BODISEN BIOTECH, INC Files SEC form 10QSB, Quarterly Report

Form 10QSB for BODISEN BIOTECH, INC

3-Nov-2004

Quarterly Report

MANAGEMENT'S DISCUSSION AND ANALYSIS

The following discussion should be read in conjunction with the unaudited condensed consolidated financial statements and notes thereto set forth in Item 1of this Quarterly Report. In addition to historical information, this discussion and analysis contains forward-looking statements that involve risks, uncertainties and assumptions, which could cause actual results to differ materially from Management's expectations. Factors that could cause differences include, but are not limited to, expected market demand for the Company's services, fluctuations in pricing for products distributed by the Company and services offered by competitors, as well as general conditions of the agricultural products marketplace.

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

Some of the information in this Form 10-QSB contains forward-looking statements that involve substantial risks and uncertainties. You can identify these statements by forward-looking words such as "may," "will," "expect," "anticipate," "believe," "estimate" and "continue," or similar words. You should read statements that contain these words carefully because they:

o discuss our future expectations;
o contain projections of our future results of operations or of our financial condition; and
o state other "forward-looking" information.

We believe it is important to communicate our expectations. However, there may be events in the future that we are not able to accurately predict or over which we have no control. Our actual results and the timing of certain events could differ materially from those anticipated in these forward-looking statements as a result of certain factors, including those set forth in our filings with the Securities and Exchange Commission.

Overview

We are incorporated under the laws of the state of Delaware and are headquartered in the Shaanxi Province, People's Republic of China. We engage in the business of manufacturing and marketing a brand of organic fertilizer in China. We produce numerous proprietary product lines, from pesticides to crop specific fertilizer. These products are then marketed and sold to farmers throughout the 20 provinces of China. We conduct research and development to further improve existing products and develop new formulas and products.

Significant Accounting Policies

Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires us 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.

Accounts Receivable

We maintain reserves for potential credit losses on accounts receivable. We review the composition of accounts receivable and analyze historical bad debts, customer concentrations, customer credit worthiness, current economic trends and changes in customer payment patterns to evaluate the adequacy of these reserves. Reserves are recorded primarily on a specific identification basis.

Inventories

Inventories are valued at the lower of cost (determined on a weighted average basis) or market. We compare the cost of inventories with the market value and allowance is made for writing down the inventories to their market value, if lower.

Property & Equipment

Property and equipment are stated at cost. Expenditures for maintenance and repairs are charged to earnings as incurred; additions, renewals and betterments are capitalized. When property and equipment are retired or otherwise disposed of, the related cost and accumulated depreciation are removed from the respective accounts, and any gain or loss is included in operations. Depreciation of property and equipment is provided using the straight-line method for substantially all assets with estimated lives of: 30 years for building, 10 years for machinery, 5 years for office equipment and 8 years for vehicles.

Intangible Assets

Intangible assets consist of rights to use land and proprietary technology rights to fertilizers. We evaluate intangible assets for impairment, at least on an annual basis and whenever events or changes in circumstances indicate that the carrying value may not be recoverable from its estimated future cash flows. Recoverability of intangible assets, other long-lived assets and, goodwill is measured by comparing their net book value to the related projected undiscounted cash flows from these assets, considering a number of factors including past operating results, budgets, economic projections, market trends and product development cycles. If the net book value of the asset exceeds the related undiscounted cash flows, the asset is considered impaired, and a second test is performed to measure the amount of impairment loss. Potential impairment of goodwill after July 1, 2002 is being evaluated in accordance with SFAS No. 142. The SFAS No. 142 is applicable to the financial statements of the Company beginning July 1, 2002.

Revenue Recognition

Our revenue recognition policies are in compliance with Staff accounting bulletin (SAB) 101. Sales revenue is recognized at the date of shipment to customers when a formal arrangement exists, the price is fixed or determinable, the delivery is completed, no other significant obligations by us exist and collectibility is reasonably assured. Payments received before all of the relevant criteria for revenue recognition are satisfied are recorded as unearned revenue.

Stock-based Compensation

In October 1995, the FASB issued SFAS No. 123, "Accounting for Stock-Based Compensation". SFAS No. 123 prescribes accounting and reporting standards for all stock-based compensation plans, including employee stock options, restricted stock, employee stock purchase plans and stock appreciation rights. SFAS No. 123 requires compensation expense to be recorded (i) using the new fair value method or (ii) using the existing accounting rules prescribed by Accounting Principles Board Opinion No. 25, "Accounting for stock issued to employees" (APB 25) and related interpretations with proforma disclosure of what net income and earnings per share would have been had we adopted the new fair value method. We use the intrinsic value method prescribed by APB 25 and have opted for the disclosure provisions of SFAS No.123.

Income Taxes

We utilize SFAS No. 109, "Accounting for Income Taxes," which requires the recognition of deferred tax assets and liabilities for the expected future tax consequences of events that have been included in the financial statements or tax returns. Under this method, deferred income taxes are recognized for the tax consequences in future years of differences between the tax bases of assets and liabilities and their financial reporting amounts at each period end based on enacted tax laws and statutory tax rates applicable to the periods in which the differences are expected to affect taxable income. Valuation allowances are established, when necessary, to reduce deferred tax assets to the amount expected to be realized.

According to the Provisional Regulations of the People's Republic of China on Income Tax, the Document of Reductions and Exemptions of Income Tax for us have been approved by the local tax bureau and the Management Regulation of Yang Ling

Agricultural High-Tech Industries Demonstration Zone. We are exempted from income tax in our first two years of operations.

Foreign Currency Transactions and Comprehensive Income (Loss)

Accounting principles generally require that recognized revenue, expenses, gains and losses be included in net income. Certain statements, however, require entities to report specific changes in assets and liabilities, such as gain or loss on foreign currency translation, as a separate component of the equity section of the balance sheet. Such items, along with net income, are components of comprehensive income. Our transactions occur in Chinese Renminbi. The unit of Renminbi is in Yuan.

Recent Accounting Pronouncements

On May 15 2003, the FASB issued FASB Statement No. 150 ("SFAS 150"), Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity. SFAS 150 changes the accounting for certain financial instruments that, under previous guidance, could be classified as equity or "mezzanine" equity, by now requiring those instruments to be classified as liabilities (or assets in some circumstances) in the statement of financial position. Further, SFAS 150 requires disclosure regarding the terms of those instruments and settlement alternatives. SFAS 150 affects an entity's

classification of the following freestanding instruments: a) Mandatorily redeemable instruments b) Financial instruments to repurchase an entity's own equity instruments c) Financial instruments embodying obligations that the issuer must or could choose to settle by issuing a variable number of its shares or other equity instruments based solely on (i) a fixed monetary amount known at inception or (ii) something other than changes in its own equity instruments d) SFAS 150 does not apply to features embedded in a financial instrument that is not a derivative in its entirety. The guidance in SFAS 150 is generally effective for all financial instruments entered into or modified after May 31, 2003, and is otherwise effective at the beginning of the first interim period beginning after June 15, 2003. For private companies, mandatorily redeemable financial instruments are subject to the provisions of SFAS 150 for the fiscal period beginning after December 15, 2003. The Company does not expect the adoption of SFAS No. 150 to have a material impact on its financial position or results of operations or cash flows.

In December 2003, the Financial Accounting Standards Board (FASB) issued a revised Interpretation No. 46, "Consolidation of Variable Interest Entities" (FIN 46R). FIN 46R addresses consolidation by business enterprises of variable interest entities and significantly changes the consolidation application of consolidation policies to variable interest entities and, thus improves comparability between enterprises engaged in similar activities when those activities are conducted through variable interest entities. The Company does not hold any variable interest entities.

Three Months Ended September 30, 2004 Compared To Three Months Ended September 30, 2003

Revenue. For the three-month period ended September 30, 2004 as compared to the three-month period ended September 30, 2003, the Company generated net revenues of $5,407,841 and $3,308,192, respectively, reflecting an increase of $2,099,649 or 63%. The increase in revenues was primarily attributable to increased marketing efforts, which resulted in increases in our customer base and related volume of recurring and new customer sales as well as an increase in the sale price of the Company's compound fertilizer products.

Gross profit. The Company achieved a gross profit of $2,019,105 for the three months ended September 30, 2004, an increase of $1,160,574 or 135%, compared to $858,531 for the three months ended September 30, 2003. Gross margin, as a percentage of revenues, increased from 26% for the three months ended September 30, 2003, to 37% for the three months ended September 30, 2004. The increase in gross margin was primarily attributable to increased sales of products with a higher profit margin such as liquid fertilizers and pesticides, and an increase in purchase volume discounts for raw materials.

Operating expenses. The Company incurred operating expenses of $406,319 for the three months ended September 30, 2004, an increase of $134,534 or 50%, compared to $271,785 for the three months ended September 30, 2003. This increase is a direct result of the increase in the use of sales and marketing staff, higher transportation costs and increased reliance on advertising. Aggregated selling expenses of $228,624 account for expenses related to costs associated with sales and marketing of the Company's products. Operating expenses include general and administrative expenses of $177,695 for third quarter 2004 and relate to cost of maintaining the company's facilities, salaries and research and development.

Net income. The Company's net income was $1,596,832 for the three months ended September 30, 2004, an increase of $1,033,998 or 184% compared to $562,834 for the three months ended September 30, 2003. The increase is attributed to the substantial growth in the demand for the Company's products throughout China and increased sales of products with a higher profit margin in the period ended September 30, 2004.

Nine Months Ended September 30, 2004 Compared To Nine Months Ended September 30, 2003

Revenue. For the nine-month period ended September 30, 2004 as compared to the nine-month period ended September 30, 2003, the Company generated net revenues of $11,824,135 and $8,198,163, respectively, reflecting an increase of $3,625,972 or 44%. The increase in revenues was primarily attributable to increased marketing efforts, which resulted in increases in our customer base and related volume of recurring and new customer sales as well as an increase in the sale price of the Company's compound fertilizer products.

Gross profit. The Company achieved a gross profit of $4,879,262 for the nine months ended September 30, 2004, an increase of $2,468,214 or 102%, compared to $2,411,048 for the nine months ended September 30, 2003. Gross margin, as a percentage of revenues, increased from 29% for the nine months ended September 30, 2003, to 41% for the nine months ended September 30, 2004. The increase in gross margin was primarily attributable to increased sales of products with a higher profit margin such as liquid fertilizers and pesticides, and an increase in purchase volume discounts for raw materials.

Operating expenses. The Company incurred operating expenses of $990,728 for the nine months ended September 30, 2004, an increase of $157,776 or 19%, compared to $832,952 for the nine months ended September 30, 2003. This increase represents our continued development and implementation of our business during 2004, and the increase in revenue from the 2003 to 2004 period. Aggregated selling expenses of $459,579 account for expenses related to costs associated with sales and marketing of the Company's products and with transportation of Company's products. Operating expenses include general and administrative expenses of $531,149 for the first nine months of 2004 and relate to cost of maintaining the company's facilities, salaries and research and development.

Net income. The Company's net income was $3,841,821 for the nine months ended September 30, 2004, an increase of $2,343,567 or 156% compared to $1,498,254 for the nine months ended September 30, 2003. The increase was attributed to the substantial growth in the demand for the Company's products throughout China and increased sales of products with a higher profit margin in the nine-month period ended September 30, 2004.

Liquidity and Capital Resources

As of September 30, 2004 the Company had $2,585,020 cash and cash equivalents, and it believes that its current cash needs for at least the next twelve months can be met from working capital. The Company had net cash flows provided by operations of $1,127,798 for the nine month period ended September 30, 2004 as compared to net cash provided by operations of $96,031 in the corresponding period last year. The increase in net cash flows from operations in the current period as compared to corresponding period last year was mainly due to increase in net income and decrease in advances to suppliers resulting in gain of cash flow by $3,841,821 and $933,986, respectively. The Company does not currently have any contracts, plans or agreements in place for any additional financing. There can be no assurance that financing will be available in amounts or on terms acceptable to the Company, if at all.

Cashflows from investing activities resulted in net usage of $1,584,176 in the current period as compared to net usage of $196,096 in the corresponding period last year. The greater usage in the current period was mainly due to increase of investment in property and equipment of $305,633 in the nine-month period ended September 30, 2004 as compared to $26,158 in the corresponding period last year. The Company also invested in the expansion of the Company's manufacturing capacity by construction of a new manufacturing facility, which resulted in usage of $1,278,543. The construction was in progress through September 30, 2004.

The Company had a net decrease in cash and cash equivalent of $389,753 in the current period as compared to a net increase of $313,697 in the corresponding period last year.

The majority of the Company's revenues and expenses were denominated primarily in Renminbi ("RMB"), the currency of the People's Republic of China. There is no assurance that exchange rates between the RMB and the U.S. dollar will remain stable. A revaluation of the RMB relative to the U.S. dollar could adversely affect our business, financial condition and results of operations. The Company does not engage in currency hedging. Inflation has not had a material impact on the Company's business.

BODISEN BIOTECH, INC.