PETMED EXPRESS INC
Form 10-K
May 28, 2013

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-K

x ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended March 31, 2013

OR

o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from ___________ to ___________
Commission File Number 000-28827

PETMED EXPRESS, INC.
(Exact name of registrant as specified in its charter)

FLORIDA	65-0680967
(State or other jurisdiction of incorporation or organization)	(IRS Employer Identification No.)

1441 S.W. 29th Avenue, Pompano Beach, Florida 33069
(Address of principal executive offices) (Zip Code)

Registrant's telephone number, including area code: (954) 979-5995

Securities registered under Section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
COMMON STOCK, $.001 PAR VALUE	The NASDAQ Stock Market LLC (NASDAQ Global Select Market)

Securities registered under Section 12(g) of the Act:

NONE

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes o No x

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes o No x

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 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 o

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 229.405 of this chapter) during the preceeding12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No o

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. x

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See definition of "accelerated filer", "large accelerated filer", and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (check one):

Large accelerated filer	o	Accelerated filer	x
Non-accelerated filer	o	Smaller reporting company	o

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes o No x

The aggregate market value of the registrant's common stock held by non-affiliates of the registrant as of September 30, 2012, the last business day of the registrant's most recently completed second fiscal quarter, was $192.6 million based on the closing sales price of the registrant's Common Stock on that date, as reported on the NASDAQ Global Select Market.

The number of shares of the registrant's Common Stock outstanding as of May 28, 2013 was 20,108,773.

DOCUMENTS INCORPORATED BY REFERENCE

Information to be set forth in our Proxy Statement relating to our 2013 Annual Meeting of Stockholders to be held on July 26, 2013 is incorporated by reference in Items 10, 11, 12, 13, and 14 of Part III of this report.

PETMED EXPRESS, INC.

2013 Annual Report on Form 10-K

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PART I

CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING INFORMATION

Certain information in this Annual Report on Form 10-K includes forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. You can identify these forward-looking statements by the words “believes,” “intends,” “expects,” “may,” “will,” “should,” “plan,” “projects,” “contemplates,” “intends,” “budgets,” “predicts,” “estimates,” “anticipates,” or similar expressions. These statements are based our beliefs, as well as assumptions we have used based upon information currently available to us. Because these statements reflect our current views concerning future events, these statements involve risks, uncertainties and assumptions. Actual future results may differ significantly from the results discussed in the forward-looking statements. A reader, whether investing in our common stock or not, should not place undue reliance on these forward-looking statements, which apply only as of the date of this Annual Report.

When used in this Annual Report on Form 10-K, “PetMed Express,” “1-800-PetMeds,” “PetMeds,” “PetMed,” “PetMeds.com,” “PetMed Express.com,” “the Company,” “we,” “our,” and “us” refer to PetMed Express, Inc. and our wholly-owned subsidiaries.

ITEM 1. BUSINESS

General

PetMed Express, Inc. and subsidiaries, d/b/a 1-800-PetMeds, is a leading nationwide pet pharmacy. The Company markets prescription and non-prescription pet medications, and other health products for dogs and cats, direct to the consumer. The Company offers consumers an attractive alternative for obtaining pet medications in terms of convenience, price, and speed of delivery.

The Company markets its products through national television, online, and direct mail/print advertising campaigns, which aim to increase the recognition of the “1-800-PetMeds” brand name, and “PetMeds” family of trademarks, increase traffic on its website at www.1800petmeds.com, acquire new customers, and maximize repeat purchases. Our fiscal year end is March 31, our executive offices are located at 1441 S.W. 29th Avenue, Pompano Beach, Florida 33069, and our telephone number is (954) 979-5995.

Our Products

We offer a broad selection of products for dogs and cats. Our current product line contains approximately 3000 SKUS of the most popular pet medications, health products, and supplies. These products include a majority of the well-known brands of medication, such as Frontline Plus®, K9 Advantix® II, Advantage® II, Heartgard Plus®, Sentinel®, Revolution®, and Rimadyl®. Generally, our prices are competitive with the prices for medications charged by veterinarians and retailers. In March 2010, the Company started offering for sale additional pet supplies on our website, which are drop shipped to our customers by third parties. These pet supplies include: food, beds, crates, stairs, strollers, and other popular pet supplies.

We research new products, and regularly select new products or the latest generation of existing products to become part of our product selection. In addition, we also refine our current products to respond to changing consumer-purchasing habits. Our website is designed to give us the flexibility to change featured products or promotions. Our product line provides customers with a wide variety of selections across the most popular health categories for dogs and cats. Our current products include:

Non-Prescription Medications (OTC) and supplies: Flea and tick control products, bone and joint care products, vitamins, treats, nutritional supplements, hygiene products, and supplies.

Prescription Medications (Rx): Heartworm preventatives, arthritis, thyroid, diabetes, pain medications, antibiotics, and other specialty medications, as well as generic substitutes.

Sales

The following table provides a breakdown of the percentage of our total sales by each category during the indicated periods:

	Year Ended March 31,					
	2013		2012		2011	
Non-prescription medications and supplies	59	%	59	%	61	%
Prescription medications	40	%	40	%	38	%
Shipping and handling charges and other	1	%	1	%	1	%
Total	100	%	100	%	100	%

We offer our products through three main sales channels: Internet through our website, telephone contact center through our toll-free number, and direct mail/print through 1-800-PetMeds catalogs, brochures, and postcards. We have designed our catalogs and website to provide a convenient, cost-effective, and informative shopping experience that encourages consumers to purchase products important for a pet's health and quality of life. We believe that these multiple channels allow us to increase the visibility of our brand name and provide our customers with increased shopping flexibility and excellent service.

Internet

We seek to combine our product selection and pet health information with the shopping ease of the Internet to deliver a convenient and personalized shopping experience. Our website offers health and nutritional product selections for dogs and cats, and relevant editorial and easily obtainable or retrievable resource information. From our home page, customers can search our website for products and access resources on a variety of information on dogs and cats. Customers can shop at our website by category, product line, individual product, or symptom. We attracted approximately 22.7 million visitors to our website during fiscal 2013, approximately 10% of those visitors placed an order, and our website generated approximately 77% of our total sales for the same time period. On our website pet owners have access to health information covering pets' behavior and illnesses, and natural and pharmaceutical remedies specifically for a pet's problems. The pet education content on our main website is periodically updated with the latest research for pet owners.

Telephone Contact Center

Our customer care representatives receive and process inbound and outbound customer calls, facilitate our live web chat, and process customer e-mails. Our telephone system is equipped with certain features including pop-up screens and call blending capabilities that give us the ability to efficiently utilize our customer care representatives' time, providing excellent customer care, service, and support. Our customer care representatives receive a base salary and are rewarded with commissions for sales, and bonuses and other awards for achieving certain quality goals.

Direct Mail/Print

The 1-800-PetMeds catalog is a full-color catalog that features our most popular products. The catalog is produced by a combination of in-house writers, production artists, and independent contractors. We mail catalogs, brochures, and postcards in response to requests generated from our advertising and as part of direct mail campaigns to our customers.

Our Customers

Approximately 2.7 million customers have purchased from us within the last two years. We attracted approximately 630,000 and 722,000 new customers in fiscal 2013 and 2012, respectively. Our customers are located throughout the United States, with approximately 50% of customers residing in California, Florida, New York, Texas, Pennsylvania, Virginia, North Carolina, and New Jersey. Our primary focus has been on retail customers and the average purchase was approximately $73 for fiscal 2013 compared to $76 for fiscal 2012.

Marketing

The goal of our marketing strategy is to build brand recognition, increase customer traffic, add new customers, build strong customer loyalty, maximize reorders, and develop incremental revenue opportunities. We have an integrated marketing campaign that includes television advertising, online marketing, direct mail/print and e-mail.

Television Advertising

Our television advertising is designed to build brand equity, create brand awareness, and generate initial purchases of products via the telephone and the Internet. We have used :30 and :15 second television commercials to attract new customer orders. Our television commercials typically focus on our ability to rapidly deliver to customers the same medications offered by veterinarians, but at reduced prices. We generally purchase advertising on national cable channels to target our key demographic group – women, ages 30 to 65. We believe that television advertising is particularly effective and instrumental in building brand awareness.

Online Marketing

We supplement our traditional advertising with online advertising and marketing efforts. We make our brand available to Internet consumers by purchasing targeted keywords and achieving prominent placement on the top search engines and search engine networks, including Google, Bing™, and Yahoo®. We utilize Internet display and video advertisements, social media, and comparison shopping, and we are also members of the LinkShare Network, which is an affiliate program with merchant clients and affiliate websites.

Direct Mail/Print and E-mail

We use direct mail/print and e-mail to acquire new customers and to remind our existing customers to reorder.

Operations

Order Processing

Our website allows customers to easily browse and purchase all of our products online. Our website is designed to be fast, secure, and easy to use with order and shipping confirmations, and with online order tracking capabilities. We provide our customers with toll-free telephone access to our customer care representatives. Our call center generally operates from 8:00 AM to 11:00 PM, Monday through Thursday, 8:00 AM to 9:00 PM on Friday, 9:00 AM to 6:00 PM on Saturday, and 10:00 AM to 5:00 PM on Sunday, Eastern Time. The process of customers purchasing products from 1-800-PetMeds consists of a few simple steps. A customer first places a call to our toll-free telephone number or visits our website. The following information is needed to process prescription orders: pet information, prescription information, and the veterinarian's name and phone number. This information is entered into our computer system. Then our pharmacists and pharmacy technicians verify all prescriptions. The order process system checks for the verification for prescription medication orders and a valid payment method for all orders. An invoice is generated and printed in our fulfillment center, where items are picked, and then shipped via United States Postal Service, Federal Express, or UPS. Our customers enjoy the convenience of rapid home delivery, with approximately 80% of all orders being shipped within 24 hours of ordering.

Customer Care and Support

We believe that a high level of customer care and support is critical in retaining and expanding our customer base. Customer care representatives participate in ongoing training programs under the supervision of our training managers. These training sessions include a variety of topics such as product knowledge, computer usage, customer service tips, and the relationship between our Company and veterinarians. Our customer care representatives respond to customers' e-mails, calls, and live chats that are related to products, order status, prices, and shipping. We believe our customer care representatives are a valuable source of feedback regarding customer satisfaction.

Warehousing and Shipping

We inventory our products and fill most customer orders from our corporate headquarters in Pompano Beach, Florida. We have an in-house fulfillment and distribution operation, which is used to manage the entire supply chain, beginning with the placement of the order, continuing through order processing, and then fulfilling and shipping of the product to the customer. We offer a variety of shipping options, including next day delivery. We ship to anywhere in the United States served by the United States Postal Service, Federal Express, or UPS. Priority orders are expedited in our fulfillment process. Our goal is to ship the products the same day that the order is received. For prescription medications, our goal is to ship the product immediately after the prescription has been authorized by the customer's veterinarian.

Purchasing

We purchase our products from a variety of sources, including certain manufacturers, domestic distributors, and wholesalers. There were five suppliers from whom we purchased approximately 50% of all products in fiscal 2013. We purchase the majority of our health and nutritional supplements directly from manufacturers. We believe having strong relationships with product manufacturers will ensure the availability of an adequate volume of products ordered by our customers, and will enable us to provide more and better product information. Historically, substantially all the major manufacturers of prescription and non-prescription medications have declined to sell these products to direct marketing companies, such as our Company. (See Risk Factors.) Part of our growth strategy includes developing direct relationships with the leading pharmaceutical manufacturers of the more popular prescription and non-prescription medications.

Technology

We utilize integrated technologies in our call centers, e-commerce, order entry, and inventory control/fulfillment operations. Our systems are custom configured by the Company to optimize our computer telephone integration and mail-order processing. The systems are designed to maintain a large database of specialized information and process a large volume of orders efficiently and effectively. Our systems provide our customer care representatives, and our customers on our website, with real time product availability information and updated customer information to enhance our customer care. We also have an integrated direct connection for processing credit cards to ensure that a valid credit card number and authorization have been received at the same time our customer care representatives are on the phone with the customer or when a customer submits an order on our website. Our information systems provide our customer care representatives with records of all prior contact with a customer, including the customer's address, phone number, e-mail address, prescription information, order history, payment history, and notes.

Competition

The pet medications market is competitive and highly fragmented. Our competitors consist of veterinarians, and online and traditional retailers. We believe that the following are the principal competitive factors in our market:

- Product selection and availability, including the availability of prescription and non-prescription medications;
- Brand recognition;
- Reliability and speed of delivery;
- Personalized service and convenience;
- Price; and
- Quality of website content.

We compete with veterinarians for the sale of prescription and non-prescription pet medications and other health products. Many pet owners may prefer the convenience of purchasing their pet medications or other health products at the time of a veterinarian visit. In order to effectively compete with veterinarians, we must continue to educate pet owners about the service, convenience, and savings offered by our Company.

According to the American Pet Products Manufacturers Association, pet spending in the United States increased 4.7% to $53.3 billion in 2012. Pet supplies and medications represented $12.6 billion, or 24% of the total spending on pets in the United States. The pet medication market that we participate in is estimated to be approximately $4.0 billion, with veterinarians having the majority of the market share. The dog and cat population is approximately 165 million, with approximately 62% of all households having a pet.

We believe that the following are the main competitive strengths that differentiate 1-800-PetMeds from the competition:

- Channel leader, in an estimated $4.0 billion industry;
- “1-800-PetMeds” brand name;
- Licensed pharmacy to conduct business in 50 states, and awarded Vet-VIPPSCM (Veterinary-Verified Internet Pharmacy Practice Site) accreditation by the National Association of Boards of Pharmacy®;
- Exceptional customer care and support

Intellectual Property

We conduct our business under the trade name “1-800-PetMeds” and use a family of names all containing the term “PetMeds” or “PetMed” in some form. We believe this trade name, which is also our toll-free telephone number, and the “PetMeds” family of trademarks, have added significant value and are an important factor in the marketing of our products. We have also obtained the right to use and control the Internet addresses www.1800petmeds.com, www.1888petmeds.com, www.petmedexpress.com, www.petmed.com, and www.petmeds.com. We do not expect to lose the ability to use the Internet addresses; however, there can be no assurance in this regard and the loss of these addresses may have a material adverse effect on our financial position and results of operations. We are the exclusive owners of United States Trademark Registrations for “PetMed Express and Design®,” “1888PetMeds and Design®,” “1-800-PetMeds and Design®,” 1-800-PetMeds®,” and “PetMeds®.”

Government Regulation

Dispensing prescription medications is governed at the state level by the Boards of Pharmacy, or similar regulatory agencies, of each state where prescription medications are dispensed. We are subject to regulation by the State of Florida and are licensed as a community pharmacy by the Florida Board of Pharmacy. Our current license is valid until February 28, 2015, and prior to that date a renewal application will be submitted to the Board of Pharmacy. Our pharmacy practice is also licensed and/or regulated by 49 other state pharmacy boards and, with respect to our products, by other regulatory authorities including, but not necessarily limited to, the United States Food and Drug Administration (“FDA”) and the United States Environmental Protection Agency. As a licensed pharmacy in the State of Florida, we are subject to the Florida Pharmacy Act and regulations promulgated thereunder. To the extent that we are unable to maintain our license as a community pharmacy with the Florida Board of Pharmacy, or if we do not maintain the licenses granted by other state pharmacy boards, or if we become subject to actions by the FDA, or other enforcement regulators, our distribution of prescription medications to pet owners could cease, which could have a material adverse effect on our financial condition and results of operations.

Employees

We currently have 206 full time employees, including: 126 in customer care and marketing; 33 in fulfillment and purchasing; 36 in our pharmacy; 3 in information technology; 3 in administrative positions; and 5 in management. None of our employees are represented by a labor union, or governed by any collective bargaining agreements. We consider relations with our employees to be satisfactory.

Available Information

We file annual, quarterly, and current reports, proxy statements, and other information with the Securities and Exchange Commission ("SEC"). Our SEC filings, including our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and any amendments to those reports filed or furnished pursuant to the Exchange Act are available free of charge over the Internet on our website at www.1800petmeds.com or at the SEC's web site at www.sec.gov. Our SEC filings will be available through our website as soon as reasonably practicable after we have electronically filed or furnished them to the SEC. Information contained on our website is not incorporated by reference into this annual report on Form 10-K.

ITEM 1A. RISK FACTORS

You should carefully consider the risks and uncertainties described below, and all the other information included in this Annual Report on Form 10-K before you decide to invest in our common stock. Any of the following risks could materially adversely affect our business, financial condition, or operating results and could result in a loss of your investment.

We may inadvertently fail to comply with various state regulations covering the dispensing of prescription pet medications which may subject us to reprimands, sanctions, probations, fines, suspensions, or the loss of one or more of our pharmacy licenses.

The sale and delivery of prescription pet medications is generally governed by state laws and state regulations. Since our pharmacy is located in the State of Florida, the Company is governed by the laws and regulations of the State of Florida. Each prescription pet medication sale we make is likely also to be covered by the laws of the state where the customer is located. The laws and regulations relating to the sale and delivery of prescription pet medications vary from state to state, but generally require that prescription pet medications be dispensed with the authorization from a prescribing veterinarian. To the extent that we are unable to maintain our license as a community pharmacy with the Florida Board of Pharmacy, or if we do not maintain the licenses granted by other state boards, or if we become subject to actions by the FDA, or other enforcement regulators, our dispensing of prescription medications to pet owners could cease, which could have a material adverse effect on our operations.

The Company is a party to routine litigation and administrative complaints incidental to its business. Management does not believe that the resolution of any or all of such routine litigation and administrative complaints is likely to have a material adverse effect on the Company’s financial condition or results of operations. While we make every effort to fully comply with all applicable state rules, laws, and regulations, from time to time we have been the subject of administrative complaints regarding the authorization of prescriptions prior to shipment. We cannot assure you that we will not continue to be the subject of administrative complaints in the future. We cannot guarantee you that we will not be subject to reprimands, sanctions, probations, or fines, or that one or more of our pharmacy licenses will not be suspended or revoked. If we were unable to maintain our license as a community pharmacy in the State of Florida, or if we are not granted licensure in a state that begins to require licensure, or if one or more of the licenses granted by other state boards should be suspended or revoked, our ability to continue to sell prescription medications and to continue our business as it is presently conducted could be in jeopardy.

We currently purchase a portion of our prescription and non-prescription medications from third party distributors and we are not an authorized distributor of these products. We do not have any guaranteed supply of medications at any pre-established prices.

The majority of our sales were attributable to sales of prescription and non-prescription medications. Historically, substantially all the major pharmaceutical manufacturers have declined to sell prescription and non-prescription pet medications directly to us. In order to assure a supply of these products, we purchase medications from various secondary sources, including a variety of domestic distributors. Our business strategy includes seeking to establish direct purchasing arrangements with major pet pharmaceutical manufacturing companies. If we are not successful in achieving this goal, we will continue to rely upon secondary sources.

We cannot guarantee that if we continue to purchase prescription and non-prescription pet medications from secondary sources that we will be able to purchase an adequate supply to meet our customers’ demands, or that we will be able to purchase these products at competitive prices. As these products represent a significant portion of our sales, our failure to fill customer orders for these products could adversely impact our sales. If we are forced to pay higher prices for these products to ensure an adequate supply, we cannot guarantee that we will be able to pass along to our customers any increases in the prices we pay for these medications. This inability to pass along increased prices could materially adversely affect our financial condition and results of operations.

Our failure to properly manage our inventory may result in excessive inventory carrying costs, or inadequate supply of products, which could materially adversely affect our financial condition and results of operations.

Our current product line contains approximately 3,000 SKUs. A significant portion of our sales is attributable to products representing approximately 100 SKUs, including the most popular flea and tick, and heartworm preventative brands. We need to properly manage our inventory to provide an adequate supply of these products and avoid excessive inventory of the products representing the balance of the SKUs. We generally place orders for products with our suppliers based upon our internal estimates of the amounts of inventory we will need to fill future orders. These estimates may be significantly different from the actual orders we receive.

In the event that subsequent orders fall short of original estimates, we may be left with excess inventory. Significant excess inventory could result in price discounts and increased inventory carrying costs. Similarly, if we fail to have an adequate supply of some SKUs, we may lose sales opportunities. We cannot guarantee that we will maintain appropriate inventory levels. Any failure on our part to maintain appropriate inventory levels may have a material adverse effect on our financial condition and results of operations.

Resistance from veterinarians to authorize prescriptions, or attempts/efforts on their part to discourage pet owners to purchase from internet mail-order pharmacies could cause our sales to decrease and could materially adversely affect our financial condition and results of operations.

Since we began our operations some veterinarians have resisted providing our customers with a copy of their pet's prescription or authorizing the prescription to our pharmacy staff, thereby effectively preventing us from filling such prescriptions under state law. We have also been informed by customers and consumers that veterinarians have tried to discourage pet owners from purchasing from internet mail-order pharmacies. Sales of prescription medications represented approximately 40% of our sales for the fiscal year. Although veterinarians in some states are required by law to provide a pet owner with a prescription if medically appropriate, if the number of veterinarians who refuse to authorize prescriptions should increase, or if veterinarians are successful in discouraging pet owners from purchasing from internet mail-order pharmacies, our sales could decrease and our financial condition and results of operations may be materially adversely affected.

Significant portions of our sales are made to residents of eight states. If we should lose our pharmacy license in one or more of these states, our financial condition and results of operations would be materially adversely affected.

While we ship pet medications to customers in all 50 states, approximately 50% of our sales for the fiscal year ended March 31, 2013 were made to customers located in the states of California, Florida, New York, Texas, Pennsylvania, Virginia, North Carolina, and New Jersey. If for any reason our license to operate a pharmacy in one or more of those states should be suspended or revoked, or if it is not granted or renewed, our ability to sell prescription medications to residents of those states would cease and our financial condition and results of operations in future periods would be materially adversely affected.

We face significant competition from veterinarians and online and traditional retailers and may not be able to compete profitably with them.

We compete directly and indirectly with veterinarians for the sale of pet medications and other health products. Veterinarians hold a competitive advantage over us because many pet owners may find it more convenient or preferable to purchase these products directly from their veterinarians at the time of an office visit. We also compete directly and indirectly with both online and traditional retailers. Both online and traditional retailers may hold a competitive advantage over us because of longer operating histories, established brand names, greater resources, and/or an established customer base. Online retailers may have a competitive advantage over us because of established affiliate relationships to drive traffic to their website. Traditional retailers may hold a competitive advantage over us because pet owners may prefer to purchase these products from a store instead of online or through catalog or telephone methods. In order to effectively compete in the future, we may be required to offer promotions and other incentives, which may result in lower operating margins and adversely affect the results of operations.

We also face a significant challenge from our competitors forming alliances with each other, such as those between online and traditional retailers. These relationships may enable both their retail and online stores to negotiate better pricing and better terms from suppliers by aggregating the demand for products and negotiating volume discounts, which could be a competitive disadvantage to us.

The content of our website could expose us to various kinds of liability, which, if prosecuted successfully, could negatively impact our business.

Because we post product and pet health information and other content on our website, we face potential liability for negligence, copyright infringement, patent infringement, trademark infringement, defamation, and/or other claims based on the nature and content of the materials we post. Various claims have been brought, and sometimes successfully prosecuted, against Internet content distributors. We could be exposed to liability with respect to the unauthorized duplication of content or unauthorized use of other parties' proprietary technology. Although we maintain general liability insurance, our insurance may not cover potential claims of this type, or may not be adequate to indemnify us for all liability that may be imposed. Any imposition of liability that is not covered by insurance, or is in excess of insurance coverage, could materially adversely affect our financial condition and results of operations.

We may not be able to protect our intellectual property rights, and/or we may be found to infringe on the proprietary rights of others.

We rely on a combination of trademarks, trade secrets, copyright laws, and contractual restrictions to protect our intellectual property rights. These afford only limited protection. Despite our efforts to protect our proprietary rights, unauthorized parties may attempt to copy our non-prescription private label generic equivalents, when and if developed, as well as aspects of our sales formats, or to obtain and use information that we regard as proprietary, including the technology used to operate our website and our content, and our trademarks. Litigation or proceedings before the United States Patent and Trademark Office or other bodies may be necessary in the future to enforce our intellectual property rights, to protect our trade secrets and domain names, or to determine the validity and scope of the proprietary rights of others. Any litigation or adverse proceeding could result in substantial costs and diversion of resources, and could seriously harm our business and operating results. Third parties may also claim infringement by us with respect to past, current, or future technologies. We expect that participants in our market will be increasingly involved in infringement claims as the number of services and competitors in our industry segment grows. Any claim, whether meritorious or not, could be time-consuming, result in costly litigation, cause service upgrade delays, or require us to enter into royalty or licensing agreements. These royalty or licensing agreements might not be available on terms acceptable to us or at all.

If we are unable to protect our Internet addresses or to prevent others from using Internet addresses that are confusingly similar, our business may be adversely impacted.

Our Internet addresses, www.1800petmeds.com, www.1888petmeds.com, www.petmedexpress.com, www.petmed.com, and www.petmeds.com are critical to our brand recognition and our overall success. If we are unable to protect these Internet addresses, our competitors could capitalize on our brand recognition. There may be similar Internet addresses used by competitors. Governmental agencies and their designees generally regulate the acquisition and maintenance of Internet addresses. The regulation of Internet addresses in the United States and in foreign countries has changed, and may undergo further change in the near future. Furthermore, the relationship between regulations governing Internet addresses and laws protecting trademarks and similar proprietary rights is unclear. Therefore, we may not be able to protect our own Internet addresses, or prevent third parties from acquiring Internet addresses that are confusingly similar to, infringe upon, or otherwise decrease the value of our Internet addresses.

Since all of our operations are housed in a single location, we are more susceptible to business interruption in the event of damage to or disruptions in our facility.

Our headquarters and distribution center are located in two buildings in one location in South Florida, and most of our shipments of products to our customers are made from this sole distribution center. We have no present plans to establish any additional distribution centers or offices. Because we consolidate our operations in one location, we are more susceptible to power and equipment failures, and business interruptions in the event of fires, floods, and other natural disasters than if we had additional locations. Furthermore, because we are located in South Florida, which is a hurricane-sensitive area, we are particularly susceptible to the risk of damage to, or total destruction of, our headquarters and distribution center and surrounding transportation infrastructure caused by a hurricane. We cannot assure you that we are adequately insured to cover the amount of any losses relating to any of these potential events, business interruptions resulting from damage to or destruction of our headquarters and distribution center, or power and equipment failures relating to our call center or websites, or interruptions or disruptions to major transportation infrastructure, or other events that do not occur on our premises. The occurrence of one or more of these events could adversely impact our ability to generate revenues in future periods.

Our operating results are difficult to predict and may fluctuate, and a portion of our sales are seasonal.

Factors that may cause our operating results to fluctuate include:

- Our ability to obtain new customers at a reasonable cost, retain existing customers, or encourage reorders;
- Our ability to increase the number of visitors to our website, or our ability to convert visitors to our website into customers;
- The mix of medications and other pet products sold by us;
- Our ability to manage inventory levels or obtain an adequate supply of products;
- Our ability to adequately maintain, upgrade, and develop our website, the systems that we use to process customers' orders and payments, or our computer network;
- Increased competition within our market niche;
- Price competition;
- New products introduced to the market, including generics;
- Increases in the cost of advertising;
- The amount and timing of operating costs and capital expenditures relating to expansion of our product line or operations;
- Disruption of our toll-free telephone service, technical difficulties, or systems and Internet outages or slowdowns; and
- Unfavorable general economic trends.

Because our operating results are difficult to predict, we believe that quarter-to-quarter comparisons of our operating results are not a good indication of our future performance. The majority of our product sales are affected by the seasons, due to the seasonality of mainly heartworm, and flea and tick medications. For the quarters ended June 30, 2012, September 30, 2012, December 31, 2012, and March 31, 2013, Company sales were 30%, 26%, 22%, and 22%, respectively. In addition to the seasonality of our sales, our annual and quarterly operating results have fluctuated in the past and may fluctuate significantly in the future due to a variety of factors, including weather, many of which are out of our control. Any change in one or more of these factors could materially adversely affect our financial condition and results of operations in future periods.

Our stock price fluctuates from time to time and may fall below expectations of securities analysts and investors, and could subject us to litigation, which may result in you suffering a loss on your investment.

The market price of our common stock may fluctuate significantly in response to a number of factors, many of which are out of our control. These factors include: quarterly variations in operating results; changes in accounting treatments or principles; announcements by us or our competitors of new products and services offerings; significant contracts, acquisitions, or strategic relationships; additions or departures of key personnel; any future sales of our common stock or other securities; stock market price and volume fluctuations of publicly-traded companies; and general political, economic, and market conditions.

In some future quarter our operating results may fall below the expectations of securities analysts and investors, which could result in a decrease in the trading price of our common stock. In the past, securities class action litigation has often been brought against a company following periods of volatility in the market price of its securities. We may be the target of similar litigation in the future. Securities litigation could result in substantial costs and divert management's attention and resources, which could seriously harm our business and operating results.

We may issue additional shares of preferred stock that could defer a change of control or dilute the interests of our common stockholders. Our charter documents could defer a takeover effort which could inhibit your ability to receive an acquisition premium for your shares.

Our charter permits our Board of Directors to issue up to 5.0 million shares of preferred stock without stockholder approval. Currently there are 2,500 shares of our Convertible Preferred Stock issued and outstanding. This leaves a little less than 5.0 million shares of preferred stock available for issuance at the discretion of our Board of Directors. These shares, if issued, could contain dividend, liquidation, conversion, voting, or other rights which could adversely affect the rights of our common stockholders and which could also be utilized, under some circumstances, as a method of discouraging, delaying, or preventing a change in control. Provisions of our articles of incorporation, bylaws and Florida law could make it more difficult for a third party to acquire us, even if many of our stockholders believe it is in their best interest.

The United States Environmental Protection Agency ("EPA") has announced its intention to increase restrictions on flea and tick products and to caution consumers to use these products with extra care. The Company's sales and profits in future periods could be adversely impacted if sales for these products decline.

The EPA is taking a series of actions to increase the safety of spot-on pesticide products for flea and tick control for cats and dogs. In the past the EPA received complaints about certain "spot-on" pest prevention products, including some flea and tick control products that the Company currently sells. The complaints reported adverse reactions ranging from mild effects such as skin irritations to more serious effects such as seizures and, in some cases, death of the pet. Since that time, the EPA received additional information from the pet spot-on pesticide registrants and others and began an intensive evaluation of these products. Among immediate actions that the EPA is going to pursue are: requiring manufacturers of spot-on pesticide products to improve labeling, making instructions clearer to prevent product misuse; requiring more precise label instructions to ensure proper dosage per pet weight; requiring clear markings to differentiate between dog and cat products, and disallowing similar brand names for dog and cat products. There can be no assurances that this action by the EPA will not adversely affect our future sales and profits.

A failure of our information systems or any security breach or unauthorized disclosure of confidential information could have a material adverse effect on our business.

Our business is dependent upon the efficient operation of our information systems. In particular, we rely on our information systems to effectively manage our business model strategy, with tools to track and manage sales, inventory, marketing, customer service efforts, the preparation of our consolidated financial and operating data, credit card information, and customer information. The failure of our information systems to perform as designed or the failure to maintain and enhance or protect the integrity of these systems could disrupt our business operations, impact sales and the results of operations, expose us to customer or third-party claims, or result in adverse publicity. Additionally, we collect, process, and retain sensitive and confidential customer information in the normal course of our business. Despite the security measures we have in place and any additional measures we may implement in the future, our facilities and systems, and those of our third-party service providers, could be vulnerable to security breaches, computer viruses, lost or misplaced data, programming errors, human errors, acts of vandalism, or other events. Any security breach or event resulting in the misappropriation, loss, or other unauthorized disclosure of confidential information, whether by us directly or our third-party service providers, could damage our reputation, expose us to the risks of litigation and liability, disrupt our business, or otherwise affect our results of operations.

ITEM 1B. UNRESOLVED STAFF COMMENTS

None

ITEM 2. PROPERTIES

Our facilities, including our principal executive offices, are located at 1441 S.W. 29th Avenue and 2900 Gateway Drive, Pompano Beach, Florida 33069. The Company leases its 65,300 square foot executive offices, warehouse facility and customer service and pharmacy contact centers under a non-cancelable operating lease, through May 31, 2015. The Company is responsible for certain maintenance costs, taxes, and insurance under this lease. The future minimum annual lease payments are as follows: $784,000 for fiscal 2014, $794,000 for fiscal 2015, and $133,000 for fiscal 2016, a lease payment total of $1.7 million. Rent expense was $767,000, $745,000, and $724,000 for the years ended March 31, 2013, 2012 and 2011, respectively. We believe that our facilities are sufficient for our current needs and are in good condition in all material respects.

ITEM 3. LEGAL PROCEEDINGS

The Company has settled complaints that had been filed with various states' pharmacy boards in the past. There can be no assurances made that other states will not attempt to take similar actions against the Company in the future. The Company initiates litigation to protect its trade or service marks. There can be no assurance that the Company will be successful in protecting its trade or service marks. Legal costs related to the above matters are expensed as incurred.

ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

PART II

ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

Our common stock is traded on the NASDAQ Global Select Market ("NASDAQ") under the symbol "PETS." The prices set forth below reflect the range of high and low closing sale prices per share in each of the quarters of fiscal 2013 and 2012 as reported by the NASDAQ.

Fiscal 2013:	High	Low
First Quarter	$ 13.76	$ 11.07
Second Quarter	$ 12.35	$ 9.36
Third Quarter	$ 12.39	$ 9.95
Fourth Quarter	$ 14.37	$ 11.09

Fiscal 2012:	High	Low
First Quarter	$ 15.89	$ 11.53
Second Quarter	$ 12.28	$ 8.91
Third Quarter	$ 10.55	$ 8.57
Fourth Quarter	$ 12.72	$ 10.17

There were 77 holders of record of our common stock at May 27, 2013, and approximately 15,000 of our holders are "street name" or beneficial holders, whose shares are held by banks, brokers, or other financial institutions.

Dividend Policy

On August 3, 2009, the Company's Board of Directors declared its first quarterly dividend of $0.10 per share on its common stock. On August 2, 2010, the Company's Board of Directors increased the quarterly dividend to $0.125 per share, and then on January 27, 2012, the Company's Board of Directors increased the quarterly dividend to $0.15 per share. On December 3, 2012, the Company's Board of Directors declared a special dividend of $1.00 per share on its common stock. The Company intends to continue to pay regular quarterly dividends; however the declaration and payment of future dividends is discretionary and will be subject to a determination by the Board of Directors each quarter following its review of the Company's financial performance.

During fiscal 2013, our Board of Directors declared the following dividends:

Declaration Date	Per Share Dividend	Record Date	Total Amount (In thousands)	Payment Date
May 7, 2012	$ 0.150	May 14, 2012	$ 3,050	May 25, 2012
July 30, 2012	$ 0.150	August 13, 2012	$ 3,049	August 24, 2012
October 29, 2012	$ 0.150	November 9, 2012	$ 3,001	November 23, 2012
December 3, 2012	$ 1.000	December 14, 2012	$ 20,001	December 24, 2012
January 28, 2013	$ 0.150	February 8, 2013	$ 3,000	February 22, 2013

On May 3, 2013, the Company's Board of Directors declared a quarterly dividend of $0.15 per share on its common stock. The $3.0 million dividend was paid on May 24, 2013, to shareholders of record at the close of business on May 15, 2013.

Share Repurchase Plan

On November 8, 2006, the Company's Board of Directors approved a share repurchase plan of up to $20.0 million. On October 31, 2008, November 1, 2010, and August 1, 2011, the Company's Board of Directors approved a second, third, and fourth share repurchase plan, respectively, each for an additional $20.0 million. The repurchase plan is intended to be implemented through purchases made from time to time in either the open market or through private transactions at the Company's discretion, subject to market conditions and other factors, in accordance with Securities and Exchange Commission requirements. There can be no assurances as to the precise number of shares that will be repurchased under the share repurchase plan, and the Company may discontinue the share repurchase plan at any time subject to compliance with applicable regulatory requirements. Shares purchased pursuant to the share repurchase plan will either be cancelled or held in the Company's treasury.

During fiscal 2013 the Company repurchased approximately 397,000 shares of the Company’s outstanding common stock for approximately $3.9 million, averaging approximately $9.74 per share. As of March 31, 2013, the Company had approximately $10.2 million remaining under the Company’s share repurchase plan. During fiscal 2012 the Company repurchased approximately 2.1 million shares of the Company’s outstanding common stock for approximately $23.7 million, averaging approximately $11.36 per share. All shares repurchased in fiscal 2013 and 2012 were subsequently retired. Since the inception of the share repurchase plan, approximately 5.6 million shares have been repurchased under the plan for approximately $69.8 million, averaging approximately $12.54 per share, with approximately $10.2 million remaining available for repurchase, as of May 27, 2013.

Performance Graph

Set forth below is a graph comparing the five year cumulative performance of our Common Stock with the Standard & Poor’s Composite-500 Stock Index (the “S&P 500”), the Nasdaq Composite, and the Russell 2000, from March 31, 2008 to March 31, 2013. The graph assumes that $100 was invested on March 31, 2008 in each of our Common Stock, the S&P 500, the Nasdaq Composite, and the Russell 2000 and that all dividends were reinvested. The performance graph and related information below shall not be deemed “filed” with the Securities and Exchange Commission, nor shall such information be incorporated by reference into any future filing under the Securities Act of 1933 or Securities Exchange Act of 1934, each as amended, except to the extent that we specifically incorporate it by reference into such filing.

Performance graph data:

	Fiscal Year Ended March 31,					
	2008	2009	2010	2011	2012	2013
Nasdaq Composite	100.00	67.07	105.22	122.02	135.65	143.37
S&P 500	100.00	60.32	88.41	100.24	106.48	118.64
Russell 2000	100.00	61.45	98.64	122.61	120.69	138.31
PetMed Express, Inc.	100.00	148.60	199.91	143.01	111.63	121.01

Securities Authorized for Issuance under Equity Compensation Plans

The following table sets forth securities authorized for issuance under equity compensation plans, including individual compensation arrangements, by us under our 2006 Employee Equity Compensation Restricted Stock Plan and 2006 Outside Director Equity Compensation Restricted Stock Plan as of March 31, 2013:

EQUITY COMPENSATION PLAN INFORMATION
(In thousands, except for per share amounts)

Plan category	Number of securities to be issued upon exercise of outstanding options, warrants and rights	Weighted average exercise price of outstanding options, warrants and rights	Number of securities remaining available for future issuance under equity compensation plans
2006 Employee Restricted Stock Plan	680	-	420
2006 Director Restricted Stock Plan	182	-	258
Total	862		678

ITEM 6. SELECTED FINANCIAL DATA

The following selected financial data should be read together with “Management’s Discussion and Analysis of Financial Condition and Results of Operations,” the Consolidated Financial Statements and notes thereto, and other financial information included elsewhere in this Annual Report on Form 10-K. The Consolidated Statements of Income data set forth below for the fiscal years ended March 31, 2013, 2012, and 2011 and the Consolidated Balance Sheet data as of March 31, 2013 and 2012 have been derived from our audited Consolidated Financial Statements which are included elsewhere in this Annual Report on Form 10-K. The Consolidated Statements of Income data set forth below for the fiscal years ended March 31, 2010 and 2009 and the Consolidated Balance Sheet data as of March 31, 2011, 2010 and 2009 have been derived from our audited Consolidated Financial Statements which are not included in this Annual Report on Form 10-K.

CONSOLIDATED STATEMENTS OF INCOME DATA
(In thousands, except for per share amounts)

	Fiscal Year Ended March 31,				
	2013	2012	2011	2010	2009
Sales	$ 227,829	$ 238,250	$ 231,642	$ 238,266	$ 219,412
Cost of sales	150,708	158,085	147,686	146,405	134,085
Gross profit	77,121	80,165	83,956	91,861	85,328
Operating expenses	50,116	54,143	50,932	51,319	51,127
Net income	17,165	16,659	20,871	26,002	22,976
Net income per common share:					
Basic	0.86	0.81	0.93	1.15	0.99
Diluted	0.86	0.80	0.92	1.14	0.98
Weighted average number of common shares outstanding:					
Basic	19,926	20,613	22,514	22,617	23,306
Diluted	20,049	20,708	22,643	22,746	23,482
Cash dividends declared per common share	1.600	0.525	0.475	0.300	-

CONSOLIDATED BALANCE SHEET DATA
(In thousands)

	March 31,				
	2013	2012	2011	2010	2009
Working capital	$ 61,190	$ 78,216	$ 80,643	$ 79,412	$ 54,630
Total assets	73,179	91,064	106,287	104,170	81,963
Total liabilities	9,165	9,883	9,282	7,313	6,995
Shareholders’ equity	64,014	81,181	97,005	96,857	74,968

NON FINANCIAL DATA (UNAUDITED)
(In thousands)

	March 31, 2013	2012	2011	2010	2009
New customers acquired	630	722	645	815	802
Total accumulated customers (1)	7,460	6,830	6,108	5,463	4,648

(1) includes both active and inactive customers

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Executive Summary

PetMed Express was incorporated in the state of Florida in January 1996. The Company's common stock is traded on the NASDAQ Global Select Market under the symbol "PETS." The Company began selling pet medications and other pet health products in September 1996. In March 2010 the Company started offering for sale additional pet supplies on its website, and these items are drop shipped to customers by third party vendors. Presently, the Company's product line includes approximately 3,000 of the most popular pet medications, health products, and supplies for dogs and cats.

The Company markets its products through national television, online, and direct mail/print advertising campaigns which aim to increase the recognition of the "1-800-PetMeds" brand name, and "PetMeds" family of trademarks, increase traffic on its website at www.1800petmeds.com, acquire new customers, and maximize repeat purchases. Approximately 77% of all sales were generated via the Internet in fiscal 2013, compared to 75% in fiscal 2012. The Company's sales consist of products sold mainly to retail consumers. The twelve-month average purchase was approximately $73 and $76 per order for the fiscal years ended March 31, 2013 and 2012, respectively.

Critical Accounting Policies

Our discussion and analysis of our financial condition and the results of our operations are based upon our Consolidated Financial Statements and the data used to prepare them. The Company's Consolidated Financial Statements have been prepared in accordance with accounting principles generally accepted in the United States of America. On an ongoing basis we re-evaluate our judgments and estimates including those related to product returns, bad debts, inventories, long term investments, and income taxes. We base our estimates and judgments on our historical experience, knowledge of current conditions, and our beliefs of what could occur in the future considering available information. Actual results may differ from these estimates under different assumptions or conditions. Our estimates are guided by observing the following critical accounting policies.

Revenue recognition

The Company generates revenue by selling pet medication products and pet supplies primarily to retail consumers. The Company's policy is to recognize revenue from product sales upon shipment, when the rights of ownership and risk of loss have passed to the customer. Outbound shipping and handling fees are included in sales and are billed upon shipment. Shipping expenses are included in cost of sales. The majority of the Company's sales are paid by credit cards and the Company usually receives the cash settlement in two to three banking days. Credit card sales minimize accounts receivable balances relative to sales. The Company maintains an allowance for doubtful accounts for losses that the Company estimates will arise from customers' inability to make required payments, arising from either credit card charge-backs or insufficient funds checks. The Company determines its estimates of the uncollectibility of accounts receivable by analyzing historical bad debts and current economic trends. At both March 31, 2013 and 2012 the allowance for doubtful accounts was approximately $5,000.

Valuation of inventory

Inventories consist of prescription and non-prescription pet medications and pet supplies that are available for sale and are priced at the lower of cost or market value using a weighted average cost method. The Company writes down its inventory for estimated obsolescence. The inventory reserve was approximately $79,000 and $66,000 as of March 31, 2013 and 2012, respectively.

Advertising

The Company’s advertising expense consists primarily of television advertising, Internet marketing, and direct mail/print advertising. Television advertising costs are expensed as the advertisements are televised. Internet costs are expensed in the month incurred and direct mail/print advertising costs are expensed when the related catalogs, brochures, and postcards are produced, distributed, or superseded.

Accounting for income taxes

The Company accounts for income taxes under the provisions of ASC Topic 740, ("Accounting for Income Taxes"), which generally requires the recognition of deferred tax assets and liabilities for the expected future tax benefits or consequences of events that have been included in the Consolidated Financial Statements or tax returns. Under this method, deferred tax assets and liabilities are determined based on differences between the financial reporting carrying values and the tax bases of assets and liabilities, and are measured by applying enacted tax rates and laws for the taxable years in which those differences are expected to reverse.

Results of Operations

The following should be read in conjunction with the Company's Consolidated Financial Statements and the related notes thereto included elsewhere herein. The following table sets forth, as a percentage of sales, certain operating data appearing in the Company's Consolidated Statements of Income and Comprehensive Income:

	Fiscal Year Ended March 31,					
	2013		2012		2011	
Sales	100.0	%	100.0	%	100.0	%
Cost of sales	66.1		66.3		63.8	
Gross profit	33.9		33.7		36.2	
Operating expenses:						
General and administrative	9.5		9.4		9.6	
Advertising	12.0		12.8		11.8	
Depreciation	0.5		0.6		0.6	
Total operating expenses	22.0		22.8		22.0	
Income from operations	11.9		10.9		14.2	
Total other income	0.1		0.2		0.2	
Income before provision for income taxes	12.0		11.1		14.4	
Provision for income taxes	4.5		4.1		5.4	
Net income	7.5	%	7.0	%	9.0	%

Fiscal 2013 Compared to Fiscal 2012

Sales

Sales decreased by approximately $10.5 million, or 4.4%, to approximately $227.8 million for the fiscal year ended March 31, 2013, from approximately $238.3 million for the fiscal year ended March 31, 2012. The reduction in sales for the fiscal year ended March 31, 2013 can be attributed to a reduction in new order sales, due to reduced advertising spending, and reorder sales. Our sales were negatively impacted because of the unavailability of Novartis brands during the year due to the manufacturer's suspended production. Our sales were also down because of a decline in average order size, which was due to a change in product mix to lower priced items, including generics, additional discounts given, and increased competition. The Company acquired approximately 630,000 new customers for the year ended March 31, 2013, compared to approximately 722,000 new customers for the same period the prior year.

The following chart illustrates sales by various sales classifications:

Year Ended March 31, Sales (In thousands)	2013	%	2012	%	$ Variance	% Variance
Reorder Sales	$ 184,814	81.1 %	$ 186,991	78.5 %	$ (2,177)	-1.2 %
New Order Sales	$ 43,015	18.9 %	$ 51,259	21.5 %	$ (8,244)	-16.1 %
Total Net Sales	$ 227,829	100.0 %	$ 238,250	100.0 %	$ (10,421)	-4.4 %
Internet Sales	$ 175,984	77.2 %	$ 178,758	75.0 %	$ (2,774)	-1.6 %
Contact Center Sales	$ 51,845	22.8 %	$ 59,492	25.0 %	$ (7,647)	-12.9 %
Total Net Sales	$ 227,829	100.0 %	$ 238,250	100.0 %	$ (10,421)	-4.4 %

Sales may be adversely affected in fiscal 2014 due to increased competition and consumers giving more consideration to price and trading down to less expensive brands, including generics. In response to these trends, the Company will focus on advertising efficiency to improve new order sales and shifting sales to higher margin items, including generics, combined with expanding our product offerings. No guarantees can be made that the Company's efforts will be successful, or that sales will grow in the future. The majority of our product sales were affected by the seasons, due to the seasonality of mainly heartworm, and flea and tick medications. For the quarters ended June 30, September 30, December 31, and March 31 of Fiscal 2013, the Company's sales were approximately 30%, 26%, 22%, and 22%, respectively. For the quarters ended June 30, September 30, December 31, and March 31 of Fiscal 2012, the Company's sales were approximately 31%, 24%, 21%, and 24%, respectively. Sales in the March quarter of fiscal 2013 were negatively impacted by the colder than normal weather compared to the warmer than normal weather in the March quarter of fiscal 2012.

Cost of sales

Cost of sales decreased by $7.4 million, or 4.7%, to $150.7 million for the fiscal year ended March 31, 2013, from $158.1 million for the fiscal year ended March 31, 2012. The decrease in cost of sales is directly related to decreased sales. As a percentage of sales, cost of sales was 66.1% in fiscal 2013, as compared to 66.3% in fiscal 2012. The cost of sales percentage decrease can be related to a change in product mix to lower cost items, which includes generics.

Gross profit

Gross profit decreased by $3.1 million, or 3.8%, to $77.1 million for the fiscal year ended March 31, 2013, from $80.2 million for the fiscal year ended March 31, 2012. Gross profit as a percentage of sales for fiscal 2013 was 33.9% compared to 33.7%, for fiscal 2012. The gross profit percentage increase can be mainly attributed to a change in product mix to higher margin items, which includes generics.

General and administrative expenses

General and administrative expenses decreased by $771,000, or 3.4%, to $21.6 million for the fiscal year ended March 31, 2013 from $22.4 million for the fiscal year ended March 31, 2012. The decrease in general and administrative expenses for the fiscal year ended March 31, 2013 was primarily due to the following: a $543,000 decrease in bank service fees due to a reduction in credit card fees; a $293,000 reduction in payroll expenses related primarily to a decrease in stock compensation expense; a $147,000 decrease in professional fees, with the majority of the decrease relating to legal and accounting fees; and a $95,000 decrease in telephone expenses. Offsetting the decrease was an $111,000 increase in property expenses related to our website, an $110,000 increase in licenses and fees, and an

$86,000 net increase in other expenses including office expense and insurance expense. General and administrative expenses as a percentage of sales was 9.5% compared to 9.4% for the fiscal years ended March 31, 2013 and 2012, respectively. The increase in general and administrative expenses as a percentage of sales can mainly be attributed to a reduction in sales in fiscal 2013.

Advertising expenses

Advertising expenses decreased by approximately $3.0 million, or 9.7%, to approximately $27.4 million for the year ended March 31, 2013, from approximately $30.4 million for the year ended March 31, 2012. The decrease in advertising expenses for fiscal 2013 can be mainly attributed to reduced advertising due to the unavailability of television remnant space inventory. The advertising costs of acquiring a new customer, defined as total advertising costs divided by new customers acquired, was $44 for the fiscal year ended March 31, 2013, compared to $42 for the fiscal year ended March 31, 2012. Advertising cost of acquiring a new customer can be impacted by the advertising environment, the effectiveness of our advertising creative, increased advertising spending, and price competition. Historically, the advertising environment fluctuates due to supply and demand. A more favorable advertising environment may positively impact future new order sales, whereas a less favorable advertising environment may negatively impact future new order sales. As a percentage of sales, advertising expense was 12.0 % and 12.8% for the fiscal years ended March 31, 2013 and 2012, respectively. The decrease in advertising expense as a percentage of total sales for the fiscal year ended March 31, 2013 can be attributed to a reduction in advertising expense, due to the unavailability of television remnant space inventory. The Company currently anticipates advertising as a percentage of sales to be approximately 13% for fiscal 2014. However, the advertising percentage will fluctuate quarter to quarter due to seasonality and advertising availability. For the fiscal year ended March 31, 2013, quarterly advertising expenses as a percentage of sales ranged between 9% and 14%.

Depreciation

Depreciation decreased by approximately $320,000, to approximately $1.1 million for the year ended March 31, 2013, from approximately $1.4 million for the year ended March 31, 2012. This decrease to depreciation for the year ended March 31, 2013 can be attributed to a reduction in new property and equipment additions, and an increase in fully depreciated fixed assets.

Other income

Other income decreased by approximately $48,000, to approximately $301,000 for the year ended March 31, 2013 from approximately $349,000 for the year ended March 31, 2012. The decrease to other income for the year ended March 31, 2013 can be attributed to a reduction in advertising income. Interest income may decrease in the future as the Company utilizes its cash balances on its share repurchase plan, with approximately $10.2 million remaining as of March 31, 2013, on any quarterly dividend payment, or on its operating activities.

Provision for income taxes

For the fiscal years ended March 31, 2013 and 2012, the Company recorded an income tax provision for approximately $10.1 million and $9.7 million, respectively. The effective tax rate for the fiscal years ended March 31, 2013 and 2012 were 37.1% and 36.8%, respectively. The effective tax rate increase for the fiscal year ended March 31, 2013, was due to a one-time charge related to a fiscal 2012 income tax under-accrual, which was recognized in the quarter ended December 31, 2012. The Company estimates its effective tax rate will be approximately 37.0% for fiscal 2014.

Net income

Net income increased by approximately $506,000, or 3.0%, to approximately $17.2 million for the fiscal year ended March 31, 2013 from approximately $16.7 million for the fiscal year ended March 31, 2012. The increase was primarily due to a decrease in operating expenses offset by a decrease in gross profit in fiscal 2013..

Fiscal 2012 Compared to Fiscal 2011

Sales

Sales increased by approximately $6.7 million, or 2.9%, to approximately $238.3 million for the fiscal year ended March 31, 2012, from approximately $231.6 million for the fiscal year ended March 31, 2011. The increase in sales for the fiscal year ended March 31, 2012 was primarily due to increased new order and reorder sales. The increase in new order sales may be attributed to increased advertising expenses, with flat customer acquisition costs. The Company acquired approximately 722,000 new customers for the year ended March 31, 2012, compared to approximately 645,000 new customers for the same period the prior year.

The following chart illustrates sales by various sales classifications:

Year Ended March 31,						
Sales (In thousands)	2012	%	2011	%	$ Variance	% Variance
Reorder Sales	$186,991	78.5 %	$184,341	79.6 %	$2,650	1.4 %
New Order Sales	$51,259	21.5 %	$47,301	20.4 %	$3,958	8.4 %
Total Net Sales	$238,250	100.0 %	$231,642	100.0 %	$6,608	2.9 %
Internet Sales	$178,758	75.0 %	$165,473	71.4 %	$13,285	8.0 %
Contact Center Sales	$59,492	25.0 %	$66,169	28.6 %	$(6,677)	-10.1 %
Total Net Sales	$238,250	100.0 %	$231,642	100.0 %	$6,608	2.9 %

Sales may be adversely affected in fiscal 2013 due to increased competition and consumers giving more consideration to price and trading down to less expensive brands, including generics. In response to these trends, the Company will maintain a more aggressive advertising and pricing strategy combined with expanding our product offerings to pet supplies and generics. This more aggressive pricing strategy has resulted in a decrease to gross profit margins, and no guarantees can be made that the Company's efforts will be successful, or that sales will grow in the future. The majority of our product sales are affected by the seasons, due to the seasonality of mainly heartworm, and flea and tick medications. For the quarters ended June 30, September 30, December 31, and March 31 of fiscal 2012, the Company's sales were approximately 31%, 24%, 21%, and 24%, respectively.

In January 2012, the manufacturer Novartis Consumer Health, Inc. announced that it halted production of their animal health products, including the following brands: Sentinel®, Interceptor®, Program®, Deramaxx®, and Clomicalm®. This disruption is industry wide, and at this time, there is no expected date for production to resume. We are currently asking prescribing veterinarians to prescribe alternate brands as we run out of inventory. This disruption in production has negatively impacted our sales, and if the disruption is prolonged it may negatively impact future sales.

Cost of sales

Cost of sales increased by $10.4 million, or 7.0%, to $158.1 million for the fiscal year ended March 31, 2012, from $147.7 million for the fiscal year ended March 31, 2011. The increase in cost of sales is directly related to increased sales and increased product costs. As a percentage of sales, cost of sales was 66.3% in fiscal 2012, as compared to 63.8% in fiscal 2011. The cost of sales percentage increase can be mainly attributed to more aggressive sales pricing and increases in our product costs.

Gross profit

Gross profit decreased by $3.8 million, or 4.5%, to $80.2 million for the fiscal year ended March 31, 2012, from $84.0 million for the fiscal year ended March 31, 2011. Gross profit as a percentage of sales for fiscal 2012 and 2011 was 33.7% and 36.2%, respectively. The gross profit percentage decrease can be mainly attributed to more aggressive sales promotions and increases in our product costs.

General and administrative expenses

General and administrative expenses increased by $163,000, or 0.7%, to $22.4 million for the fiscal year ended March 31, 2012 from $22.2 million for the fiscal year ended March 31, 2011. The increase in general and administrative expenses for the fiscal year ended March 31, 2012 was primarily due to the following: a $307,000 increase in payroll expenses relating to the customer care and pharmacy departments and a $220,000 increase in property expenses which was primarily related to our website. Offsetting the increase was a $220,000 decrease in professional fees, with the majority of the decrease relating to investor relations and pharmacy fees, a $98,000 decrease in bank service fees due to a reduction in credit card fees, and a $46,000 net decrease in other expenses including telephone, office expenses, and licenses. General and administrative expenses as a percentage of sales was 9.4% compared to 9.6% for the fiscal years ended March 31, 2012 and 2011, respectively. The decrease in general and administrative expenses as a percentage of sales can mainly be attributed to a reduction in bank service fees and professional fees in fiscal 2012.

Advertising expenses

Advertising expenses increased by approximately $3.0 million, or 11.0%, to approximately $30.4 million for the year ended March 31, 2012, from approximately $27.4 million for the year ended March 31, 2011. The increase in advertising expenses for fiscal 2012 can be mainly attributed to a more aggressive advertising strategy during the year. The advertising costs of acquiring a new customer, defined as total advertising costs divided by new customers acquired, was $42 for both the fiscal years ended March 31, 2012 and 2011. Advertising cost of acquiring a new customer can be impacted by the advertising environment, the effectiveness of our advertising creative, increased advertising spending, and price competition. Historically, the advertising environment fluctuates due to supply and demand. A more favorable advertising environment may positively impact future new order sales, whereas a less favorable advertising environment may negatively impact future new order sales.

As a percentage of sales, advertising expense was 12.8 % and 11.8% for the fiscal years ended March 31, 2012 and 2011, respectively. The increase in advertising expense as a percentage of total sales for the fiscal year ended March 31, 2012 can be attributed to a more aggressive advertising strategy during fiscal 2012. The Company currently anticipates advertising as a percentage of sales to be approximately 13% for fiscal 2013. However, the advertising percentage will fluctuate quarter to quarter due to seasonality and advertising availability. For the fiscal year ended March 31, 2012, quarterly advertising expenses as a percentage of sales ranged between 11% and 14%.

Depreciation

Depreciation increased by approximately $36,000, to approximately $1.4 million for the year ended March 31, 2012, from approximately $1.4 million for the year ended March 31, 2011. This increase to depreciation for the year ended March 31, 2012 can be attributed to new property and equipment additions relating to the warehouse, pharmacy, and customer call center over the past 2 fiscal years.

Other income

Other income increased by approximately $96,000, to approximately $349,000 for the year ended March 31, 2012 from approximately $253,000 for the year ended March 31, 2011. The increase to other income for the year ended March 31, 2012 can be attributed to the recognition of a federal tax penalty in fiscal 2011. Interest income may decrease in the future as the Company utilizes its cash balances on its share repurchase plan, with approximately $14.0 million remaining as of March 31, 2012, on any quarterly dividend payment, or on its operating activities.

Provision for income taxes

For the fiscal years ended March 31, 2012 and 2011, the Company recorded an income tax provision for approximately $9.7 million and $12.4 million, respectively. The effective tax rate for the fiscal years ended March 31, 2012 and 2011 were 36.8% and 37.3%, respectively. The effective tax rate decrease for the fiscal year ended March 31, 2012, was due to a one-time $280,000 tax adjustment, which was recognized in fiscal 2011, to reconcile the remaining net operating loss carryforward. The Company estimates its effective tax rate will be approximately 37.0% for fiscal 2013.

Net income

Net income decreased by approximately $4.2 million, or 20.2%, to approximately $16.7 million for the fiscal year ended March 31, 2012 from approximately $20.9 million for the fiscal year ended March 31, 2011. The decrease was primarily due to a decrease in gross profit margins as a result of more aggressive pricing, and an increase in advertising spending to revitalize sales in fiscal 2012.

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Liquidity and Capital Resources

The Company's working capital at March 31, 2013 and 2012 was approximately $61.2 million and approximately $78.2 million, respectively. The $17.0 million decrease in working capital was primarily attributable the special dividend issued in December 2012, along with share repurchases and quarterly dividends paid during fiscal 2013, offset by cash flow generated from operations. Net cash provided by operating activities was $13.3 million and $20.4 million for the fiscal years ended March 31, 2013 and 2012, respectively. This change can be attributed to a significant increase in the Company's inventory balance due to buying opportunities during fiscal 2013, along with an increase to prepaid expenses and other current assets. Net cash used in investing activities was $5.8 million for the year ended March 31, 2013, compared to net cash provided by investing activities of $11.6 million for the year ended March 31, 2012. This change can be attributed to the redemption of the Company's long term investments balance during fiscal 2012, compared to the purchasing of short term investments during fiscal 2013. Net cash used in financing activities was $36.1 million and $34.9 million for the years ended March 31, 2013 and 2012, respectively. This change was primarily due to the Company paying $32.0 million in dividends in fiscal 2013, compared to paying $11.0 million in dividends in fiscal 2012, and repurchasing approximately 397,000 shares of its common stock for approximately $3.9 million in fiscal 2013, compared to repurchasing approximately 2.1 million shares of its common stock for approximately $23.7 million in fiscal 2012.

As of March 31, 2013 the Company had approximately $10.2 million remaining under the Company's share repurchase plan. Subsequent to March 31, 2013, the Company's Board of Directors declared a $0.15 per share dividend on May 3, 2013. The Board established a May 15, 2013 record date and a May 24, 2013 payment date. Depending on future market conditions the Company may utilize its cash and cash equivalents on the remaining balance of its current share repurchase plan, on quarterly dividends, or on its operating activities.

As of both March 31, 2013 and 2012 the Company had no outstanding lease commitments except for the lease for its 65,300 square foot facility. We are not currently bound by any long or short term agreements for the purchase or lease of capital expenditures. Any material amounts expended for capital expenditures would be the result of an increase in the capacity needed to adequately provide for any increase in our business. To date we have paid for any needed additions to our capital equipment infrastructure from working capital funds and anticipate this being the case in the future. Presently, we have approximately $1.5 million forecasted for capital expenditures in fiscal 2014 which will be funded through cash from operations. The Company's primary source of working capital is cash from operations. The Company presently has no need for alternative sources of working capital, and has no commitments or plans to obtain additional capital.

Off-Balance Sheet Arrangements

The Company had no off-balance sheet arrangements as of March 31, 2013.

Contractual Obligations and Commitments (In thousands)

	Total	Less than 1 year	1-2 years	3-5 Years	More than 5 years
Property lease	$ 1,711	$ 784	$ 794	$ 133	$ -
Executive employment contract	$ 1,650	$ 550	$ 550	$ 550	$ -
Total obligations	$ 3,361	$ 1,334	$ 1,344	$ 683	$ -

Recent Accounting Pronouncements

The Company does not believe that any recently issued, but not yet effective, accounting standards, if currently adopted, will have a material effect on the Company’s consolidated financial position, results of operations, or cash flows.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Market risk generally represents the risk that losses may occur in the value of financial instruments as a result of movements in interest rates, foreign currency exchange rates, and commodity prices. Our financial instruments include cash and cash equivalents, short term investments, accounts receivable, and accounts payable. The book values of cash equivalents, short term investments, accounts receivable, and accounts payable are considered to be representative of fair value because of the short maturity of these instruments. Interest rates affect our return on excess cash and investments. As of March 31, 2013, we had $18.2 million in cash and cash equivalents and $15.5 million in short term investments. A majority of our cash and cash equivalents and investments generates interest income based on prevailing interest rates.

A significant change in interest rates would impact the amount of interest income generated from our excess cash and investments. It would also impact the market value of our investments. Our investments are subject to market risk, primarily interest rate and credit risk. Our investments are managed by a limited number of outside professional managers within investment guidelines set by our Board of Directors. Such guidelines include security type, credit quality, and maturity, and are intended to limit market risk by restricting our investments to high-quality debt instruments with both short and long term maturities. We do not hold any derivative financial instruments that could expose us to significant market risk. At March 31, 2013, we had no debt obligations.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

PETMED EXPRESS, INC. AND SUBSIDIARIES

INDEX TO CONSOLIDATED FINANCIAL STATEMENTS

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Shareholders
PetMed Express, Inc. and subsidiaries

We have audited the accompanying consolidated balance sheets of PetMed Express, Inc. and subsidiaries as of March 31, 2013 and 2012, and the related consolidated statements of comprehensive income, shareholders' equity and cash flows for each of the three years in the period ended March 31, 2013. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of PetMed Express, Inc. and subsidiaries as of March 31, 2013 and 2012, and the results of their operations and their cash flows for each of the three years in the period ended March 31, 2013, in conformity with U.S. generally accepted accounting principles.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), PetMed Express, Inc. and subsidiaries' internal control over financial reporting as of March 31, 2013, based on criteria established in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission, and our report dated May 28, 2013 expressed an unqualified opinion on the effectiveness of PetMed Express, Inc. and subsidiaries' internal control over financial reporting.

/s/ McGladrey
LLP
McGladrey LLP

Fort Lauderdale, Florida
May 28, 2013

PETMED EXPRESS, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
(In thousands)

	March 31, 2013	March 31, 2012
ASSETS		
Current assets:		
Cash and cash equivalents	$18,155	$46,801
Short term investments - available for sale	15,490	10,347
Accounts receivable, less allowance for doubtful accounts of $5 and $5, respectively	1,439	1,572
Inventories - finished goods	31,601	26,217
Prepaid expenses and other current assets	2,520	1,241
Deferred tax assets	982	1,230
Prepaid income taxes	-	199
Total current assets	70,187	87,607
Property and equipment, net	2,132	2,597
Intangible asset	860	860
Total assets	$73,179	$91,064
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$6,454	$6,619
Accrued expenses and other current liabilities	2,381	2,772
Income taxes payable	162	-
Total current liabilities	8,997	9,391
Deferred tax liabilities	168	492
Total liabilities:	9,165	9,883
Commitments and contingencies		
Shareholders' equity:		
Preferred stock, $.001 par value, 5,000 shares authorized; 3 convertible shares issued and outstanding with a liquidation preference of $4 per share	9	9
Common stock, $.001 par value, 40,000 shares authorized; 20,109 and 20,338 shares issued and outstanding, respectively	20	20
Retained earnings	63,987	81,108
Accumulated other comprehensive gain (loss)	(2)	44
Total shareholders' equity	64,014	81,181
Total liabilities and shareholders' equity	$73,179	$91,064

See accompanying notes to consolidated financial statements.

PETMED EXPRESS, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(In thousands, except for per share amounts)

	Year Ended March 31, 2013	2012	2011
Sales	$227,829	$238,250	$231,642
Cost of sales	150,708	158,085	147,686
Gross profit	77,121	80,165	83,956
Operating expenses:			
General and administrative	21,592	22,363	22,200
Advertising	27,433	30,369	27,357
Depreciation	1,091	1,411	1,375
Total operating expenses	50,116	54,143	50,932
Income from operations	27,005	26,022	33,024
Other income (expense):			
Interest income, net	306	288	381
Other, net	(5)	61	(128)
Total other income	301	349	253
Income before provision for income taxes	27,306	26,371	33,277
Provision for income taxes	10,141	9,712	12,406
Net income	$17,165	$16,659	$20,871
Net change in unrealized gain (loss) on short and long term investments	(46)	185	(33)
Comprehensive income	$17,119	$16,844	$20,838
Net income per common share:			
Basic	$0.86	$0.81	$0.93
Diluted	$0.86	$0.80	$0.92
Weighted average number of common shares outstanding:			
Basic	19,926	20,613	22,514
Diluted	20,049	20,708	22,643
Cash dividends declared per common share	$1.600	$0.525	$0.475

See accompanying notes to consolidated financial statements.

PETMED EXPRESS, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY
Fiscal years ended March 31, 2011, March 31, 2012, and March 31, 2013
(In thousands)

	Convertible Preferred Stock Shares	Convertible Preferred Stock Amounts	Common Stock Shares	Common Stock Amounts	Additional Paid-In Capital	Retained Earnings	Other Comprehensive Gain (Loss)	Total
Balance, March 31, 2010	3	$ 9	22,990	$ 23	$ 2,628	$ 94,305	$ (108)	$ 96,857
Issuance of common stock from exercise of stock options	-	-	46	-	340	-	-	340
Issuance of restricted stock, net	-	-	86	-	-	-	-	-
Share based compensation	-	-	-	-	2,171	-	-	2,171
Dividends declared	-	-	-	-	-	(10,822)	-	(10,822)
Repurchased and retired shares	-	-	(791)	(1)	(12,246)	-	-	(12,247)
Deferred tax adjustment related to resticted stock and stock options	-	-	-	-	(132)	-	-	(132)
Allocation of retirement of repurchased shares of additional paid in capital and retained earnings	-	-	-	-	7,239	(7,239)	-	-
Net income	-	-	-	-	-	20,871	20,871	20,871
Other comprehensive loss:								
Net Change in unrealized loss on short term investments							(31)	(31)
Net Change in unrealized loss on long term							(2)	(2)

investments								
Total comprehensive income							$ 20,838	-
Balance, March 31, 2011	3	9	22,331	22	-	97,115	(141)	97,005
Issuance of restricted stock, net	-	-	91	-	-	-	-	-
Share based compensation	-	-	-	-	2,246	-	-	2,246
Dividends declared	-	-	-	-	-	(10,989)	-	(10,989)
Repurchased and retired shares	-	-	(2,084)	(2)	(23,683)	-	-	(23,685)
Deferred tax adjustment related to resticted stock	-	-	-	-	(240)	-	-	(240)
Allocation of retirement of repurchased shares of additional paid in capital and retained earnings	-	-	-	-	21,677	(21,677)	-	-
Net income	-	-	-	-	-	16,659	16,659	16,659
Other comprehensive gain:								
Net Change in unrealized gain on short term investments							75	75
Net Change in unrealized gain on long term investments							110	110
Total comprehensive income							$ 16,844	-
Balance, March 31, 2012	3	9	20,338	20	-	81,108	44	81,181
Issuance of restricted stock, net	-	-	168	-	-	-	-	-

Share based compensation	-	-	-	-	1,943	-	-	1,943
Dividends declared	-	-	-	-	-	(32,080)	-	(32,080)
Repurchased and retired shares	-	-	(397)	-	(3,865)	-	-	(3,865)
Deferred tax adjustment related to resticted stock	-	-	-	-	(284)	-	-	(284)
Allocation of retirement of repurchased shares of additional paid in capital and retained earnings	-	-	-	-	2,206	(2,206)	-	-
Net income	-	-	-	-	-	17,165	17,165	17,165
Other comprehensive loss: Net Change in unrealized loss on short term investments							(46)	(46)
Total comprehensive income							$ 17,119	-
Balance, March 31, 2013	3	$ 9	20,109	$ 20	$ -	$ 63,987	$ (2)	$ 64,014

See accompanying notes to consolidated financial statements.

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PETMED EXPRESS, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)

	Year Ended March 31, 2013	2012	2011
Cash flows from operating activities:			
Net income	$17,165	$16,659	$20,871
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation	1,091	1,411	1,375
Share based compensation	1,943	2,246	2,171
Deferred income taxes	(76)	(56)	348
Bad debt expense	56	47	48
(Increase) decrease in operating assets and increase (decrease) in liabilities:			
Accounts receivable	77	366	64
Inventories - finished goods	(5,384)	(1,077)	3,924
Prepaid income taxes	199	465	(335)
Prepaid expenses and other current assets	(1,279)	(205)	(426)
Accounts payable	(165)	297	1,964
Accrued expenses and other current liabilities	(499)	238	102
Income taxes payable	162	-	-
Net cash provided by operating activities	13,290	20,391	30,106
Cash flows from investing activities:			
Net change in investments	(5,189)	12,344	(10,146)
Purchases of property and equipment	(626)	(705)	(667)
Purchases of intangible asset	-	-	(10)
Net cash provided by (used in) investing activities	(5,815)	11,639	(10,823)
Cash flows from financing activities:			
Dividends paid	(31,972)	(10,964)	(10,727)
Purchases of treasury stock	(3,865)	(23,685)	(12,247)
Proceeds from the exercise of stock options	-	-	340
Tax adjustment related to stock compensation	(284)	(240)	(132)
Net cash used in financing activities	(36,121)	(34,889)	(22,766)
Net decrease in cash and cash equivalents	(28,646)	(2,859)	(3,483)
Cash and cash equivalents, at beginning of year	46,801	49,660	53,143
Cash and cash equivalents, at end of year	$18,155	$46,801	$49,660
Supplemental disclosure of cash flow information:			
Cash paid for income taxes	$10,140	$9,543	$12,578
Retirement of treasury stock	$3,865	$23,685	$12,247

Property and equipment purchases in accounts payable	$-	$-	$130
Dividends payable in accrued expenses	$276	$168	$143

See accompanying notes to consolidated financial statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(1) Summary of Significant Accounting Policies

Organization

PetMed Express, Inc. and subsidiaries, d/b/a 1-800-PetMeds (the “Company”), is a leading nationwide pet pharmacy. The Company markets prescription and non-prescription pet medications, health products, and supplies for dogs and cats, direct to the consumer. The Company markets its products through national television, online, and direct mail/print advertising campaigns, which aim to increase the recognition of the “1-800-PetMeds” brand name and “PetMeds” family of trademarks, increase traffic on its website at www.1800petmeds.com, acquire new customers, and maximize repeat purchases. The majority of all of the Company’s sales are to residents in the United States. The Company’s executive offices are located in Pompano Beach, Florida. The Company’s fiscal year end is March 31, and references herein to fiscal 2013, 2012, or 2011 refer to the Company’s fiscal years ended March 31, 2013, 2012, and 2011, respectively.

Principles of Consolidation

The consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries. All significant intercompany transactions have been eliminated in consolidation.

Revenue Recognition

The Company generates revenue by selling pet medication products and pet supplies mainly to retail consumers. The Company’s policy is to recognize revenue from product sales upon shipment, when the rights of ownership and risk of loss have passed to the customer. Outbound shipping and handling fees are included in sales and are billed upon shipment. Shipping expenses are included in cost of sales. The majority of the Company’s sales are paid by credit cards and the Company usually receives the cash settlement in two to three banking days. Credit card sales minimize the accounts receivable balances relative to sales. The Company maintains an allowance for doubtful accounts for losses that the Company estimates will arise from the customers’ inability to make required payments, arising from either credit card charge-backs or insufficient funds checks. The Company determines its estimates of the uncollectibility of accounts receivable by analyzing historical bad debts and current economic trends. At both March 31, 2013 and 2012, the allowance for doubtful accounts was approximately $5,000.

Cash and Cash Equivalents

The Company considers all highly liquid investments with maturity of three months or less when purchased to be cash equivalents. Cash and cash equivalents at March 31, 2013 and 2012 consisted of the Company’s cash accounts and money market accounts with a maturity of three months or less. The carrying amount of cash equivalents approximates fair value. The Company maintains its cash in bank deposit accounts which, at times, may exceed federally insured limits. The Company has not experienced any losses in such accounts.

Short Term Investments

The Company’s short term investments balance consists of short term bond mutual funds. In accordance with ASC Topic 320 (“Accounting for Certain Investments in Debt and Equity Securities”), short term investments are accounted for as available for sale securities with any changes in fair value to be reflected in other comprehensive income (loss). The Company had a short term investments balance of $15.5 million and $10.3 million as of March 31, 2013 and March 31, 2012, respectively.

Use of Estimates

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(1) Summary of Significant Accounting Policies (Continued)

Inventories

Inventories consist of prescription and non-prescription pet medications and pet supplies that are available for sale and are priced at the lower of cost or market value using a weighted average cost method. The Company writes down its inventory for estimated obsolescence. The inventory reserve was approximately $79,000 and $66,000 at March 31, 2013 and 2012, respectively.

Property and Equipment

Property and equipment are stated at cost and depreciated using the straight-line method over the estimated useful lives of the assets. The furniture, fixtures, equipment, and computer software are depreciated over periods ranging from three to seven years. Leasehold improvements and assets under capital lease agreements are amortized over the shorter of the underlying lease agreement or the useful life of the asset.

Long-lived Assets

Long-lived assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. Recoverability of assets is measured by a comparison of the carrying amount of the asset to the undiscounted cash flows expected to be generated from the asset.

Intangible Asset

The intangible asset consists of a toll-free telephone number and an internet domain name. In accordance with the ASC Topic 350 (“Goodwill and Other Intangible Assets”) the intangible assets are not being amortized, and are subject to an annual review for impairment.

Fair Value of Financial Instruments

The carrying amounts of the Company’s cash and cash equivalents, accounts receivable, and accounts payable approximate fair value due to the short-term nature of these instruments.

Advertising

The Company’s advertising expenses consist primarily of television advertising, online marketing, and direct mail/print advertising. Television advertising costs are expensed as the advertisements are televised. Internet costs are expensed in the month incurred and direct mail/print costs are expensed when the related catalogs, brochures, and postcards are produced, distributed, or superseded.

Business Concentrations

The Company purchases its products from a variety of sources, including certain manufacturers, domestic distributors, and wholesalers. We have multiple suppliers for each of our products to obtain the lowest cost. There were five suppliers from whom we purchased approximately 50% of all products in fiscal 2013, compared to four suppliers from whom we purchased approximately 50% of all products in fiscal 2012.

Accounting for Share Based Compensation

The Company records compensation expense associated with stock options and restricted stock in accordance with ASC Topic 718 ("Share Based Payment"). The Company adopted the modified prospective transition method provided under ASC Topic 718. The compensation expense related to all of the Company's stock-based compensation arrangements is recorded as a component of general and administrative expenses.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(1) Summary of Significant Accounting Policies (Continued)

Comprehensive Income

The Company applies ASC Topic 220 ("Reporting Comprehensive Income") which requires that all items that are recognized under accounting standards as components of comprehensive income be reported in a financial statement that is displayed with the same prominence as other financial statements. The items of other comprehensive income that are typically required to be displayed are foreign currency items, minimum pension liability adjustments, and unrealized gains and losses on certain investments in debt and equity securities. At March 31, 2013 the Company recorded an unrealized loss of $46,000 on its short term investments, and at March 31, 2012 the Company recorded an unrealized gain of $75,000 on its short term investments. At March 31, 2012 the Company also recognized an unrealized recovery of $110,000, within accumulated other comprehensive income, based upon receiving full par value of its long term investments.

The following is a summary of our comprehensive income (in thousands):

	March 31, 2013	2012	2011
Net income	$ 17,165	$ 16,659	$ 20,871
Net change in unrealized gain (loss) on short term investments	(46)	75	(31)
Net change in unrealized gain (loss) and redemptions on long term investments	-	110	(2)
Comprehensive income	$ 17,119	$ 16,844	$ 20,838

Income Taxes

The Company accounts for income taxes under the provisions of ASC Topic 740 ("Accounting for Income Taxes") which generally requires the recognition of deferred tax assets and liabilities for the expected future tax benefits or consequences of events that have been included in the consolidated financial statements or tax returns. Under this method, deferred tax assets and liabilities are determined based on differences between the financial reporting carrying values and the tax bases of assets and liabilities, and are measured by applying enacted tax rates and laws for the taxable years in which those differences are expected to reverse. The Company adopted the provisions of ASC Topic 740 ("Accounting for Uncertainty in Income Taxes", in the first quarter of fiscal 2008. As required by "Accounting for Uncertainty in Income Taxes" guidance, which clarifies ASC Topic 740, the Company recognizes the financial statement benefit of a tax position only after determining that the relevant tax authority would more likely than not sustain the position following an audit. For tax positions meeting the more-likely-than-not threshold, the amount recognized in the Consolidated Financial Statements is the largest benefit that has a greater than 50 percent likelihood of being realized upon ultimate settlement with the relevant tax authority. At the adoption date, the Company applied "Accounting for Uncertainty in Income Taxes" guidance to all tax positions for which the statute of limitations remained open. The Company files tax returns in the U.S. federal jurisdiction and Florida and Georgia. With few exceptions, the Company is no longer subject to U.S. federal, state or local income tax examinations by tax authorities for years ending March 31, 2008.

Upon implementing "Accounting for Uncertainty in Income Taxes" guidance, the Company did not recognize any additional liabilities for unrecognized tax positions. The adoption of "Accounting for Uncertainty in Income Taxes" guidance had no material impact on the Company's consolidated financial position, results of operations, or cash flows in fiscal 2013. Any interest and penalties related to income taxes will be recorded to other income (expenses).

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(1) Summary of Significant Accounting Policies (Continued)

Recent Accounting Pronouncements

The Company does not believe that any recently issued, but not yet effective, accounting standards, if currently adopted, will have a material effect on the Company's consolidated financial position, results of operations, or cash flows.

(2) Fair Value Measurements

The Company carries various assets at fair value in the Consolidated Balance Sheets. Fair value is defined as an exit price, representing the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants. As such, fair value is a market-based measurement that should be determined based on assumptions that market participants would use in pricing an asset or a liability. ASC Topic 820 ("Fair Value Measurements") establishes a three-tier fair value hierarchy, which prioritizes the inputs used in the valuation methodologies in measuring fair value:

Level 1 - Observable inputs that reflect quoted prices (unadjusted) for identical assets or liabilities in active markets.
Level 2 - Include other inputs that are directly or indirectly observable in the marketplace.
Level 3 - Unobservable inputs which are supported by little or no market activity.

The fair value hierarchy also requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The Company's cash equivalents and short term investments are classified within Level 1. Assets and liabilities measured at fair value are summarized below (in thousands):

	Fair Value Measurement at March 31, 2013 Using			
	March 31, 2013	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets:				
Cash and Cash equivalents - money markets funds	$ 18,155	$ 18,155	$ -	$ -
Short term investments - bond mutual funds	15,490	15,490	-	-
	$ 33,645	$ 33,645	$ -	$ -

(3) Property and Equipment

Major classifications of property and equipment consist of the following (in thousands):

	March 31, 2013	2012

Leasehold improvements	$ 1,116	$ 1,092
Computer software	2,735	2,406
Furniture, fixtures and equipment	5,748	5,475
	9,599	8,973
Less: accumulated depreciation	(7,467)	(6,376)
Property and equipment, net	$ 2,132	$ 2,597

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(4) Accrued Expenses and Other Current Liabilities

Major classifications of accrued expenses and other current liabilities consist of the following (in thousands):

	March 31, 2013	2012
Accrued sales tax	$ 473	$ 499
Accrued credit card fees	269	323
Accrued salaries and benefits	899	948
Accrued professional expenses	225	319
Accrued advertising expenses	-	230
Accrued sales return allowance	138	167
Accrued dividends payable	276	168
Other accrued liabilities	101	118
Accrued expenses and other current liabilities	$ 2,381	$ 2,772

(5) Net Income Per Share

In accordance with the provisions of ASC Topic 260 ("Earnings Per Share") basic net income per share is computed by dividing net income available to common shareholders by the weighted average number of common shares outstanding during the period. Diluted net income per common share includes the dilutive effect of potential restricted stock and stock options exercised and the effects of the potential conversion of preferred shares, calculated using the treasury stock method. Outstanding stock options, restricted stock, and convertible preferred shares issued by the Company represent the only dilutive effect reflected in diluted weighted average shares outstanding.

The following is a reconciliation of the numerators and denominators of the basic and diluted net income per share computations for the periods presented (in thousands, except for per share amounts):

	Year Ended March 31, 2013	2012	2011
Net income (numerator):			
Net income	$ 17,165	$ 16,659	$ 20,871
Shares (denominator)			
Weighted average number of common shares outstanding used in basic computation	19,926	20,613	22,514
Common shares issuable upon exercise of stock options and vesting of restricted stock	113	85	119
Common shares issuable upon conversion of preferred shares	10	10	10
Shares used in diluted computation	20,049	20,708	22,643
Net income per common share:			
Basic	$ 0.86	$ 0.81	$ 0.93
Diluted	$ 0.86	$ 0.80	$ 0.92

At March 31, 2013 and 2012, all restricted stock was included in the diluted net income per common share computation.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(6) Income Taxes

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amount of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. The tax effects of temporary differences that give rise to significant portions of deferred tax assets and deferred tax liabilities are as follows (in thousands):

	March 31, 2013	2012
Deferred tax assets:		
Bad debt and inventory reserves	$ 31	$ 26
Accrued expenses	608	535
Deferred stock compensation	244	331
Net operating loss carryforward	152	250
Deferred tax assets	1,035	1,142
Less: valuation allowance	-	-
Total deferred tax assets	1,035	1,142
Deferred tax liabilities:		
Property and equipment	(221)	(404)
Total net deferred taxes	$ 814	$ 738

There was no change in the valuation allowance which was $0 for both the fiscal years ended March 31, 2013 and 2012. At March 31, 2013, the Company had federal net operating loss carryforwards of approximately $409,000. The federal net operating loss carryforwards expire in the year 2020. The use of such net operating loss carryforwards is limited to approximately $266,000 annually due to a change of control on November 22, 2000.

The components of the income tax provision consist of the following (in thousands):

	Year Ended March 31, 2013	2012	2011
Current taxes			
Federal	$ 9,588	$ 9,138	$ 11,007
State	913	870	1,052
Total current taxes	10,501	10,008	12,059
Deferred taxes			
Federal	(329)	(270)	317
State	(31)	(26)	30
Total deferred taxes	(360)	(296)	347
Total provision for income taxes	$ 10,141	$ 9,712	