HYDRON TECHNOLOGIES INC
Form 10-Q
May 15, 2001

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

FORM 10-Q

(Mark One)
[X] Quarterly Report Pursuant to Section 13 or 15 (d) of the Securities Exchange Act of 1934
For the Quarterly Period Ended: MARCH 31, 2001

or

[ ] Transition Report Pursuant to Section 13 or 15 (d) of the Securities Exchange Act of 1934 For the Period from _____ to _____

Commission File Number: 0-6333

HYDRON TECHNOLOGIES, INC.
(Exact name of Registrant as specified in its charter)

New York	13-1574215
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

1001 Yamato Road, Suite 403, Boca Raton, Florida	33431
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code: (561) 994-6191

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 [ ] No [X]

Number of shares of common stock outstanding as of April 25, 2001: 4,975,136

HYDRON TECHNOLOGIES, INC. AND SUBSIDIARIES

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HYDRON TECHNOLOGIES, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEETS

	MARCH 31, 2001	DECEMBER 31, 2000
	(Unaudited)	(Note)
ASSETS		
Current Assets		
Cash and cash equivalents	$ 132,954	$ 190,946
Trade accounts receivable	13,751	136,306
Inventories	1,444,345	1,489,396
Prepaid expenses and other current assets	24,236	39,619
Total current assets	1,615,286	1,856,267
Property and equipment, less accumulated depreciation of $958,982 and $931,232 at 2001 and 2000, respectively	83,252	111,002
Deposits	57,405	60,403
Deferred product costs, less accumulated amortization of $5,266,802 and $5,194,952 at 2001 and 2000, respectively	700,993	772,843
Total Assets	$ 2,456,936	$ 2,800,515
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities		

Accounts payable	$ 103,896	$ 194,791
Accrued liabilities	431,563	464,084
Total current liabilities	535,459	658,875
Commitments and contingencies	--	--
Shareholders' equity		
Common stock - $.01 par value 30,000,000 shares authorized; 5,035,336 shares issued; and 4,975,136 shares outstanding	50,353	50,353
Additional paid-in capital	19,501,837	19,501,837
Accumulated deficit	(17,191,555)	(16,971,392)
Treasury stock, at cost; 60,200 shares	(439,158)	(439,158)
Total Shareholders' equity	1,921,477	2,141,640
Total liabilities and shareholders equity	$ 2,456,936	$ 2,800,515

Note: The balance sheet at December 31. 2000 has been derived from the audited financial statements at that date but does not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements.

SEE NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS.

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HYDRON TECHNOLOGIES, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENT OF OPERATIONS
(Unaudited)

	THREE MONTHS ENDED MARCH 31	
	2001	2000
Net Sales	$ 329,693	$ 672,390
Cost of sales	55,607	216,316
Gross profits	274,086	456,074
Expenses		
Royalty expense	16,485	33,953
Research and development	15,379	18,150
Selling, general & administration	364,599	447,301
Depreciation & amortization	99,600	111,300
Total expenses	496,063	610,704
Operating loss	(221,977)	(154,630)
Interest income	1,814	6,176
Loss before income taxes	(220,163)	(148,454)

Income taxes expense	--	--
Net loss	$ (220,163)	$ (148,454)
Basic and diluted loss per share		
Net loss per common share	$ (0.04)	$ (0.03)

SEE NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS.

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HYDRON TECHNOLOGIES, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOW
(Unaudited)

	THREE MONTHS ENDED MARCH 31	
	2001	2000
OPERATING ACTIVITIES		
Net Loss	$ (220,163)	$ (148,454)
Adjustments to reconcile net loss to net cash used by operating activities		
Depreciation and amortization	99,600	111,300
Write-down of inventory		2,475
Change in operating assets and liabilities		
Trade accounts receivable	122,555	(37,848)
Inventories	45,051	(132,115)
Prepaid expenses and other current assets	15,383	36,985
Deposits	2,998	51,836
Accounts payable	(90,895)	(79,386)
Accrued liabilities	(32,521)	807
Net cash provided (used) by operating activities	(57,992)	(194,400)
INVESTING ACTIVITIES		
Net cash provided (used) by investing activities	--	--
FINANCING ACTIVITIES		
Net cash provided (used) by financing activities	--	--
Net increase (decrease) in cash and cash equivalents	(57,992)	(194,400)
Cash and cash equivalents at beginning of period	190,946	653,916

Cash and cash equivalents at end of period	$ 132,954	$ 459,516

SEE NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS.

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HYDRON TECHNOLOGIES, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

MARCH 31, 2001

NOTE A - BASIS OF PRESENTATION

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. 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 of Hydron Technologies, Inc. (the "Company"), all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for the three-month period ended March 31, 2001 are not necessarily indicative of the results that may be expected for the year ending December 31, 2001. 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 December 31, 2000.

NOTE B - INVENTORIES

Inventories consist of the following:

	MARCH 31, 2001	DECEMBER 31, 2000
Finished goods	$ 906,852	$ 869,082
Raw materials and components	537,493	620,314
	$ 1,444,345	$ 1,489,396

NOTE C - DISTRIBUTION

- Catalog Sales

In November 1996, Hydron Technologies, Inc. (the Company) opened a new channel of distribution for Hydron products with the launch of its proprietary Catalog. The Catalog provides information on new Hydron products, educates consumers on proper skin and hair care and facilitates re-ordering. The Company Orders are taken by phone, mail and through the redesigned Hydron website (www.hydron.com).

- Direct Response Television

Effective September 1, 1999, the Company entered into a marketing and distribution agreement (the "Home Shopping Agreement") with HSN that grants HSN an exclusive worldwide license to

HYDRON TECHNOLOGIES, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

MARCH 31, 2001

NOTE C - DISTRIBUTION (CONTINUED)

market and distribute certain of the Company's proprietary consumer products through various forms of electronic retailing. The Home Shopping Agreement also grants HSN a non-exclusive license to market Hydron products through all other methods of distribution in certain countries outside the United States.

Under the terms of the Home Shopping Agreement, HSN was required to make specified product purchases during the period ending 12 months following the date on which the products first aired on HSN's television programs. Should HSN have exceeded a certain threshold amount in retail sales of Hydron products to consumers during the first twelve months, it was required to make specified product purchases during the second 12 months following the date of the first airing. The term of the Home Shopping Agreement may be automatically renewed after the Initial Term (two years after date of the first airing) for an indefinite number of successive one-year periods, subject to HSN's achieving certain escalating threshold levels in product purchases. However, beginning in the third contract year, HSN will no longer be required to meet specified product purchases, except to maintain exclusivity.

The Company launched its products on HSN's television network on September 16, 1999. Hydron products have since been featured in "Hydron Skin Care Solutions" hours during 7 of the first 12 months of the Home Shopping Agreement. While HSN has not met its purchase commitment for the first 12 months and Hydron has not been on the domestic network since August of 2000, Management is continuing to work with HSN to re-establish Hydron's presence through their domestic network in 2001.

In November 2000 the Company also began marketing on HSE, the Spanish language subsidiary of HSN. Hydron has secured a two-year agreement with Home Shopping Espanol (HSE), a rapidly expanding division of Home Shopping, L.P., to air Hydron products on HSE's Spanish-language television shopping programming in the Untied States and internationally.

Although Management believes that there are other avenues for selling its products, including the Hydron catalog, the loss of HSN as a customer would have a material adverse effect on the Company's business.

The Company entered into a license agreement with QVC, Inc. in 1993 ("QVC License Agreement"), whereby QVC was granted exclusive rights to market and distribute the Company's proprietary consumer products using Hydron polymers in the Western Hemisphere. In 1996, the Company and QVC modified the QVC License Agreement ("Amended License Agreement"), whereby the Company reacquired certain retail marketing rights to the Hydron product line. Effective May 31, 1999, the

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

MARCH 31, 2001

NOTE C - DISTRIBUTION (CONTINUED)

Company terminated the Renegotiated License Agreement as a result of QVC's failure to satisfy the annual minimum product purchase requirements for the period ended May 31, 1999.

The Company continues to sell certain products to QVC, on a non-exclusive basis, so that QVC can resell these products to their customers who had previously purchased the products and wish to re-order Hydron products.

- Private Label Contracting

In March 2000 the Company signed a contract with a U.S. corporation to provide exclusive skin care products based on Hydron's patented formula technology. The product launch will include, facial moisturizers, skin treatment products and related prestige quality formulas. The contract has escalating minimums over three years to maintain exclusivity.

- International

The majority of the Company's products are currently sold in the United States. The Company entered an agreement in 1995 with an Australian-based health and beauty products distributor, Doctors Formula Pty. Ltd., to market Hydron products in retail salon stores and medical offices in Australia and New Zealand. The company also distributes dental products into Spain and, to a lesser extent, other countries.

HYDRON TECHNOLOGIES, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

MARCH 31, 2001

NOTE D - EARNINGS PER SHARE

The following table sets forth the computation of basic and diluted loss per share:

	THREE MONTHS ENDED MARCH 31,	
	2001	2000
Numerator:		
Net loss is both the numerator for basic loss per share (income available to common shareholders) and the numerator for diluted loss per share (income available to common shareholders after assumed conversions)	$ (220,163)	$ (148,454)

Denominator:		
Denominator for basic loss per share (weighted-average shares)	4,975,136	4,975,136
Effect of dilutive securities: Stock options and warrants	--	--
Denominator for dilutive loss per share (adjusted weighted-average)	4,975,136	4,975,136
Basic loss per share	$ (.04)	$ (.03)
Diluted loss per share	$ (.04)	$ (.03)

Options and warrants to purchase 552,500 shares of common stock were outstanding at March 31, 2001, but were not included in the computation of diluted earnings per share because the effect would be anti-dilutive to the net loss per share for the period.

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

BUSINESS

Hydron Technologies, Inc. markets a broad range of consumer and oral health care products using a moisture-attracting ingredient (the "Hydron(R) polymers"), and owns a non-prescription drug delivery system for topically applied pharmaceuticals, which uses such polymer. The Company holds U.S. and international patents on, what Management believes is the only known cosmetically acceptable method to suspend the Hydron polymer in a stable emulsion for use in personal care/cosmetic products. The Company has concentrated its sales and development activities primarily on the application of these biocompatible, hydrophilic polymers in various personal care/cosmetic products for consumers and, to a lesser extent; oral care products for dental professionals. The Company entered into a license agreement for supply of the polymer with National Patent Development Corp. ("National Patent"), which provides for reciprocal royalty payments based on the sale of certain of each party's products. The Company currently has thirty-nine individual products available (excluding shade variations) in the following product lines: skin care (22 products), hair care (7 products), bath and body (8 products) and sun care (2 products). Of the company's products, nine are classified Over-the-Counter (OTC) drug products.

The Company is developing other cosmetic/personal care and OTC drug products for consumers using Hydron polymers. The Company intends to continue to explore using its technology as a topical drug delivery system and would, when appropriate, either seek licensing arrangements with third parties, or develop and market proprietary products through its own efforts. Management believes that, because of their unique properties, products that utilize Hydron polymers have the potential for wide acceptance in consumer and professional health care markets. The Company is also developing other technology based and possibly patentable delivery systems that will expand its product line.

Management believes that the Company's Hydron product lines are unique and offer the following competitive benefits: the moisturizers self-adjust to match the skin's optimal pH balance soon after they are applied to the skin; they become

water-insoluble on the skin's surface, and unlike all other water-based cremes and lotions, are not removed by the skin's perspiration or plain water; they are oxygen-permeable, allowing the skin to breathe and leave no greasy after-feel. They do not emulsify the skin's natural moisturizing agents, as do conventional cremes and lotions; and they attract and hold water, creating a cushion of moisture on the skin's surface that promotes penetration of other beneficial product ingredients. The Company's products are dermatologist tested and approved for all skin types. Products for use around the eye area are also ophthalmologist tested and safe for contact lens wearers. Most of the Company's moisturizing products are based on the Company's patented emulsion system, which permits the product ingredients to deliver their intended benefits over an extended period of time and in a more efficient manner.

Hydron products had been marketed on QVC through regularly scheduled hour-long programs from April 1994 through May 1999 under licensing agreement. The Company continues to sell certain products to QVC, on a non-exclusive basis, so that QVC can resell these products to their customers who had previously purchased the products and wish to re-order Hydron products.

BUSINESS (CONTINUED)

Effective September 1, 1999, the Company entered into a marketing and distribution agreement (the "Home Shopping Agreement") with Home Shopping, L.P. (HSN) that grants HSN an exclusive worldwide license to market and distribute certain of the Company's proprietary consumer products through various forms of electronic retailing. The agreement established purchase commitments for the first twelve months. In subsequent years, minimum purchase levels are required in order for HSN to maintain its' exclusive rights. The Home Shopping Agreement also grants HSN a non-exclusive license to market Hydron products through all other methods of distribution in certain countries outside the United States.

The Company launched its products on HSN's domestic television network on September 16, 1999. Hydron products have since been featured in "Hydron Skin Care Solutions" shows. While HSN has not met its purchase commitment for the first 12 months and Hydron has not been on the domestic network since August of 2000, Management is continuing to work with HSN to re-establish Hydron's presence through their domestic network in 2001.

In November 2000 the Company also began marketing on HSE, the Spanish language subsidiary of HSN. Hydron has secured a two-year agreement with Home Shopping Espanol (HSE), a rapidly expanding division of Home Shopping, L.P., to air Hydron products on HSE's Spanish-language television shopping programming in the Untied States and internationally. Hydron has retained Charytin Goyco, a well-known Latin celebrity, as Spokesperson for the Latin American Market for the same two-year period. The HSE program has already expanded beyond the US border to include Puerto Rico. Further HSE international expansion into Mexico is anticipated in the first half of 2001.

In November 1996, the Company opened a new channel of distribution for Hydron products with the launch of its proprietary Catalog. This full color Catalog offers the Company's personal care products for sale directly to consumers. The Catalog also provides information on new Hydron products, educates consumers on proper skin and hair care and facilitates re-ordering. Catalog sales also include sales of products from the Hydron website (www.hydron.com) which was redesigned and re-launched in January 2001. The Company is currently exploring new ways to enhance Catalog sales and operations.

In March 2001, the Company announced that it signed a contract to provide a major international corporation with exclusive skin care products based on

Hydron's patented formula technology. The product line will include facial moisturizers, skin treatment products and related prestige quality formulas. The contract has escalating minimums totaling $1.5 million over three years to maintain exclusivity. The first order has been received with initial deliveries planned for Mid-2001.

On an international level, the Company is currently working with HSN's international subsidiary HSE to include its Spanish language show in the United States and Puerto Rico. It is anticipated HSE will eventually expand to Mexico, Latin America and South America. Management is also reviewing other opportunities to exploit its consumer products through various retail marketing and distribution methods in regions not covered under agreements with HSN. The company is currently talking with several overseas distributors regarding expansion of Hydron products to their respective markets.

BUSINESS (CONTINUED)

The majority of Hydron products are sold in connection with on-air marketing. Although Management believes that there are other avenues for selling the Company's products, including the Hydron Catalog, private label contracting and international distribution, the loss of HSN as a customer would have a material adverse effect on the Company's business. The Company has not decided what actions, if any, it plans to take under such circumstances.

RESULTS OF OPERATIONS

Net sales for the three months ended March 31, 2001 decreased $342,697 to $329,693, or 51%, from net sales of $672,390 for the three months ended March 31, 2000. Catalog net sales for the three months ended March 31, 2001 were $305,684; an increase of $76,103, or 33%, from catalog net sales of $229,581 for the three months ended March 31, 2000. The increase in catalog net sales was the result of a managed increase in catalog consumer promotion against the Company's in-house customer list and against new customers. The Company's database of customers was increased by over 30% in the first three months of 2001.

Non-catalog net sales, including all sales to HSN and QVC, for the three months ended March 31, 2001 were $24,009; a decrease of $418,800, or 95%, from $442,809 for the three months ended March 31, 2000. The decrease in 2001 was due to the lack of airtime on HSN, and order timing with QVC. Orders from QVC and HSE have been received subsequent to the quarter.

Approximately 7% and 66% of the Company's sales during the three months ended March 31, 2001 and 2000, respectively, were to electronic retailers.

The Company's overall gross profit margin was 83% for the three months ended March 31, 2001 and 68% for the three months ended March 31, 2000 consistent with the significant sales distribution shift from television to catalog. The gross profit margins on catalog sales were 85% and 84% for the three months ended March 31, 2001 and 2000, respectively. The gross profit margins on non-catalog sales were 59% and 61% for the three months ended March 31, 2001 and 2000, respectively. The decrease in non-catalog gross profit margin was the result of the mix of products sold.

Royalty expenses for the three months ended March 31, 2001 were $16,485, representing a decrease of $17,468, or 51%, from royalty expenses of $33,953 for the three months ended March 31, 2000. This decrease is commensurate with the decrease in sales. These expenses are related primarily to the Patent Agreement with National Patent and pertain to the use of the Hydron polymers as a formula ingredient for many of the Company's products.

Research and development ("R&D") expenses reflect the Company's efforts to identify new product opportunities, develop and package the products for commercial sale, perform appropriate efficacy and safety tests, and conduct consumer panel studies and focus groups. R&D expenses in the first quarter of Fiscal 2001 were $15,379, a decrease of $2,771, or 15%, from R&D expenses of $18,150 in the first quarter of Fiscal 2000. The amount of R&D expenses per year varies, depending on the nature of the

RESULTS OF OPERATIONS (CONTINUED)

development work during each year, as well as the number and type of products under development at such time.

Selling, general and administrative ("SG&A") expenses for the three months ended March 31, 2001 were $364,599, a decrease of $82,702, or 18%, from SG&A expenses of $447,301 for the three months ended March 31, 2000. The decrease in SG&A expenses was the result primarily of reduction of rents associated with warehousing and reduced consultant expenses.

Interest and investment income for the three months ended March 31, 2001 was $1,814, a decrease of $4,362, or 71%, from interest and investment income of $6,176 for the three months ended March 31, 2000. This decrease is due to lower cash balances as a result of the factors discussed above. The Company maintains a conservative investment strategy, deriving investment income primarily from U.S. Treasury securities.

The net loss for the three months ended March 31, 2001 was $220,163, as compared to a loss of $148,454 for the three months ended March 31, 2000. This increase in net loss was the result primarily of the factors discussed above.

LIQUIDITY AND FINANCIAL RESOURCES

The Company's working capital was approximately $1,079,827 at March 31, 2001, including cash and cash equivalents of approximately $132,954.

There were no investing activities during the three months ended March 31, 2001.

There were no financing activities during the three months ended March 31, 2001.

The Company has incurred significant losses over the past four years. The ability of the Company to continue, as a going concern is dependent on increasing sales and reducing operating expenses.

Management's plan to increase sales and reduce operating expenses includes several specific actions. Catalog sales will be emphasized since they have higher profit margins and represent markets that are growing more rapidly than the Company's traditional television market. Direct marketing techniques will be used to reach new and current consumers such as promotions mailed to targeted consumers, Web site specials, promotions to other Web site customers, and direct e-mail promotions to current customers. Management also plans to increase international expansion at a controlled level.

Based on the above plan and the Company's present cash position, the absence of any short or long term debt, arrangements with third parties for contractual manufacturing and R&D, and the Company's present business strategy, management believes that the Company has adequate resources to meet normal, recurring obligations, for at least the next twelve months, as they become due. Further, in view

LIQUIDITY AND FINANCIAL RESOURCES (CONTINUED)

of the payment terms in connection with sales to HSN, management does not anticipate any difficulty in financing foreseeable inventory requirements.

The Company does not have the financial resources to sustain a national advertising campaign to market its products in a conventional retail mode. In view of the foregoing, Management's strategy has been to enter into marketing, licensing and distribution agreements with third parties (such as HSN, QVC, private label agreements) which have greater financial resources than those of the Company and that can enhance the Company's product introductions with appropriate national marketing support programs.

The effect of inflation has not been significant upon either the operations or financial condition of the Company.

CAUTIONARY STATEMENT REGARDING FORWARD LOOKING STATEMENTS

The statements contained in this Report on Form 10-Q that are not purely historical are forward looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934, including statements regarding the Company's expectations, hopes, intentions, beliefs or strategies regarding the future. Forward-looking statements include the Company's liquidity, anticipated cash needs and availability, and the anticipated expense levels under the heading "Management's Discussion and Analysis of Financial Condition and Results of Operations." All forward looking statements included in this document are based on information available to the Company on the date of this Report, and the Company assumes no obligation to update any such forward looking statement. It is important to note the Company's actual results could differ materially from those expressed or implied in such forward-looking statements. You should also consult the Company's Annual Report on Form 10-K for the year ended December 31, 2000 as well as those factors listed from time to time in the Company's other reports filed with the Securities and Exchange Commission pursuant to the Securities Exchange Act of 1934 and the Securities Act of 1933.

PART II - OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

The Company is not a party to, and its property is not the subject of, any material pending legal proceedings.

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

None

SIGNATURES

Pursuant to the requirements 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.

HYDRON TECHNOLOGIES, INC.

BY: /s/ WILLIAM A. FAGOT

William A. Fagot
Chief Financial Officer

Dated: May 14, 2001