

Edgar Filing: LEATHER FACTORY INC - Form 10-Q/A

LEATHER FACTORY INC
Form 10-Q/A
November 10, 2003

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q/A

Amendment No. 1

QUARTERLY REPORT UNDER SECTION 13 OR 15(D)
OF THE SECURITIES EXCHANGE ACT OF 1934

FOR THE QUARTER ENDED SEPTEMBER 30, 2003

COMMISSION FILE NUMBER 1-12368

THE LEATHER FACTORY, INC.
A DELAWARE CORPORATION
IRS EMPLOYER IDENTIFICATION NO. 75-2543540
3847 EAST LOOP 820 SOUTH, FT. WORTH, TEXAS 76119
(817) 496-4414

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

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

Yes No X
----- -----

Number of shares of Common Stock, Par Value \$0.0024, outstanding as of October 31, 2003: 10,470,461

EXPLANATORY NOTE: This Form 10-Q/A amends the Registrant's quarterly report on Form 10-Q for the quarter ended September 30, 2003 as filed on November 7, 2003 to correct the table containing the sales and operating income by segment for the nine months ended September 30, 2002 as presented in Part 1, Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations under the caption "Results of Operations".

Edgar Filing: LEATHER FACTORY INC - Form 10-Q/A

FORM 10-Q

FOR THE QUARTERLY PERIOD ENDED SEPTEMBER 30, 2003

TABLE OF CONTENTS

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

Consolidated Balance Sheets
September 30, 2003 and December 31, 2002

Consolidated Statements of Operations
Three and nine months ended September 30, 2003 and 2002

Consolidated Statements of Cash Flows
Nine months ended September 30, 2003 and 2002

Consolidated Statements of Stockholders' Equity
Nine months ended September 30, 2003 and 2002

Notes to Consolidated Financial Statements

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

Item 3. Quantitative and Qualitative Disclosures About Market Risk

PART II. OTHER INFORMATION

Item 4. Controls and Procedures

Item 6. Exhibits and Reports on Form 8-K

SIGNATURES

2

THE LEATHER FACTORY, INC.
CONSOLIDATED BALANCE SHEETS

SEPTEMBER 30, D

2003

(unaudited)

ASSETS

Edgar Filing: LEATHER FACTORY INC - Form 10-Q/A

| | | | |
|--|----|-------------|-------|
| CURRENT ASSETS: | | | |
| Cash | \$ | 188,199 | \$ |
| Cash restricted for payment on revolving credit facility | | 510,155 | |
| Accounts receivable-trade, net of allowance for doubtful accounts of \$45,000 and \$78,000, respectively | | 2,329,505 | |
| Inventory | | 11,621,127 | |
| Prepaid income taxes | | 52,707 | |
| Deferred income taxes | | 148,111 | |
| Other current assets | | 709,270 | |
| | | ----- | ----- |
| Total current assets | | 15,559,074 | |
| | | ----- | ----- |
| PROPERTY AND EQUIPMENT, at cost | | 5,517,844 | |
| Less accumulated depreciation and amortization | | (3,547,038) | |
| | | ----- | ----- |
| Property and equipment, net | | 1,970,806 | |
| GOODWILL, net of accumulated amortization of \$753,000 and \$734,000 in 2003 and 2002, respectively | | 700,262 | |
| OTHER INTANGIBLES, net of accumulated amortization of \$151,000 and \$113,000 in 2003 and 2002, respectively | | 445,289 | |
| OTHER ASSETS | | 331,776 | |
| | | ----- | ----- |
| | \$ | 19,007,207 | \$ |
| | | ===== | ===== |
| LIABILITIES AND STOCKHOLDERS' EQUITY | | | |
| CURRENT LIABILITIES: | | | |
| Accounts payable | \$ | 1,432,291 | \$ |
| Accrued expenses and other liabilities | | 964,989 | |
| Notes payable and current maturities of long-term debt | | 2,671,929 | |
| | | ----- | ----- |
| Total current liabilities | | 5,069,209 | |
| | | ----- | ----- |
| DEFERRED INCOME TAXES | | 234,605 | |
| NOTES PAYABLE AND LONG-TERM DEBT, net of current maturities | | - | |
| COMMITMENTS AND CONTINGENCIES | | - | |
| STOCKHOLDERS' EQUITY: | | | |
| Preferred stock, \$0.10 par value; 20,000 shares authorized, none issued or outstanding | | - | |
| Common stock, \$0.0024 par value; 25,000,000 shares authorized, 10,470,461 and 10,149,961 shares issued | | 25,129 | |
| Paid-in capital | | 4,488,819 | |
| Retained earnings | | 9,219,247 | |
| Less: notes receivable secured by common stock | | (20,000) | |
| Accumulated other comprehensive loss | | (9,802) | |
| | | ----- | ----- |
| Total stockholders' equity | | 13,703,393 | |
| | | ----- | ----- |
| | \$ | 19,007,207 | \$ |
| | | ===== | ===== |

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

Edgar Filing: LEATHER FACTORY INC - Form 10-Q/A

THE LEATHER FACTORY, INC.
CONSOLIDATED STATEMENTS OF OPERATIONS
(UNAUDITED)
THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2003 AND 2002

| | THREE MONTHS | |
|---|---------------|--------------|
| | 2003 | 2002 |
| NET SALES | \$ 10,119,070 | \$ 9,484,730 |
| COST OF SALES | 4,529,258 | 4,396,332 |
| Gross profit | 5,589,812 | 5,088,398 |
| OPERATING EXPENSES | 4,672,820 | 4,246,873 |
| INCOME FROM OPERATIONS | 916,992 | 841,525 |
| OTHER INCOME (EXPENSE): | | |
| Interest expense | (40,735) | (54,108) |
| Other, net | (6,089) | (18,578) |
| Total other income (expense) | (46,824) | (72,686) |
| INCOME BEFORE INCOME TAXES and CUMULATIVE EFFECT OF CHANGE IN ACCOUNTING PRINCIPLE. | 870,168 | 768,839 |
| PROVISION FOR INCOME TAXES | 268,488 | 234,747 |
| INCOME BEFORE CUMULATIVE EFFECT OF CHANGE IN ACCOUNTING PRINCIPLE | 601,680 | 534,092 |
| CUMULATIVE EFFECT OF CHANGE IN ACCTG PRINCIPLE, net of income taxes | - | - |
| NET INCOME (LOSS) | \$ 601,680 | \$ 534,092 |

NET INCOME (LOSS) PER COMMON SHARE - BASIC:

| | | | | |
|---|--------|--------|--------|----------|
| INCOME BEFORE CUMULATIVE EFFECT OF CHANGE IN ACCOUNTING PRINCIPLE | \$0.06 | \$0.05 | \$0.21 | \$ 0.21 |
| CUMULATIVE EFFECT OF CHANGE IN ACCOUNTING PRINCIPLE, NET. | - | - | - | (0.37) |
| NET INCOME (LOSS) PER COMMON SHARE-BASIC | \$0.06 | \$0.05 | \$0.21 | \$(0.19) |

NET INCOME (LOSS) PER COMMON SHARE - DILUTED:

| | | | | |
|---|--------|--------|--------|---------|
| INCOME BEFORE CUMULATIVE EFFECT OF CHANGE IN ACCOUNTING PRINCIPLE | \$0.06 | \$0.05 | \$0.20 | \$ 0.19 |
| CUMULATIVE EFFECT OF CHANGE IN ACCOUNTING PRINCIPLE, NET. | - | - | - | (0.37) |

Edgar Filing: LEATHER FACTORY INC - Form 10-Q/A

NET INCOME (LOSS) PER COMMON SHARE-DILUTED. \$0.06 \$0.05 \$0.20 \$(0.18)
 =====

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

4

THE LEATHER FACTORY, INC.
 CONSOLIDATED STATEMENTS OF CASH FLOWS
 (UNAUDITED)
 NINE MONTHS ENDED SEPTEMBER 30, 2003 AND 2002

| | 2003 | 2002 |
|--|--------------|-------------|
| | ----- | ----- |
| CASH FLOWS FROM OPERATING ACTIVITIES: | | |
| Net income (loss) | \$ 2,154,902 | \$(1,923,38 |
| Adjustments to reconcile net income (loss) to net cash (used in) provided by operating activities- | | |
| Depreciation & amortization | 397,959 | 370,23 |
| Loss on disposal of assets | 9,372 | |
| Amortization of deferred financing costs | - | 37,03 |
| Deferred income taxes | 59,508 | (42,71 |
| Other | 14,960 | (3,11 |
| Cumulative effect of change in accounting principle | - | 4,008,83 |
| Net changes in assets and liabilities: | | |
| Accounts receivable-trade, net | (390,808) | (102,45 |
| Inventory | 1,074,217 | (1,222,30 |
| Income taxes | 2,936 | (94,69 |
| Other current assets | (37,153) | (343,10 |
| Accounts payable | (162,618) | 321,88 |
| Accrued expenses and other liabilities | (1,538,342) | 244,92 |
| | ----- | ----- |
| Total adjustments | (569,969) | 3,174,52 |
| | ----- | ----- |
| Net cash provided by operating activities | 1,584,933 | 1,251,13 |
| | ----- | ----- |
| CASH FLOWS FROM INVESTING ACTIVITIES: | | |
| Purchase of property and equipment | (326,284) | (429,25 |
| Payments in connection with businesses acquired | - | (227,74 |
| Proceeds from sale of assets | 6,217 | |
| Increase in other assets | (22,305) | (415,80 |
| | ----- | ----- |
| Net cash used in investing activities | (342,372) | (1,072,80 |
| | ----- | ----- |
| CASH FLOWS FROM FINANCING ACTIVITIES: | | |
| Net increase (decrease) in revolving credit loans | (1,544,417) | (601,04 |
| Payments on notes payable and long-term debt | (4,878) | (25,90 |
| Decrease in cash restricted for payment on revolving credit facility | 43,685 | 5,09 |
| Payments received on notes secured by common stock | 24,003 | 26,28 |
| Proceeds from issuance of common stock | 325,688 | 120,30 |
| | ----- | ----- |
| Net cash used in financing activities | (1,155,919) | (475,27 |
| | ----- | ----- |
| NET CHANGE IN CASH | 86,642 | (296,94 |

Edgar Filing: LEATHER FACTORY INC - Form 10-Q/A

| | | |
|---|------------|-----------|
| CASH, beginning of period | 101,557 | 409,04 |
| CASH, end of period | \$ 188,199 | \$ 112,10 |
| SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION: | | |
| Interest paid during the period | \$ 178,558 | \$ 157,91 |
| Income taxes paid during the period, net of (refunds) | 819,602 | 1,076,31 |

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

5

THE LEATHER FACTORY, INC.
CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY
(UNAUDITED)
NINE MONTHS ENDED SEPTEMBER 30, 2003 AND 2002

| | Common Stock | | |
|--|---------------------|--------------|--------------------|
| | Number of shares | Par value | Paid-in capital |
| BALANCE, December 30, 2001 | 9,991,161 | \$ 23,979 | \$ 4,030,508 |
| Payments on notes receivable - secured by common stock | - | - | - |
| Shares issued - warrants and employee stock options exercised | 73,000 | 175 | 76,320 |
| Net loss | - | - | - |
| Translation adjustment | - | - | - |
| BALANCE, September 30, 2002 | 10,064,161 | \$ 24,154 | \$ 4,106,828 |

| | Notes receivable - secured by common stock | Accumulated other comprehensive loss | Tota |
|--|---|---|----------|
| BALANCE, December 30, 2001 | \$ (71,939) | \$ (37,064) | \$ 12,42 |
| Payments on notes receivable - secured by common stock | 24,636 | - | 2 |
| Shares issued - warrants and employee stock options exercised | - | - | 7 |
| Net loss | - | - | (2,45 |
| Translation adjustment | - | 3,197 | |

Edgar Filing: LEATHER FACTORY INC - Form 10-Q/A

| | | | |
|-----------------------------|-------------|-------------|----------|
| BALANCE, September 30, 2002 | \$ (47,303) | \$ (33,867) | \$ 10,07 |
|-----------------------------|-------------|-------------|----------|

Comprehensive loss for the nine months ended September 30, 2002

| | Common Stock | | Paid-in capital |
|---|------------------|-----------|-----------------|
| | Number of shares | Par value | |
| BALANCE, December 31, 2002 | 10,149,961 | \$24,360 | \$4,163,90 |
| Payments on notes receivable - secured by common stock | - | - | |
| Shares issued - warrants and employee stock options exercised | 320,500 | 769 | 198,53 |
| Warrants to acquire 100,000 shares of common stock issued | - | - | 126,38 |
| Net income | - | - | |
| Translation adjustment | - | - | |
| BALANCE, September 30, 2003 | 10,470,461 | \$25,129 | \$4,488,81 |

| | Notes receivable - secured by common stock | Accumulated other comprehensive loss | Total |
|---|--|--------------------------------------|---------------|
| BALANCE, December 31, 2002 | \$ (44,003) | \$ (38,541) | \$ 11,170,062 |
| Payments on notes receivable - secured by common stock | 24,003 | - | 24,003 |
| Shares issued - warrants and employee stock options exercised | - | - | 199,306 |
| Warrants to acquire 100,000 shares of common stock issued | - | - | 126,381 |
| Net income | - | - | 2,154,902 |
| Translation adjustment | - | 28,739 | 28,739 |
| BALANCE, September 30, 2003 | \$ (20,000) | \$ (9,802) | \$ 13,703,393 |

Comprehensive income for the nine months ended September 30, 2003

Edgar Filing: LEATHER FACTORY INC - Form 10-Q/A

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

6

THE LEATHER FACTORY, INC. NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. BASIS OF PRESENTATION AND CERTAIN SIGNIFICANT ACCOUNTING POLICIES

In the opinion of management, the accompanying consolidated financial statements for The Leather Factory, Inc. and its consolidated subsidiaries ("TLF") contain all adjustments necessary to present fairly its financial position as of September 30, 2003 and December 31, 2002, and its results of operations and cash flows for the three and nine month periods ended September 30, 2003 and 2002. Certain reclassifications have been made to prior year amounts in order to conform to the current year presentation. Operating results for the three and nine month periods ended September 30, 2003 are not necessarily indicative of the results that may be expected for the year ended December 31, 2003. These consolidated financial statements should be read in conjunction with the audited consolidated financial and accompanying notes included in our Annual Report on Form 10-K for the year ended December 31, 2002.

The preparation of financial statements in accordance with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

Recent Accounting Pronouncements

In December 2002, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards ("SFAS") No. 148, Accounting for Stock-Based Compensation - Transition and Disclosure - an amendment of FASB Statement 123, ("SFAS 148"). SFAS 148 amends SFAS No.123, Accounting for Stock-Based Compensation, ("SFAS 123"), to provide alternative transition methods for an entity's voluntary change in their accounting for stock-based compensation from the intrinsic value method prescribed by Accounting Principles Board Opinion No. 25, Accounting for Stock Issued to Employees, ("APB No. 25") and related interpretations to the fair value method under SFAS 123. In addition, SFAS No. 148 amends the disclosure requirements of SFAS No. 123 to require disclosure of the pro forma effects of using the fair value method of accounting for stock-based compensation in interim as well as annual financial statements. The Company currently accounts for its stock-based compensation using the intrinsic value method as prescribed by APB No. 25. The disclosure provisions of SFAS No. 148 were adopted on December 31, 2002 and are discussed in Note 2.

Revenue Recognition

The Company recognizes revenue for over-the-counter sales as transactions occur and other sales upon shipment of product provided that there are no significant post-delivery obligations to the customer and collection is reasonably assured, which generally occurs upon shipment. Net sales represent gross sales less negotiated price allowances, product returns, and allowances for defective merchandise.

Inventory

Inventory is stated at the lower of cost or market and is accounted for on the "first in, first out" method. In addition, the value of inventory is periodically reduced for slow-moving or obsolete inventory based on management's

Edgar Filing: LEATHER FACTORY INC - Form 10-Q/A

review of items on hand compared to their estimated future demand. The components of inventory consist of the following as of:

| | SEPTEMBER 30, 2003 | DECEMBER 31, 2002 |
|-----------------------------------|-----------------------|----------------------|
| | ----- | ----- |
| Finished goods held for sale | \$ 10,457,893 | \$ 11,693,868 |
| Raw materials and work in process | 1,163,234 | 1,001,476 |
| | ----- | ----- |
| | \$ 11,621,127 | \$ 12,695,344 |
| | ===== | ===== |

7

Goodwill and Other Intangibles

Statement of Financial Accounting Standards ("SFAS") No. 142, "Goodwill and Other Intangible Assets," prescribes a two-phase process for impairment testing of goodwill, which is performed once annually, absent indicators of impairment. The first phase screens for impairment, while the second phase (if necessary) measures the impairment. As a result of SFAS 142, we incurred an impairment write-down in the first quarter of 2002 of our investment in our subsidiary, Roberts, Cushman & Company, Inc., in the amount of \$4.0 million. The remaining goodwill on our balance sheet is analyzed by management periodically to determine the appropriateness of its carrying value. We have elected to perform our annual analysis during the fourth calendar quarter of each year. As of December 31, 2002, management determined that the present value of the discounted estimated future cash flows of the stores associated with the goodwill is sufficient to support their respective goodwill balances. No indicators of impairment were identified during the first nine months of 2003.

Other intangibles consist of the following:

| | AS OF SEPTEMBER 30, 2003 | | | AS OF DECEMBER 31, 2002 | | |
|------------------------|--------------------------|-----------------------------|-----------|-------------------------|-----------------------------|-----------|
| | ----- | ----- | ----- | ----- | ----- | ----- |
| | GROSS | ACCUMULATED AMORTIZATION | NET | GROSS | ACCUMULATED AMORTIZATION | NET |
| | ----- | ----- | ----- | ----- | ----- | ----- |
| Trademarks, Copyrights | \$ 544,369 | \$ 129,247 | \$415,122 | \$544,369 | \$ 102,029 | \$442,340 |
| Non-Compete Agreements | 52,000 | 21,833 | 30,167 | 52,000 | 10,833 | 41,167 |
| | ----- | ----- | ----- | ----- | ----- | ----- |
| | \$ 596,369 | \$ 151,080 | \$445,289 | \$596,369 | \$ 112,862 | \$483,507 |
| | ===== | ===== | ===== | ===== | ===== | ===== |

The Company recorded amortization expense of \$39,161 during the first nine months of 2003 compared to \$35,401 during the first nine months of 2002. The Company has no intangible assets not subject to amortization under SFAS 142. Based on the current amount of intangible assets subject to amortization, the estimated amortization expense for each of the succeeding 5 years are as follows:

ROBERTS

Edgar Filing: LEATHER FACTORY INC - Form 10-Q/A

| | LEATHER FACTORY. | TANDY LEATHER | CUSHMAN | TOTAL |
|------|------------------|---------------|---------|----------|
| | ----- | ----- | ----- | ----- |
| 2003 | \$ 5,918 | \$ 45,004 | \$ 0 | \$50,922 |
| 2004 | 5,918 | 45,004 | 0 | 50,922 |
| 2005 | 5,918 | 35,004 | 0 | 40,922 |
| 2006 | 5,918 | 34,337 | 0 | 40,255 |
| 2007 | 5,918 | 33,504 | 0 | 39,422 |

2. STOCK-BASED COMPENSATION

The Company accounts for stock options granted to its directors and employees using the intrinsic value method prescribed by APB No. 25 which requires compensation expense be recognized for stock options when the quoted market price of the Company's common stock on the date of grant exceeds the option's exercise price. No compensation cost has been reflected in net income for the granting of director and employee stock options as all options granted had an exercise price equal to the quoted market price of the Company's common stock on the date the options were granted. Had compensation cost for the Company's stock options been determined consistent with the SFAS 123 fair value approach, the Company's net income and net income per common share for the three and nine months ended September 30, 2003 and 2002, on a pro forma basis, would have been as follows:

| | THREE MONTH |
|--|---------------|
| | ----- |
| | SEPTEMBER 30, |
| | 2003 |
| | ----- |
| Net income (loss), as reported | \$ 601,680 |
| Add: Stock-based compensation expense included in reported net income (loss) | - |
| Deduct: Stock-based compensation expense determined under fair value method | 24,546 |
| Net income (loss), pro forma | \$ 577,134 |
| Net income (loss) per share: | |
| Basic - as reported | \$ 0.06 |
| Basic - pro forma | \$ 0.06 |
| Diluted - as reported | \$ 0.06 |
| Diluted - pro forma | 0.05 |
| | NINE MONTH |
| | ----- |
| | SEPTEMBER 30, |
| | 2003 |
| | ----- |
| Net income (loss), as reported | \$ 2,154,902 |
| Add: Stock-based compensation expense included in reported net income (loss) | - |
| Deduct: Stock-based compensation expense determined under fair value method | 73,639 |
| Net income (loss), pro forma | \$ 2,081,263 |

Edgar Filing: LEATHER FACTORY INC - Form 10-Q/A

| | | |
|------------------------------|----|------|
| Net income (loss) per share: | | |
| Basic - as reported | \$ | 0.21 |
| Basic - pro forma | \$ | 0.20 |
| | | |
| Diluted - as reported | \$ | 0.20 |
| Diluted - pro forma | \$ | 0.19 |

The fair values of stock options granted were estimated on the dates of grant using the Black-Scholes option pricing model with the following weighted average assumptions: risk-free interest rate of 3.125% for 2003 and 3.00% for 2002; dividend yields of 0% for both periods; volatility factors of .706 for 2003 and .736 for 2002; and an expected life of the valued options of 4 years.

8

3. EARNINGS PER SHARE

The following table sets forth the computation of basic and diluted earnings per share ("EPS"):

| | THREE MONTHS ENDED SEPTEMBER 30, | | NI |
|--|-------------------------------------|------------|---------|
| | 2003 | 2002 | |
| Numerator: | | | |
| Net income (loss) | \$ 601,680 | \$ 534,092 | \$ 2,15 |
| Numerator for basic and diluted earnings per share | 601,680 | 534,092 | 2,15 |
| Denominator: | | | |
| Weighted-average shares outstanding-basic | 10,394,374 | 10,064,249 | 10,26 |
| Effect of dilutive securities: | | | |
| Stock options | 422,000 | 448,836 | 42 |
| Warrants | 86,420 | 210,318 | 14 |
| Dilutive potential common shares | 508,420 | 659,154 | 57 |
| Denominator for diluted earnings per share- weighted-average shares | 10,902,794 | 10,723,403 | 10,84 |
| Basic earnings (loss) per share | \$ 0.06 | \$ 0.05 | \$ |
| Diluted earnings (loss) per share | \$ 0.06 | \$ 0.05 | \$ |

The net effect of converting stock options to purchase 924,700 and 1,081,000 shares of common stock at option prices less than the average market prices has been included in the computations of diluted EPS for the three and nine months ended September 30, 2003 and 2002, respectively.

4. SEGMENT INFORMATION

The Company identifies its segments based on the activities of three distinct

Edgar Filing: LEATHER FACTORY INC - Form 10-Q/A

businesses:

a. The Leather Factory, which sells primarily to wholesale customers through a chain of 30 outlet stores located in the United States and Canada;

b. Tandy Leather Company, which sells primarily to retail customers through a chain of retail stores located in the United States; and

c. Roberts, Cushman & Company, manufacturer of decorative hat trims sold directly to hat manufacturers and distributors.

The Company's reportable operating segments have been determined as separately identifiable business units. The Company measures segment earnings as operating earnings, defined as income before interest and income taxes.

| | LEATHER FACTORY | TANDY LEATHER | ROBERTS, CUSHMAN | T |
|--|-----------------|---------------|---------------------|------|
| | | | | |
| FOR THE QUARTER ENDED SEPTEMBER 30, 2003 | | | | |
| Net sales | \$ 7,372,159 | \$ 2,334,127 | \$ 412,784 | \$10 |
| Gross profit | 3,996,866 | 1,475,312 | 117,634 | 5 |
| Operating earnings | 784,322 | 117,514 | 15,156 | |
| Interest expense | (40,735) | - | - | |
| Other, net | (6,315) | 226 | - | |
| Income before income taxes | 737,272 | 117,740 | 15,156 | |
| Depreciation and amortization | 99,489 | 20,978 | 2,365 | |
| Fixed asset additions | 33,230 | 21,300 | 1,377 | |
| Total assets | \$ 15,300,407 | \$ 2,802,218 | \$ 904,582 | \$19 |
| FOR THE QUARTER ENDED SEPTEMBER 30, 2002 | | | | |
| Net sales | 7,244,610 | 1,727,925 | 512,195 | \$ 9 |
| Gross profit | 3,848,893 | 1,026,681 | 212,824 | 5 |
| Operating earnings | 631,125 | 76,231 | 134,169 | |
| Interest expense | (53,995) | (113) | - | |
| Other, net | (18,578) | - | - | |
| Income before income taxes | 558,552 | 76,118 | 134,169 | |
| Depreciation and amortization | 94,369 | 29,612 | 3,399 | |
| Fixed asset additions | 139,454 | 55,050 | 1,936 | |
| Total assets | \$ 14,528,938 | \$ 2,241,064 | \$ 921,378 | \$17 |

9

| | LEATHER FACTORY | TANDY LEATHER | ROBERTS, CUSHMAN | T |
|--|-----------------|---------------|---------------------|------|
| | | | | |
| FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2003 | | | | |
| Net sales | \$ 23,375,158 | \$ 6,312,145 | \$1,452,527 | \$31 |
| Gross profit | 12,477,180 | 3,981,715 | 497,475 | 16 |
| Operating earnings | 2,626,394 | 430,737 | 129,998 | 3 |
| Interest expense | (174,555) | - | - | |
| Other, net | 68,064 | 369 | - | |

Edgar Filing: LEATHER FACTORY INC - Form 10-Q/A

| | | | | |
|--|---------------|--------------|-------------|------|
| Income before income taxes | 2,519,903 | 431,106 | 129,998 | 3 |
| Depreciation and amortization | 335,184 | 55,064 | 7,711 | --- |
| Fixed asset additions | 201,862 | 122,189 | 2,233 | --- |
| Total assets | \$ 15,300,407 | \$ 2,802,218 | \$ 904,582 | \$19 |
| ----- | | | | |
| FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2002 | | | | |
| Net sales | \$ 22,769,549 | \$ 5,420,108 | \$1,551,060 | \$29 |
| Gross profit | 12,151,507 | 3,179,498 | 561,614 | 15 |
| Operating earnings | 2,625,651 | 315,268 | 305,214 | 3 |
| Interest expense | (190,903) | (516) | - | --- |
| Other, net | (44,566) | (633) | - | --- |
| Income before income taxes | 2,390,182 | 314,119 | 305,214 | 3 |
| Depreciation and amortization | 279,033 | 81,256 | 9,945 | --- |
| Fixed asset additions | 267,823 | 157,953 | 3,474 | --- |
| Total assets | \$ 14,528,938 | \$ 2,241,064 | \$ 921,378 | \$17 |
| ----- | | | | |

Net sales for geographic areas were as follows:

| | THREE MONTHS ENDED SEPTEMBER 30, | | NINE MONTHS ENDED SEPTEMBER 30, | |
|---------------------|-------------------------------------|--------------|------------------------------------|--------------|
| | 2003 | 2002 | 2003 | 2002 |
| United States | \$ 9,456,440 | \$ 8,941,654 | \$29,038,861 | \$28,052,774 |
| All other countries | 662,630 | 543,076 | 2,100,969 | 1,687,943 |
| | \$ 10,119,070 | \$ 9,484,730 | \$31,139,830 | \$29,740,717 |
| | ===== | ===== | ===== | ===== |

Geographic sales information is based on the location of the customer. Net sales from no single foreign country was material to the Company's consolidated net sales for the three and nine month periods ended September 30, 2003 and 2002. The Company does not have any significant long-lived assets outside of the United States.

10

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

The Leather Factory, Inc. ("TLF" or the "Company") is a Delaware corporation whose common stock trades on the American Stock Exchange under the symbol "TLF". The Company is managed on a business entity basis, with those businesses being The Leather Factory ("Leather Factory"), Tandy Leather Company ("Tandy" or "Tandy Leather"), and Roberts, Cushman & Company, Inc. ("Cushman"). See Note 4 to the Consolidated Financial Statements for additional information concerning the Company's segments, as well as its foreign operations.

Leather Factory, founded in 1980 by Wray Thompson and Ron Morgan, distributes leather and related products, including leatherworking tools, buckles and adornments for belts, leather dyes and finishes, saddle and tack hardware, and do-it-yourself kits. The products are sold primarily through 30 company-owned outlets located throughout the United States and Canada.

Edgar Filing: LEATHER FACTORY INC - Form 10-Q/A

Tandy Leather is the best-known supplier of leather and related supplies used in the leathercraft industry. From its founding in 1919, Tandy has been the primary leathercraft resource world wide. Products include quality tools, leather, accessories, kits and teaching materials. In early 2002, we initiated a plan to expand Tandy by opening retail stores. As of October 31, 2003, we have opened 26 Tandy Leather retail stores located throughout the United States.

Cushman, whose origins date back to the mid-1800's, custom designs and manufactures a product line of decorative hat trims for headwear manufacturers.

CRITICAL ACCOUNTING POLICIES

A description of the Company's critical accounting policies appears in "Item 2. Management's Discussions and Analysis of Financial Condition and Results of Operations" in the Company's Annual Report on Form 10-K for the year ended December 31, 2002.

RESULTS OF OPERATIONS

The following tables present selected financial data of each of the Company's three segments for the quarters and nine months ended September 30, 2003 and 2002:

| | QUARTER ENDED SEPTEMBER 30, 2003 | | QUARTER ENDED SEPTEMBER 30, 2002 | |
|------------------|----------------------------------|---------------------|----------------------------------|---------------------|
| | SALES | OPERATING INCOME | SALES | OPERATING INCOME |
| Leather Factory | \$ 7,372,159 | \$ 784,322 | \$ 7,244,610 | \$ 631,125 |
| Tandy | 2,334,127 | 117,514 | 1,727,925 | 76,231 |
| Cushman | 412,784 | 15,156 | 512,195 | 134,169 |
| Total Operations | \$ 10,119,070 | \$ 916,992 | \$ 9,484,730 | \$ 841,525 |
| | ===== | ===== | ===== | ===== |

| | NINE MONTHS ENDED SEPTEMBER 30, 2003 | | NINE MONTHS ENDED SEPTEMBER 30, 2002 | |
|------------------|--------------------------------------|---------------------|--------------------------------------|---------------------|
| | SALES | OPERATING INCOME | SALES | OPERATING INCOME |
| Leather Factory | \$ 23,375,158 | \$ 784,322 | \$ 22,769,549 | \$ 2,625,651 |
| Tandy | 6,312,145 | 117,514 | 5,420,108 | 315,268 |
| Cushman | 1,452,527 | 15,156 | 1,551,060 | 305,214 |
| Total Operations | \$ 31,139,830 | \$ 916,992 | \$ 29,740,717 | \$ 3,246,133 |
| | ===== | ===== | ===== | ===== |

Consolidated net sales for the quarter ended September 30, 2003 increased \$634,000, or 6.7%, compared to the same period in 2002. Leather Factory's sales increase was \$127,000; Tandy contributed \$606,000 while Cushman recorded a sales

Edgar Filing: LEATHER FACTORY INC - Form 10-Q/A

reduction of \$99,000. Operating income on a consolidated basis for the quarter ended September 30, 2003 increased 9.0% or \$75,000 over the third quarter of 2002.

Total consolidated net sales for the nine months ended September 30, 2003 increased \$1.4 million, or 4.7%, compared to the same period in 2002. Leather Factory contributed \$606,000 of the sales gain while Tandy added \$892,000. Cushman's 2003 sales were down \$98,000 compared to a year ago. Operating income on a consolidated basis for the nine months ended September 30, 2003 was down 1.8% or \$59,000 over last year.

The following table shows in comparative form our consolidated net income (loss) for the third quarters of 2003 and 2002 and the first nine months of the two years, both before and after the cumulative effect of a previously reporting change in accounting principle in 2002:

| | FOR THE THREE MONTHS ENDED SEPTEMBER 30, | | |
|---|---|-----------|----------|
| | 2003 | 2002 | % CHANGE |
| Income before cumulative effect of change in accounting principle | \$601,680 | \$534,092 | 12.6% |
| Cumulative effect of change in accounting principle* | - | - | - |
| | ----- | ----- | ----- |
| Net income (loss) | \$601,680 | \$534,092 | 12.6% |
| | ===== | ===== | ===== |

| | FOR THE NINE MONTHS ENDED SEPTEMBER 30, | | |
|---|--|----------------|-------|
| | 2003 | 2002 | % C |
| Income before cumulative effect of change in accounting principle | \$2,154,902 | \$ 2,085,444 | |
| Cumulative effect of change in accounting principle* | - | (4,008,831) | |
| | ----- | ----- | ----- |
| Net income (loss) | \$2,154,902 | \$ (1,923,387) | |
| | ===== | ===== | ===== |