

DAG MEDIA INC (DAGM)

Quarterly Report (SEC form 10QSB)

25-Oct-2004
Quarterly Report

Item 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OR PLAN OF OPERATION
The following discussion and analysis of our result of operations should be read in conjunction with our unaudited financial statements and notes thereto contained elsewhere in this report. This discussion contains forward-looking statements based on current expectations that involve risks and uncertainties. Actual results and the timing of certain events may differ significantly from those projected in such forward-looking statements.

We publish and distribute print and online business directories for domestic niche markets. Our principal source of revenue comes from the sale of ads in these directories. As a sales incentive we also provide our advertisers with added values, such as referral services and consumer discount club. We also operate Internet portals, JewishYellow.com targeting worldwide Jewish communities and JewishMasterguide.com, targeting the ultra-orthodox and Hasidic communities as well as Newyellow.com.

Our principal directories are: the Jewish Israeli Yellow Pages, a bilingual, English and Hebrew, yellow page directory distributed free through local commercial and retail establishments in the New York metropolitan area and Florida. The Jewish Master Guide also known as The Kosher Yellow Pages, a yellow page directory designed to meet the special needs of the Hasidic and ultra-Orthodox Jewish communities in the New York metropolitan area and Florida.

Blackbook Photography Inc., Dag Media's wholly owned subsidiary was sold on August 24, 2004 to Modern Holdings Incorporated for \$2.25 million.

Advertising fees, whether collected in cash or evidenced by a receivable, generated in advance of publication dates, are recorded as "Advanced billings for unpublished directories" on our balance sheet. Many of our advertisers pay the ad fee over a period of time. In that case, the entire amount of the deferred payment is booked as a receivable. Revenues are recognized at the time the directory in which the ad appears is published. Thus, costs directly related to the publication of a directory in advance of publication are recorded as "Directories in progress" on our balance sheet and are recognized when the directory to which they relate is published. All other costs are expensed as incurred.

The principal operating costs incurred in connection with publishing the directories are commissions payable to sales representatives and costs for paper and printing. Generally, advertising commissions are paid as advertising revenue is collected. We do not have any long term agreements with paper suppliers or printers. Since ads are sold before we purchase paper and print a particular directory, a substantial increase in the cost of paper or printing costs would reduce our profitability. Administrative and general expenses include expenditures for marketing, insurance, rent, sales and local franchise taxes, licensing fees, office overhead and wages and fees paid to employees and contract workers (other than sales representatives).

Three Months Ended September 30, 2004 Compared to Three Months Ended September 30, 2003

Advertising revenues

Advertising revenues for the three months ended September 30, 2004 were \$1,987,000 compared to \$2,043,000 for the three months ended September 30, 2003, a decrease of \$56,000. The decrease was primarily attributable to the slight decrease in recognized revenue related to the Jewish Yellow Pages Directory, recognized in the third quarter.

Publishing costs

Publishing costs for the three months ended September 30, 2004 were \$225,000 compared to \$226,000, for the corresponding period in 2003, a decrease of \$1,000. As a percentage of advertising revenues, publishing costs were 11.32% in the three month period ending September 30, 2004 compared to 11.06%, in the corresponding period in 2003. The publishing costs for the quarter ended September 30, 2004 and the corresponding period in 2003 primarily reflect the printing and distribution costs of the Jewish Yellow Pages Directory.

Selling expenses

Selling expenses for the three months ended September 30, 2004 were \$963,000 compared to \$922,000 for the corresponding period in 2003, an increase of \$41,000. This increase in selling expenses was primarily attributable to more sales made by agencies with higher commission rates versus sales made by representatives who work directly for the company.

Administrative and general costs

General and administrative expenses for the three months period ended September 30, 2004 were \$745,000 compared to \$731,000 for the same period in 2003, an increase of 1.92%. This increase is primarily attributable to increased legal fees.

Other income

For the three month period ended September 30, 2004, we had other income consisting of dividends, interest and realized gains of \$85,000 compared to other income of \$96,000 and gain from sale of the New Yellow Manhattan Directory of \$1,208,000 for the three month period ended September 30, 2003.

Discontinued Activity

On August 24, 2004, the company sold its wholly owned subsidiary, Blackbook Photography Inc. to Modern Holdings Incorporated, for \$2.25 million. The Company's net profit from the sale, after direct related costs of finder's fee, compensation to sales franchisees, bonuses to employees and payments to legal advisors, before provision for income taxes, totaled \$1.169 million in addition to a gain from operation of \$16,000. Net gain from discontinued operations totaled \$1.186 million.

Provision for income taxes

The provision for income taxes for the three months ended September 30, 2004 was \$134,000 compared to a provision of \$190,000 for the three months ended September 30, 2003. The Company used its deferred tax asset incurred during the second quarter of 2004 to decrease its income tax liabilities.

Nine Months Ended September 30, 2004 Compared to Nine Months Ended September 30, 2003

Advertising revenues

Advertising revenues for nine months ended September 30, 2004 were \$5,027,000 compared to \$5,580,000 for the nine months ended September 30, 2003, a decrease of \$553,000. The decrease was primarily attributable to the deduction of recognized revenues related to the New Yellow Manhattan Directory ninth edition (sold) partly offset by the increase in recognized revenues of the tenth edition of the Jewish Master Guide Directory.

Publishing costs

Publishing costs for the nine months ended September 30, 2004 were \$773,000 compared to \$929,000, for the corresponding period in 2003, a decrease of \$156,000. As a percentage of advertising revenues, publishing costs were 15.37% in the nine month period ending September 30, 2004, compared to 16.65% in the corresponding period in 2003. The decrease in publishing costs primarily reflects the decrease in the printing and distribution costs of the ninth edition of the New Yellow Manhattan Directory.

Selling expenses

Selling expenses for the nine months ended September 30, 2004 were \$2,281,000 compared to \$2,372,000 for the corresponding period in 2003, a decrease of \$91,000. This decrease in selling expenses was primarily the result of the general decreased in sales offset by higher commission rates paid for revenue generated by the Jewish Master Guide Directory compared to commission rates paid for revenues generated by the New Yellow Manhattan Directory, previously published.

Administrative and general costs

General and administrative expenses for the nine month period ended September 30, 2004 were \$2,016,000 compared to \$1,899,000 for the same period in 2003, an increase of 6.16%. This increase is primarily attributable to increased salaries, advertising costs and legal fees

Other income

For the nine month period ended September 30, 2004, we had other income consisting of dividend, interest and realized gains of \$329,000 compared to other income of \$201,000 and gain from sale of the New Yellow Manhattan Directory of \$1,208,000 for the nine month period ended September 30, 2003.

Discontinued Activity

On August 24, 2004, the company sold its wholly owned subsidiary, Blackbook Photography Inc. to Modern Holdings Incorporated, for \$2.25 million. The

Company's net profit from the sale, after direct related costs of finder's fee, compensation to sales franchisees, bonuses to employees and payments to legal advisors, before provision for income taxes, totaled \$1.169 million in addition to a loss from operation of \$183,000. Net gain from discontinued operation totaled \$986,000.

Provision for income taxes

The provision for income taxes for the nine months ended September 30, 2004 was \$134,000 compared to \$206,000 for the nine months ended September 30, 2003. The Company used its deferred tax asset incurred during the second quarter of 2004 to decrease its income tax liabilities for the period.

Liquidity and Capital Resources

At September 30, 2004, we had cash and cash equivalents, marketable securities and short term investments of \$9,982,000 and working capital of \$8,853,000 as compared to cash and cash equivalents, marketable securities and short term investments of \$8,320,000 and working capital of \$6,901,000 at September 30, 2003. The increase in cash and cash equivalents and marketable securities also reflects the \$2.125 million cash provided by the sale of Blackbook Photography Inc. received in August of 2004. The increase in working capital primarily reflects the increase in cash offset by decrease in accounts receivable and \$744,000 dividend payments to shareholders made on January 5, 2004.

Net cash used in operating activities was \$122,000 for the nine months ended September 30, 2004. For the comparable period in 2003, net cash provided by operating activities was \$232,000. The decrease in net cash provided by operating activities reflects the cost of converting the New Yellow sales force to a sale force for Jewish Master Guide and increased legal fees.

Net cash provided by investing activities was \$3,845,000 for the nine months ended September 30, 2004 compared to net cash used in investing activities of \$239,000 for the comparable period in 2003. Net cash provided by investing activities was primarily the result of our sales of marketable securities and a change in our investment strategy as well as the net cash received from the sale of the Blackbook Photography Inc.

Net cash used in financing activities for the nine months ended September 30, 2004 was \$599,000 compared to net cash provided by financing activity in the corresponding period in 2003 of \$11,000. The net cash used in financing activities for the nine months ended September 30, 2004 was accounted for by the dividend paid to the Company's shareholders on January 5, 2004, offset by the proceeds received from the exercise of stock options and the issuance of common shares, respectively.

We anticipate that our current cash balances together with our cash flows from operations will be sufficient to fund the production of our directories and the maintenance of our Web sites as well as increases in our marketing and promotional activities for the next 12 months. However, we expect our working capital requirements to increase over the next 12 months as we continue to market our directories and expand our on-line services.

Forward Looking Statements

This report contains forward-looking statements within the meaning of Section

27A of the Securities Act of 1933, as amended, and section 21E of the Securities Exchange Act of 1934, as amended (the "Exchange Act"). Forward-looking statements are typically identified by the words "believe", "expect", "intend", "estimate" and similar expressions. Those statements appear in a number of places in this report and include statements regarding our intent, belief or current expectations or those of our directors or officers with respect to, among other things, trends affecting our financial

conditions and results of operations and our business and growth strategies. These forward-looking statements are not guarantees of future performance and involve risks and uncertainties. Actual results may differ materially from those projected, expressed or implied in the forward-looking statements as a result of various factors (such factors are referred to herein as "Cautionary Statements"), including but not limited to the following: (i) our limited operating history, (ii) potential fluctuations in our quarterly operating results, (iii) challenges facing us relating to our rapid growth and (iv) our dependence on a limited number of suppliers. The accompanying information contained in this report, including the information set forth under "Management's Discussion and Analysis of Financial Condition and Results of Operations", identifies important factors that could cause such differences. These forward-looking statements speak only as of the date of this report, and we caution potential investors not to place undue reliance on such statements. We undertake no obligation to update or revise any forward-looking statements. All subsequent written or oral forward-looking statements attributable to us or persons acting on our behalf are expressly qualified in their entirety by the Cautionary Statements.

