DYNATRONICS CORP
Form 10QSB
May 15, 2002

UNITED STATES
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 MARCH 31, 2002.

[ ] TRANSITION REPORT UNDER SECTION 13 OR 15(D) OF THE EXCHANGE ACT FOR THE TRANSITION PERIOD FROM __________ TO __________

Commission File Number: 0-12697

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

Utah	87-0398434
(State or other jurisdiction of incorporation or organization)	(IRS Employer Identification No.)

7030 Park Centre Drive, Salt Lake City, UT 84121
(Address of principal executive offices)

(801) 568-7000
(Issuer's telephone number)

Check whether the issuer (1) filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the past 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes X No __

The number of shares outstanding of the issuer's common stock, no par value, as of May 10, 2002 is 8,869,335.

Transitional Small Business Disclosure Format (Check One): Yes __ No X

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DYNATRONICS CORPORATION
Condensed Balance Sheets
(Unaudited)

ASSETS	March 31, 2002
Current assets:	
Cash and cash equivalents	$ 320,110
Trade accounts receivable, less allowance for doubtful accounts of $169,657 at March 31, 2002 and $140,735 at June 30, 2001	3,809,506
Other receivables	145,522
Inventories	4,341,539
Prepaid expenses	326,188
Prepaid income taxes	0
Deferred tax asset-current	268,735
Total current assets	9,211,600
Net property and equipment	3,151,360
Excess of cost over book value, net of accumulated amortization of $627,948 at March 31, 2002 and $568,640 at June 30, 2001	811,226
Other assets	286,497
	$ 13,460,683

LIABILITIES AND STOCKHOLDERS' EQUITY	
Current liabilities:	
Current installments of long-term debt	$ 206,414
Line of credit	2,451,671
Accounts payable	625,676
Accrued expenses	371,949
Accrued payroll and benefit expenses	244,489
Income tax payable	15,949

Total current liabilities	3,916,148
Long-term debt, excluding current installments	1,702,755
Deferred compensation	276,826
Deferred tax liability - noncurrent	78,846
Total liabilities	5,974,575
Stockholders' equity:	
Common stock, no par value. Authorized 50,000,000 shares; issued 8,928,774 shares at March 31, 2002 and 8,840,422 at June 30, 2001	2,638,026
Treasury stock, 59,439 shares at March 31, 2002 and 35,584 shares at June 30, 2001	(159,696)
Retained earnings	5,007,778
Total stockholders' equity	7,486,108
	$ 13,460,683

See accompanying notes to condensed financial statements.

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DYNATRONICS CORPORATION
Condensed Statements Of Income
(Unaudited)

	Three Months Ended March 31		N
	2002	2001	200
Net sales	$ 4,159,244	4,417,682	12,2
Cost of sales	2,539,529	2,513,796	7,3
Gross profit	1,619,715	1,903,886	4,9
Selling, general, and administrative expenses	1,250,614	1,407,076	3,8
Research and development expenses	171,891	276,778	4
Operating income	197,210	220,032	5
Other income (expense):			
Interest income	800	2,775	
Interest expense	(66,492)	(75,484)	(2
Other income, net	1,241	5,445	
Total other income (expense)	(64,451)	(67,264)	(2
Income before income taxes	132,759	152,768	3
Income tax expense	49,837	61,755	1

Net income	$ 82,922	91,013	2
Basic and diluted net income per common share	$ 0.01	0.01	
Weighted average basic and diluted common shares outstanding (note 2)			
Basic	8,865,835	8,787,871	8,8
Diluted	8,898,061	9,475,180	8,9

See accompanying notes to condensed financial statements.

DYNATRONICS CORPORATION

Condensed Statements of Cash Flows
(Unaudited)

	Nine Months Ended March 31 2002	200
Cash flows from operating activities:		
Net income (loss)	$ 226,286	25
Adjustments to reconcile net income to net cash used in operating activities:		
Depreciation and amortization of property and equipment	243,613	22
Other amortization	65,411	7
Provision for doubtful accounts	36,000	2
Provision for inventory obsolescence	153,000	15
Provision for warranty reserve	184,600	16
Deferred compensation	16,227	1
Compensation expense on stock options	0	
Decrease (increase) in operating assets and liabilities:		
Receivables	(372,779)	(26
Inventories	251,784	(47
Prepaid expenses and other assets	(124,627)	(18
Prepaid income tax	9,450	
Trade accounts payable and accrued expenses	9,012	14
Income taxes payable	36,237	8
Net cash provided by operating activities	734,214	22
Cash flows from investing activities-capital expenditures	(117,515)	(16
Cash flows from financing activities:		

Principal payments on long-term debt	(164,885)	(18
Net change in line of credit	(419,353)	18
Proceeds from sale of common stock	28,765	
Net cash used in financing activities	(555,473)	1
Net increase in cash and cash equivalents	61,226	7
Cash and cash equivalents at beginning of period	258,884	23
Cash and cash equivalents at end of period	$ 320,110	30
Supplemental cash flow information		
Cash paid for interest	227,276	24
Cash paid for income taxes	96,100	8
Supplemental disclosure of non-cash investing and financing activities		
Common stock and options issued for license agreement	0	7
Common stock and options issued in exchange for mature stock	39,600	

See accompanying notes to condensed financial statements.

DYNATRONICS CORPORATION
NOTES TO CONDENSED FINANCIAL STATEMENTS
March 31, 2002
(Unaudited)

NOTE 1. PRESENTATION

The financial statements as of March 31, 2002 and June 30, 2001 and for the three and nine months ended March 31, 2002 and 2001 were prepared by the Company without audit pursuant to the rules and regulations of the Securities and Exchange Commission (SEC). Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted pursuant to such rules and regulations. In the opinion of management, all necessary adjustments, which consist only of normal recurring adjustments, to the financial statements have been made to present fairly the financial position and results of operations and cash flows. Certain prior period amounts have been reclassified to conform with the current year presentation. The results of operations for the respective periods presented are not necessarily indicative of the results for the respective complete years. The Company has previously filed with the SEC an annual report on Form 10-KSB which included audited financial statements for the two years ended June 30, 2001. It is suggested that the financial statements contained in this filing be read in conjunction with the statements and notes thereto contained in the Company's 10-KSB filing.

NOTE 2. NET INCOME PER COMMON SHARE

Net income per common share is computed based on the weighted-average number of common shares and, as appropriate, dilutive common stock equivalents outstanding during the period. Stock options are considered to be common stock equivalents.

Basic net income per common share is the amount of net income for the period available to each share of common stock outstanding during the reporting period. Diluted net income per common share is the amount of net income for the period available to each share of common stock outstanding during the reporting period and to each share that would have been outstanding assuming the issuance of common shares for all dilutive potential common shares outstanding during the period.

In calculating net income per common share, the net income was the same for both the basic and diluted calculation. A reconciliation between the basic and diluted weighted-average number of common shares for the three and nine months ended March 31, 2002 and 2001 is summarized as follows:

	(Unaudited) Three Months Ended March 31,		(Unaudit Nine Months March 31	
	2002	2001	2002	
Basic weighted average number of common shares outstanding during the period	8,865,835	8,787,871	8,850,350	8
Weighted average number of dilutive common stock options outstanding during the period	32,225	687,309	52,577	
Diluted weighted average number of common and common equivalent shares outstanding during the period	8,898,061	9,475,180	8,902,927	9

Outstanding options not included in the computation of diluted net income per share for the three month periods ended March 31, 2002 and 2001 total 504,238 and 63,000 and for the nine month periods ended March 31, 2002 and 2001 total 211,471 and 207,829 respectively, because to do so would have been anti-dilutive.

NOTE 3. COMPREHENSIVE INCOME

For the periods ended March 31, 2002 and 2001, comprehensive income was equal to the net income as presented in the accompanying condensed statements of income.

NOTE 4. INVENTORIES

Inventories consisted of the following:

	March 31	June 30

	2002	2001
Raw Material	$ 2,492,075	2,914,710
Finished Goods	2,238,124	2,071,822
Inventory Reserve	(388,660)	(240,209)
	$ 4,341,539	4,746,323

NOTE 5. PROPERTY AND EQUIPMENT

Property and equipment were as follows:

	March 31 2001	June 30 2001
Land	$ 354,743	354,743
Buildings	2,820,894	2,802,894
Machinery and equipment	1,375,125	1,335,828
Office equipment	348,569	288,351
Vehicles	61,771	61,771
	4,961,102	4,843,587
Less accumulated depreciation and amortization	1,809,742	1,566,129
	$ 3,151,360	3,277,458

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

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with the Condensed Financial Statements (unaudited) and Notes thereto appearing elsewhere in this Form 10-QSB.

Results of Operations

Sales during the quarter ended March 31, 2002 were $4,159,244, compared to $4,417,682 during the same period last year. Sales for the nine-month period ended March 31, 2002 were $12,282,961 compared to $12,531,726 during the nine months ended March 31, 2001. The economy of the United States has been recovering from an economic downturn since March of 2001. The slowing economy

was adversely affected by the terrorist attacks on financial and government centers of the United States in September 2001. The Company believes that its business has also been adversely affected by these factors. Management believes the Company has fared better than expected through these economic challenges in its primary geographic market during the past two quarters, primarily as a result of the stability of core product sales including sales of the new STS chronic pain device. By comparison, the introduction of the STS device in the third fiscal quarter of 2001 boosted revenues by nearly $700,000 in that period as distributors placed large initial stocking orders for these units. This spike in sales is primarily responsible for the difference in sales in the third fiscal quarter of last year compared to the third quarter of fiscal year 2002.

Total gross profit during the quarter ended March 31, 2002 was $1,619,715 or 38.9% of sales compared to $1,903,886 or 43.1% of sales in the quarter ended March 31, 2001. Gross profit during the nine-month period ended March 31, 2002 was $4,947,632 or 40.3% of sales compared to $5,286,680 or 42.2% of sales in the nine months ended March 31, 2001. Gross profit during the three and nine months ended March 31, 2001 was higher primarily due to sales associated with the introduction of the STS chronic pain device. The large volume of high margin sales significantly increased gross margins in the prior year, compared to the nine- and three-month periods in fiscal year 2002.

Selling, general and administrative (SG&A) expenses for the three-month period ended March 31, 2002, decreased to $1,250,614 or 30.1% of sales compared to $1,407,076 or 31.9% of sales in the same period of the prior year. SG&A expenses for the nine-month period ended March 31, 2002 were $3,869,262 or 31.5% of sales compared to $4,031,561 or 32.2% of sales for the nine months ended March 31, 2001. The decline in SG&A reflects management's efforts to reduce operating expenses. One such change has been the migration away from direct sales representatives to the use of dealers for marketing the Company's line of Synergie products. During the quarter ended March 31, 2002, the Company took additional steps to increase its profitability through an expense reduction program that it expects will generate future annual savings of as much as $500,000.

Research and development (R&D) expenses during the three- and nine-month periods ended March 31, 2002 totaled $171,891 and $497,981, respectively compared to $276,778 and $613,715, respectively for the same periods in 2001. Development work for the STS chronic pain device resulted in higher research and development expenses in the three- and nine-month periods ended March 31, 2001. The Company

remains committed to its objective of investing significantly in R&D to develop technological enhancements as well as new technologies that address unmet patient and clinical needs.

Pre-tax profit for the quarter ended March 31, 2002 was $132,759 compared to $152,768 during the same period of the prior year. Pre-tax profit for the nine months ended March 31, 2002 was $368,073 compared to $424,278 in the similar period in 2001.

Income tax expense for the three and nine months ended March 31, 2002 was $49,837 and $141,787, respectively compared to $61,755 and $167,590, respectively in the three and nine months ended March 31, 2001.

Net income for the quarter ended March 31, 2002 was $82,922 (approximately $.01 per share), compared to $91,013 (approximately $.01 per share) in the same

quarter in 2001. Net income for the nine months ended March 31, 2002 was $226,286 (approximately $.03 per share) compared to $256,688 (approximately $.03 per share) in the nine months ended March 31, 2001. Despite the economic difficulties facing the nation during the past six months, the Company has been able to maintain profitability due to the stability in demand for its core products and the success of the Dynatron STS and Dynatron STS Rx products. In addition, the Company has worked to reduce operating expenses, which is expected to improve profitability going forward.

Liquidity and Capital Resources

We expect that revenues from operations, together with amounts available under an existing bank line of credit will be adequate to meet working capital needs related to our business and planned capital expenditures for the next 12 months.

The current ratio at March 31, 2002 increased to 2.4 to 1 compared to 2.2 to 1 at June 30, 2001. Current assets represent 68% of total assets at March 31, 2002.

Net accounts receivable at March 31, 2002 were $3,809,506 compared to $3,426,404 at June 30, 2001. Accounts receivable are from the dealer network and are generally considered to be within term.

All accounts payable are within term. The Company continues to take advantage of available payment discounts when possible.

The Company has a revolving line of credit facility with a commercial bank in the amount of $4,500,000. Borrowing limitations are based on 30% of eligible inventory and up to 80% of eligible accounts receivable. The outstanding balance on the line of credit at March 31, 2002 was $2,451,671 compared to $2,871,024 at June 30, 2001. The line of credit is secured by inventory and accounts receivable and bears interest at the bank's "Prime Rate," which was 4.75% per annum at March 31, 2002. This line is subject to annual renewal and matures on December 1, 2002. Accrued interest is payable monthly.

Inventory levels, net of reserves, totaled $4,341,539 at March 31, 2002, compared to $4,746,323 at June 30, 2001. The Company expects inventory levels to continue to decline over the course of the year as inventories are managed more

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closely, and as sales of the new STS devices accelerate as a result of new marketing plans and initiatives. Sustained sales of aesthetic devices will also contribute to a reduction in overall inventories.

Long-term debt excluding current installments totaled $1,702,755 at March 31, 2002, compared to $1,834,903 at June 30, 2001. Long-term debt is comprised primarily of the mortgage loans on our office and manufacturing facilities in Utah and Tennessee. The principal balance on the mortgage loans is approximately $1.8 million with monthly principal and interest payments of $26,900.

Critical Accounting Policies

The Company has disclosed in Note 1 to the consolidated financial statements included in its Annual Report on Form 10-KSB for the year ended June 30, 2001 those accounting policies that it considers to be significant in determining the results of operations and its financial position. In all material respects, the accounting principles utilized by the Company are in conformity with generally accepted accounting principles in the United States of America.
The preparation of consolidated financial statements requires the Company to

make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses. On an on-going basis, the Company evaluates its estimates, including those related to bad debts, inventories, intangible assets, warranty obligations, product liability, revenue, and income taxes. The Company bases its estimates on historical experience and other facts and circumstances that are believed to be reasonable, and the results form the basis for making judgments about the carrying value of assets and liabilities. The actual results may differ from these estimates under different assumptions or conditions.

With respect to inventory reserves, revenue recognition and allowance for doubtful accounts, the Company applies the following critical accounting policies in the preparation of its financial statements:

Inventory Reserves

The nature of Dynatronics' business requires it to maintain sufficient inventory on hand at all times to meet the requirements of its customers. Dynatronics records finished goods inventory at the lower of standard cost, which approximates actual costs (first-in, first-out) or market. Raw materials are stated at the lower of cost (first-in, first-out), or market. General inventory reserves are maintained for the possible impairment of the inventory. Impairment may be a result of slow moving or excess inventory, product obsolescence or changes in the valuation of the inventory. In determining the adequacy of its reserves, Dynatronics analyzes the following, among other things:

- Current inventory quantities on hand;
- Product acceptance in the marketplace;
- Customer demand;
- Historical sales;
- Forecast sales;
- Product obsolescence; and
- Technological innovations.

Any modifications to Dynatronics' estimates of its reserves are reflected in the cost of goods sold within the statement of operations during the period in which such modifications are determined necessary by management.

Revenue Recognition

The Company's products are sold primarily through a network of independent distributors. Sales revenues are generally recorded at the time the products are shipped to the distributor or customer. The distributors, who sell the products to other customers, take title to the products, have no special rights of return, and assume the risk for credit and obsolescence.

Allowance for Doubtful Accounts

Dynatronics must make estimates of the collectibility of accounts receivables. In doing so, management analyzes accounts receivable and historical bad debts, customer credit-worthiness, current economic trends and changes in customer payment patterns when evaluating the adequacy of the allowance for doubtful accounts.

Recent Accounting Pronouncements

In July 2001, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) No. 141 Business Combinations, and SFAS No. 142 Goodwill and Other Intangible Assets. SFAS 141 prohibits the use of the pooling-of-interests method of accounting and requires that the purchase method

of accounting be used for all business combinations initiated after June 30, 2001 and is applicable to all purchase method business combinations completed after June 30, 2001. SFAS No. 141 also specifies criteria that intangible assets acquired in a purchase method business combination must meet in order to be recognized and reported apart from goodwill. Effective for the Company beginning July 1, 2002, SFAS No. 142 will require that goodwill and intangible assets with indefinite useful lives no longer be amortized, but instead be tested for impairment at least annually in acceptance with the provisions of SFAS No. 142. SFAS No. 142 will also require that intangible assets with definite useful lives be amortized over their respective estimated useful lives to their estimated residual values, and review for impairment in accordance with SFAS No. 121, Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of.

As of the date of adoption, we expect to have unamortized goodwill and other intangibles in the amount of approximately $849,000, which will be subject to the transition provision of SFAS Nos. 141 and 142. Amortization expense related to goodwill and other intangibles was $70,905 for the nine-month period ended March 31, 2002. Because of the extensive effort needed to comply with adopting SFAS Nos. 141 and 142, it is not practicable to reasonably estimate the impact of adopting these Statements on our financial statements at the date of this report, including whether any transitional impairment losses will be required to be recognized as the cumulative effect of a change in accounting principles.

In June 2001, the FASB issued SFAS No. 143, Accounting for Asset Retirement Obligations, which addresses financial accounting and reporting for obligations associated with the retirement of tangible long-lived assets and the associated asset retirement costs. The standard applies to legal obligations associated

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with the retirement of long-lived assets that result from the acquisition, construction, development and/or normal use of the asset.

The Company is required and plans to adopt the provisions of SFAS No. 143 for the quarter ending September 30, 2002. To accomplish this, the Company must identify legal obligations for asset retirement obligations, if any, and determine the fair value of these obligations on the date of adoption. Because of the effort necessary to comply with the adoption of SFAS No. 143, it is not practicable for management to estimate the impact of adopting this Statement at the date of this report.

In August 2001, the FASB issued SFAS No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets, which supersedes both SFAS No. 121, Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of and the accounting and reporting provisions of APB Opinion No. 30, Reporting the Results of Operations--Reporting the Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual and Infrequently Occurring Events and Transactions, for the disposal of a segment of a business. SFAS No. 144 retains the fundamental provisions in SFAS No. 121 for recognizing and measuring impairment losses on long-lived assets held for use and long-lived assets to be disposed of by sale, while also resolving significant implementation issues associated with SFAS No. 121. SFAS No. 144 retains the basic provisions of APB Opinion 30 on how to present discontinued operations in the income statement but broadens that presentation to include a component of an entity rather than a segment of a business.

The Company is required and plans to adopt the provisions of SFAS No. 144 for the quarter ending September 30, 2002. Management does not expect the adoption

of SFAS No. 144 for long-lived assets held for use to have a material impact on the Company's financial statements because the impairment assessment under SFAS No. 144 is largely unchanged from SFAS No. 121. The provisions of the Statement for assets held for sale or other disposal generally are required to be applied prospectively after the adoption date to newly initiated disposal activities. Therefore, management cannot determine the potential effects that adoption of SFAS No. 144 will have on the Company's financial statements.

Business Plan

Over the past seven years, Dynatronics' annual net sales have more than tripled from $4.9 million in fiscal year 1994 to $16.8 million in fiscal year 2001. The Company believes that this growth is the result of many factors including acquisitions, strategic alliances, the introduction of new products and increasing market share. During the quarter ended March 31, 2002, the Company continued to implement a strategy of expanding product lines, strengthening channels of distribution, and developing new products for the rehabilitation and aesthetic markets.

As part of this strategy, in August 2000, the Company announced the signing of an agreement with Alan Neuromedical Technologies (ANT) granting Dynatronics the exclusive license for ANT's patented technology for treating chronic pain. Two devices incorporating the new technology - the Dynatron STS clinical unit and the Dynatron STS Rx prescription unit for home use - were introduced in February 2001 to distributors from around the world at meetings held in Salt Lake City, Utah. Currently, many medical professionals are using STS therapy to treat

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chronic pain associated with a variety of conditions in patients who had previously experienced only marginal results with traditional therapy regimens. According to the American Pain Foundation, millions of people around the world suffer from chronic pain. The associated costs in the United States alone are estimated to exceed $100 billion annually. There is great demand for an effective treatment in the battle against chronic pain.

In a research study published in the January, 2002 edition of the American Journal of Pain Management, test results showed 85% of chronic pain patients receiving STS treatments realized some reduction of pain -- with 50% of the patients becoming totally pain-free. The Company believes that the fact these results were achieved with patients who had suffered on average for eight years with their chronic pain condition further attests to the effectiveness of this therapy. Additional research studies are planned to further validate the efficacy of this innovative technology. Having the study published in a peer-reviewed medical journal has been an important factor in improving acceptance among medical practitioners and insurance carriers.

As with any new medical therapy or technology, we expect that insurance reimbursement may influence the rate of growth of the STS technology. Presently, limited reimbursement is available for STS treatments or home units. Most are reviewed on a case-by-case basis. However, as medical practitioners experience positive outcomes and further research supports the efficacy of this therapy, it is anticipated that reimbursements will be more broadly established. It will take time, perhaps years, to obtain broad acceptance and reimbursement for this new therapy. Notably, this technology potentially holds the key to not only relieving suffering for many chronic pain patients, but significantly reducing the long-term costs of supporting chronic pain patients through reducing intake of expensive narcotic medications or avoiding costly invasive procedures. We believe that as these potential cost savings are realized, insurance companies

should begin to view STS treatments as an economical alternative to the traditional treatments for chronic pain sufferers. STS treatments are not a panacea and do not help every chronic pain sufferer. However, it seems to be particularly effective with pain conditions that present with a sympathetic bias.

Interest in STS technology is experiencing particular growth in the workers compensation market. Workers' compensation carriers in several states have adopted or are considering offering an STS trial program to their clients. Management believes the development of the workers compensation market represents an important step in expanding STS treatment programs because a significant number of chronic pain patients are covered under workers' compensation plans.

During the reporting quarter, the Company made application to Medicare seeking coverage for STS treatments. While this process can often take years to obtain final approval, Medicare patients represent a major segment of chronic pain sufferers.

Dynatronics began selling the Dynatron STS clinical device during the quarter ended March 31, 2001, and the Dynatron STS Rx home unit during the fourth quarter of fiscal year 2001. The home unit is available to patients by prescription from their medical practitioner with financing terms available through third party finance companies.

Another important part of our strategic plan is the expansion of worldwide marketing efforts, particularly into the European Community. In March 2001, Dynatronics' Salt Lake operations, where all electrotherapy, ultrasound, STS devices and Synergie products are manufactured, was designated an ISO 9001 certified facility. With this designation in place, the Company can market products manufactured in this facility in any country that recognizes the CE Mark. We are now working to establish effective distribution of these products in the European Community.

A third strategic component of our growth plan is further expansion into the aesthetics market. The Synergie Peel microdermabrasion device was developed as a companion to the Synergie AMS (aesthetic massage system). Microdermabrasion technology is very popular in the aesthetics industry because of its distinct advantages over chemical and laser peels. The Synergie Peel device has unique competitive advantages in the market due to its patent-pending design, which eliminates clogging. Furthermore, the combination of the Synergie AMS and Synergie Peel make it not only unique, but the most affordable combination device of its kind on the market.

To take full advantage of the opportunities of the aesthetics market, Dynatronics has continued efforts to establish effective distribution for its aesthetic products. The Company's Chairman, Kelvyn H. Cullimore, is personally managing the effort to establish this distribution. We recently shifted our distribution strategy to establishing dealers who are uniquely focused on the aesthetics market and also to cultivating national accounts. Previously, we had attempted to establish a direct sales force for Synergie products. We changed our strategy because we believe that the dealer strategy requires less overhead expense, is more easily managed and will result in better local control of sales. Controlling and expanding the channels of distribution for these products is expected to ultimately increase sales and allow us to more fully access the potential of the aesthetics products market. We perceive this market to be both lucrative and expanding, particularly as aging baby boomers continue to look for

ways to retain a youthful appearance.

Over the past year, we have allocated resources to enhance the Company's presence in the e-business arena. Dynatronics has undertaken to improve the appearance and application of its corporate website and is researching ways to apply electronic media and Internet solutions to better serve customer needs, access new business opportunities, reduce cost of operations, and stay technologically current in the way business is conducted. We believe the allocation of resources to developing e-business capabilities is critical to improving future performance and have made the establishment of these capabilities a focal strategy for the next fiscal year. The site may be viewed at www.dynatronics.com. This reference to the Company's website is not intended to incorporate the contents of the website into or as a part of this report.

Based on these strategic initiatives, we are focusing the Company's resources in the following areas:

- Introducing the new Dynatron STS and Dynatron STS Rx therapy products to the billion-dollar chronic pain market. This includes efforts to maximize sales in the face of limited reimbursement by focusing on specific target markets that will embrace STS treatments such as workers compensation programs and thus better educate the medical and insurance communities on the efficacy of STS treatments. Additional

research and other related efforts will also be evaluated to obtain broader support of the medical and insurance communities.

- Improving sales and distribution of rehabilitation products domestically through strengthened relationships with dealers, particularly the high-volume specialty dealers.

- Expanding distribution of both rehabilitation and aesthetic products internationally.

- Introducing other new rehabilitation products and aesthetic products that fit the Dynatronics distribution system.

- Applying e-commerce solutions to improving overall performance.

Cautionary Statement Concerning Forward-Looking Statements

The statements contained in this Report on Form 10-QSB that are not purely historical are "forward-looking statements" within the meaning of Section 21E of the Securities Exchange Act. These statements refer to our expectations, hopes, beliefs, anticipations, commitments, intentions and strategies regarding the future. They may be identified by the use of the words or phrases "believes," "expects," "anticipates," "should," "plans," "estimates," "intends," and "potential," among others. Forward-looking statements include, but are not limited to, statements contained in Management's Discussion and Analysis or Plan of Operation regarding product development, clinical results, market acceptance, financial performance, revenue and expense levels in the future and the sufficiency of its existing assets to fund future operations and capital spending needs. Actual results could differ materially from the anticipated results or other expectations expressed in such forward-looking statements for the reasons detailed in our Annual Report on Form 10-KSB under the headings "Description of Business" and "Risk Factors." The fact that some of the risk factors may be the same or similar to past reports filed with the Securities and

Exchange Commission means only that the risks are present in multiple periods. We believe that many of the risks detailed here and in our other SEC filings are part of doing business in the industry in which we operate and compete and will likely be present in all periods reported. The fact that certain risks are endemic to the industry does not lessen their significance.

The forward-looking statements contained in this Report are made as of the date of this Report and we assume no obligation to update them or to update the reasons why actual results could differ from those projected in such forward-looking statements. Among others, risks and uncertainties that may affect the business, financial condition, performance, development, and results of operations include:

- The terrorist attacks in New York and Washington, D.C. on September 11, 2001, and the subsequent anthrax attacks on the East Coast of the United States appear to be having an adverse effect on business, financial and general economic conditions in the United States. At this time we cannot predict the nature, extent, or duration of these effects on overall economic conditions generally, or on our business and operations specifically.

- Market acceptance of our technologies, particularly our core therapy devices, Synergie AMS/MDA product line and the new Dynatron STS and Dynatron STS Rx products;
- Insurance company reimbursement for STS treatments or the home prescription Dynatron STS Rx device not materializing as expected;
- The ability to hire and retain the services of trained personnel at cost-effective rates;
- Rigorous government scrutiny or the possibility of additional government regulation of the industry in which we market our products;
- Reliance on key management personnel;
- Foreign government regulation of our products and manufacturing practices that may bar or significantly increase the expense of expanding to foreign markets;
- Economic and political risks related to expansion into international markets;
- Failure to sustain or manage growth including the failure to continue to develop new products or to meet demand for existing products;
- Reliance on information technology;
- The timing and extent of research and development expenses;
- The ability to keep pace with technological advances, which can occur rapidly;

- The loss of product market share to competitors;
- Potential adverse effect of taxation;
- The ability to obtain required financing to meet changes or other risks described above;

SIGNATURES

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

DYNATRONICS CORPORATION
Registrant

Date 5/14/02

/s/ Kelvyn H. Cullimore, Jr.
Kelvyn H. Cullimore, Jr.
President, Chief Executive Officer and Principal Accounting Officer