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NICHOLAS FINANCIAL INC
Form 10QSB
November 14, 2001

UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, DC 20549

FORM 10-QSB

X QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE
SECURITIES ACT OF 1934 FOR THE PERIOD ENDED SEPTEMBER 30, 2001

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE
SECURITIES EXCHANGE ACT OF 1934 (NO FEE REQUIRED)

For the transition period from _____ to _____.

Commission file number: 0-26680

NICHOLAS FINANCIAL, INC.
(Exact name of registrant as specified in its Charter)

British Columbia, Canada	8736-3354
(State or Other Jurisdiction of	(I.R.S. Employer
Incorporation or Organization)	Identification No.)

2454 McMullen Booth Road, Building C	
Clearwater, Florida	33759
(Address of Principal Executive Offices)	(Zip Code)

(727) 726-0763
(Registrant's telephone number, including area code)

Not applicable
(Former name, former address and former fiscal year, if changed
since last report)

Indicate by check mark whether the registrant (1) has filed all
reports required to be filed by Section 13 and 15(d) of the
Securities Exchange Act of 1934 during the preceding 12 months
(or for such shorter periods that the Registrant was required to
file such reports), and (2) has been subject to such filing
requirements for the past 90 days. Yes X No ____.

As of October 31st, 2001 there were 4,980,560 shares of common
stock outstanding

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Nicholas Financial, Inc. Condensed Consolidated Balance Sheet (Unaudited)

	September 30 2001 -----
Assets	
Cash	\$ 39,539
Finance receivables, net	69,185,266
Accounts receivable	17,444
Prepaid expenses and other assets	696,498
Property and equipment, net	338,384

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Deferred income taxes	981,503

Total assets	\$71,258,634
	=====
Liabilities	
Line of credit	\$50,323,426
Notes payable - related party	268,008
Accounts payable	3,005,193
Derivatives	1,859,305
Deferred revenues	676,419

Total liabilities	56,132,351
Shareholders' equity	
Preferred stock, no par: 5,000,000 shares authorized; none issued and outstanding	-
Common stock, no par: 50,000,000 shares authorized; 4,980,860 shares issued and outstanding	4,365,780
Other comprehensive loss	(1,877,577)
Retained earnings	12,638,080

	15,126,283

Total liabilities and shareholders' equity	\$71,258,634
	=====
See accompanying notes.	

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Nicholas Financial, Inc. Condensed Consolidated Statements of Income (Unaudited)

	Three months ended September 30		Six months ended September 30	
	2001	2000	2001	2000

Revenue:				
Interest income on finance receivables	\$4,857,907	\$4,250,555	\$9,389,658	\$8,160,070
Sales	89,922	99,057	189,042	215,867

	4,947,829	4,349,612	9,578,700	8,375,937
Expenses:				
Cost of sales	19,873	19,771	43,562	45,628
Marketing	138,014	119,164	248,471	217,442
Administrative	1,798,052	1,545,740	3,482,578	3,069,876
Provision for credit losses	427,776	305,079	780,425	676,789
Depreciation and amortization	60,000	39,000	105,000	66,000
Interest expense	1,010,581	955,488	2,006,413	1,790,511

	3,454,296	2,984,242	6,666,449	5,866,246

Operating income before income taxes	1,493,533	1,365,370	2,912,251	2,509,691

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Income tax expense (benefit):				
Current	468,024	526,951	1,011,146	1,042,958
Deferred	95,000	-	89,583	(75,000)
	-----	-----	-----	-----
	563,024	526,951	1,100,729	967,958
	-----	-----	-----	-----
Net Income	\$930,509	\$838,419	\$1,811,522	\$1,541,733
	=====	=====	=====	=====
Earnings per share - basic	\$0.19	\$0.18	\$0.38	\$0.33
	=====	=====	=====	=====
Earnings per share - diluted	\$0.18	\$0.17	\$0.35	\$0.31
	=====	=====	=====	=====

See accompanying notes.

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Nicholas Financial, Inc. Condensed Consolidated Statements of Cash Flows (Unaudited)

	Six months ended September 30	
	2001	2000
	-----	-----
Operating activities		
Net income	\$1,811,522	\$1,541,733
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation of property and equipment	105,000	66,000
Provision for credit losses	780,425	676,789
Deferred income taxes	89,385	(75,000)
Changes in operating assets and liabilities:		
Accounts receivable	(2,976)	(2,014)
Prepaid expenses and other assets	(147,312)	(203,358)
Deferred revenues	64,690	58,431
Accounts payable	(30,583)	(165,198)
Income taxes payable	(93,819)	(9,043)
	-----	-----
Net cash provided by operating activities	2,576,332	1,888,340
Investing activities		
Increase in finance receivables, net of principal collected	(4,924,823)	(9,207,202)
Purchase of property and equipment	(109,625)	(101,595)
	-----	-----
Net cash used in investing activities	(5,034,448)	(9,308,797)
Financing activities		
Repayment of notes payable - related party	-	(200,000)
Net proceeds from line of credit	2,200,000	7,505,000
Issuance (repurchase) of common stock	64,488	(45,505)
	-----	-----

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Net cash provided by financing activities	2,264,488	7,259,495
	-----	-----
Net decrease in cash	(193,628)	(160,962)
Cash, beginning of period	233,167	259,183
	-----	-----
Cash, end of period	\$39,539	\$98,221
	=====	=====

See accompanying notes.

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Nicholas Financial, Inc.
Notes to the Condensed Consolidated Financial Statements
(Unaudited)

September 30, 2001

1. Basis of Presentation

The accompanying unaudited condensed consolidated financial statements of Nicholas Financial Inc (the "Company") have been prepared in accordance with accounting principles generally accepted in the United States for interim financial information and with the instructions to Form 10-QSB pursuant to the Securities and Exchange Act of 1934, as amended in Article 10 of Regulation SB, as amended. 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 September 30, 2001 are not necessarily indicative of the results that may be expected for the year ending March 31, 2002. For further information, refer to the consolidated financial statements and footnotes thereto included in the Company's Annual Report on Form 10-K for the year ended March 31, 2001.

2. Earnings Per Share

On August 8, 2001, the Company declared a two-for-one stock split in the form of a stock dividend payable on September 10, 2001 to shareholders of record as of the close of business on August 28, 2001. All applicable share and per share amounts in the accompanying unaudited financial statements have been retroactively adjusted to take into account the effect of this split.

Basic earnings per share excludes any dilutive effects of common stock equivalents such as options, warrants, and convertible securities. Diluted earnings per share includes the effects of dilutive options, warrants, and convertible securities. Basic and diluted earnings per share have been computed as follows:

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Nicholas Financial, Inc.
Notes to the Condensed Consolidated Financial Statements
(Unaudited)

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	Three months ended September 30,		Six months ended September 30,	
	2001	2000	2001	2000

Numerator:				
Numerator for basic earnings per share - Net income available to common stockholders	\$930,509	\$838,419	\$1,811,522	\$1,541,733
Effect of dilutive securities:				
Convertible debt	4,068	15,554	13,423	31,108

Numerator for dilutive earnings per share - income available to common stockholders after assumed conversions	\$934,577	\$853,973	\$1,824,945	\$1,572,841
Denominator:				
Denominator for basic earnings per share - weighted average shares	4,875,683	4,686,016	4,756,949	4,694,718
Effect of dilutive securities: (A)				
Employee stock options	307,967	112,420	264,676	126,644
Convertible debt	96,618	361,112	203,865	361,112

Denominator for diluted earnings per share - adjusted weighted-average shares and assumed conversions	5,280,268	5,159,548	5,225,490	5,182,474
=====				
Earnings per share - basic	\$0.19	\$0.18	\$0.38	\$0.33
=====				
Earnings per share - diluted	\$0.18	\$0.17	\$0.35	\$0.31
=====				

Footnote A:

The following options were outstanding but not included in the computation of diluted earnings per share because the exercise price was greater than the average market price of the common shares and, therefore, the effect would be antidilutive.

Options	-	35,500	-	35,500
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Finance receivables consist of automobile finance installment contracts and direct consumer loans and are detailed as follows:

Finance receivables, gross contract	\$109,777,221
Less:	
Unearned interest	(25,894,881)

	83,882,340
Nonrefundable dealer reserves	(10,755,104)
Allowance for credit losses	(3,941,970)

Finance receivables, net	\$69,185,266
	=====

The terms of the receivables range from 12 to 60 months and bear a weighted average effective interest rate of 24%.

4. Line of Credit

The Company has a \$75 million line of credit facility (the Line) which expires on November 30, 2002. Borrowings under the Line bear interest at the prime rate. The Company also has several LIBOR pricing options available. If the outstanding balance falls below \$10 million the Line bears interest at the prime rate plus 1.75%. Pledged as collateral for this credit facility are all of the assets of Nicholas Financial, Inc. and its subsidiaries.

5. Notes Payable - Related Party

Notes payable consisted of the following:

Note payable, unsecured, interest at 12%, principal and interest due through August 2002, at which time the entire principal balance is due.	268,008
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Nicholas Financial, Inc.
Notes to the Condensed Consolidated Financial Statements
(Unaudited)

6. Derivatives and Hedging

In June 1998, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards ("SFAS") No. 133, "Accounting for Derivative Instruments and Hedging Activities" ("SFAS 133"). This statement establishes requirements for accounting and reporting of derivative instruments and hedging activities. SFAS 133

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was updated by the issuance of SFAS No. 137, "Accounting for Derivative Instruments and Hedging Activities - Deferral of the Effective Date of SFAS No. 133" and SFAS No. 138 "Accounting for Certain Derivative Instruments and Certain Hedging Activities - amendment of FASB Statement No. 133." As amended, SFAS 133 establishes accounting and reporting standards for derivative instruments, including certain derivative instruments embedded in other contracts (collectively referred to as derivatives), and for hedging activities.

The Company adopted the provisions of SFAS 133, as amended by SFAS 137 and SFAS 138, on April 1, 2001, which require that all derivative instruments be recorded on the balance sheet at fair value. The estimated fair value of derivative financial instruments represents the amount required to enter into similar offsetting contracts with similar remaining maturities based on quoted market prices.

The Company utilizes interest rate swaps to manage its interest rate exposure. The swaps effectively convert a portion of the Company's floating rate debt to a fixed rate, more closely matching the interest rate characteristics of the Company's finance receivables. When entering into contracts intended by the Company to receive hedge accounting treatment, the Company formally designates and documents the financial instrument as a hedge of a specific underlying exposure, as well as the risk management objectives and strategies for undertaking the hedge transaction.

The Company has entered into the following cash-flow hedges:

On May 11, 1999 the Company entered into an interest rate swap with a notional amount of \$10 million at a fixed rate of 5.81%, maturing on May 24, 2002. On May 21, 1999 the Company entered into two interest rate swaps with notional amounts of \$5 million each, at fixed rates of 5.81% and 6.08%, maturing on May 24, 2001 and May 24, 2004, respectively.

On August 18, 1999 the Company terminated a \$5 million swap maturing on May 24, 2004 in exchange for \$52,000. In addition the Company entered into an interest rate swap with a notional amount of \$10 million at a fixed rate of 5.80%, maturing on August 1, 2003.

On May 17, 2000 the Company entered into an interest rate swap with a notional amount of \$10 million at a fixed rate of 6.87%, maturing on May 17, 2004.

On March 30, 2001 the Company entered into an interest rate swap with a notional amount of \$10 million at a fixed rate of 4.89%, maturing on March 30, 2003.

The Company has also entered into various interest rate option agreements with maturities through May 17, 2004.

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Nicholas Financial, Inc.
Notes to the Condensed Consolidated Financial Statements
(Unaudited)

For cash-flow hedge transactions, changes in the fair value of the derivative instrument are recorded as a component of other

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comprehensive income, and reclassified into earnings in the same period or periods during which earnings are affected by the variability of the cash flows of the hedged item. Any ineffective portion of a derivative instrument's change in fair value is immediately recognized in earnings.

In connection with the adoption of SFAS 133, the Company recorded the fair value of its derivatives as a liability totaling approximately (\$975k) on April 1, 2001. The fair value of such derivative was approximately (\$1.86m) as of September 30, 2001. The fair value of the options, approximately (\$37k), was accounted for in the consolidated statement of income as an increase to current period earnings.

7. Subsequent Events

On October 5, 2001 the Company entered into an interest rate swap with a notional amount of \$10 million at a fixed rate of 3.85%, maturing on October 5, 2004.

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Part I. Item 2

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Introduction

Consolidated net income increased for the three month period ended September 30, 2001 to \$930,509 from \$838,419 for the three month period ended September 30, 2000. Earnings were favorably impacted by an increase in the outstanding loan portfolio. The Company's NDS subsidiary did not contribute significantly to consolidated operations in the three month periods ended September 30, 2001 or 2000.

Consolidated net income increased for the six month period ended September 30, 2001 to \$1,811,522 from \$1,541,733 for the six month period ended September 30, 2001. Earnings were favorably impacted by an increase in the outstanding loan portfolio. The Company's NDS subsidiary did not contribute significantly to consolidated operations in the six month periods ended September 30, 2001 or 2000.

	Three Months Ended September 30		Six Months Ended September 30	
	2001	2000	2001	2000

Average Net Finance Receivables(1)	\$83,284,788	\$72,742,751	\$81,937,694	\$70,043,032
Average Indebtedness(2)	50,374,767	46,669,224	50,158,101	44,409,224
Total Interest Revenues	4,857,907	4,250,555	9,389,658	8,160,069
Interest Expense	1,010,581	955,488	2,006,413	1,790,511

Net Interest Income	3,847,326	3,295,067	7,383,245	6,369,558
Gross Portfolio Yield(3)	23.33%	23.37%	22.92%	23.30%

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Average Cost of Borrowed Funds (2)	8.02%	8.19%	8.00%	8.06%
Net Interest Spread (4)	15.31%	15.18%	14.92%	15.24%
Net Portfolio Yield (3)	18.48%	18.12%	18.02%	18.19%
Write-off to Liquidation (5)	9.37%	8.13%	8.38%	6.94%
Net Charge-Off Percentage (6)	8.24%	6.78%	7.30%	5.83%