FEMALE HEALTH CO
Form 10QSB
February 14, 2003

U.S. SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-QSB

(MARK ONE)
[X] QUARTERLY REPORT UNDER SECTION 13 OR 15 (d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended December 31, 2002

[ ] TRANSITION REPORT UNDER SECTION 13 OR 15 (d) OF THE EXCHANGE ACT

For the transition period from _____ to _____

Commission File Number 0-18849

THE FEMALE HEALTH COMPANY
(Exact Name of Small Business Issuer as Specified in Its Charter)

Wisconsin	39-1144397
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification No.)

515 N. State Street, Suite 2225, Chicago, IL	60610
(Address of Principal Executive Offices)	(Zip Code)

(312) 595-9123
(Issuer's Telephone Number, Including Area Code)

Not applicable
(Former Name, Former Address and Former Fiscal Year, If Changed Since Last Report)

Check whether the issuer: (1) has 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 issuer was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

YES X NO

State the number of shares outstanding of each of the issuer's classes of common equity, as of the latest practical date:

Common Stock, $.01 Par Value - 18,898,901 shares outstanding as of February 10, 2003

Transitional Small Business Disclosure Format (check one):

Yes _____ No X

FORM 10-QSB

THE FEMALE HEALTH COMPANY AND SUBSIDIARIES

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CAUTIONARY STATEMENT REGARDING FORWARD LOOKING STATEMENTS

Certain statements included in this quarterly report on Form 10-QSB which are not statements of historical fact are intended to be, and are hereby identified as, "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995. The Company cautions readers that forward-looking statements involve known and unknown risks, uncertainties and other factors that may cause the actual results, performance or achievements of

the Company to be materially different from any future results, performance or achievement expressed or implied by such forward-looking statements. Such factors include, among others, the following: the Company's inability to secure adequate capital to fund operating losses, working capital requirements, advertising and promotional expenditures and principal and interest payments on debt obligations; factors related to increased competition from existing and new competitors including new product introduction, price reduction and increased spending on marketing; limitations on the Company's opportunities to enter into and/or renew agreements with international partners, the failure of the Company or its partners to successfully market, sell, and deliver its product in international markets, and risks inherent in doing business on an international level, such as laws governing medical devices that differ from those in the U.S., unexpected changes in the regulatory requirements, political risks, export restrictions, tariffs, and other trade barriers, and fluctuations in currency exchange rates; the disruption of production at the Company's manufacturing facility due to raw material shortages, labor shortages, and/or physical damage to the Company's facilities; the Company's inability to manage its growth and to adapt its administrative, operational and financial control systems to the needs of the expanded entity and the failure of management to anticipate, respond to and manage changing business conditions; the loss of the services of executive officers and other key employees and the Company's continued ability to attract and retain highly-skilled and qualified personnel; the costs and other effects of litigation, governmental investigations, legal and administrative cases and proceedings, settlements and investigations; and developments or assertions by or against the Company relating to intellectual property rights.

THE FEMALE HEALTH COMPANY AND SUBSIDIARIES
UNAUDITED CONDENSED CONSOLIDATED BALANCE SHEET

	DECEMBER 31, 2002
ASSETS	
Current Assets:	
Cash	$ 299,816
Accounts receivable, net	3,181,094
Inventories.	904,060
Prepaid expenses and other current assets.	223,583
TOTAL CURRENT ASSETS.	4,608,553
Certificate of Deposit.	93,208
Intellectual property rights, net	372,567
Other assets.	156,926
	622,701
PROPERTY, PLANT AND EQUIPMENT	4,170,622
Less accumulated depreciation and amortization.	(3,483,312)
Net property, plant, and equipment	687,310

TOTAL ASSETS.	$ 5,918,564
LIABILITIES AND STOCKHOLDERS' EQUITY	
Current Liabilities:	
Note payable, related party, net of unamortized discount	$ 922,051
Accounts payable	905,125
Accrued expenses and other current liabilities	678,085
Current maturities of obligations under capital leases	25,159
Preferred dividends payable.	10,250
TOTAL CURRENT LIABILITIES	2,540,670
Note payable, bank, net of unamortized discount.	1,017,034
Obligations under capital leases	47,953
Convertible debentures	250,000
Deferred gain on sale of facility.	1,283,484
TOTAL LIABILITIES	5,139,141
STOCKHOLDERS' EQUITY:	
Convertible preferred stock.	560
Common stock	185,827
Additional paid-in-capital	55,353,700
Unearned consulting compensation	(237,980)
Deferred Compensation.	(380,077)
Accumulated deficit.	(54,406,417)
Accumulated other comprehensive income	295,886
Treasury stock, at cost.	(32,076)
TOTAL STOCKHOLDERS' EQUITY.	779,423
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY.	$ 5,918,564

See notes to unaudited condensed consolidated financial statements.

THE FEMALE HEALTH COMPANY AND SUBSIDIARIES
UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

	Three Months Ended December 31,	
	2002	2001
Net revenues	$ 2,243,940	$ 1,670,171
Cost of products sold.	1,265,298	1,070,334
Gross profit	978,642	599,837

Advertising & promotion.	15,938	10,941
Selling, general and administrative.	873,623	735,818
Stock compensation	323,973	19,608
Total operating expenses	1,213,534	766,367
Operating (loss)	(234,892)	(166,530)
Interest, net and other expense.	248,594	189,760
Loss before income taxes	(483,486)	(356,290)
Provision for income taxes	-	-
Net loss	(483,486)	(356,290)
Preferred dividends, Series 1.	3,048	33,271
Net (loss) attributable to common stockholders	$ (486,534)	$ (389,561)
Net (loss) per common share outstanding.	$ (0.03)	$ (0.02)
Weighted average common shares outstanding	18,312,885	15,866,837

See notes to unaudited condensed consolidated financial statements.

THE FEMALE HEALTH COMPANY AND SUBSIDIARIES
UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

	Three Months Ended December 31, 2002	2001
OPERATIONS:		
Net (loss)	$(483,486)	$(356,290
Adjustment for noncash items:		
Depreciation and amortization	127,239	121,012
Interest added to certificate of deposit.	1,208	1,378
Amortization of discounts on notes payable.	159,190	111,557
Amortization of unearned consulting fees.	106,033	19,608
Stock compensation	217,940	---
Changes in operating assets and liabilities	(276,502)	(24,466
Net cash (used in) operating activities.	(148,378)	(127,201
INVESTING ACTIVITIES:		
Net cash (used in)investing activities, capital expenditures.	(15,107)	(11,637
FINANCING ACTIVITIES:		
Proceeds from note payable, bank	-	400,000

Dividends paid on preferred stock.	(97,194)	(95,816
Payments on capital lease obligations.	(6,134)	-
Proceeds from issuance of common stock	-	60,000
Net cash (used in) provided by financing activities.	(103,328)	364,184
Effect of exchange rate changes on cash.	7,986	(5,325
(DECREASE)INCREASE IN CASH	(258,827)	220,021
Cash at beginning of period.	558,643	469,406
CASH AT END OF PERIOD.	$ 299,816	$ 689,427

Schedule of noncash financing and investing activities:		
Common stock issued for payment of preferred stock dividends and convertible debenture interest.	$ 40,777	$ 48,600
Common stock issued for conversion of convertible debentures	200,000	-
Preferred dividends declared, Series 1	3,048	33,271

See notes to unaudited condensed consolidated financial statements.

THE FEMALE HEALTH COMPANY AND SUBSIDIARIES
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 - Basis of Presentation

The accompanying financial statements are unaudited but in the opinion of management contain all the adjustments (consisting of those of a normal recurring nature) considered necessary to present fairly the financial position and the results of operations and cash flow for the periods presented in conformity with generally accepted accounting principles for interim financial information and the instructions to Form 10-QSB and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements.

Operating results for the three months ended December 31, 2002 are not necessarily indicative of the results that may be expected for the fiscal year ending September 30, 2003. For further information, refer to the consolidated financial statements and footnotes thereto included in the Company's annual report on Form 10-KSB for the fiscal year ended September 30, 2002.

Principles of consolidation and nature of operations:

The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries, The Female Health Company - UK and The Female Health Company - UK, plc. All significant intercompany transactions and accounts have been eliminated in consolidation. The Female Health Company ("FHC" or the "Company") is currently engaged in the marketing, manufacture and distribution of a consumer health care product known as the female condom, "FC," in the U.S. and "femidom", "femy" and "the female condom" outside the U.S. The Female Health Company - UK, is the holding company of The Female Health Company - UK, plc, which operates a 40,000 sq. ft. leased manufacturing facility located in London, England.

Stock-Based compensation:

The Company accounts for its stock-based compensation plans under the recognition and measurement principles of APB Opinion No. 25, Accounting for Stock Issued to Employees, and related interpretations. The following table illustrates the effect on net income and earnings per share if the Company had applied the fair value recognition provisions of FASB Statement No. 123, Accounting for Stock-Based Compensation, to stock-based employee compensation.

	Quarter Ended December 31	
	2002	2001
Net loss, as reported	$(486,534)	$(389,561)
Deduct: Total stock-based employee compensation expense determined under fair value based method for all awards, net of related tax effects	(2,852)	(11,883)
Pro forma net loss	$(489,386)	$(401,444)
Loss per share:		
As reported	$ (0.03)	$ (0.02)
Pro forma	$ (0.03)	$ (0.02)

NOTE 1 - Basis of Presentation - (Continued)

New accounting pronouncements:

On November 2002, the Financial Accounting Standards Board (FASB) issued FASB Interpretation (FIN) No. 45, Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness to Others. FIN 45 elaborates on the disclosures to be made by a guarantor in its interim and annual financial statements about its obligations under certain guarantees that it has issued. It also clarifies that a guarantor is required to recognize, at the inception of certain guarantee contracts, a liability for the fair value of the obligation undertaken in issuing the guarantee. FIN 45 also incorporates, without change, the guidance in FIN 34, Disclosure of Indirect Guarantees of Indebtedness of Others, which is being superseded. FIN 45 is effective for financial statements issued for fiscal years ending after December 15, 2002. FIN 45 has no effect on the Company's financial statements.

In December 2002, the Financial Accounting Standards Board (FASB) issued FASB Interpretation (FIN) No. 46, Consolidation of Variable Interest Entities. FIN 46 establishes standards for identifying a variable interest entity and for determining under what circumstances a variable interest entity should be

consolidated with its primary beneficiary, including those to which the usual condition of consolidation does not apply. FIN 46 applies immediately to variable interest entities created after January 31, 2003 and applies to existing variable interest entities in the first fiscal year or interim period beginning after June 15, 2003. Management does not anticipate that the adoption of FIN 46 will have a significant effect on the Company's financial statements.

NOTE 2 - Earnings Per Share

Earnings per share (EPS): Basic EPS is computed by dividing income available to common stockholders by the weighted average number of common shares outstanding for the period. Diluted EPS is computed giving effect to all dilutive potential common shares that were outstanding during the period. Dilutive potential common shares consist of the incremental common shares issuable upon conversion of convertible preferred or convertible debt and the exercise of stock options and warrants for all periods. Fully diluted (loss) per share is not presented since the effect would be anti-dilutive.

NOTE 3 - Comprehensive Income (Loss)

Total Comprehensive Loss was $(412,553) for the three months ended December 31, 2002 and $(362,240) for the three months ended December 31, 2001.

NOTE 4 - Inventories

The components of inventory consist of the following:

	DECEMBER 31, 2002
Raw Material and work in process	$ 731,358
Finished Goods	178,421
Inventory, Gross	909,779
Less: Inventory reserves	(5,719)
Inventory, net	$ 904,060

NOTE 5 - Financial Condition

The Company's consolidated financial statements have been prepared on a going concern basis which contemplates the realization of assets and the settlement of liabilities and commitments in the normal course of business. The Company incurred a net loss of $.5 million for the three months ended December 31, 2002 and as of December 31, 2002 had an accumulated deficit of $54.4 million. At

December 31, 2002, the Company had working capital of $2.1 million and stockholders' equity of $.8 million. In the near term, the Company expects operating and capital costs to continue to exceed funds generated from operations due principally to the Company's manufacturing costs relative to current production volumes and the ongoing need to commercialize the Female Condom around the world. As a result, operations in the near future are expected to continue to use working capital. Management recognizes that the Company's continued operations may depend on its ability to raise additional capital through a combination of equity or debt financing, strategic alliances and increased sales volumes.

At various points during the developmental stage of the product, the Company was able to secure resources, in large part through the sale of equity and debt securities, to satisfy its funding requirements. As a result, the Company was able to obtain FDA approval, worldwide rights, manufacturing facilities and equipment and to commercially launch the Female Condom.

NOTE 5- Financial Condition - (Continued)

Management believes that developments, including the Company's agreement with the UNAIDS, a joint United Nations program on HIV/AIDS, and various distribution partners in major countries, provide an indication of the Company's success in broadening awareness and distribution of the Female Condom and may benefit future efforts to raise additional capital and to secure additional agreements to promote and distribute the Female Condom throughout other parts of the world. On May 18, 2001, the Company entered into an agreement with Heartland Bank providing for a $2,000,000 credit facility. The unpaid balances on the credit facility are due May 18, 2004 and bear interest payable at a rate of 10% per year. The agreement contains certain covenants which include restrictions on the payment of dividends and distributions and on the issuance of warrants, which the Company was in violation of at September 30, 2002. Under the terms of the agreement, Heartland Bank would have had the right to demand payment of the entire balance of the credit facility as a result of this violation. On December 13, 2002, the Company obtained a waiver from Heartland Bank through the entire fiscal year ending September 30, 2003. The Company may borrow under the credit facility from time to time subject to a number of conditions, including obtaining personal guarantees of 125% of the amount outstanding under the credit facility. As of December 31, 2002 the Company had paid down $100,000 of the $2,000,000 borrowed under the credit facility. The credit facility is recorded at December 31, 2002, net of unamortized discount of $1,017,034.

On June 1, 2001 the Company issued an aggregate of $200,000 of convertible debentures to two accredited investors. The debentures were due May 30, 2004, bore interest payable at a rate of 10% per annum, and were convertible into the Company's common stock based on a price per share equal of $0.50. The Company did not issue warrants in connection with the issuance of the convertible debentures. On December 5, 2002, the investors converted their debentures into an aggregate of 400,000 shares of the Company's common stock.

On March 30, 2001 the Company issued a $250,000 convertible debenture to one accredited investor. The debenture was due March 30, 2004, bore interest payable at a rate of 12% per annum, and was convertible into the Company's common stock based at a price per share equal to 70% of the market price of the Company's common stock at the time of exercise, but in no event will the purchase price be less than $0.50 per share or more than $1.00 per share. The Company did not issue warrants in connection with the issuance of the convertible debenture. On

January 12, 2003, the investor converted his debenture into 250,000 shares of the Company's common stock.

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NOTE 5 - Financial Condition - (Continued)

While the Company believes that its existing capital resources will be adequate to fund its currently anticipated capital needs, if they are not, the Company may need to raise additional capital until its sales increase sufficiently to cover operating expenses.

Until internally generated funds are sufficient to meet cash requirements, FHC will remain dependent upon its ability to generate sufficient capital from outside sources. While management believes that revenue from sales of the Female Condom will eventually exceed operating costs and that ultimately operations will generate sufficient funds to meet capital requirements, there can be no assurance that such level of operations will ultimately be achieved, or be achieved in the near term. Likewise, there can be no assurance that the Company will be able to source all or any portion of its required capital through the sale of debt or equity or, if raised, the amount will be sufficient to operate the Company until sales of the Female Condom generate sufficient revenues to fund operations. In addition, any funds raised may be costly to the Company and/or dilutive to stockholders. If the Company is not able to source the required funds or any future capital which becomes required, the Company may be forced to sell certain of its assets or rights or cease operations.

NOTE 6 - Stock Compensation

In September 2001, the holders of exercisable stock options waived their rights to exercise their options until the Company amended its articles of incorporation to increase the number of shares of common stock authorized for issuance. To obtain this waiver, the Company agreed to re-price these options at $0.56 per share once the amendment was approved. The Company's common stock was trading at less than $0.56 per share when the waivers were obtained. The total number of options that were waived at September 30, 2001, was 2,659,800.

On May 8, 2002, the shareholders approved an amendment to the Amended and Restated Articles of Incorporation to increase the total number of authorized shares of common stock from 27,000,000 to 35,500,000 shares. Since the amendment was approved, the stock options have been re-priced to $0.56 per share. The Company has accounted for all of these stock options in accordance with variable plan accounting guidance provided in APB No. 25 and related interpretations. The reduction in the exercise price of the re-priced options and the increase in the stock price of the Company's common stock as of September 30, 2002 resulted in $1,720,322 of stock compensation expense due to the repricing for the year ended September 30, 2002.

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NOTE 6 - Stock Compensation - (Continued)

Effective September 2002, the holders of outstanding options to purchase a total of 2,365,980 shares of common stock agreed to exchange their options for:

- a total of 469,000 shares of restricted common stock in the case of U.S. option holders or the right to receive a total of 122,495 shares of deferred common stock in September 2003 in the case of U.K. option holders; and

- the right to receive a grant of new options to purchase a total of 2,365,980 shares of common stock on the first business day that is at least six months and one day after the effective date of the exchange.

The shares of restricted common stock and the right to receive the shares of deferred common stock are subject to forfeiture if the participant voluntarily resigns or is terminated for cause on or before September 26, 2003 and may not be transferred on or before September 26, 2003. As of September 30, 2002, the Company had issued the restricted common stock to U.S. option holders and accrued for the issuance of deferred common stock to U.K. option holders. The restricted and deferred shares have been recorded as deferred compensation within stockholders' equity as of September 30, 2002, and will be amortized over the employees' one-year service periods.

The new options will have an exercise price equal to 100% of the fair market value of the common stock on the grant date and a vesting schedule of 1/36 per month for each of the first 36 months after the date of grant. The new options, when granted, will be accounted for in accordance with fixed plan accounting guidance provided in APB No. 25. Options to purchase a total of 320,000 shares of common stock did not participate in the exchange and will continue to be accounted for in accordance with variable plan accounting guidance.

NOTE 7. PREFERRED STOCK

During September 2002, the Company offered the holders of the outstanding preferred stock the right to convert their shares of preferred stock into shares of common stock based on a price of $1.80 per share. This resulted in a conversion rate of approximately 1.39 shares of common stock per share of preferred stock rather than the 1 to 1 conversion rate set forth in the Company's Articles of Incorporation. As of December 31, 2002, a total of 604,000 shares of Series 1 Preferred Stock were converted into a total of 838,799 shares of common stock.

The Company has 56,000 outstanding shares of 8 percent cumulative convertible preferred stock (Series 1). Each share of preferred stock is convertible into one share of the Company's common stock on or after August 1, 1998. Annual preferred stock dividends will be paid if and as declared by the Company's Board of Directors. No dividends or other distributions will be payable on the Company's common stock unless dividends are paid in full on the preferred stock. The preferred stock may be redeemed at the option of FHC, in whole or in part, on or after August 1, 2000, subject to certain conditions, at $2.50 per share plus accrued and unpaid dividends. In the event of a liquidation or dissolution of the Company, the preferred stock would have priority over the Company's common stock.

NOTE 8 - Industry Segments And Financial Information About Foreign and

Domestic Operations

The Company currently operates primarily in one industry segment which includes the development, manufacture and marketing of consumer health care products.

The Company operates in foreign and domestic regions. Information about the Company's operations by geographic area is as follows:

(Amounts in Thousands)

	Net Sales to External Customers For the Three months ended December 31,		Long-Term Assets as of December 31,	
	2002	2001	2002	2001
United States.	$ 700	$ 790	$ 139	$ 143
Botswana	128	*	-	-
Brazil	*	89	-	-
Japan.	*	102	-	-
Kenya.	267	*	-	-
Nigeria.	248	*	-	-
United Kingdom	*	*	1,171	1,465
Zimbabwe	283	473	-	-
Other.	618	216	-	-
	$2,244	$1,670	$1,310	$1,607

* Less than 5 percent of total net sales

NOTE 9 - Contingent Liabilities

The testing, manufacturing and marketing of consumer products by the Company entail an inherent risk that product liability claims will be asserted against the Company. The Company maintains product liability insurance coverage for claims arising from the use of its products. The coverage amount is currently $5,000,000 for FHC's consumer health care product.

THE FEMALE HEALTH COMPANY AND SUBSIDIARIES
MANAGEMENT'S DISCUSSION AND ANALYSIS

GENERAL

The Female Health Company ("FHC" or the "Company") manufactures, markets and sells the female condom, the only FDA-approved product under a woman's control

which can prevent unintended pregnancy and sexually transmitted diseases ("STDs"), including HIV/AIDS.

The female condom has undergone extensive testing for efficacy, safety and acceptability, not only in the United States but also in many countries around the world. Certain of these studies show that having the female condom available allows women to have more options, resulting in an increase in protected sex acts and a decrease in STDs, including HIV/AIDS.

The product is currently sold or available in various venues including commercial (private sector) and public sector clinics in over 100 countries. It is commercially marketed in 21 countries by various FHC country specific partners, including the United States, United Kingdom, Japan, Canada, Holland, France, Venezuela, and Brazil. On November 29, 2001, the Company signed a non-binding memorandum of understanding with Hindustan Latex Limited for distribution in India.

As noted above, the female condom is sold to the global public sector. In the U.S., the product is marketed to city and state public health clinics as well as not-for-profit organizations such as Planned Parenthood. The product is available to developing countries under the umbrella of an agreement with UNAIDS. This agreement facilitates the availability and distribution of the female condom at a reduced price based on the Company's cost of production. The current price per unit is approximately 0.38 (Pounds), or approximately $0.61. Currently 87 developing countries purchase the female condom under the terms of this agreement.

Product

The female condom is made of polyurethane, a thin but strong material which is resistant to rips and tears during use. The female condom consists of a soft, loose fitting sheath and two flexible O rings. One of the rings is used to insert the device and helps to hold it in place. The other ring remains outside the vagina after insertion. The female condom lines the vagina, preventing skin from touching skin during intercourse. The female condom is pre-lubricated and disposable and is intended for use during only one sex act.

Raw Materials

Polyurethane is the principal raw material the Company uses to produce the female condom. The Company has entered into a supply agreement with Deerfield Urethane, Inc. for the purchase of all of the Company's requirements of polyurethane. Under this agreement, the parties negotiate pricing on an annual basis. The original term of the agreement extended to December 31, 1995 and thereafter automatically renews for additional one year periods unless either party gives at least 12 months prior written notice of termination.

Global Market Potential

It is more than twenty years since the first clinical evidence of AIDS was noted. HIV/AIDS is the most devastating pandemic that humankind has faced in recorded history. UNAIDS and the World Health Organization ("WHO") estimate that more than 60 million people have been infected with the virus and that, at the end of 2002, 44 million people globally were living with HIV. Women now comprise the majority of the new cases. AIDS is not the only sexually transmitted disease that the global public health community is battling. In the United States, the Center for Disease Control and Protection noted that one in five Americans over the age of 12 has Herpes and 1 in every 3 sexually active people will get an STD by age 24.

Currently there are only two products that prevent the transmission of HIV/AIDS through sexual intercourse --the latex male condom and the female condom.

Male Condom Market: It is estimated the global annual market for male condoms is close to 5 billion units. However, the majority of all acts of sexual intercourse, excluding those intended to result in pregnancy, are completed without protection. As a result, it is estimated the potential market for barrier contraceptives is much larger than the identified male condom market.

Advantages Versus the Male Condom

The female condom is currently the only available barrier contraceptive method controlled by women which allows them to protect themselves from unintended pregnancy and STDs, including HIV/AIDS. The most important advantage is that using the female condom, a woman has a prevention method she controls as many men do not like to wear male condoms and may refuse to do so.

The polyurethane material that is used for the female condom offers a number of benefits over latex, the material that is most commonly used in male condoms. Polyurethane is much stronger than latex, reducing the probability that the female condom sheath will tear during use. Unlike latex, polyurethane quickly transfers heat, so the female condom immediately warms to body temperature when it is inserted, which may result in increased pleasure and sensation during use. The product offers an additional benefit to the 7% to 20% of the population that is allergic to latex and who, as a result, may be irritated by latex male condoms. To the Company's knowledge, there is no reported allergy to date to polyurethane. The female condom is also more convenient, providing the option of insertion hours before sexual arousal and as a result is less disruptive during sexual intimacy than the male condom which requires sexual arousal for application.

Cost Effectiveness

Various studies have been reported in the literature on the cost-effectiveness of the female condom. The studies show that making the female condom available is highly cost effective in reducing public health costs in developing countries as well as in the U.S. Further studies show that including the female condom in prevention programs to high risk groups is not only cost-effective but cost-saving.

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Worldwide Regulatory Approvals

The female condom received Pre-Market Approval ("PMA") as a Class III Medical Device from the U.S. Food and Drug Administration ("FDA") in 1993. The extensive clinical testing and scientific data required for FDA approval laid the foundation for approvals throughout the rest of the world, including receipt of a CE Mark in 1997 which allows the Company to market the female condom throughout the European Union ("EU"). In addition to the United States and the EU, several other countries have approved the female condom for sale, including Canada, Russia, Australia, Japan, South Korea and Taiwan.

The Company believes that the female condom's PMA and FDA classification as a Class III Medical Device create a significant barrier to entry. The Company estimates that it would take a minimum of four to six years to implement, execute and receive FDA approval of a PMA to market another type of female condom.

The Company believes there are no material issues or material costs associated

with the Company's compliance with environmental laws related to the manufacture and distribution of the female condom.

Strategy

The Company's strategy is to act as a manufacturer, selling the female condom to the global public sector, United States public sector and commercial partners for country-specific marketing. The public sector and commercial partners assume the cost of shipping and marketing the product. As a result, as volume increases, the Company's operating expenses will not increase significantly.

Commercial Markets

The Company markets the product directly in the United Kingdom. The Company has distribution agreements with commercial partners in 17 countries including the United States, Japan, Canada, Brazil, Venezuela, Denmark, Holland and France, and on November 20, 2001, the Company signed a non-binding memorandum of understanding with Hindustan Latex Limited in India. The agreements are generally exclusive for a single country. Under these agreements, each partner markets and distributes the female condom in a single country and the Company manufacturers the female condom and sells the product to the partner for distribution in that country.

Relationships and Agreements with Public Sector Organizations

Currently, it is estimated more than 1.5 billion male condoms are distributed worldwide by the public sector each year. The female condom is seen as an important addition to prevention strategies by the public sector because studies show that the availability of the female condom decreases the amount of unprotected sex by as much as 25% over male condoms alone.

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The Company has an agreement with UNAIDS to supply the female condom to developing countries at a reduced price which is negotiated each year based on the Company's cost of production. The current price per unit is approximately 0.38 (pounds), or approximately $0.61. Under the agreement, UNAIDS and the Company cooperate in education efforts and marketing the female condom in developing countries. Sales of the female condom are made directly to public health authorities in each country at the price established by the agreement with UNAIDS. The term of the agreement currently expires on December 31, 2003, but automatically renews for additional one-year periods unless either party gives at least 90 days prior written notice of termination. The female condom is available in 87 countries through public sector distribution. Twenty-seven countries have significant programs and are using The Female Condom - the Guide To Programming and Planning, published by UNAIDS and WHO with the Company's input. This is up from eight countries the previous year.

In the United States, the product is marketed to city and state public health clinics, as well as not-for-profit organizations such as Planned Parenthood.

State-of-the-Art Manufacturing Facility

The Company manufactures the female condom in a 40,000 square-foot leased facility in London, England. The facility is currently capable of producing 60 million units per year. With additional equipment, this capacity can be significantly increased.

Government Regulation

In the U.S., the female condom is regulated by the FDA. Pursuant to section

515(a)(3) of the Safe Medical Amendments Act of 1990 (the "SMA Act"), the FDA may temporarily suspend approval and initiate withdrawal of the PMA if the FDA finds that the female condom is unsafe or ineffective, or on the basis of new information with respect to the device, which, when evaluated together with information available at the time of approval, indicates a lack of reasonable assurance that the device is safe or effective under the conditions of use prescribed, recommended or suggested in the labeling. Failure to comply with the conditions of FDA approval invalidates the approval order. Commercial distribution of a device that is not in compliance with these conditions is a violation of the SMA Act.

Competition

The Company's female condom participates in the same market as male condoms but is not seen as directly competing with male condoms. Rather, the Company believes that providing the female condom is additive in terms of prevention and choice. Latex male condoms cost less and have brand names that are more widely recognized than the female condom. In addition, male condoms are generally manufactured and marketed by companies with significantly greater financial resources than the Company. It is also possible that other parties may develop a female condom. These competing products could be manufactured, marketed and sold by companies with significantly greater financial resources than those of the Company.

Patents and Trademarks

The Company currently holds product and technology patents in the United States, Japan, the United Kingdom, France, Italy, Germany, Spain, the European Patent Convention, Canada, The People's Republic of China, Brazil, South Korea and Australia. Additional technology patents are pending in Japan. The patents cover the key aspects of the female condom, including its overall design and manufacturing process. The Company has the registered trademark "FC Female Condom" in the United States. The Company has also secured, or applied for, 12 trademarks in 22 countries to protect the various names and symbols used in marketing the product around the world. These include 'femidom', 'femy' and others. In addition, the experience that has been gained through years of manufacturing the female condom has allowed the Company to develop trade secrets and know-how, including certain proprietary production technologies that further secure its competitive position.

RESULTS OF OPERATIONS

THREE MONTHS ENDED DECEMBER 31, 2002 COMPARED TO THREE MONTHS ENDED DECEMBER 31, 2001

The Company had net revenues of $2,243,940 and a net loss attributable to common stockholders of $(486,534) or $(0.03) for the three months ended December 31, 2002 compared to net revenues of $1,670,171 and a net loss attributable to common stockholders of $(389,561) or $(0.02) for the three months ended December 31, 2001. During first quarter of fiscal 2003, the Company recorded non-cash charges of $323,973 consisting of stock compensation primarily related to accounting for stock issued for outstanding stock options and costs incurred for consulting services. During the first quarter of fiscal 2002, the Company recorded non-cash charges of $19,608 consisting of stock compensation primarily for consulting services. Excluding these non-cash charges in both fiscal years, the net loss attributable to common stockholders for the three months ended December 31, 2002 would be $(162,561) or $(0.01) per share and the net loss attributable to common stockholders for the three months ended December 31, 2001

would be $(369,953) or $(0.02) per share.

Gross profit increased $378,805, or 63%, to $978,642 for the three months ended December 31, 2002 from $599,837 for the three months ended December 31, 2001. The increase was a result of improved net revenues combined with a less than proportionate increase in cost of products sold. Gross profit as a percentage of net revenues increased to 44% for the three months ended December 31, 2002 compared to 36% for the three months ended December 31, 2001.

Net revenues increased $573,769 in the current quarter, or 34%, compared with the same period last year. The higher sales occurred because of higher unit sales shipped to global and domestic public sector customers. Overall, unit sales in the current quarter increased 35% from the same period last year.

The Company expects significant quarter to quarter variation due to the timing of receipt of large orders, subsequent production scheduling, and shipping of products as various countries launch the product. The Company believes this variation between quarters will continue for several quarters to come until reorders form an increasing portion of total net revenues.

Cost of products sold increased $194,964 to $1,265,298 in the current quarter from $1,070,334 for the same period last year. The cost of products sold increase of 18% on a 34% sales increase resulted in a reduction in costs of products sold as a percentage of sales to 56% in the current quarter from 64% during the same period in the prior year. As unit sales increase, those manufacturing costs that are fixed in nature do not require additional costs to be incurred enabling the Company to produce at a lower cost of goods sold per unit.

Advertising and promotional expenditures increased $4,997 to $15,938 in the current quarter from $10,941 for the same period in the prior year.

Selling, general and administrative expenses increased $137,805, or 19%, to $873,623 in the current quarter from $735,818 for the same period last year. The increase was not in proportion with the sales increase due to the primarily fixed nature of the selling, general and administrative costs. As a percentage of net revenues, selling, general and administrative expenses decreased from 44% for the three months ended December 31, 2001 to 39% for the three months ended December 31, 2002.

The Company's operating loss for the three months ended December 31, 2002 was $234,892 compared to $166,530 for the same period last year for a increase of 41%. Excluding the non-cash charges for stock compensation, the Company would have recorded operating income of $89,081 for the three months ended December 31, 2002 compared to an operating loss of $(146,922) for the three months ended December 31, 2001.

Net interest and other expenses increased $58,834 to $248,594 for the current period from $189,760 for the same period last year. The increase occurred primarily because the Company had a larger amount of non-cash expenses incurred from the amortization of discounts on notes payable and convertible debentures than the first quarter of the prior year.

Factors That May Affect Operating Results and Financial Condition

The Company's future operating results and financial condition are dependent on the Company's ability to increase demand for and to cost-effectively manufacture sufficient quantities of the female condom. Inherent in this process is a

number of factors that the Company must successfully manage in order to achieve favorable future results and improve its financial condition.

Reliance on a Single Product

The Company expects to derive the vast majority, if not all, of its future revenues from the female condom, its sole current product. While management believes the global potential for the female condom is significant, the product is in the early stages of commercialization and, as a result, the ultimate level of consumer demand around the world is not yet known. To date, sales of the female condom have not been sufficient to cover the Company's operating costs, on an annual basis.

Distribution Network

The Company's strategy is to act as a manufacturer and to develop a global distribution network for the product by completing partnership arrangements with companies with the necessary marketing and financial resources and local market expertise. To date, this strategy has resulted in numerous in-country distributions in the public sector, particularly in Africa, Latin America and recently in India. Several partnership agreements have been completed for the commercialization of the female condom in private sector markets around the world. However, the Company is dependent on country governments as well as city and state public health departments within the United States to continue their commitment to prevention of STDs, including AIDS, by including female condoms in their programs. The Company is also dependent on finding appropriate partners for the private sector markets around the world. Once an agreement is completed, the Company is reliant on the effectiveness of its partners to market and distribute the product. Failure by the Company's partners to successfully market and distribute the female condom or failure of country governments to implement prevention programs which include distribution of barrier methods against the AIDS crisis, or an inability of the Company to secure additional agreements for AIDS crisis, or an inability of the Company to secure additional agreements for new markets either in the public or private sectors could adversely affect the Company's financial condition and results of operations.

As part of this strategy the Company has entered into two agreements in the year ended September 30, 2002.

On November 29, 2001, the Company signed a non-binding memorandum of understanding with Hindustan Latex Limited ("HLL"), an Indian government Organization and India's largest male condom manufacturer. HLL distributes to public sector customers including government and non-government organizations and to consumers through 160,000 retail outlets. Jointly with HLL a marketing strategy will be developed for the country of India. Over time, the Company anticipates that HLL and the Company will explore manufacturing options within India.

On December 18, 2001, the Company announced the appointment of Total Access Group ("TAG") as the exclusive distributor for public sector sales within a 15 state region in the western United States. TAG is a privately held national distributor to the United States public sector and serves over 2,500 customers, which include state and local health departments, community based organizations, HIV/STD prevention organizations, Planned Parenthood clinics and family planning organizations. TAG is a full service distributor and will provide marketing, education and customer service support. TAG is required to purchase 2,190,000 units within a three year period to retain exclusive distribution rights.

Inventory and Supply

All of the key components for the manufacture of the female condom are essentially available from either multiple sources or multiple locations within a source.

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Global Market and Foreign Currency Risks

The Company manufactures the female condom in a leased facility located in London, England. Further, a material portion of the Company's sales are in foreign markets. Manufacturing costs and sales to foreign markets are subject to normal currency risks associated with changes in the exchange rate of foreign currencies relative to the United States dollar. To date, the Company's management has not deemed it necessary to utilize currency hedging strategies to manage its currency risks. On an ongoing basis, management continues to evaluate its commercial transactions and is prepared to employ currency hedging strategies when it believes such strategies are appropriate. In addition, some of the Company's future international sales may be in developing nations where dramatic political or economic changes are possible. Such factors may adversely affect the Company's results of operations and financial condition.

Government Regulation

The female condom is subject to regulation by the FDA, pursuant to the federal Food, Drug and Cosmetic Act (the "FDC Act"), and by other state and foreign regulatory agencies. Under the FDC Act, medical devices must receive FDA clearance before they can be sold. FDA regulations also require the Company to adhere to certain "Good Manufacturing Practices," which include testing, quality control and documentation procedures. The Company's compliance with applicable regulatory requirements is monitored through periodic inspections by the FDA. The failure to comply with applicable regulations may result in fines, delays or suspensions of clearances, seizures or recalls of products, operating restrictions, withdrawal of FDA approval and criminal prosecutions. The Company's operating results and financial condition could be materially adversely affected in the event of a withdrawal of approval from the FDA.

Liquidity and Sources of Capital

Historically, the Company has incurred cash operating losses relating to expenses incurred to develop and promote the Female Condom. During the three months ended December 31, 2002, cash used in operations totaled $.1 million. The Company was able to fund cash used in its operations, capital expenditures, and payments of preferred stock dividends and capital lease obligations during the three months ended December 31, 2002 without any debt or equity financing.

At December 31, 2002, the Company had current liabilities of $2.5 million including a $1.0 million note payable due March 25, 2003 to Mr. Dearholt, a Director of the Company. As of December 31, 2002, Mr. Dearholt beneficially owns 4,435,305 shares of the Company's Common Stock. The Company and Mr. Dearholt plan to extend this note in the current fiscal year as the note's term expires.

On January 15, 2003, the Company entered into a line of credit agreement with Heartland Bank. The line of credit facility allows the Company to borrow up to $1,000,000 in $100,000 increments and matures on December 1, 2004. Interest is due monthly at the prime rate plus 1 percent (prime was 4.25 percent on January 15, 2003) and it is collateralized by the Company's inventory and letter of credit backed by accounts receivables.

In the near term, the Company's management expects operating and capital costs

to continue to exceed funds generated from operations, due principally to the Company's fixed manufacturing costs relative to current production volumes and the ongoing need to commercialize the Female Condom around the world. It is estimated that the Company's cash burn rate, with revenues, is approximately $0.1 million per quarter.

While the Company believes that revenue from sales of the female condom will eventually exceed operating costs, and that, ultimately, operations will generate sufficient funds to meet capital requirements, the Company can make no assurance that it will achieve such level of operations in the near term or at all. Likewise, the Company can make no assurance that the Company will be able to source all or any portion of its required capital through the sale of debt or equity or, if raised, the amount will be sufficient to operate until sales of the female condom generate sufficient revenues to fund operations. In addition, any funds raised may be costly to the Company and/or dilutive to its shareholders. If the Company is unable to raise adequate financing when needed, the Company may be required to sharply curtail the Company's efforts to promote the female condom, to attempt to sell certain of its assets and rights or to curtail certain of its operations and may ultimately be forced to cease operations. Currently, the Company is focused on growing its business and, therefore, the Company has made no plans to sell any assets nor has it identified any assets to be sold or potential buyers. In the event that the Company lacks sufficient capital to continue its operations, neither the Company nor its shareholders may be able to realize any significant value from the Company's assets.

IMPACT OF INFLATION AND CHANGING PRICES

Although the Company cannot accurately determine the precise effect of inflation, the Company has experienced increased costs of product, supplies, salaries and benefits, and increased selling, general and administrative expenses. Historically, the Company has absorbed increased costs and expenses without increasing selling prices.

CONTROLS AND PROCEDURES

Within 90 days prior to the date of this report, the Company carried out an evaluation, under the supervision and with the participation of the Company's management, including the Company's Chief Executive Officer and the Company's Principal Accounting Officer, of the effectiveness of the design and operation of the Company's disclosure controls and procedures. Based on this evaluation, the Company's Chief Executive Officer and Principal Accounting Officer concluded that the Company's disclosure controls and procedures were effective in timely alerting them to material information relating to the Company required to be included in the Company's periodic filings with the Securities and Exchange Commission. It should be noted that in designing and evaluating the disclosure controls and procedures, management recognized that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, and management necessarily was required to apply its judgment in evaluating the cost-benefit relationship of possible controls and procedures.

There have been no significant changes in the Company's internal controls or in other factors that could significantly affect the internal controls subsequent to the date the Company completed its evaluation.

PART II - OTHER INFORMATION

ITEMS 1-5

ITEM 2 (C)

On June 1, 2001 the Company issued an aggregate of $200,000 of convertible debentures to two accredited investors. The debentures were due May 30, 2004, bore interest payable at a rate of 10% per annum, and were convertible into the Company's common stock based on a price per share equal of $0.50. The Company did not issue warrants in connection with the issuance of the convertible debentures. On December 5, 2002, the investors converted their debentures into an aggregate of 400,000 shares of the Company's common stock.

On March 30, 2001 the Company issued a $250,000 convertible debenture to one accredited investor. The debenture was due March 30, 2004, bore interest payable at a rate of 12% per annum, and was convertible into the Company's common stock based at a price per share equal to 70% of the market price of the Company's common stock at the time of exercise, but in no event will the purchase price be less than $0.50 per share or more than $1.00 per share. The Company did not issue warrants in connection with the issuance of the convertible debenture. On January 12, 2003, the investor converted his debenture into 250,000 shares of the Company's common stock.

The Company believes it has satisfied the exemption from the securities registration requirement provided by section 3(a)(9) of the Securities Act for these offerings.

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

(a) Exhibits

Exhibit Number	Description
3.1	Amended and Restated Articles of Incorporation. (1)
3.2	Articles of Amendment to the Amended and Restated Articles of Incorporation of the Company increasing the number of authorized shares of common stock to 27,000,000 shares (2)
3.3	Articles of Amendment to the Amended and Restated Articles of Incorporation of the Company increasing the number of authorized shares of common stock to 35,500,000 shares (3)
3.4	Amended and Restated By-Laws. (4)
4.1	Amended and Restated Articles of Incorporation. (same as Exhibit 3.1)

4.2 Articles of Amendment to the Amended and Restated Articles of Incorporation of the Company (same as Exhibit 3.2)

4.3 Articles of Amendment to the Amended and Restated Articles of Incorporation of the Company increasing the number of authorized shares of common stock to 35,500,000 shares (same as Exhibit 3.3)

4.4 Articles II, VII, and XI of the Amended and Restated By-Laws (included in Exhibit 3.4).

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(1) Incorporated herein by reference to the Company's Registration Statement on Form SB-2, filed with the Securities and Exchange Commission on October 19, 1999.

(2) Incorporated by reference to the Company's Registration Statement on Form SB-2, filed with the Securities and Exchange Commission on September 21, 2000.

(3) Incorporated by reference to the Company's Registration Statement on Form SB-2, filed with the Securities and Exchange Commission on September 6, 2002.

(4) Incorporated herein by reference to the Company's Registration Statement on Form S-18, as filed with the securities and Exchange Commission on May 25, 1999.

(b) Report on Form 8-K - No reports on Form 8-K were filed during the quarter ended December 31, 2002.

SIGNATURES

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

THE FEMALE HEALTH COMPANY

DATE: February 14, 2003

/s/ O.B. Parrish

O.B. Parrish, Chairman and
Chief Executive Officer

/s/ Robert R. Zic

Robert R. Zic, Principal
Accounting Officer

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CERTIFICATIONS

I, O.B. Parrish, Chairman and Chief Executive Officer of The Female Health Company, certify that:

1. I have reviewed this quarterly report on Form 10-QSB of The Female Health Company;

2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;

3. Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this quarterly report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and we have:

(a) designed such disclosure controls and procedures to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;

(b) evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this quarterly report (the "Evaluation Date"); and

(c) presented in this quarterly report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent function):

(a) all significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and

(b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and

6. The registrant's other certifying officer and I have indicated in this quarterly report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

DATE: February 14, 2003 /s/ O.B. Parrish

O.B. Parrish, Chairman and
Chief Executive Officer

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CERTIFICATIONS

I, Robert R. Zic, Principal Accounting Officer of The Female Health Company, certify that:

1. I have reviewed this quarterly report on Form 10-QSB of The Female Health Company;

2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;

3. Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this quarterly report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and we have:

(a) designed such disclosure controls and procedures to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;

(b) evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this quarterly report (the "Evaluation Date"); and

(c) presented in this quarterly report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent function):

(a) all significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and

(b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and

6. The registrant's other certifying officer and I have indicated in this quarterly report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

DATE: February 14, 2003

/s/ Robert R. Zic

Robert R. Zic, Principal Accounting Officer

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