily to a decrease in revenues. The increase in the net loss for the six-month period ended June 30, 2003 vs. the same periods in 2002 is due primarily to increases in marketing expenses and research and development expenses as detailed below.

Revenues in the quarter ended June 30, 2003 were $1,520,552 compared to $1,818,096 for the same period in 2002. Revenues in the six-month period ended June 30, 2003 were $2,918,331 compared to revenues of $2,975,026 for the same period in 2002. We believe revenues decreased in the second quarter of 2003 due to the seasonally poor weather experienced across the United States during this period. The users of our sports drinks tend to be serious outdoor athletes such as bicyclists, runners, and triathletes. Inclement weather forces such athletes to workout less, thereby lessening the demand for our sports drinks. For the six-month period ending June 30, 2003, sales of our ACCELERADE Sports Drink increased 22% over the same period in 2002.

Gross profit was $783,280 for the three months ended June 30, 2003 compared to $1,010,911 for the three months ended June 30, 2002. Gross profit was $1,461,338 for the six months ended June 30, 2003 compared to $1,604,102 for the six months ended June 30, 2002. Gross profit margin on product sales was 51.5% for the three months ended June 30, 2003, compared to 55.6% for the three months ended June 30, 2002. Our gross profit margin on product sales was 50.1% for the six-month period ended June 30, 2003 versus 53.9% for the six-month period ended June 30, 2002. The reasons for the decrease in gross profit margins are increases in warehouse costs as we bring on additional warehouses, increases in freight costs, and slotting fees paid in the first quarter of 2003 in the form of product for getting our ACCELERADE product sold in 990 Rite-Aid drug stores that feature a special nutrition section.

Our selling, general, and administrative ("S, G, & A") expenses were $1,029,219 for the three-month period ended June 30, 2003 compared to $1,024,723 for the three-month period ended June 30, 2002. Our S, G, & A expenses increased to $2,026,922 for the six-month period ended June 30, 2003 from $1,842,317 for the six-month period ended June 30, 2002. The primary reason for the increase in S, G, & A expenses in the six-month period ended June 30, 2003, compared to the same period in 2002 was an increase in salaries and employee benefits as we expanded our marketing and sales team.

Research and development ("R & D") expenses were $43,248 for the three months ended June 30, 2003 versus $24,523 for the three months ended June 30, 2002. R & D expenses were $130,539 for the six months ended June 30, 2003 versus $47,360 for the six months ended June 30, 2002. R & D expenses increased during the second quarter of 2003 compared to the same period in 2002 due to a study we conducted to further enhance our SATIETROL weight loss technology. In addition, R & D expenses increased in the six-month period ended June 30, 2003 compared to the same period in 2002 due to R & D expenses associated with the test market of the ready-to-drink form of our ACCELERADE product in the first quarter of 2003. We anticipate R & D expenses will increase as additional clinical trials and studies are conducted on all of our products as we continue to seek out additional patents and claims for our products.

(c) Liquidity and Capital Resources

At June 30, 2003, the Company's current assets exceeded its current liabilities by approximately $1.475 million with a ratio of current assets to current liabilities of approximately 2.5 to 1. At June 30, 2003, cash on hand was $210,616, a decrease of $417,820 from December 31, 2002, primarily because of our net loss for the first six months of 2003 as well as an increase of $433,749 in accounts receivable from December 31, 2002 that was offset by an increase in notes payable of $195,075 and an increase in accounts payable/accrued expenses of $413,112. Inventory levels decreased by $328,512 at June 30, 2003 as compared to December 31, 2002, as we more efficiently turned our inventory in 2003.

During the second quarter of 2003, the Company secured a $750,000 asset-based credit facility from USA Funding of Dallas, TX. The amount of available credit is based on the value of the Company's eligible receivables from time to time. This credit facility bears interest at a rate of prime plus 2% as well as a 0.75% discount rate on all advances. At June 30, 2003, we had approximately $400,000 of availability under this credit facility and as of August 14, 2003, we had approximately $325,000 of availability under this credit facility.

The Company anticipates significantly reducing its advertising and marketing expenditures in the second half of 2003 since the Company's primary advertising season is generally in the second quarter of its fiscal year. The Company also has the ability to borrow against its credit facility as described above and is currently in negotiations to raise additional equity capital. Should the Company not be successful in raising additional equity capital, we may have to significantly alter our operations.

ITEM 3. CONTROLS AND PROCEDURES

Evaluation of disclosure controls and procedures. Based on their evaluation of the Company's disclosure controls and procedures (as defined in Rules 13a-14(c) and 15d-14(c) promulgated under the Securities Exchange Act of 1934, as amended (the "Exchange Act")) as of June 30, 2003, the Company's chief executive officer and chief financial officer have concluded that the Company's disclosure controls and procedures are designed to ensure that information required to be disclosed by the Company in the reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms.

Changes in internal controls. There were no significant changes in the

Company's internal controls or in other factors that could significantly affect these controls subsequent to the date of their most recent evaluation.

II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

None.

ITEM 2. CHANGES IN SECURITIES

(a), (b) Changes in Securities:

None.

(c) Recent Sales of Unregistered Securities:

None.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

(a) On June 11, 2003, the Company held its Annual Meeting of Stockholders, pursuant to information contained in the Company's Notice of Annual Meeting of Stockholders and Proxy Statement that were mailed to stockholders on May 19, 2003.

(b) One of the matters listed in the Company's Proxy for the meeting was the annual Election of Directors. There were six nominees for election who were elected by the shareholders to serve for a one-year term. The results of the balloting were as follows (Shares voting: 5,294,658 of 6,115,703):

Nominee	For	Against	Abstain
Robert Portman	5,270,488	-0-	24,170
Stephen P. Kuchen	5,271,888	-0-	22,770
David Portman	5,270,888	-0-	23,770
T. Colin Campbell	5,271,788	-0-	22,870
Michael Cahr	5,273,388	-0-	21,270
Joseph Harris	5,273,288	-0-	21,370

(c) Another matter voted upon by the stockholders was the ratification of the appointment of Eisner, LLP as independent auditors for the Company for the fiscal year ending December 31, 2003. This matter was approved. The results of the balloting for this matter was as follows:

Matter	For	Against	Abstain
Appointment of auditors	5,265,680	19,678	9,300

(d) The final matter voted upon by the stockholders was the ratification of a proposal to authorize the Board of Directors to issue up to 2,000,000 shares of common stock for less than market value in excess of amounts permitted by NASDAQ rule 435(I)(1)(D) without stockholder approval. This matter was approved. The results of the balloting for this matter was as follows:

Matter	For	Against
Authorization to sell excess common stock	2,724,839	104,326

Broker Non-Votes: 2,456,493

ITEM 5. OTHER INFORMATION

None.

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

(a) Exhibits:

31.1 Section 302 Certification of Robert Portman, Chief Executive Officer.

31.2 Section 302 Certification of Stephen P. Kuchen, Chief Financial Officer

32 Certification of Chief Executive Officer and Chief Financial Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

(b) Reports on Form 8-K:

None.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

PACIFICHEALTH LABORATORIES, INC.

By: /S/ STEPHEN P. KUCHEN

STEPHEN P. KUCHEN
Vice President (Principal Financial Officer
and Principal Accounting Officer)

12