

Edgar Filing: LOTUS PACIFIC INC - Form 10-Q

LOTUS PACIFIC INC
Form 10-Q
February 15, 2001

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, DC 20549

FORM 10-Q

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

For the Quarterly Period Ended December 31, 2000

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

Commission File Number: 000-24999

LOTUS PACIFIC, INC.
(Exact name of registrant as specified in its charter)

Delaware
(State of Organization)

52-1947160
(I.R.S. Employer Identification Number)

200 Centennial Avenue, Suite 201, Piscataway, New Jersey 08854
(Address of Principal Executive Offices)

(732) 885-0100
(Registrant's Telephone Number, Including Area Code)

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 proceeding 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.

(1) Yes No (2) Yes No

Indicate the number of shares outstanding of each of the Registrant's classes of common stock, as of December 31, 2000:

| Class | Number of Shares |
|----------------------------|------------------|
| Common Stock | 64,133,795 |
| Par Value \$.001 Per Share | |

LOTUS PACIFIC, INC.

INDEX

Edgar Filing: LOTUS PACIFIC INC - Form 10-Q

PART I FINANCIAL INFORMATION

Item 1. Financial Statements

- a) Condensed Consolidated Balance Sheets as of December 31, 2000 (unaudited) and June 30, 2000 (audited)
- b) Condensed Consolidated Statements of Operations (unaudited) for the Three and Six Months Ended December 31, 2000 and 1999
- c) Condensed Consolidated Statements of Cash Flows (unaudited) for the Six Months Ended December 31, 2000 and 1999
- d) Notes to Interim Consolidated Financial Statements

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

Item 3. Quantitative and Qualitative Disclosure about Market Risk

PART II OTHER INFORMATION

- Item 1. Legal Proceedings
- Item 2. Changes in Securities
- Item 3. Defaults upon Senior Securities
- Item 4. Submission of Matters to a Vote of Security Holders
- Item 5. Other Information

Signatures

LOTUS PACIFIC, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS

ASSETS

| | December 31, 2000 ----- (Unaudited) | June 30, 2000 ----- (Audited) |
|--------------------------|--|--|
| Current Assets: | | |
| Cash..... | \$ 16,959,509 | \$ 27,942,258 |
| Accounts receivable..... | 55,477,961 | 19,534,974 |

Edgar Filing: LOTUS PACIFIC INC - Form 10-Q

| | | |
|--|---------------|---------------|
| Accounts receivable from related parties | 21,869,996 | 5,653,533 |
| Inventory..... | 20,144,385 | 13,185,391 |
| Prepaid expenses..... | 1,526,545 | 1,533,045 |
| Other..... | --- | 89,633 |
| Deferred tax asset..... | 1,313,000 | --- |
| | ----- | ----- |
| Total current assets..... | 117,291,396 | 67,938,834 |
| Property and equipment: | | |
| Furniture and office equipment.... | 3,267,968 | 2,717,683 |
| Equipment..... | 1,854,612 | 1,175,859 |
| Leasehold improvements..... | 446,989 | 234,086 |
| | ----- | ----- |
| | 5,569,569 | 4,127,628 |
| Less: accumulated depreciation.... | 1,833,632 | 1,317,636 |
| | ----- | ----- |
| | 3,735,937 | 2,809,992 |
| Other assets: | | |
| Restricted cash..... | --- | 300,000 |
| Notes receivable..... | 8,300,000 | 11,860,000 |
| Goodwill, net of accumulated amortization of \$14,875,186 at December 31, 2000 and \$11,091,760 at June 30, 2000.... | 60,793,323 | 64,576,749 |
| Investment in unconsolidated subsidiary | 3,250,732 | 4,329,925 |
| Other..... | 173,044 | 745,003 |
| | ----- | ----- |
| | 72,517,099 | 81,811,677 |
| | ----- | ----- |
| | \$193,544,432 | \$152,560,503 |
| | ===== | ===== |
| LIABILITIES AND STOCKHOLDERS' EQUITY | | |
| Current liabilities: | | |
| Line of credit..... | \$ 3,000,000 | \$ 1,278,000 |
| Accounts payable and accrued expenses | 27,899,398 | 19,233,547 |
| Accounts payable to related parties | 30,151,704 | 15,261,506 |
| Notes payable..... | 622,372 | 1,500,000 |
| Deposits..... | 32,047 | --- |
| Income taxes payable..... | 3,188,463 | 2,434,150 |
| | ----- | ----- |
| Total current liabilities..... | 64,893,984 | 39,707,203 |
| Minority interest in subsidiaries.... | 18,332,440 | 6,425,633 |
| Commitments | | |
| Stockholders' equity: | | |
| Common stock..... | 64,133 | 64,133 |
| Deferred stock compensation..... | (15,291,461) | (16,643,967) |
| Preferred stock, Series A..... | 4 | 4 |
| Additional paid-in capital..... | 201,020,689 | 191,037,695 |
| Treasury stock..... | (7,057,102) | (7,057,102) |
| Accumulated deficit..... | (68,418,255) | (60,973,096) |
| | ----- | ----- |
| | 110,318,008 | 106,427,667 |
| | ----- | ----- |
| | \$193,544,432 | \$152,560,503 |
| | ===== | ===== |

Edgar Filing: LOTUS PACIFIC INC - Form 10-Q

See Notes to Interim Consolidated Financial Statements

LOTUS PACIFIC, INC. AND SUBSIDIARIES
 CONSOLIDATED STATEMENTS OF OPERATIONS
 FOR THE THREE AND SIX MONTHS ENDED DECEMBER 31, 2000 AND 1999
 (Unaudited)

| | Three Months Ended December 31, | | Six Months Ended December 31, | |
|--|------------------------------------|----------------|----------------------------------|----------------|
| | 2000 | 1999 | 2000 | 1999 |
| Sales..... | \$105,643,919 | \$19,609,595 | \$205,550,849 | \$30,847,338 |
| Cost of sales..... | 93,857,107 | 14,821,931 | 175,191,338 | 23,974,463 |
| Gross profit..... | 11,786,812 | 4,787,664 | 30,359,511 | 6,872,875 |
| Operating expenses: | | | | |
| Selling, general, and administrative expenses... | 8,934,780 | 8,582,549 | 17,353,728 | 14,786,874 |
| Research and development... | 3,935,870 | 959,010 | 12,280,835 | 2,049,610 |
| | 12,870,650 | 9,541,559 | 29,634,563 | 16,836,484 |
| Operating income (loss)..... | (1,083,838) | (4,753,895) | 724,948 | (9,963,609) |
| Other income (expense): | | | | |
| Interest income..... | 425,382 | 62,138 | 854,785 | 128,443 |
| Interest expense..... | 82,819 | --- | (1,286) | --- |
| Other income..... | (7,286) | --- | 3,754 | 23,680 |
| Minority interest in (income) loss of consolidated subsidiaries.. | 408,015 | (172,909) | (553,654) | 465,257 |
| Foreign exchange gain..... | 107,782 | --- | 127,993 | --- |
| Equity in earnings (loss) of unconsolidated subsidiaries .. | (1,020,854) | 63,130 | (1,079,193) | 326,048 |
| | (4,142) | (47,641) | (647,601) | 943,428 |
| Net income (loss) before income taxes..... | (1,087,980) | (4,801,536) | 77,347 | (9,020,181) |
| Income tax expense | 2,879,578 | --- | 7,522,507 | --- |
| Net loss..... | \$ (3,967,558) | \$ (4,801,536) | \$ (7,445,160) | \$ (9,020,181) |
| Loss per share | | | | |
| Basic and diluted..... | \$ (0.06) | \$ (0.07) | \$ (0.12) | \$ (0.14) |
| Weighted average shares..... | 64,133,795 | 64,544,474 | 64,133,795 | 64,544,474 |

Edgar Filing: LOTUS PACIFIC INC - Form 10-Q

See Notes to Interim Consolidated Financial Statements

LOTUS PACIFIC, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
FOR THE SIX MONTHS ENDED DECEMBER 31, 2000 AND 1999
(Unaudited)

| | 2000 | 1999 |
|--|-----------------------|----------------------|
| | ----- | ----- |
| Cash flows from operating activities: | | |
| Net loss..... | \$ (7,445,160) | \$ (9,020,181) |
| Adjustments to reconcile net loss to net cash provided by operating activities: | | |
| Equity in earnings of unconsolidated subsidiaries | 1,079,193 | (326,048) |
| Depreciation and amortization..... | 4,392,867 | 5,658,072 |
| Amortization of deferred stock compensation | 10,393,017 | --- |
| Minority interest in subsidiary..... | (553,654) | (872,923) |
| Changes in assets and liabilities: | | |
| Increase in accounts receivable..... | (35,942,987) | 1,683,219 |
| Increase in accounts receivable from related parties..... | (16,164,463) | --- |
| Increase in inventory..... | (6,958,994) | (328,792) |
| Decrease in prepaid expenses..... | 6,500 | --- |
| Decrease (increase) in other current assets | 89,633 | (1,236,338) |
| Decrease in restricted cash..... | 300,000 | --- |
| Increase in deposits..... | --- | (3,935,931) |
| Decrease in other assets..... | 571,959 | 120,835 |
| Increase in deferred tax asset..... | (1,313,000) | --- |
| Increase in accounts payable and accrued expenses | 8,665,851 | 3,561,011 |
| Increase in accounts payable to related parties | 14,890,198 | --- |
| Increase in income taxes payable..... | 754,313 | --- |
| Net cash used in operating activities..... | ----- (27,234,727) | ----- 4,697,076 |
| Cash flows from investing activities: | | |
| Purchase of property and equipment..... | (1,441,941) | (459,906) |
| Purchase of investments | --- | (3,466,800) |
| Proceeds from sale of subsidiary preferred stock | 13,257,500 | --- |
| Net cash provided by (used in) investing activities | ----- 11,815,559 | ----- (3,926,706) |
| Cash flows from financing activities: | | |
| Increase in investment deposits | 32,047 | --- |
| Decrease in loans receivable..... | 3,560,000 | --- |
| Proceeds from line of credit..... | 1,722,000 | --- |
| Repayments of notes payable..... | (877,628) | --- |

Edgar Filing: LOTUS PACIFIC INC - Form 10-Q

| | | |
|---|--------------|--------------|
| Net cash provided by financing activities.. | 4,436,419 | --- |
| Net decrease in cash..... | (10,982,749) | (8,623,782) |
| Cash, beginning of year..... | 27,942,258 | 30,779,486 |
| Cash, end of year..... | \$16,959,509 | \$22,155,704 |
| Supplemental disclosure of cash flow information: | | |
| Cash paid for interest..... | \$ 84,105 | \$ --- |
| Cash paid for taxes..... | \$ 9,050,000 | \$ --- |

See Notes to Interim Consolidated Financial Statements

LOTUS PACIFIC, INC. AND SUBSIDIARIES
NOTES TO INTERIM CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2000
(Unaudited)

NOTE 1 GENERAL

Lotus Pacific, Inc. creates, manages, and operates communications and network technology companies. LPFC and its subsidiaries (the "Company") provide solutions for the communications and network technology markets. The Company is primarily engaged in the development, manufacture, and distribution of products used for broadband Internet access, including "DOCSIS certified" data-over-cable equipment, digital subscriber line ("DSL") access and networking devices.

NOTE 2 BASIS OF PRESENTATION

The accompanying unaudited condensed consolidated financial statements have been prepared by the Company in accordance with the instructions to Form 10-Q and Article 10 of Regulation S-X relating to interim financial statements. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements and should be read in conjunction with the consolidated financial statements and notes thereto included in the Annual Report on Form 10-K of Lotus Pacific, Inc. for the year ended June 30, 2000 ("fiscal 2000").

In the opinion of management, all adjustments (consisting of normal recurring accruals) necessary to present fairly the information set forth in the accompanying condensed consolidated financial statements have been included. The results reported in these condensed consolidated financial statements for the six-month period ended December 31, 2000, should not be regarded as necessarily indicative of results that may be expected for the year ended June 30, 2001 ("fiscal 2001").

Edgar Filing: LOTUS PACIFIC INC - Form 10-Q

The accompanying unaudited condensed consolidated financial statements include the accounts of LPFC and its four majority-owned subsidiaries: Arescom, Inc. (81%), Correlant Communications, Inc. (64.7%), and Lotus World, Inc. (90.5%), and Regent Electronics Corp. (92.3% owned). The minority interests in the subsidiaries are reflected as such on the balance sheet in accordance with generally accepted accounting principles. All intercompany transactions have been eliminated in consolidation.

NOTE 3 INVENTORIES

As of December 31, 2000, inventories consist of the following:

| | |
|-----------------|--------------|
| Raw materials | --- |
| Work-in-process | --- |
| Finished goods | \$20,144,385 |
| | ----- |
| | \$20,144,385 |

The above inventory balances as of December 31, 2000 are net of reserves for potential excess quantities and obsolescence of approximately \$3,192,503.

NOTE 4 STOCK BASED COMPENSATION

The Company's subsidiary, Arescom, Inc. (Arescom), granted 550,000 Incentive Stock Options (ISOS) to employees during the six months ended December 31, 2000. Arescom recorded deferred compensation of \$1,100,000 and amortized deferred compensation of \$99,304. The amortization of deferred compensation for ISOS granted in the prior year is \$3,661,686.

The Company's subsidiary, Correlant Communications, Inc. (Correlant), also has an Incentive Stock Option Plan and it has elected to follow APB Opinion 25 "Accounting of Stock Issued to Employees" in accounting for its employee stock options. When calculating the deferred compensation, the options had to be split between Lotus shares and Correlant shares because the Lotus shares granted include a contingent component associated with the grant. The contingent component was that the shares of Lotus stock could be sold when certain financial goals were met. Lotus lifted the restriction during the six months and, accordingly, Correlant amortized all of the deferred compensation from the original grant date. The total amortization amounted to \$6.7 million. The amortization expense was charged to research and development, \$4.8 million and to general and administrative expense, \$1.3 million.

NOTE 5 INCOME TAXES

The Company's December 31, 2000 provision for income taxes differed from the amount computed by applying the statutory U.S. Federal income tax rate to income before income taxes and minority interest as follows:

| | |
|---|-----------|
| U.S. Federal income tax provision | |
| at Federal statutory rate | \$ 30,000 |
| Amortization of goodwill..... | 1,325,000 |
| Deferred compensation amortization.... | 3,661,500 |
| Minority Interest in subsidiaries..... | 195,000 |
| Equity in loss of unconsolidated subsidiaries | 400,000 |
| State income taxes net of federal income tax effect | 1,650,000 |
| Other..... | 261,007 |
| | ----- |

Edgar Filing: LOTUS PACIFIC INC - Form 10-Q

\$7,522,507
=====

NOTE 6 PREFERRED STOCK

During the six months ended December 31, 2000, Arescom sold preferred stock to third parties for net proceeds of \$13,257,500.

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

Lotus Pacific, Inc. ("LPFC") creates, manages, and operates communications and network technology companies. LPFC and its subsidiaries (the "Company") provide solutions for the communications and network technology markets. The Company is primarily engaged in the development, manufacture, and distribution of products used for broadband Internet access, including "DOCSIS certified" data-over-cable equipment, digital subscriber line ("DSL") access and networking devices.

RESULTS OF OPERATIONS

REVENUES

For the quarter ended December 31, 2000, the Company's revenue was \$105.6 million, compared with \$19.6 million for the same period of the previous year. Revenue in the first half of fiscal 2000 was \$205.6 million, an increase of 566% over the first two quarters of fiscal 1999. The revenue growth in the three- and six-month periods was primarily due to increases in sales by Correlant Communications, Inc. ("Correlant") and Arescom, Inc. ("Arescom"), which were acquired by LPFC in March 1999. For the three-month period ended December 31, 2000, Regent Electronics Corp. ("Regent") and Lotus World, Inc. ("Lotus World"), two subsidiaries of the Company, had insignificant operating revenues.

COST OF SALES

Cost of sales consisted principally of the cost of components, contracted manufacturing charges, other materials, in certain case labor related to testing and warranty expenses. The company outsourced substantially all of its manufacturing operation, and had no manufacturing plant. Cost of sales increased from \$14.8 million during the three-month period ended December 31, 1999 to \$93.9 million in the corresponding period ended December 31, 2000. Cost of sales increased from \$24.0 million during the six-month period ended December 31, 1999 to \$175.2 million in the corresponding period ended December 31, 2000. This increase in cost of sales reflected the increase level of sales. The gross margin were 11.2% and 14.8% for the three-month period and six-month period ended December 31, 2000, respectively. The Company expects that gross margin will fluctuate due to changing product mix, different sales prices, and product quantities shipped to various customers.

SELLING, GENERAL AND ADMINISTRATIVE EXPENSES

Selling, general and administrative expenses were \$8.9 million in the second quarter of fiscal 2000 compared to \$8.6 in the corresponding quarter of the prior year, a 4% increase. For the first two quarters of fiscal 2000, selling, general and administrative expenses were \$17.4 million, compared to \$14.8 million in the first two quarter of fiscal 1999, a 17.4% of increase. The

Edgar Filing: LOTUS PACIFIC INC - Form 10-Q

increase was primarily the result of increased staffing and growth in recruiting and facility related expenses.

RESEARCH AND DEVELOPMENT

In the second quarter of fiscal 2000, research and development expenses increased \$3.0 million to \$3.9 million, or 310%, from \$1.0 million in the same quarter of fiscal 1999. For the six-month period ended December 31, 2000, the Company's research and development expenses increased approximately 500% compared to the same period of the last year. The increase was primarily due to the growth of our research and development staff and consultants to support the commercial development of current and future products and nonrecurring engineering charges.

DEPRECIATION & GOODWILL AMORTIZATION

The Company has accumulated approximately \$75.7 million of goodwill from acquisitions of businesses since September 1997. For the six-month period ended December 31, 2000, the Company's depreciation and goodwill amortization expenses were approximately \$4.4 million, compared to \$5.7 million for the same period of the prior year.

NET LOSS AND LOSS PER SHARE

For the second quarter of fiscal 2001, the Company had a net loss of \$4.0 million, or \$0.06 per share, compared to \$4.8 million or \$0.07 per share of net loss for the same period of the prior year. The decrease in net loss was mainly due to the increase in sales revenue accompanied by relatively less increase in operating expenses. Excluding \$2.1 million of depreciation and goodwill amortization expenses, the net loss would be \$1.9 million, or \$0.03 per share.

For the six-month period ended December 31, 2000, the Company had a net loss of \$7.4 million, or \$0.12 per share, compared to \$9.0 million, or \$0.14 per share, of net loss for the same period of the prior year. Excluding \$4.4 million of depreciation and goodwill amortization expenses, the net loss would be \$3.0 million, or \$0.05 per share.

LIQUIDITY AND CAPITAL RESOURCES

As of December 31, 2000, the Company's liquid assets, consisting of cash and cash equivalents, totaled \$17.0 million, compared with \$27.9 million as of June 30, 2000.

For the six-month period ended December 31, 2000, net cash used by operating activities was \$27.2 million, compared with \$4.7 million used at the same period of the previous year. The increase in net cash used by operating activities was primarily due to the combination of substantial increase in accounts receivables, offset partially by the increase of accounts payable.

For the six-month period ended December 31, 2000, net cash provided by investing activities were \$11.8 million. The Company purchased \$1.4 million of equipment. Arescom, one of the Company's subsidiaries, sold preferred stock to third parties for net proceeds of \$13.3 million.

For the six-month period ended December 31, 2000, net cash provided by financial activities were \$4.4 million, primarily from decrease in loan receivable and proceeds from line of credit.

The Company has no material long-term debt.

The Company believes that existing cash and cash equivalents together with funds generated from operations will be sufficient to meet its operating and

Edgar Filing: LOTUS PACIFIC INC - Form 10-Q

investment requirements for the next 12 months. The Company's continuing operating and investing activities may nevertheless make it necessary or desirable that LPFC obtain additional financing, through loans or public or private offerings of its securities or securities of its subsidiaries. There can be no assurance that any additional financing will be available to the Company on commercially reasonable terms, if at all.

ITEM 3. Quantitative and Qualitative Disclosure about Market Risk

The Company has not entered into any transactions using derivative financial instruments or derivative commodity instruments and believes that its exposure to market risk associated with other financial instruments is not material.

PART II

OTHER INFORMATION

Item 1. Legal Proceedings

None

Item 2. Changes in Securities and Use of Proceeds

None

Item 3. Defaults by the Registrant on its Senior Securities

None

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

None

Item 5. Other Information

- a) On January 5, 2001, the Board of Directors of the Company appointed William G. Hu as Chief Executive Officer of the Company to succeed the late president, Jeremy Wang, and as Chairman of the Board of Directors of Acumen Technology, Inc. ("Acumen"), a wholly-owned subsidiary of the Company. Jeremy Wang, the late President of the Company, passed away in an accident in late December 2000.
- b) Due to scheduling conflicts, Mr. Kuan C. Tsai resigned as director of the Company in January 2001.

Edgar Filing: LOTUS PACIFIC INC - Form 10-Q

SIGNATURES

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

LOTUS PACIFIC, INC.

Date: February 15, 2001

By: /s/ William G. Hu

William G. Hu, Chief Executive Officer

By: /S/ David Li

David Li, Chief Financial Officer