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NICHOLAS FINANCIAL INC
Form 10QSB
February 13, 2002

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 DECEMBER 31, 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 (State or Other Jurisdiction of Incorporation or Organization)	8736-3354 (I.R.S. Employer Identification No.)
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2454 McMullen Booth Road, Building C Clearwater, Florida (Address of Principal Executive Offices)	33759 (Zip Code)
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(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 January 31st, 2002 there were 4,980,860 shares of common stock outstanding

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Part I. Item 1

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

	December 31 2001 -----
Assets	
Cash	\$ 303,075
Finance receivables, net	70,780,073
Accounts receivable	13,147
Prepaid expenses and other assets	651,872
Property and equipment, net	284,656
Deferred income taxes	820,036

Total assets	\$72,852,859 =====

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Liabilities	
Line of credit	\$50,973,426
Notes payable - related party	491,281
Accounts payable	2,739,112
Derivatives	1,687,902
Deferred revenues	685,805

Total liabilities	56,577,526
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	4,374,025
Other comprehensive loss	(1,685,305)
Retained earnings	13,586,613

	16,275,333

Total liabilities and shareholders' equity	\$72,852,859
	=====

See accompanying notes.

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

	Three months ended		Nine months ended	
	December 31		December 31	
	2001	2000	2001	2000

Revenue:				
Interest income on finance receivables	\$4,923,210	\$4,329,865	\$14,312,868	\$12,489,935
Sales	85,852	90,744	274,894	306,611
	-----	-----	-----	-----
	5,009,062	4,420,609	14,587,762	12,796,546
Expenses:				
Cost of sales	15,932	19,857	59,494	65,485
Marketing	134,724	100,816	383,196	318,258
Administrative	1,846,227	1,554,953	5,328,805	4,624,829
Provision for credit losses	500,679	390,312	1,281,104	1,067,101
Depreciation and amortization	60,365	40,500	165,365	106,500
Interest expense	949,068	1,002,433	2,955,481	2,792,944
	-----	-----	-----	-----
	3,506,995	3,108,871	10,173,445	8,975,117
	-----	-----	-----	-----
Operating income before income taxes	1,502,067	1,311,738	4,414,317	3,821,429
Income tax expense (benefit):				
Current	392,265	504,182	1,403,411	1,547,140
Deferred	161,269	-	250,852	(75,000)
	-----	-----	-----	-----

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	553,534	504,182	1,654,263	1,472,140
Net Income	\$ 948,533	\$ 807,556	\$2,760,054	\$2,349,289
Earnings per share - basic	\$0.19	\$0.17	\$0.57	\$0.50
Earnings per share - diluted	\$0.18	\$0.16	\$0.53	\$0.46

See accompanying notes.

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

	Nine months ended December 31	
	2001	2000
Operating activities		
Net income	\$ 2,760,054	\$ 2,349,289
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation of property and equipment	165,365	106,500
Provision for credit losses	1,281,104	1,067,101
Deferred income taxes	250,852	(75,000)
Changes in operating assets and liabilities:		
Accounts receivable	1,321	2,896
Prepaid expenses and other assets	(102,686)	(247,393)
Deferred revenues	74,076	93,208
Accounts payable	(275,795)	(420,885)
Income taxes payable	(93,819)	15,139
Net cash provided by operating activities	4,060,472	2,890,855
Investing activities		
Increase in finance receivables, net of principal collected	(7,020,309)	(10,908,418)
Purchase of property and equipment	(116,262)	(129,594)
Net cash used in investing activities	(7,136,571)	(11,038,012)
Financing activities		
Issuance (repayment) of notes payable - related party	223,274	(200,000)
Net proceeds from line of credit	2,850,000	8,558,500
Issuance (repurchase) of common stock	72,733	(126,941)
Net cash provided by financing activities	3,146,007	8,231,559
Net increase in cash	69,908	84,402
Cash, beginning of period	233,167	259,183

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Cash, end of period	\$303,075	\$343,585
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See accompanying notes.

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

December 31, 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 nine months ended December 31, 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)

Three months ended		Nine months ended	
December 31,		December 31,	
2001	2000	2001	2000

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Numerator:

Numerator for basic earnings per share - Net income available to common stockholders	\$948,533	\$807,556	\$2,760,054	\$2,349,289
Effect of dilutive securities:				
Convertible debt	-	15,283	17,491	46,391

Numerator for dilutive earnings per share - income available to common stockholders after assumed conversions	\$948,533	\$822,839	\$2,777,545	\$2,395,680
	=====			
Denominator:				
Denominator for basic earnings per share - weighted average shares	4,980,860	4,668,940	4,831,586	4,686,124
Effect of dilutive securities: (A)				
Employee stock options	294,768	102,984	290,794	118,756
Convertible debt	-	355,612	135,910	359,278

Denominator for diluted earnings per share - adjusted weighted-average shares and assumed conversions	5,275,628	5,127,536	5,258,290	5,164,158
	=====			
Earnings per share - basic	\$0.19	\$0.17	\$0.57	\$0.50
	=====			
Earnings per share - diluted	\$0.18	\$0.16	\$0.53	\$0.46
	=====			

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	-	105,500	-	58,833
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Nicholas Financial, Inc.
Notes to the Condensed Consolidated Financial Statements
(Unaudited)

3. Finance Receivables

Finance receivables consist of automobile finance installment contracts and direct consumer loans and are detailed as follows:

Finance receivables, gross contract	\$111,884,862
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Less:	
Unearned interest	(26,388,932)

	85,495,930
Nonrefundable dealer reserves	(11,063,746)
Allowance for credit losses	(3,652,111)

Finance receivables, net	\$ 70,780,073
	=====

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 9.5%, principal and interest due through August 2002, at which time the entire principal balance is due.	491,281
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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 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

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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.

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.

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)

6. Derivatives and Hedging (continued)

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

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fair value of its derivatives as a liability totaling approximately (\$975k) on April 1, 2001. The fair value of such derivative was approximately (\$1.69m) as of December 31, 2001. The fair value of the options, approximately (\$2.6k), was accounted for in the consolidated statement of income as a decrease to current period earnings.

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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 December 31, 2001 to \$948,533 from \$807,556 for the three month period ended December 31, 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 December 31, 2001 or 2000.

Consolidated net income increased for the nine month period ended December 31, 2001 to \$2,760,054 from \$2,349,289 for the nine month period ended December 31, 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 nine month periods ended December 31, 2001 or 2000.

	Three Months Ended December 31		Nine Months Ended December 31	
	2001	2000	2001	2000
Average Net Finance Receivables (1)	\$84,882,208	\$74,852,495	\$82,919,199	\$71,646,186
Average Indebtedness(2)	50,611,434	47,689,890	50,271,434	45,502,779
Total Interest Revenues	4,923,210	4,329,865	14,312,868	12,489,935
Interest Expense	949,068	1,002,433	2,955,481	2,792,944
Net Interest Income	3,974,142	3,327,432	11,357,387	9,696,991
Gross Portfolio Yield(3)	23.20%	23.14%	23.01%	23.24%
Average Cost of Borrowed Funds(2)	7.50%	8.41%	7.84%	8.18%
Net Interest Spread(4)	15.70%	14.73%	15.17%	15.06%
Net Portfolio Yield(3)	18.73%	17.78%	18.26%	18.05%
Write-off to Liquidation(5)	10.06%	9.02%	8.97%	7.68%
Net Charge-Off Percentage(6)	9.10%	7.75%	7.92%	6.50%

