

Edgar Filing: GOLFGEAR INTERNATIONAL INC - Form 10QSB

GOLFGEAR INTERNATIONAL INC
Form 10QSB
August 20, 2003

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

FORM 10-QSB

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

For the Quarterly Period Ended June 30, 2003

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

For the transition period from _____ to _____

Commission File Number: 0-28007

GOLFGEAR INTERNATIONAL, INC.

(Exact name of small business issuer as specified in its charter)

Nevada

43-1627555

(State or other jurisdiction of incorporation or organization)

(I.R.S. Employer Identification Number)

5285 Industrial Drive, Huntington Beach, California 92649

(Address of principal executive offices)

(714) 899-4274

(Issuer's telephone number)

Not applicable

(Former name, former address and former fiscal year, if changed since last report.)

Check whether the issuer (1) filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the past 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

As of June 30, 2003, the Company had 37,569,154 shares of common stock issued and outstanding.

Transitional Small Business Disclosure Format: Yes No

Documents incorporated by reference: None.

Edgar Filing: GOLFGEAR INTERNATIONAL INC - Form 10QSB

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

Consolidated Balance Sheets - June 30, 2003 (Unaudited) and
December 31, 2002

Consolidated Statements of Operations (Unaudited) - Three Months
and Six Months Ended June 30, 2003 and 2002

Consolidated Statements of Cash Flows (Unaudited) - Six Months
Ended June 30, 2003 and 2002

Notes to Consolidated Financial Statements (Unaudited) - Three
Months and Six Months Ended June 30, 2003 and 2002

Item 2. Management's Discussion and Analysis or Plan of Operation

PART II. OTHER INFORMATION

Item 1 - Legal Proceedings

Item 2 - Securities

Item 3 - Defaults Upon Senior Securities

Item 4 - Submission of Matters to a Vote of Security Holders

Item 5 - Other Information

Item 6 - Exhibits and Reports on Form 8-K

SIGNATURES

EXHIBITS

2

GolfGear International, Inc. and Subsidiaries Consolidated Balance Sheets

	June 30, 2003	Dece
	-----	-----
ASSETS	(Unaudited)	
Current assets:		
Cash	\$ 2,728	\$
Accounts receivable, net of allowance for doubtful accounts of \$136,135 and \$99,079, respectively	213,067	
Inventories	546,699	
Prepaid expenses	1,550	
	-----	-----
Total current assets	764,044	
Property and equipment, net of accumulated depreciation	85,453	
Other assets:		
Patents and trademarks, net of accumulated amortization	83,419	
Deferred financing costs	118,747	
Prepaid marketing costs and other assets	610,002	

Edgar Filing: GOLFGEAR INTERNATIONAL INC - Form 10QSB

Total assets	\$ 1,661,665	\$

LIABILITIES AND STOCKHOLDERS' DEFICIT		
Current liabilities:		
Accounts payable and accrued expenses	\$ 1,019,413	\$
Accrued product warranties	119,925	
Accrued interest payable	172,674	
Bank line of credit	157,979	
Notes payable to stockholders	200,000	
Notes payable	83,177	
Convertible debentures	2,100,000	
Deferred licensing revenue	47,958	
Other current liabilities	1,600	

Total current liabilities	3,918,124	
Stockholders' deficit:		
Common stock, \$.001 par value; authorized - 50,000,000 shares; issued and outstanding - 37,569,154 shares and 34,856,154 shares, respectively	37,569	
Additional paid-in capital	13,061,699	
Common stock purchase receivable note	(958,839)	
Deferred compensation	(83,675)	
Accumulated deficit	(14,297,815)	

Total stockholders' deficit	(2,241,061)	

Total liabilities and stockholders' deficit	\$ 1,661,665	\$
=====		

See notes to consolidated financial statements.

GolfGear International, Inc. and Subsidiaries
Consolidated Statements of Operations (Unaudited)

	The Three Months Ended June 30,		The Six Months Ended June 30,	
	2003	2002	2003	2002
	-----	-----	-----	-----
SALES	\$ 643,257	\$ 386,066	\$ 1,176,404	\$ 763,846
COST OF GOODS SOLD	339,482	347,959	667,821	564,222
	-----	-----	-----	-----
GROSS PROFIT	303,775	38,107	508,583	199,624
	-----	-----	-----	-----
EXPENSES:				

Edgar Filing: GOLFGEAR INTERNATIONAL INC - Form 10QSB

Selling and marketing	118,259	160,119	308,210	273,458
Tour and pro contracts	17,792	9,795	39,026	18,666
Bad debt expense	19,298	11,582	37,055	22,915
General and administrative	434,249	352,207	818,933	574,109
Depreciation and amortization	17,127	16,474	36,635	29,884
	-----	-----	-----	-----
TOTAL EXPENSES	606,725	550,177	1,239,859	919,032
	-----	-----	-----	-----
NET LOSS FROM OPERATIONS	(302,950)	(512,070)	(731,278)	(719,408)
OTHER INCOME (EXPENSE):				
Gain on settlement of old AP	33,027	57,274	73,208	57,274
Interest income	6,874	6,712	13,751	6,712
Royalty income	20,093	-	32,192	-
Interest expense	(143,170)	(184,547)	(276,535)	(190,730)
Other Expenses	(2,058)	-	(2,058)	(26,769)
	-----	-----	-----	-----
NET LOSS	\$ (388,184)	\$ (632,631)	\$ (890,785)	\$ (872,921)
	=====	=====	=====	=====
LOSS PER COMMON SHARE -				
BASIC AND DILUTED	\$ (0.01)	\$ (0.02)	\$ (0.02)	\$ (0.03)
	=====	=====	=====	=====
WEIGHTED AVERAGE NUMBER OF COMMON				
SHARES OUTSTANDING - BASIC AND DILUTED	37,681,154	33,793,354	36,855,325	25,875,571
	=====	=====	=====	=====

See notes to consolidated financial statements.

4

Consolidated Statements of Cash Flows (Unaudited)

	June 30, 2003	June 30, 2002
	-----	-----
CASH FLOWS FROM OPERATING ACTIVITIES		
Net loss	\$ (890,785)	\$ (872,921)
Adjustments to reconcile net loss to net cash used in operating activities		
Depreciation and amortization	36,635	29,884
Accrued interest income	(13,675)	-
Amortization of deferred compensation	16,734	-
Amortization of deferred financing cost	172,018	28,670
Provision for bad debts	37,055	22,915
Gain on settlement of accounts payable	(73,208)	(57,274)
Amortization of beneficial conversion discount	-	147,053
Provision for obsolete inventory	-	93,680
Other	-	26,769
Changes in operating assets and liabilities:		
(Increase) decrease in:		
Accounts receivable	52,094	11,025
Inventories	(53,795)	(44,449)
Prepaid expenses	56,503	(21,059)
Prepaid marketing	(468)	(167,678)
Other	-	4,630

Edgar Filing: GOLFGEAR INTERNATIONAL INC - Form 10QSB

Increase (decrease) in:		
Accounts payable and accrued expenses	125,513	(222,249)
Income tax payable	-	(4,000)
Accrued product warranties	3,823	8,641
Accrued interest	83,225	4,850
Prepaid royalties	(27,042)	-
Other	-	(20,896)
NET CASH PROVIDED (USED) IN OPERATING ACTIVITIES	(475,373)	(1,032,409)
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchase of property and equipment	(6,252)	(22,924)
CASH FLOWS FROM FINANCING ACTIVITIES		
Proceeds from sale of common stock and exercise of warrants	280,250	200,025
Proceeds from sale of convertible debenture	-	2,040,000
Decrease in notes payable shareholders	-	(97,166)
Increase (decrease) in notes payable	-	(35,914)
Borrowings under bank line	1,071,819	-
Repayments of borrowings under bank line	(984,734)	(6,031)
Other	-	(29,934)
NET CASH PROVIDED (USED) BY FINANCING ACTIVITIES	367,335	2,070,980
CASH:		
NET INCREASE (DECREASE)	(114,290)	1,015,647
AT BEGINNING OF PERIOD	117,018	120,135
AT END OF PERIOD	\$ 2,728	\$ 1,135,782
Cash paid for interest	\$ 18,292	\$ 7,283
Cash paid for taxes	\$ -	\$ 6,643

See notes to consolidated financial statements.

GolfGear International, Inc. and Subsidiaries
Notes to Consolidated Financial Statements (Unaudited)
Three Months and Six Months Ended June 30, 2003 and 2002

1. BASIS OF PRESENTATION

The consolidated financial statements as of and for the three months and six months ended June 30, 2003 have been prepared assuming that the Company will continue as a going concern, which contemplates the realization of assets and the satisfaction of liabilities in the normal course of business. The carrying amounts of assets and liabilities presented in the consolidated financial statements do not purport to represent the realizable or settlement values. The Company has suffered recurring operating losses and requires additional financing to continue operations. For the three months and the six months ended June 30, 2003 the Company incurred losses from operations of \$302,950 and \$731,278 and a net loss of \$388,184 and \$890,785 respectively. The Company used cash in operating activities of \$475,373 and as of June 30, 2003 had a working capital deficit of \$3,154,080 and a stockholder's deficit of \$2,241,061. As a result of these factors, there is a substantial doubt about the Company's

Edgar Filing: GOLFGEAR INTERNATIONAL INC - Form 10QSB

ability to continue as a going concern.

The Company is attempting to increase revenues through various means, including expanding brands and product offerings, new marketing programs, and possibly direct marketing to customers, subject to the availability of operating working capital resources. To the extent that the Company is unable to increase revenues in 2003, the Company's liquidity and ability to continue to conduct operations may be impaired.

The Company will require additional capital to fund operating requirements. The Company is exploring various alternatives to raise this required capital, including convertible debentures, private infusion of equity and various collateralized debt instruments, but there can be no assurances that the Company will be successful in this regard. To the extent that the Company is unable to secure the capital necessary to fund its future cash requirements on a timely basis and/or under acceptable terms and conditions, the Company may have to substantially reduce its operations to a level consistent with its available working capital resources. The Company may also be required to consider a formal or informal restructuring or reorganization.

GolfGear International, Inc. and its subsidiaries (collectively, "GolfGear" or the "Company") designs, develops and markets golf clubs and related golf products.

2. INVENTORIES

6

Inventories consisted of the following:

	June 30, 2003	December 31, 2002	
	-----	-----	
	(unaudited)		
Component parts	\$ 326,926	\$ 189,616	
Finished goods	219,773	303,288	
	-----	-----	
	\$ 546,699	\$ 492,904	
	=====	=====	

3. BANK LINES OF CREDIT

The Company has a \$250,000 bank line collateralized by eligible accounts receivable. The line of credit matures on December 9, 2003 and bears interest at 28% annually. Interest is payable monthly. Outstanding borrowings at June 30, 2003 and December 31, 2002, were \$120,158 and \$26,253 respectively.

The Company also has an unsecured \$70,000 line of credit with another bank. Interest is payable monthly at a variable rate (10.25% at June 30, 2003). Outstanding borrowings at June 30, 2003 and December 31, 2002, were \$37,821 and \$44,641, respectively. This is a revolving line of credit with no maturity date personally guaranteed by the Company's Founder.

4. NOTES PAYABLE AND NOTES PAYABLE TO STOCKHOLDERS

Edgar Filing: GOLFGEAR INTERNATIONAL INC - Form 10QSB

Notes payable consisted of the following:

	June 30, 2003 -----	December 31, 2002 -----
	(unaudited)	
Notes payable to individuals, payable on demand plus interest at rates ranging from prime to 18%	\$ 83,177 =====	\$ 83,177 =====

On November 20, 2002 the Company entered into a loan agreement with Peter Pocklington, its Chairman and Chief Executive Officer whereby Mr. Pocklington loaned the Company \$200,000. As consideration for the loan the Company agreed to an amendment to a stock pledge agreement and released 9,029,518 shares of Common Stock held by the Company as security for payment of a promissory note due for Pocklington's purchase of 15,000,000 shares of Common Stock. The promissory note remains collateralized by 3,303,482 shares of Common Stock to secure the unpaid balance of the promissory note less the loan to the Company. The loan bears interest at 9 1/2% and was due on June 20, 2003. (See Note 7, Subsequent Events.) The Company's board of directors unanimously approved the transaction by written consent on November 20, 2002.

On June 6, 2002, GolfGear International, Inc. (the "Company") completed the sale of

7

\$2,100,000 of convertible debentures. The debentures are convertible into common stock at \$0.25 per share for a period of 12 months commencing 6 months after the initial sale of the debentures. The Company's patents, trademarks, and other intangible assets secured the debentures. For each share of common stock issued upon conversion of the debentures, 1 common stock purchase warrant will be issued, which will be exercisable for a period of 18 months at \$0.10 per share. The costs associated with the issuance of the Debentures have been capitalized and are being amortized over the 18 months. If the Debentures convert to equity prior to the 18-month term the unamortized portion will be debited to additional paid in capital. Pursuant to the terms as outlined above the balance of any debentures that do not convert to equity is due and payable December 6, 2003.

5. STOCKHOLDERS' EQUITY

During the six months ended June 30, 2003 the Company issued 2,800,000 shares of common stock for exercised warrants at \$0.10 per share. During the six months ended June 30, 2003 the Company issued 25,000 shares of common stock for exercised options at \$0.01 per share.

On June 28, 2003 the Company canceled 112,000 shares of common stock, which were originally issued in connection with the convertible debenture as a finders fee and recorded as a deferred financing cost. The deferred financing costs were being amortized over the life of the debenture. Net of the par value the balance of the deferred financing costs (\$24,489) was debited to additional paid in capital.

Edgar Filing: GOLFGEAR INTERNATIONAL INC - Form 10QSB

During the six months ended June 30, 2002 the Company canceled 100,000 shares issued to a former employee and issued 5,000 shares in consideration to the extension granted on a certain note payable.

On April 8, 2002, the Company entered into a stock purchase agreement (the "Agreement") with Wyngate Limited, a Jersey Limited Company ("Wyngate"), whereby Wyngate agreed to purchase 15,000,000 shares of the Company's Common Stock at \$0.075 per share for an aggregate purchase price of \$1,125,000. Of the purchase price, \$200,025 was paid upon execution of the Agreement and Wyngate executed a promissory note with interest at 2.88% per annum in favor of the Company for the balance of \$924,975. Pursuant to the promissory note, the balance is due and payable October 8, 2003.

On May 30, 2002, the Company entered into a settlement agreement and mutual general release (the "Settlement Agreement") with MC Corporation. The Settlement Agreement provided that the Company issue a total of 3,000,000 shares of common stock to MC Corporation, of which 2,450,330 shares have already been reflected as issued and outstanding in the Company's financial statements at December 31, 2001 and March 31, 2002. The additional 549,700 shares of common stock are reflected as issued and outstanding in the June 30 2002.

6. MAJOR CUSTOMER INFORMATION

During the three months and six months ended June 30, 2003, two customers accounted for 48.5% and 54.9% of total sales respectively. At June 30, 2003, three customers accounted

8

for \$157,785 (74%) of net accounts receivable. During the three months and six months ended June 30, 2002, one customer accounted for approximately 15.6% and 13.5% of total sales respectively. At June 30, 2002, no customers accounted for more than 8% of net accounts receivable.

7. SUBSEQUENT EVENTS

On July 17, 2003 Peter Pocklington, Wyngate Limited and Quincy Investments (the Parties) jointly and collectively entered into an agreement with the Company whereby the Parties paid the Company the amount of \$225,000 under an existing note (the Note) with the balance of the note due no later than December 5, 2003. Additionally the Parties converted the note due them for \$200,000 into a payment against the Note. The Company forgave \$150,000 of the Note in consideration for the Parties cancellation of their right to merge the Company with Meditron Medical, Inc., an option that they had acquired under the terms of their original investment.

8. CRITICAL ACCOUNTING POLICIES

Patents and Trademarks - Patents and trademarks are being amortized on the -----

straight-line method over the estimated useful life, which vary from two to 17 years. SFAS No. 142 requires companies to cease amortizing goodwill that exists at the date of adoption. SFAS No. 142 establishes a new method of testing intangible assets for impairment on an annual basis or an interim basis if an event occurs or circumstances change that would reduce the fair value of a reporting unit carrying value. The Company effectively adopted these standards as of January 1, 2002. No impairments were recorded in 2002.

Deferred Financing Costs - Deferred Financing Costs are amortized over the

Edgar Filing: GOLFGEAR INTERNATIONAL INC - Form 10QSB

life of the convertible debentures on the straight-line basis, which approximates the effective interest method due to the short maturity of the debentures.

Revenue Recognition - Revenue is recognized in accordance with SAB No. 101

"Revenue Recognition in Financial Statements". Sales of products are recognized when the products are shipped from the Company's facility. The Company generally provides a lifetime warranty against defects. The Company makes a provision for warranty costs in the period of sale. The Company periodically reviews the adequacy of the accrued product warranties.

Stock-Based Compensation - The Company periodically issues Common Stock

options and Common Stock purchase warrants to employees and non-employees in non-capital raising transactions for services rendered and to be rendered, and as financing costs.

The Company adopted Statement of Financial Accounting Standards ("SFAS) No. 123, "Accounting for Stock-Based Compensation", which establishes a fair value method of accounting for stock-based compensation plans.

The provisions of SFAS No. 123 allow companies to either expense the estimated fair value of stock options or to continue to follow the intrinsic value method set forth in Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees", but to disclose the pro forma effect on net loss and net loss per share had the fair value of the stock

9

options been exercised. The Company has elected to continue to account for stock-based compensation plans utilizing the intrinsic value method. Accordingly, compensation cost for stock options is measured as the excess, if any, of the fair market price of the Company's Common Stock at the date of grant above the amount an employee must pay to acquire the Common Stock.

In accordance with SFAS No. 123, the Company has provided footnote disclosure with respect to stock-based employee compensation. The cost of stock-based employee compensation is measured at the grant date based on the value of the award and is recognized over the vesting period. The value of the stock-based award is determined using the Black-Scholes option-pricing model whereby compensation cost is the excess of the fair value of the award as determined by the pricing model at the grant date or other measurement date above the amount an employee must pay to acquire the stock. The resulting amount is charged to expense on the straight-line basis over the period in which the Company expects to receive benefit, which is generally the vesting period. Stock options issued to non-employee directors at fair market value are accounted for under the intrinsic value method.

Prepaid Marketing Costs - Prepaid marketing costs are capitalized as

incurred then amortized to expense on a cost-pool-by-cost-pool basis over the period during which the future benefits are expected to be received.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OR PLAN OF OPERATION

Cautionary Statement Pursuant to Safe Harbor Provisions of the Private Securities Litigation Reform Act of 1995:

Edgar Filing: GOLFGEAR INTERNATIONAL INC - Form 10QSB

This Quarterly Report on Form 10-QSB for the quarterly period ended June 30, 2003 contains "forward-looking" statements within the meaning of Section 27A of the Securities Act of 1933, as amended, including statements that include the words "believes", "expects", "anticipates", or similar expressions. These forward-looking statements include, among others, statements concerning the Company's expectations regarding its working capital requirements, gross margin, results of operations, business, growth prospects, competition and other statements of expectations, beliefs, future plans and strategies, anticipated events or trends, and similar expressions concerning matters that are not historical facts. The forward-looking statements included in this Quarterly Report on Form 10-QSB for the quarterly period ended June 30, 2003 involve known and unknown risks, uncertainties and other factors that could cause the actual results, performance or achievements of the Company to differ materially from those expressed in or implied by the forward-looking statements contained herein.

Overview:

The consolidated financial statements as of and for the three months and six months ended June 30, 2003 have been prepared assuming that the Company will continue as a going concern, which contemplates the realization of assets and the satisfaction of liabilities in the normal course of business. The carrying amounts of assets and liabilities presented in the consolidated financial statements do not purport to represent the realizable or settlement

10

values. The Company has suffered recurring operating losses and requires additional financing to continue operations. For the three months and the six months ended June 30, 2003 the Company incurred losses from operations of \$302,950 and \$731,278 and a net loss of \$388,184 and \$890,785 respectively. The Company used cash in operating activities of \$475,373 and as of June 30, 2003 had a working capital deficit of \$3,154,080 and a stockholders deficit of \$2,241,061. As a result of these factors, there is a substantial doubt about the Company's ability to continue as a going concern.

The Company is attempting to increase revenues through various means, including expanding brands and product offerings, new marketing programs, and possibly direct marketing to customers, subject to the availability of operating working capital resources. To the extent that the Company is unable to increase revenues in 2003, the Company's liquidity and ability to continue to conduct operations may be impaired.

The Company will require additional capital to fund operating requirements. The Company is exploring various alternatives to raise this required capital, including convertible debentures, private infusion of equity and various collateralized debt instruments, but there can be no assurances that the Company will be successful in this regard. To the extent that the Company is unable to secure the capital necessary to fund its future cash requirements on a timely basis and/or under acceptable terms and conditions, the Company may have to substantially reduce its operations to a level consistent with its available working capital resources. The Company may also be required to consider a formal or informal restructuring or reorganization.

Results of Operations

Three Months ended June 30, 2003 and 2002 - (unaudited)

Edgar Filing: GOLFGEAR INTERNATIONAL INC - Form 10QSB

Net sales increased to \$643,257 in 2003 from \$386,066 in 2002, an increase of \$257,191 or 66.6%. The increase in net sales in 2003 as compared to 2002 is a result of the Company's new marketing efforts and the public acceptance/demand for the Company's new product line. In order to continue to increase sales, the Company will require additional capital to fund the increased sales and marketing activities, as well as increased inventory levels.

Gross profit increased to \$303,775 in 2003 from \$38,107 in 2002, an increase as a percentage of net sales to 47.2% in 2003 from 9.9% in 2002. In 2002, the gross profit would have been \$169,483 or 43.9% if it had not been for several factors including a 10% increase in freight-in expense a result of the lack of working capital and the Company's inability to take advantage of greater lead times. The Company also chose to write-down older inventory - a total of \$93,681 or 24% of the gross profit. This was done in anticipation of the introduction of new product preventing the Company from recovering its cost on the older inventory. In 2003, the Company reduced its wholesale prices and increased some key component costs while offering a new and improved product line.

Selling and marketing expenses decreased to \$118,259 in 2003 (18.4% of net sales) from \$160,119 in 2002 (41.5% of net sales), a decrease of \$41,860 or 26.1%. Selling and marketing expenses decreased in 2003 as compared to 2002 as a result of the Company

11

limiting its "new" marketing efforts in favor of focusing on the key customer accounts that have been responsible for the increased sales in 2003.

Tour and pro contract expenses increased to \$17,792 in 2003 (2.8% of net sales) from \$9,795 in 2002 (2.5% of net sales), an increase of \$7,997 or 81.6%. Tour and pro contract expenses increased in 2003 as compared to 2002 as the Company has entered into new obligations with nationally known golf professionals.

Bad debt expense increased to \$19,298 in 2003 from \$11,582 in 2002, an increase of \$7,716. Bad debt in these two periods was calculated as a percentage of sales - the increase in the bad debt expense is a reflection of the increase in sales.

General and administrative expenses increased to \$434,249 in 2003 (67.5% of net sales) from \$352,207 in 2002 (91.2% of net sales), an increase of \$82,042 (23.3%). The \$82,042 increases in general and administrative expenses is due to increase in salaries, insurance and legal expenses. The increases in salaries are due to new hires (President and SVP of Sales and Marketing). The increases in insurance are due to expanded coverage and all of the legal expenses were in the normal course of business.

Depreciation and amortization increased to \$17,127 in 2003 from \$16,474 in 2002, an increase of \$653 or 4.0%. The increase is a result of the acquisition of certain intangible and fixed assets.

Interest expense decreased to \$143,170 in 2003 from \$184,547 in 2002, a decrease of \$41,377 or 22.4%. This decrease is due to the settlement of prior outstanding notes payable.

Net loss was \$388,184 for the three months ended June 30, 2003, as compared to a net loss of \$632,631 for the three months ended June 30, 2002. The

Edgar Filing: GOLFGEAR INTERNATIONAL INC - Form 10QSB

primary reason for the decreased loss was the increase in sales and the overall increase in the gross profit.

Six Months ended June 30, 2003 and 2002 - (unaudited)

Net sales increased to \$1,176,404 in 2003 from \$763,846 in 2002, an increase of \$412,558 or 54.6%. The increase in net sales in 2003 as compared to 2002 is a result of the Company's new marketing efforts and the public acceptance/demand for the Company's new product line. In order to continue to increase sales, the Company will require additional capital to fund the increased sales and marketing activities, as well as increased inventory levels.

Gross profit increased to \$508,583 in 2003 from \$199,624 in 2002, an increase as a percentage of net sales to 43.2% in 2003 from 26.1% in 2002. In 2002 the gross profit would have been \$330,524 or 43.3% if it had not been for several factors including a 10% increase in freight-in expense a result of the lack of working capital and the Company's inability to take advantage of greater lead times. The Company also chose to write-down older inventory - a total of \$93,681 or 12% of the gross profit. This was done in anticipation of the introduction of new product preventing the Company from recovering its cost on the older inventory.

12

Selling and marketing expenses increased to \$308,210 in 2003 (26.2% of net sales) from \$273,458 in 2002 (35.8% of net sales), an increase of \$34,752 or 12.7% but an overall decrease as a percentage of sales of 9.6%. Selling and marketing expenses increased in 2003 as compared to 2002 as a result of the Company's continued efforts to increase sales in 2003. The Company has launched several new marketing programs offering promotional point of purchase displays, printed brochures, and other promotional materials, as well as a print advertisement campaign.

Tour and pro contract expenses increased to \$39,026 in 2003 (3.3% of net sales) from \$18,666 in 2002 (2.4% of net sales), an increase of \$20,360 or 109.1%. Tour and pro contract expenses increased in 2003 as compared to 2002 as the Company has entered into new obligations with nationally known golf professionals.

Bad debt expense increased to \$37,055 in 2003 from \$22,915 in 2002, an increase of \$14,140. Bad debt in these two periods was calculated as a percentage of sales - the increase in the bad debt expense is a reflection of the increase in sales.

General and administrative expenses increased to \$818,934 in 2003 (69.6% of net sales) from \$574,109 in 2002 (75.2% of net sales), an increase of \$244,825 (42.6%). The \$244,825 increases in general and administrative expenses is due to increase in salaries, insurance and legal expenses. The increases in salaries are due to new hires (President and SVP of Sales and Marketing). The increases in insurance are due to expanded coverage and all of the legal expenses were in the normal course of business.

Depreciation and amortization increased to \$36,635 in 2003 from \$29,884 in 2002, an increase of \$6,751 or 22.6%. The increase is a result of the acquisition of certain intangible and fixed assets.

Interest expense increased to \$276,535 in 2003 from \$190,730 in 2002, an increase of \$88,805 or 45.0%. The primary reason for the increase expense was the issuance of the convertible debentures including the amortization of the finder's fees. The convertible debentures were issued in June of

Edgar Filing: GOLFGEAR INTERNATIONAL INC - Form 10QSB

2002 and they bear interest at 7%. The sale of the debenture resulted in \$516,054 in capitalized financing costs. These costs are being amortized over the 18-month life of the debenture.

Net loss was \$890,785 for the six months ended June 30, 2003, as compared to a net loss of \$872,921 for the six months ended June 30, 2002. The primary reason for the decreased loss was the increase in sales and the overall increase in the gross profit.

Liquidity and Capital Resources - June 30, 2003:

The Company is attempting to increase revenues through various means, including expanding brands and product offerings, new marketing programs, and possibly direct marketing to customers, subject to the availability of operating working capital resources. To the extent that the Company is unable to increase revenues in 2003, the Company's liquidity and ability to continue to conduct operations may be impaired.

The Company will require substantial additional capital to fund operating requirements.

13

The Company is exploring various alternatives to raise this required capital, including convertible debentures, private infusion of equity and various collateralized debt instruments, but there can be no assurances that the Company will be successful in this regard. To the extent that the Company is unable to secure the capital necessary to fund its future cash requirements on a timely basis and/or under acceptable terms and conditions, the Company may have to substantially reduce its operations to a level consistent with its available working capital resources. The Company may also be required to consider a formal or informal restructuring or reorganization.

Operating Activities. The Company's operations utilized cash of \$475,373 during the six months ended June 30, 2003, as compared to utilizing cash of \$1,032,409 during the six months ended June 30, 2002. The decrease in cash utilized in operating activities in 2003 as compared to 2002 was primarily a result of the utilization of prepaid expenses, collections of receivables and an increase in accounts payable and accrued expenses. At June 30, 2003, cash has decreased to \$2,728 as compared to \$117,018 at December 31, 2002. The Company had a working capital deficit of \$2,855,263 at June 30, 2003, as compared to a working capital deficit of \$3,138,682 at December 31, 2002, reflecting current ratios of 0.20:1 and 0.26:1 at June 30, 2003 and December 31, 2002, respectively.

Investing Activities. During the six months ended June 30, 2003 and 2002, net cash used in investing activities for the purchase of property and equipment was \$6,252 and \$22,924, respectively.

Financing Activities. The Company received \$280,250 from the exercise of common stock warrants and options during the six months ended June 30, 2003.

The Company has a \$250,000 bank line collateralized by eligible accounts receivable. The line of credit matures on December 9, 2003 and bears interest at 28% annually. Interest is payable monthly. Outstanding borrowings at June 30, 2003 and December 31, 2002, were \$120,158 and \$26,253 respectively.

Edgar Filing: GOLFGEAR INTERNATIONAL INC - Form 10QSB

The Company also has an unsecured \$70,000 line of credit with another bank. Interest is payable monthly at a variable rate (10.25% at June 30, 2003). Outstanding borrowings at June 30, 2003 and December 31, 2002, were \$37,821 and \$44,641, respectively. This is a revolving line of credit with no maturity date personally guaranteed by the Company's Founder.

During the six months ended June 30, 2002, the Company repaid certain shareholders and directors \$97,166. During the six months ended June 30, 2001, the Company borrowed \$26,164 net of payments on short-term notes from its shareholders and directors. During the six months ended June 30, 2002 and 2001, the Company reduced its bank line of credit by \$6,031 and \$1,182, respectively.

On April 8, 2002, the Company entered into a stock purchase agreement (the "Agreement") with Wyngate Limited, a Jersey Limited Company ("Wyngate"), whereby Wyngate agreed to purchase 15,000,000 shares of the Company's common stock at \$0.075 per share for an aggregate purchase price of \$1,125,000. Of the purchase price, \$200,025 was paid upon execution of the Agreement and Wyngate executed a promissory note with interest at 2.88%

14

per annum in favor of the Company for the balance of \$924,975. Pursuant to the promissory note, the balance is due and payable October 8, 2003. The promissory note is secured pursuant to a stock pledge agreement which pledges 12,333,000 shares of the common stock, which shall be held by the Company as security for payment of the promissory note.

On June 6, 2002, GolfGear International, Inc. (the "Company") completed the sale of \$2,000,000 of convertible debentures. The debentures are convertible into common stock at \$0.25 per share for a period of twelve (12) months commencing six (6) months after the initial sale of the debentures. The Company may sell up to an additional \$2,000,000 of convertible debentures in the near future. As part of this financing, the Company issued 532,000 shares of its common stock as a finders fee.

New Accounting Pronouncements:

New Accounting Pronouncements - In July 2002, the FASB issued SFAS No. 146 which nullifies Emerging Issues Task Force Issue No. 94-3: "Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity (including Certain Costs Incurred in a Restructuring)". SFAS No. 146 requires that a liability be recognized for those costs only when the liability is incurred, that is, when it meets the definition of a liability in the FASB's conceptual framework. SFAS No. 146 also establishes fair value as the object for initial measurement of liabilities related to exit or disposal activities. SFAS No. 146 is effective for exit or disposal activities that are initiated after December 31, 2002, with earlier adoption encouraged. Management does not expect the adoption of SFAS No. 146 to have a material impact on the Company's financial position or results of operations.

In December 2002 the FASB issued SFAS No. 148, "Accounting for Stock-Based Compensation-Transaction and Disclosure." SFAS No. 148 amends SFAS No. 123 to provide alternative methods of transition for a voluntary change to the fair value based method of accounting for stock-based compensation. It also amends the disclosure requirements of SFAS No. 123. If an entity elects to adopt the recognition provisions of the fair value based method of accounting for stock-based compensation in a fiscal year beginning before December 16, 2003, that change in accounting principle shall be reported using either the (i) prospective method, (ii) the modified prospective

Edgar Filing: GOLFGEAR INTERNATIONAL INC - Form 10QSB

method, or (iii) the retroactive restatement method as defined in SFAS No. 148. SFAS No. 148 is effective for fiscal years ending after December 15, 2002. Since the Company has elected to continue accounting for stock-based compensation under APB No. 25, the adoption of SFAS no. 148 has had no impact to the Company's financial position or results of operations. The Company's financial statement disclosures have been designed to conform to the new disclosure requirements prescribed by SFAS No. 148.

ITEM 3. CONTROLS AND PROCEDURES

Our Chief Executive Officer and Chief Financial Officer (the "Certifying Officers") are responsible for establishing and maintaining disclosure controls and procedures for the Company. The Certifying Officers have designed such disclosure controls and procedures to ensure that material information is made known to them, particularly during the period in which this report was prepared. The Certifying Officers have evaluated the effectiveness of the Company's disclosure controls and procedures as of the end of the period covered by this

15

report and believe that the Company's disclosure controls and procedures are effective based on the required evaluation. During the period covered by this report, there were no changes in internal controls that materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

To the best knowledge of management, there are no litigation matters pending or threatened against the Company or any subsidiaries.

ITEM 2. CHANGES IN SECURITIES AND USE OF PROCEEDS

During the six months ended June 30, 2003 the Company issued 2,800,000 shares of common stock for exercised warrants at \$0.10 per share. During the six months ended June 30, 2003 the Company issued 25,000 shares of common stock for exercised options at \$0.01 per share.

On June 28, 2003 the Company canceled 112,000 shares of common stock, which were originally issued in connection with the convertible debenture as a finders fee and recorder as a deferred financing cost. The deferred financing costs were being amortized over the life of the debenture. Net of the par value the balance of the deferred financing costs (\$24,489) was debited to additional paid in capital.

During the six months ended June 30, 2002 the Company canceled 105,000 and issued 16,702 shares of its common stock. The 105,000 shares had been granted to but never issued to former employees. 15,000,000 shares of common stock was sold and issued to Wyngate Limited - details found elsewhere in this document. In connection with that sale of stock 1,072,000 shares were issued as a finder's fee. 550,000 shares of stock have been issued to MC Corporation as part of a settlement agreement - see legal proceedings. Effective June 30, 2002 75,000 shares were issued as part of a settlement of a certain debt and 5,000 shares in consideration for the extension granted on a certain note payable.

Edgar Filing: GOLFGEAR INTERNATIONAL INC - Form 10QSB

ITEM 3. DEFAULT UPON SENIOR SECURITIES

None.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

None.

ITEM 5. OTHER INFORMATION

None.

16

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

(a) Exhibits

- 31.1 Certification of Chief Executive Officer pursuant to Securities Exchange Act of 1934 (6)
- 31.2 Certification of Chief Financial Officer pursuant to Securities Exchange Act of 1934 (6)
- 32 Certification Pursuant to 18 U.S.C Section 1350, as adopted pursuant to section 906 of the Sarbanes-Oxley Act of 2002.

(b) Reports on Form 8-K - Three Months Ended March 31, 2003: None

SIGNATURES

In accordance with Section 13 or 15(d) of the Exchange Act, the registrant caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

GOLFGEAR INTERNATIONAL, INC.

(Registrant)

Date: August 19, 2003

By: /s/ John Pierandozzi

John Pierandozzi
Director, President
(Principal Executive Officer)

Date: August 19, 2003

By: /s/ Daniel C. Wright

Daniel C. Wright
Director, Chief Financial Officer
(Principal Financial Officer and
Principal Accounting Officer)

17