NEXT INC/TN
Form 10QSB
July 05, 2006

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-QSB

(Mark One)

[X]

Quarterly Report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the Quarterly Period Ended June 2, 2006

OR

[ ]

Transition Report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

Commission File Number: 0-25247

NEXT, INC.

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

Delaware	**95-4675095**

(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

7625 Hamilton Park Drive, Suite 12

Chattanooga, Tennessee 37421

(Address and zip code of principal executive offices)

Registrant s telephone number, including area code: **(423) 296-8213**

Check whether the issuer (1) filed all reports required by Section 13 or 15(d) of the Exchange Act during the past 12 months (as 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 [X] No [ ]

The number of shares of Registrant s common stock, par value $.001 per share, issued and outstanding as of July 4, 2006 was 18,372,740.

Transitional Small Business Disclosure Format (Check one): Yes [ ] No [X]

NEXT, INC.

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Part I FINANCIAL INFORMATION

Item 1.

Financial Statements

NEXT, INC.

CONDENSED CONSOLIDATED BALANCE SHEET

		June 2, 2006 (unaudited)
Assets		
Current assets:		
Cash	$	272,203
Accounts receivable, net		3,767,324
Notes receivable		37,662
Inventories		4,884,567
Prepaid expenses and other current assets		860,584
Deferred taxes, current		300,000
Total current assets		10,122,340

Property, plant and equipment, net		2,727,369
Goodwill		4,882,171
Notes receivable		51,211
Deferred taxes		431,894
Other assets, net		1,067,606
Total Assets	$	19,282,591

Liabilities and Stockholders Equity

Current liabilities:		
Accounts payable	$	1,033,301
Accrued expenses and other current liabilities		864,395
Short-term debt and current maturities		1,226,957
Loan from stockholders		500,000
Line of credit		4,906,263
Total current liabilities		8,530,916
Long-term debt, less current maturities		3,417,247
Total liabilities		11,948,163

Commitments and contingencies		
Stockholders equity		7,334,428
Total Liabilities and Stockholders Equity	$	19,282,591

The accompanying notes to the condensed consolidated financial statements are an integral part of these statements.

NEXT, INC.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

	Three Months Ended	
	May 31, 2005 (unaudited)	June 2, 2006 (unaudited)
Net sales	$ 4,695,583	$ 4,823,634
Cost of sales	3,468,469	3,000,633
Gross profit	1,227,114	1,823,001
General, administrative, and selling expenses	1,187,513	1,542,676
Operating income	39,601	280,325
Interest	(137,987)	(175,678)
Other income (expense)	13,894	(45,213)
Income (Loss) before income taxes	(84,492)	59,434
Provision (Benefit) for income taxes	(30,947)	36,538
Net income (loss)	(53,545)	22,896
Net income (loss) per share, basic and diluted	$	$
Weighted average shares outstanding, basic	18,604,188	18,309,795

Weighted average shares outstanding, diluted		18,604,188		18,483,201

	Six Months Ended			
	May 31, 2005 (unaudited)		June 2, 2006 (unaudited)	
Net sales	$	9,413,595	$	9,674,041
Cost of sales		6,719,175		6,637,146
Gross profit		2,694,420		3,036,895
General, administrative, and selling expenses		2,602,743		3,000,176
Operating income		91,677		36,719
Interest		(255,222)		(342,991)
Other income (expense)		36,555		(53,501)
Loss before income taxes		(126,990)		(359,773)
Benefit for income taxes		(44,076)		(131,035)
Net loss		(82,914)		(228,738)
Net loss per share, basic and diluted	$		$	(.01)

Weighted average shares outstanding, basic and diluted	17,891,389	18,409,257

The accompanying notes to the condensed consolidated financial statements are an integral part of these statements.

NEXT, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

	Six Months Ended	
	May 31, 2005 (unaudited)	June 2, 2006 (unaudited)
Cash flows from operating activities:		
Net loss	$ (82,915)	$ (228,738)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:		
Depreciation and amortization	320,252	373,329
Noncash compensation	15,187	1,011
Noncash fees	24,800	7,192
Loss on sale of asset		38,922
Bad debt expense	10,653	(24,927)
Deferred taxes	(44,076)	(131,034)
Changes in operating assets and liabilities:		
Accounts receivable	1,230,195	1,481,450
Notes receivable		20,264
Inventories	(2,465,138)	975,816
Prepaid expenses	(105,069)	(391,189)
Other assets	(101,306)	(23,690)

Accounts payable	(381,196)	(790,941)
Accrued expenses and other liabilities	913,388	(243,028)
Total adjustments	(582,310)	1,293,175
Net cash provided by (used in) operating activities	(665,225)	1,064,437
Cash flows from investing activities:		
Purchases of property, plant and equipment	(930,229)	(31,714)
Cash received from proceeds on sale of asset		2,700
Cash paid for acquisition costs	(100,000)	
Cash paid for intangible assets	(92,220)	(55,292)
Net cash used in investing activities	(1,122,449)	(84,306)
Cash flows from financing activities:		
Revolving credit facility, net	(969,308)	(1,620,698)
Proceeds from loans and notes payable	615,251	912,000
Repayments of long terms debt, loans and notes payable	(527,193)	(132,091)
Fees paid for investment transaction	(64,738)	(20,240)
Issuance of common stock for investment transaction	2,691,000	500

Issuance of preferred stock, net ..		650		
Net cash provided by (used in) financing activities		1,745,662		(860,529)
Net increase (decrease) in cash		(42,012)		119,602
Cash, beginning of period		312,216		152,601
Cash, end of period	$	270,204	$	272,203

Supplemental Information:				
Cash paid during the period for interest	$	269,218	$	346,578
Non-Cash Investing and Financing Activities:				
Equity securities retired in payment of note receivable	$		$	510,000
Equity securities retired to reduce vendor obligation	$		$	23,570
Equity securities issued to acquire customer list	$	77,500	$	

Equity securities retired for purchase of note	$ 122,400	$

The accompanying notes to the condensed consolidated financial statements are an integral part of these statements.

NEXT, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1.

Organization and Operations of Company

Next, Inc. (the Company) is the parent company of six wholly owned operating subsidiaries: (i) Next Marketing, Inc. (Next Marketing), (ii) Blue Sky Graphics, Inc. (Blue Sky), (iii) CMJ Ventures, Inc. (CMJ), (iv) Lil Fan, Inc. (Lil , (v) Choice International, Inc. (Choice), and (vi) S-2-S Acquisition Corporation (S-2-S). The Company is a creative and innovative sales and marketing organization that designs, develops, markets and distributes licensed products and imprinted sportswear primarily through key licensing agreements and the Company s own proprietary designs.

2.

Basis of Presentation and Summary of Significant Accounting Policies

Basis of Presentation

The condensed consolidated financial statements contained herein have been prepared in accordance with generally accepted accounting principles for interim financial statements, the instructions to Form 10-QSB and Item 310 of Regulation S-B. Accordingly, these financial statements do not include all the information and footnotes required by generally accepted accounting principles for annual financial statements. In addition, certain comparative figures presented have been reclassified to conform the prior year s data to the Company s current financial statements. In the opinion of management, the accompanying condensed consolidated financial statements contain all the adjustments necessary (consisting only of normal recurring accruals) to fairly present the financial position of the Company at June 2, 2006, and its results of operations and cash flows for the three and six months ended May 31, 2005 and June 2, 2006. Operating results for the three and six months ended June 2, 2006, are not necessarily indicative of the results that may be expected for the fiscal year ending December 1, 2006.

The Company determined on February 28, 2006 to change its fiscal year from a calendar year ending November 30, to a 52-53 week period ending on the Friday closest to November 30, and to use a 4-4-5 week basis for quarterly reporting. The Company s first quarter in 2006 covered the transition period for this change therefore falling on March 3, 2006. Fiscal year end results on Form 10-KSB will end on December 1, 2006 therefore causing a 366 day period for fiscal year ending 2006. The Company does not believe this will materially change the operating results, however it will help the flow of monthly reporting as cut-offs are planned on Fridays for inventory counts.

Principles of Consolidation

The accompanying unaudited condensed consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries. All significant inter-company balances and transactions have been eliminated.

Customer Base and Credit Concentration

The Company has developed a large, diverse, and distinguished customer base of traditional retailers that include national as well as large regional chains, specialty retailers, corporate accounts, college bookstores, motor sports, souvenir and gift shops, and golf shops. This expansion has been achieved through the acquisition of CMJ, Lil Fan, Choice, S-2-S, and their respective customer bases, the introduction of additional major product lines and distribution channels, such as the Motor Sports Division, which sells to a national auto dealer market consisting of approximately 9,000 potential customers, as well as expansion of its traditional national retail merchant customer base. In the three and six months ended June 2, 2006, sales to the Company s top four customers accounted for 80% and 69%, respectively, of total sales. The Company s management believes that the Company s credit risk exposure is limited based on current information available with respect to the financial strength of its customers and previously recorded reserves. Such estimates could change in the future.

The Company is subject to seasonality in its sales cycle due to the amount of college-licensed products. The seasonality of sales results in the majority of the Company s revenues being generated in the third and fourth quarters.

New Pronouncements

In November 2004, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) No, 151, Inventory Costs an amendment of ARB No. 43, Chapter 4. This statement clarifies the accounting for abnormal amounts of idle facility expense, freight, handling costs and spoilage. This statement also requires the allocation of fixed production overhead costs be based on normal production capacity. The provisions of SFAS No. 151 are effective for inventory costs incurred during the fiscal years beginning after June 15, 2005. The adoption of this statement did not have a material impact on the Company s consolidated financial statements.

In December 2004, the FASB issued FASB Statement No. 123 (revised 2004), Share-Based Payment, which is a revision of FASB Statement No. 123, Accounting for Stock-Based Compensation. Statement 123(R) supersedes APB Opinion No. 25, Accounting for Stock Issued to Employees, and amends FASB Statement No. 95, Statement of Cash Flows. The approach to accounting for share-based payments in Statement 123(R) is similar to the approach described in Statement 123. However, Statement 123(R) requires all share-based payments to employees, including grants of employee stock options, to be recognized in the financial statements based on their fair values and no longer allows pro forma disclosure as an alternative to financial statement recognition. The Company adopted Statement 123(R) at the beginning of its quarter ending March 3, 2006. The adoption of this statement did not have a material impact on the Company s consolidated financial statements.

In May 2005, the FASB issued SFAS No. 154, Accounting Changes and Error Corrections (SFAS No. 154), which replaces Accounting Principles Board (APB) No. 20 Accounting Changes , and SFAS No. 3 Reporting Accounting Changes in Interim Financial Statements . SFAS No. 154 changes the requirements for the accounting for and reporting of a change in accounting principle. The statement applies to all voluntary changes in accounting principle as well as changes required by an accounting pronouncement. SFAS No. 154 requires retrospective application to

prior periods financial statements of a voluntary change in accounting principle unless it is impracticable to determine the period-specific effects or the cumulative effect of the change. SFAS No. 154 is effective for accounting changes and corrections of errors made in fiscal years beginning after December 15, 2004. The adoption of SFAS No. 154 did not have a material impact on the Company s consolidated financial statements.

In March 2005, the FASB issued Interpretation No. 47, Accounting for Conditional Asset Retirement Obligations , an Interpretation of FASB Statement No. 143: (FIN 47), which clarifies the accounting for conditional asset retirement obligations as used in SFAS No. 143, Accounting for Asset Retirement Obligations . A conditional asset retirement obligation is an unconditional legal obligation to perform an asset retirement activity in which the timing and/or method of settlement are conditional on a future event that may or may not be within the control of the entity. Under FIN 47, an entity is required to recognize a liability for the fair value of a conditional asset retirement obligations if the fair value of the liability can be reasonably estimated. Any uncertainty about the amount and/or timing of future settlement should be factored into the measurement of the liability when sufficient information exists. FIN 47 also clarifies when an entity would have sufficient information to reasonably estimate the fair value. The provisions of FIN 47 are effective for fiscal years ending after December 15, 2005. The adoption of FIN 47 is not expected to have a material impact on the Company s consolidated financial statements.

3.

Inventories

Inventories are valued at the lower of cost or market. Cost is determined by the first-in, first-out method, and market represents the lower of replacement cost or net realizable value. Inventories as of June 2, 2006, consisted of the following:

Raw materials	$	3,393,339
Finished goods		1,491,228
	$	4,884,567

4.

Deferred and Income Taxes

Income taxes have been computed in accordance with SFAS No. 109, Accounting for Income Taxes. This standard requires, among other things, recognition of future tax expenses or benefits, measured using enacted tax rates,

attributable to taxable or deductible temporary differences between financial statements and income tax reporting bases of assets and liabilities.

The ultimate realization of deferred tax assets is dependent upon the attainment of forecasted results of operations. Management has taken these and other factors into consideration in recording the deferred tax estimate. The tax effects of temporary differences that give rise to significant portions of the deferred tax assets and liabilities at June 2, 2006, are as follows:

Assets:		
Accounts receivable allowance	$	25,327
Net operating loss carryforwards		1,090,577
Total deferred tax assets	$	1,115,904
Liabilities:		
Property, plant and equipment	$	270,854
Goodwill and other intangibles		113,156
Total deferred tax liabilities	$	384,010
Deferred taxes, net	$	731,894
Current	$	300,000
Noncurrent	$	431,894

5.

Short-Term and Long-Term Debt

Short-term and long-term debt at June 2, 2006 consisted of the following:

	Short Term	Long Term

Revolving credit facility	$	4,906,263	$	
Notes payable		1,726,957		3,417,247
Total	$	6,633,220	$	3,417,247

Various assets collateralize all of the Company s debt and certain amounts are guaranteed by its principal stockholders.

On May 31, 2006, the Company entered into an amendment with National City Bank to change the maturity date of the Company s credit facility from May 31, 2006 to July 15, 2006, and increase the interest rate from prime plus one-quarter point to prime plus one point from June 1 to June 30 and prime plus two points from July 1 to July 15. On April 25, 2006, the Company entered into an amendment with National City Bank to change the maturity date of the Company s credit facility from April 30, 2006 to May 31, 2006. The Company has signed a non-binding agreement with a new lender to replace National City and is in process of working out the respective due diligence and underwriting requirements.

On April 6, 2006, the Company entered into a Subscription Agreement for Convertible Notes and Warrants with the following investors: DKR Soundshore Oasis Holding Fund Ltd., Alpha Capital Aktiengesellschaft, Monarch Capital Fund, Ltd., Iroquois Master Fund, Ltd., and Bluegrass Growth Fund, LP (collectively, the Investors), pursuant to which the Company issued to the Investors, as a group, $984,960 in principal amount of convertible promissory notes (the Notes) and warrants (the Warrants) to purchase 849,103 shares of common stock of the Company (the Common Stock). The Notes require equal monthly payments of cash or stock in the amount of $86,184 over a 12-month period starting 115 days after closing and will be fully subordinated to the Company s senior lenders. The Notes are convertible into a total of 1,698,207 shares of Common Stock at a conversion rate of $.58 in principal amount of the Notes per share. The warrants have a three-year term and an exercise price of $.68 per share of Common Stock. The Company has filed a registration statement with the Securities and Exchange Commission for the offer and sale by the Investors of the Common Stock underlying both the Notes and Warrants. In connection with these transactions, the Company will issue to JPC Capital Partners, Inc., as placement agent, warrants to purchase 152,838 shares of Common Stock on the same terms as the Warrants issued to the Investors.

On February 8, 2006, the Company entered into an amendment with National City Bank to change the maturity date of the Company s credit facility from April 1, 2007 to April 30, 2006, and reduce the maximum availability under the revolving line of credit from $9,500,000 to $6,500,000. The effective date of the amendment was February 1, 2006. The reduced line of credit is in line with the Company s lower seasonal sales cycle for the first half of its fiscal year and does not reduce cash availability below the calculated borrowing base. Pursuant to the amendment, National City waives the Company s non-compliance with certain obligations and covenants of the credit facility.

Under the Company s credit facility agreement with National City Bank, the Company may draw up to the sum of 80% of eligible accounts receivable, as defined in the credit facility agreement, and 60% of eligible raw materials and eligible finished goods inventory, as defined in the credit facility agreement. In addition, the credit facility agreement provides for monthly payments of interest at a nationally published prime rate plus 1% (8.0% was the published rate at June 2, 2006). Accounts receivable, inventory, certain personal assets and personal guarantees of the Company s Chief Financial Officer and one board member collateralize the borrowings under the credit facility.

On September 30, 2005, the Company refinanced its credit facility for its main plant in Wabash, Indiana at First Federal Savings Bank of Wabash in the amount of $3,225,809, which paid off the original loan of $2,672,922 due in January 2006, the warehouse loan of $365,479, and an equipment loan of $155,469. These balances include accrued interest on the respective indebtedness. Also included in the refinancing were loan origination fees of $31,939. The new loan requires monthly principal and interest payments of $29,263, over a 5 year term at 7.0% interest.

On July 20, 2005, the Company entered into a subordinated loan agreement with Next Investors, LLC for $500,000. The purpose of this loan was to provide working capital to be repaid out of future cash flows. The loan has a 7.5% interest rate and maturity date of November 30, 2006. Next Investors, LLC principal partners are comprised of one officer and two directors of the Company. As of June 2, 2006, interest expensed and accrued for this loan totaled $9,479 and $19,167, respectively, for the three and six months then ended.

On February 24, 2005, the Company entered into a credit agreement with First Federal Savings Bank of Wabash to finance the purchase of a warehouse in the amount of $365,000. This loan was subsequently consolidated with the refinancing of the main plant in Wabash on September 30, 2005. The Company has renovated and consolidated all offsite inventories into this building which has reduced rental cost by $11,500 per month.

On February 11, 2005, the Company entered into a credit agreement for $250,500 with First Federal Savings Bank of Wabash for certain production equipment purchased in 2005. The Company is required to make principal and interest payments of $4,895 per month at an interest rate of 6.75%. The maturity date is June 24, 2010.

6.

Stockholders Equity

Stockholders equity was comprised of the following:

	At June 2, 2006 (unaudited)
	$ 18,333

Common stock, $.001 par value; 100,000,000 shares authorized, 18,332,740 shares issued and outstanding	
Additional paid-in capital	7,187,424
Retained earnings	157,488
Unearned compensation	(28,817)
Total stockholders equity	$ 7,334,428

At November 30, 2004, 1,000,000 shares were reserved for issuance under the Next, Inc. 2002 Stock Option Plan, in addition to the 1,000,000 previously reserved under the same plan. In 2004, the Company issued 286,500 employee options, 62,000 of which have been cancelled or forfeited, at $1.07 which have a five year expiration from the vesting date and are subject to forfeiture should the grantee fail to be employed by the Company on the vesting date. The options granted in 2004 were all issued at market value and as such no expense was recorded. In 2005, the Company issued 1,037,500 employee options, with 237,500 issued at $1.50 (19,750 of which have been cancelled or forfeited, with a five year expiration from the vesting date) and 800,000 issued at $0.85 (with a ten year expiration from the grant date). All options granted in 2005 were vested by the Board of Directors as of November 30, 2005. The options issued in 2005 were all issued at market value and as such no expense was recorded.

On January 12, 2006, the Company s former Chief Executive Officer, William B. Hensley, III, returned 500,000 shares of Next, Inc. common stock to satisfy a promissory note executed for $510,000 to purchase certain inventory items. These shares were cancelled and taken out of circulation. The transaction was valued at the market price of the stock on November 17, 2005, which was the date the shares were committed to be returned to the Company and validated by the execution of the Promissory Note.

On January 24, 2005, the Company entered into a Securities Purchase Agreement (the Agreement) with Bonanza Master Fund, Ltd. (Bonanza), MidSouth Investor Fund, L.P. (MidSouth) and Itasca Capital Partners LLC (Itasca and collectively with Bonanza and MidSouth, the Purchasers) and raised $2,990,000 in a private placement. None of the Purchasers has any other material relationship with the Company. Pursuant to the Agreement, the Company issued Bonanza 2,000,000 shares of its common stock and a warrant to purchase 1,000,000 shares, issued to MidSouth 250,000 shares and a warrant to purchase 125,000 shares, and issued to Itasca 50,000 shares and a warrant to purchase 25,000 shares. The shares were issued at $1.30 per share and the warrants are exercisable at $1.75 per share for five years. In addition, the Company has issued a warrant to purchase 115,000 shares of common stock to Dougherty & Company, LLC Investment Bankers for its services in connection with the private placement. The warrants are exercisable at $1.75 per share for five years, but the average closing price of the Company s common stock must be equal to at least $2.10 for ten consecutive trading days to exercise a purchase. The total offering price was $2,990,000 in cash, less fees of $299,000, for a net cash infusion of $2,691,000.

On January 21, 2005, The William B. and Cindy S. Hensley Family Limited Partnership (the Partnership) cancelled 80,000 shares of common stock and returned these shares to the Company for the purchase of a note issued to a former salesman. Mr. Hensley was the Chief Executive Officer of the Company and a related party. The transaction was valued at the market price or $122,400; the Partnership or its designee has the right to collect this note related to cash advances to a salesman in the amount of $121,861.

7.

Earnings (Loss) Per Share

The Company accounts for earnings (loss) per share (EPS) in accordance with SFAS No. 128, Earnings (Loss) Per Share. SFAS 128 requires the presentation of basic and fully diluted EPS. Basic and diluted EPS for the three and six months ended May 31, 2005 and June 2, 2006, are calculated on the basis of the weighted average number of common shares outstanding.

8.

Acquisition of Sports-2-Schools, LLC

Pursuant to the terms of an Asset Purchase Agreement (the Agreement), dated August 12, 2005, by and among S-2-S Acquisition Corporation, a Delaware corporation and wholly owned subsidiary of the Company, Sports-2-Schools, LLC., a Kentucky corporation, and Buck Swindle Associates; a Purchase Price Addendum Agreement dated August 12, 2005 by and among Allen Gaddis, Gaddco, Inc., S-2-S and the Company; and a Purchase Price Addendum agreement dated August 12, 2005 by and among Dr. Jim Ingram, S-2-S, and the Company , through its subsidiary S-2-S Acquisition Corporation, acquired certain assets of Sports-2-Schools, LLC, including a customer list, license agreements and a vendor number to a large retailer. The Company assumed $172,000 in debt as part of the transaction and also assumed $205,000 in payables owed the Company for merchandise. S-2-S is in the licensed sportswear business.

Consideration for the acquisition was: $50,000 in cash, 50,000 shares of the Company s common stock and up to an additional $575,000 worth of common stock, on a deferred basis (November 30, 2006, 2007, 2008) and $600,000 in cash both pursuant to a performance based earn-out arrangement. The financial terms of the transaction were determined by negotiation between representatives of the Company and Sports-2-Schools, LLC. The cash portion of the purchase price was funded from the Company s line of credit with National City Bank. The Company intends to continue to operate the business of S-2-S, after the acquisition through a new independent sales staff.

The S-2-S acquisition was made to expand the Company s distribution and customer base. Goodwill was acquired since management believes that the future value of the combined profit margins will be enhanced. The results of operations of S-2-S are included in the consolidated financial statement of the Company commencing August 12, 2005. The Company did not acquire any assets other than goodwill, customer list, license agreements, and a vendor number with a large retailer that is a new customer to the company.

Item 2.

Management s Discussion and Analysis or Plan of Operation.

You should read this section together with our condensed consolidated financial statements and related notes thereto included elsewhere in this report. In addition to the historical information contained herein, this report contains forward-looking statements that involve risks and uncertainties. Forward-looking statements are not based on historical information but relate to future operations, strategies, financial results or other developments. Forward-looking statements are necessarily based upon estimates and assumptions that are inherently subject to significant business, economic and competitive uncertainties and contingencies, many of which are beyond our control and many of which, with respect to future business decisions, are subject to change. Certain statements contained in this Form 10-QSB, including, without limitation, statements containing the words believe, anticipate, estimate, expect, are of the opinion that and words of similar import constitute forward-looking statements. You should not place any undue reliance on these forward-looking statements.

You should be aware that our actual growth and results could differ materially from those contained in the forward-looking statements due to a number of factors, which include, but are not limited to the following: the risks and uncertainties set forth below; economic and business conditions specific to the promotional products and imprinted sportswear industry; competition and the pricing and mix of products offered by us and our competitors; style changes and product acceptance; relations with and performance of suppliers; our ability to control costs and expenses; carry out successful designs and effectively communicate with our customers and to penetrate their chosen distribution channels; access to capital; foreign currency risks; risks associated with our entry into new markets or distribution channels; risks related to the timely performance of third parties, such as shipping companies, including risks of strikes or labor disputes involving these third parties; maintaining satisfactory relationships with our banking partners; political and trade relations; the overall level of consumer spending; global economic conditions and additional threatened terrorist attacks and responses thereto, including war. There may be other factors not mentioned above or included elsewhere in this report that may cause actual results to differ materially from any forward-looking information. You should not place undue reliance on these forward-looking statements. We assume no obligation to update any forward-looking statements as a result of new information, future events or developments, except as required by applicable securities laws.

Introduction

As noted elsewhere in this report, the Company s principal customers are large national and regional retailers. In order to maintain its relationship with these customers, enhance revenues from them and enable them to improve their revenues and margins, the Company must work closely with these customers to ensure they receive the Company s products expeditiously and economically. The Company works diligently to maintain what Management calls supply chain excellence a way for the Company to provide value added services to its customers.

In servicing its customers, the Company faces competition from numerous other providers of licensed promotional products. Many of these competitors are larger and better capitalized than the Company. Additionally, if the Company is to continue to grow its business by adding additional products and by making strategic acquisitions, it will require additional capital. Therefore, Management may enter into negotiations with sources of equity in an effort to furnish additional capital.

In assessing the Company s performance, Management focuses on (a) increasing revenues primarily through enhancing its licensing programs and (b) protecting such revenues by diversifying its customer bases regionally and

demographically. In order to enhance profitability, Management monitors and seeks to improve gross margins primarily by internal cost controls and through international purchases of raw materials. Management also strives to reduce fixed costs as a percentage of sales, improve inventory turnover and reduce receivables measured by day s sales outstanding, all in an effort to improve profitability and cash flow.

Overview

The Company is a creative and innovative sales and marketing organization that designs, develops, markets, and distributes licensed and branded promotional products and imprinted sportswear primarily through key licensing agreements as well as the Company s own proprietary brands. Management believes that there are substantial growth opportunities in the promotional products and imprinted sportswear industries. Management believes that the Company is well positioned to take advantage of such growth opportunities. Management believes that the Company has an excellent reputation in the marketplace as a result of its ability to provide quality products and services, on-time delivery, at competitive prices. In recent years, licensed imprinted sportswear has become very popular. Licensing agreements are available for branded products and services, amateur and professional sports teams, and many other promotional areas. To maximize its potential, the Company is continually expanding its license program, which currently includes the following:

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Approximately 200 licenses and agreements to distribute its **Cadre Athletic™**, and **Campus Traditions USA™** line for most major colleges and universities in the U.S.;

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Licensing agreements with **Chevy®**, **Pontiac®**, **Hummer®**, **Cadillac®**, **Dodge®**, **GMC®, Ford® Plymouth®**, **Jeep®**, and **Chrysler®** for their respective “branded” logos for the **RPM Sports USA™** motor sports line, targeting the automotive dealership network and automotive venue markets;

.

Licensing and distribution agreements with **Sturgis “Bike Rally”**, **Indianapolis Motor Speedway**, **Professional Bull Riders**, T**he 3 Stooges**, **Fellowship of Christian Athletics**, **Legendary Notre Dame Quarterbacks**, and **GRITS (Girls Raised in the South)**.

.

Proprietary brands including **American Biker™**, **American Wildlife™**, **Cadre™**, **Varsity Classics™,** and **Campus Traditions USA™,** among others.

Operations and Expansion

The Company is one of the significant companies in the highly fragmented licensed products and imprinted sportswear industries. The Company has implemented its strategy of The Total Solution Company to meet its customers key requirements including: art design and development, manufacturing (for imprinted sportswear), sourcing (for distributed products), warehousing and fulfillment. The Company has developed a large, diverse, and distinguished customer base of traditional retailers, ranging from national as well as large regional chains, specialty retailers, corporate accounts, college bookstores, motor sports, souvenir and gift shops, and golf shops.

The Company is actively engaged in discussions with various potential acquisition targets and plans to grow through strategic acquisitions of complementary businesses. The Company has embarked on an aggressive acquisition program that targets companies servicing other segments of the promotional products and imprinted sportswear industry not currently serviced by the Company. It is anticipated that such strategic acquisition targets will enable the Company to more effectively utilize its marketing and sales expertise, acquire the ability to cross-distribute its branded products and licenses throughout a wider distribution base, lessen its dependency on the seasonality of retail customers and reduce overall operating costs by consolidating its services and distribution facilities, to the extent feasible.

The Company has expanded its business to include e-commerce web sites through which some of the Company s most popular licensed products are marketed. The Company has been successful in establishing itself as a premier supplier under various e-commerce web sites, currently the most significant of which are www.campustraditionsusa.com™; www.rpmsportswearusa.com™; and www.americanbiker.com™. The Company plans to establish additional e-commerce web sites as other product lines are established. The corporate website, www.nextinc.net, provides information to the general public about the Company.

Results of Operations

The following table sets forth certain items in the Company s condensed consolidated statement of operations for the three and six months ended May 31, 2005 and June 2, 2006. These statements should be read in conjunction with the audited financial statements of the Company as filed in the Form 10-KSB.

	Three Months Ended		Six Months Ended	
	May 31, 2005 (unaudited)	June 2, 2006 (unaudited)	May 31, 2005 (unaudited)	June 2, 2006 (unaudited)
Net sales	$ 4,695,583	$ 4,823,634	$ 9,413,595	$ 9,674,041
Cost of sales	3,468,469	3,000,633	6,719,175	6,637,146
Gross profit	1,227,114	1,823,001	2,694,420	3,036,895
Operating and other expenses:				
General and administrative expenses	611,563	648,944	1,267,523	1,331,674
	391,221	639,736	887,088	1,163,593

Royalties, commissions, and selling expenses							
Corporate expenses		184,729		253,996		448,132		504,909
Interest expenses		137,987		175,678		255,222		342,991
Other (income) expenses		(13,894)		45,213		(36,555)		53,501
Total operating and other expense		1,311,606		1,763,567		2,821,410		3,396,668
Income (Loss), before income taxes		(84,492)		59,434		(126,990)		(359,773)
Provision (Benefit) for income taxes		(30,947)		36,538		(44,076)		(131,035)
Net income (loss)	$	(53,545)	$	22,896	$	(82,914)	$	(228,738)

Net Sales

Total net sales increased 2.7% to $4,823,634 for the three months ended June 2, 2006, from $4,695,583 for the three months ended May 31, 2005. The Company has concentrated on its core sales product lines during 2006 (Collegiate, Automotive, Wildlife, and American Biker) which grew 32.1% for the three months ended June 2, 2006 from the three months ended May 31, 2005. This excludes private label and corporate/promotional products sales which were $1,045,470 for the three months ended May 31, 2005, which the Company has eliminated, and therefore had no sales in the three months ended June 2, 2006. Total net sales increased 2.7% to $9,674,041 for the six months ended June 2, 2006 from $9,413,595 for the six months ended May 31, 2005, however core sales grew 17.9% for the comparative six month period. Management believes that future sales growth will continue primarily through the diversification and expansion of the Company s customer base and its expanded product offerings.

Cost of Sales

Cost of sales was 62.2% or $3,000,633 for the three months ended June 2, 2006, compared to 73.8% or $3,468,469 for the three months ended May 31, 2005. This decrease in cost relates to raw materials (garments) and reduced production cost. The Company reduced labor cost associated with art, maintenance, and embroidery departments in the second quarter of 2006. The areas associated with direct cost were re-organized for improved efficiencies. Cost of sales was 68.6 % for the six months ended June 2, 2006 compared to 71.3% for the six months ended May 31, 2005.

Expenses included in cost of sales were primarily raw materials, labor, supplies, contract services, and the depreciation of both the Company s principal manufacturing facility in Indiana and its equipment.

Gross Profit

Gross profit for the three months ended June 2, 2006, was $1,823,001 or 37.7% of net sales compared to $1,227,114 or 26.1% of net sales for the three months ended May 31, 2005. The increase in gross profit from 2005 relates to higher volume of licensed product sales, lower production cost, and lower garment cost. Management has done an extensive review of pricing models based on historical and future cost. The Company has also sought out new, more cost effective suppliers for import orders that should yield higher profit margins for the remainder of 2006 as new orders are released.

Operating and Other Expenses

General and administrative expenses were $648,944 (13.4 % of sales) for the three months ended June 2, 2006, compared to $611,563 (13.0 % of sales) for the three months ended May 31, 2005. The primary increases in cost related to shut down of the Noblesville and Columbia sales offices. General and administrative expenses were $1,331,675 (13.7% of sales) for the six months ended June 2, 2006 compared to $1,267,523 (13.4% of sales) for the six months ended May 31, 2005. The primary increase in expenses is related to reorganization expenses and freight cost. The Company terminated employees associated with sales, human resources, and accounting in the first and second quarters and absorbed the severance cost.

Royalty, commissions, and selling expenses were $639,736 (13.2% of sales) for the three months ended June 2, 2006, compared to $391,221 (8.3% of sales) for the three months ended May 31, 2005. The increase in expense was primarily related to a higher volume of licensed products sales which comprised $188,837 of the increase associated with royalty expense. The largest increase in licensed sales for the three months ended June 2, 2006 compared to the three months ended May 31, 2005 was in the automotive line, which increased by $1,160,845, thus increasing gross profit and royalty expense. Royalty, commissions, and selling expenses were $1,163,593 (12.0% of sales) for the six months ended June 2, 2006, compared to $887,088 (9.4% of sales) for the six months ended May 31, 2005. The increase again is primarily related to a higher mix of licensed products in 2006 from 2005, as royalty expense was up by $211,657.

Corporate expenses were $253,996 for the three months ended June 2, 2006, compared to $184,729 for the three months ended May 31, 2005. The increase in corporate expenses was in banking fees, professional fees, audit fees, and franchise taxes. Corporate expenses were $504,909 for the six months ended June 2, 2006, compared to $448,132 for the six months ended May 31, 2005. The increase in expense was in banking fees, wages, professional fees, and audit fees.

Interest expense relates to the Company s short and long-term debt. Interest expense was $175,678 for the three months ended June 2, 2006, compared to $137,987 for the three months ended May 31, 2005. The increase in interest expense is related to higher interest rates than previous year and increased debt outstanding during the period. Interest expense was $342,991 for the six months ended June 2, 2006 compared to $255,222 for the six months ended May 31, 2005; the increase relates to higher interest rates and increased debt outstanding during the period.

Other income/expense was $45,213 of expense for the three months ending June 2, 2006, as compared to other income of $13,894 for the three months ended May 31, 2005. The Company has received incentive payments from Wabash County in prior years based on staffing levels, however due to staff reductions the Company has not accrued this benefit during 2006. In the second quarter the Company vacated the leased facility in Noblesville, Indiana and wrote off the leasehold improvements of approximately $35,000. Other expense was $53,500 for the six months ended June 2, 2006 compared to other income of $36,555 for the six months ended May 31, 2005.

The provision for income taxes for the three months ended June 2, 2006, was $36,538, which is attributable to the Company s quarterly operating profit adjusted by book and income tax recognition of temporary differences. The benefit for income taxes for the three month period ended May 31, 2005, was $30,947, which related to the pre-tax loss and recognition of book and tax temporary differences. The benefit for income taxes for the six months ended June 2, 2006 was $131,035, compared to the benefit of $44,076 for the six months ended May 31, 2005. The change between the periods relates to the operating loss adjusted by book and income tax recognition temporary differences.

Financial Position, Capital Resources, and Liquidity June 2, 2006 and November 30, 2005

At June 2, 2006, working capital was $1,591,424 representing a decrease of $630,175 from working capital at November 30, 2005 of $2,221,599. The decrease in working capital was primarily due to the reduction in receivables and inventory from November 30, 2005. The reduction in receivables was due to more timely cash collections, which lowered the number of days in which a sale is outstanding, and the reduction in inventory was the result of management s plan to maximize cash flow by minimizing inventory on hand. The Company is subject to seasonality in its sales cycle due to the amount of college-licensed products. The seasonality of sales results in the majority of the Company s revenues being generated in the third and fourth quarters.

Liquidity and Capital Resources

The Company has historically financed its operations through a combination of earnings and debt. The Company s principal sources of debt financing are its revolving line of credit with National City Bank of Indiana and promissory notes issued by First Federal Savings Bank of Wabash. The credit facility has a maximum limit of $6,500,000 of which the Company has drawn $4,906,263 as of June 2, 2006. The credit facility matures on July 15, 2006. The Company is in process of replacing National City with a new senior lender and has signed a non-binding agreement subject to underwriting and legal agreements. The First Federal Savings Bank Promissory Notes consist primarily of one principal loan in the amount of $3,225,809 payable in monthly installments of $29,263 of principal and interest. The balance on this principal loan was $3,159,686 at June 2, 2006.

The Company s principal use of cash is for operating activities and working capital. Cash provided by operations in the six months ended June 2, 2006, was $1,064,437 as compared to $665,225 of cash used by operations for the six months ended May 31, 2005. The increase in cash provided related primarily to a reduction in accounts receivable and inventory, offset by a decrease in accounts payable and accrued expenses.

Cash used for investing activities was $84,306 for the six months ended June 2, 2006, compared to $1,122,449 for the six months ended May 31, 2005. The Company s investing activities during the period ending June 2, 2006 were for various intangible assets in the amount of $55,292, with minimal capital equipment purchases of $31,714.

Net cash used in financing activities was $860,529 for the six months ended June 2, 2006, compared to $1,745,662 of cash provided by financing activities for the six months ended May 31, 2005. The proceeds of common stock issued on January 24, 2005 of $2,691,000 was the primary net change in cash between the six months ending June 2, 2006, and May 31, 2005, however the Company did receive $912,000 in proceeds from a Subscription Agreement for Convertible Notes and Warrant from a group of inventors that closed on April 6, 2006.

On May 31, 2006, the Company entered into an amendment with National City Bank to change the maturity date of the Company s credit facility from May 31, 2006 to July 15, 2006, and increase the interest rate from prime plus one-quarter point to prime plus one point from June 1 to June 30 and prime plus two points from July 1 to July 15. On April 25, 2006, the Company entered into an amendment with National City Bank to change the maturity date of the Company s credit facility from April 30, 2006 to May 31, 2006. The Company has signed a non-binding agreement with a new lender to replace National City and is in process of working out the respective due diligence and underwriting requirements.

On April 6, 2006, the Company entered into a Subscription Agreement for Convertible Notes and Warrants with the following investors: DKR Soundshore Oasis Holding Fund Ltd., Alpha Capital Aktiengesellschaft, Monarch Capital Fund, Ltd., Iroquois Master Fund, Ltd., and Bluegrass Growth Fund, LP (collectively, the Investors), pursuant to which the Company issued to the Investors, as a group, $984,960 in principal amount of convertible promissory notes (the Notes) and warrants (the Warrants) to purchase 849,103 shares of common stock of the Company (the Common Stock). The Notes require equal monthly payments of cash or stock in the amount of $86,184 over a 12-month period starting 115 days after closing and will be fully subordinated to the Company s senior lenders. The Notes are convertible into a total of 1,698,207 shares of Common Stock at a conversion rate of $.58 in principal amount of the Notes per share. The warrants have a three-year term and an exercise price of $.68 per share of Common Stock. The Company has filed a registration statement with the Securities and Exchange Commission for the offer and sale by the Investors of the Common Stock underlying both the Notes and Warrants. In connection with these transactions, the Company will issue to JPC Capital Partners, Inc., as placement agent, warrants to purchase 152,838 shares of Common Stock on the same terms as the Warrants issued to the Investors.

On February 8, 2006, the Company entered into an amendment with National City Bank to change the maturity date of the Company s credit facility from April 1, 2007 to April 30, 2006, and reduce the maximum availability under the revolving line of credit from $9,500,000 to $6,500,000. The effective date of the amendment was February 1, 2006. The reduced line of credit is in line with the Company s lower seasonal sales cycle for the first quarter of its fiscal year and does not reduce cash availability below the calculated borrowing base. Pursuant to the amendment, National City waives the Company s non-compliance with certain obligations and covenants of the credit facility.

On August 12, 2005, the credit agreement between the Company and National City Bank of Indiana was amended to temporarily increase the Company s line of credit to $9,500,000, reduce limitations on advances based on eligible inventory, and increase the concentration limits for a specific national customer. On May 26, 2005, the credit agreement between the Company and National City Bank of Indiana was amended to increase the line of credit to $9,000,000 and extend the term thereof until April 1, 2007. The amendment to the line of credit allowed the Company to reduce the limitation on advances based on eligible inventory. The agreement provides for monthly payments of interest at a nationally published prime rate plus .25% (7.5% was the published rate at March 3, 2006). Accounts receivable, inventory, and certain personal assets and personal guarantees of one of the Company s directors and its Chief Financial Officer collateralize borrowings under the facility.

On January 24, 2005, the Company entered into a Securities Purchase Agreement (the Agreement) with Bonanza Master Fund, Ltd. (Bonanza), MidSouth Investor Fund, L.P. (MidSouth) and Itasca Capital Partners LLC (Itasca and collectively with Bonanza and Mid South, the Purchasers), and raised $2,990,000 in a private placement. None of the Purchasers has any other material relationship with the Company. Pursuant to the Agreement, the Company issued Bonanza 2,000,000 shares of its common stock and a warrant to purchase 1,000,000 shares of common stock, issued to MidSouth 250,000 shares and a warrant to purchase 125,000 shares of common stock, and issued to Itasca 50,000 shares and a warrant to purchase 25,000 shares of common stock. The shares of common stock were issued at $1.30 per share and the warrants are exercisable at $1.75 per share for five years. In addition, the Company has issued a warrant to purchase 115,000 shares of common stock to Dougherty & Company, LLC Investment Bankers for its services in connection with the private placement. The warrants are exercisable at $1.75 per share for five years, but the average closing price of the Company s common stock must be equal to at least $2.10 for ten consecutive trading days to exercise a purchase. The total offering price was $2,990,000 in cash, less fees of $299,000, for a net cash

infusion of $2,691,000.

Item 3. Controls and Procedures

Within the 90 days prior to the date of this report, the Company s management, including the Chief Executive Officer and the Chief Financial Officer carried out an evaluation of the effectiveness of the design and operation of the Company s disclosure controls and procedures pursuant to Exchange Act Rules 13a-14(c) and 15d-14(c). Based upon the evaluation, the Company s Chief Executive Officer and Chief Financial Officer concluded that the Company s disclosure controls and procedures are effective, in all material respects, to ensure that the information required to be disclosed in the Company s periodic SEC filings is recorded, processed, summarized and reported as and when required.

There have been no significant changes in the company s internal controls or in other factors that could significantly affect internal controls subsequent to the date the Chief Executive Officer and the Chief Financial Officer carried out this evaluation.

PART II OTHER INFORMATION

Item 1. Legal Proceedings

The Company has pending various minor legal actions arising in the normal course of business. Management does not believe that such legal actions, individually or in the aggregate, will have a material impact on the Company s business, financial condition or operating results.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

On April 6, 2006, the Company entered into a Subscription Agreement with the following investors: DKR Soundshore Oasis Holding Fund Ltd., Alpha Capital Aktiengesellschaft, Monarch Capital Fund, Ltd., Iroquois Master Fund, Ltd., and Bluegrass Growth Fund, LP (collectively, the Investors), pursuant to which the Company issued to the Investors, as a group, $984,960 in principal amount of convertible promissory notes (the Notes) and warrants (the Warrants) to purchase 849,103 shares of common stock of the Company (the Common Stock). The Notes require equal monthly payments of cash or stock in the amount of $86,184 over a 12-month period starting 115 days after closing and will be fully subordinated to the Company s senior lenders. The Notes are convertible into a total of 1,698,207 shares of Common Stock at a conversion rate of $.58 in principal amount of the Notes per share. The warrants have a three-year term and an exercise price of $.68 per share of Common Stock. The Company has filed a registration statement with the Securities and Exchange Commission for the offer and sale by the Investors of the Common Stock underlying both the Notes and Warrants. In connection with these transactions, the Company will issue to JPC Capital Partners, Inc., as placement agent, warrants to purchase 152,838 shares of Common Stock on the same terms as the Warrants issued to the Investors.

On January 24, 2005, the Company entered into a Securities Purchase Agreement with Bonanza Master Fund, Ltd., MidSouth Investor Fund, L.P., and Itasca Capital Partners LLC (collectively, the Purchasers) and raised $2,990,000 in a private placement. None of the Purchasers has any material relationship with the Company. Pursuant to the Securities Purchase Agreement, the Company issued Bonanza 2,000,000 shares of its common stock and a warrant to purchase 1,000,000 shares of common stock, issued to MidSouth 250,000 shares and a warrant to purchase 125,000

shares of common stock, and issued to Itasca 50,000 shares of common stock and a warrant to purchase 25,000 shares of common stock. The shares of common stock were issued at $1.30 per share and the warrants are exercisable at $1.75 per share for five years. In addition, the Company has issued a warrant to purchase 115,000 shares of common stock to Dougherty & Company, LLC Investment Bankers for its services in connection with the private placement. The warrants are exercisable at $1.75 per share for five years, but the average closing price of the Company s common stock must be equal to at least $2.10 for ten consecutive trading days to exercise a purchase. The total offering price was $2,990,000 in cash, less fees of $299,000, for a net cash infusion of $2,691,000.

Item 6. Exhibits and Reports on Form 8-K

(a)

The following documents are incorporated by reference as exhibits to this report:

Exhibit Number	Description
31.1	Section 302 Chief Executive Officer Certification.
31.2	Section 302 Chief Financial Officer Certification.
32	Section 906 Chief Executive Officer Certification and Chief Financial Officer Certification.

(b)

Reports of Form 8-K

(1) A report on Form 8-K dated May 30, 2006, reporting an Amendment to the Company s credit facility.

(2) A report on Form 8-K dated April 25, 2006, reporting an Amendment to the Company s credit facility.

(3) A report on Form 8-K dated April 17, 2006, reporting a press release announcing the Company s earnings for the three months ended March 3, 2006.

(4) A report on Form 8-K dated April 17, 2006, reporting a press release announcing a conference call to be held with interested stockholders.

(5) A report on Form 8-K dated April 7, 2006, reporting a Subscription Agreement with various investors.

SIGNATURES

In accordance with the requirements of the Securities and Exchange Act of 1934, the Registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

NEXT, INC.

July 5, 2006

By: /s/ Robert M. Budd

Robert M. Budd,

Chief Executive Officer

By: /s/ Charles L. Thompson

Charles L. Thompson,

Chief Financial Officer and

Principal Accounting Officer

EXHIBIT INDEX

(a)

The following documents are incorporated by reference as exhibits to this report:

Exhibit Number	Description
31.1	Section 302 Chief Executive Officer Certification.
31.2	Section 302 Chief Financial Officer Certification.
32	Section 906 Chief Executive Officer Certification and Chief Financial Officer Certification.