# UNITED STATES
# SECURITIES AND EXCHANGE COMMISSION
**Washington, D.C. 20549**

# FORM 10-Q

(MARK ONE)

**[X] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

**For the quarterly period ended June 30, 2003**

or

[ ] TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

**Commission file number 000-19720**

# ABAXIS, INC.

(Exact name of registrant as specified in its charter)

| **California** | **77-0213001** |
|---|---|
| (State or Other Jurisdiction of Incorporation or Organization) | (I.R.S. Employer Identification Number) |

**3240 Whipple Road**
**Union City, California 94587**
(Address of principal executive offices including zip code)

**(510) 675-6500**
(Registrant's telephone number, including area code)

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 reports), and (2) has been subject to such filing requirements for the past 90 days. Yes [X] No [ ].

At August 11, 2003, 17,100,631 shares of Common Stock were outstanding.

This Report on Form 10-Q consists of 30 pages. The exhibit index is on page 25.

**ABAXIS, INC.**
**Report On Form 10-Q For The**
**Quarter Ended June 30, 2003**
**INDEX**

## PART I -- FINANCIAL INFORMATION

### Item 1. Financial Statements

**Abaxis, Inc.**
**Condensed Statements of Operations**
**(unaudited and in rounded thousands, except per share data)**

| | Three Months Ended June 30, | |
|---|---|---|
| | **2003** | **2002** |
| Revenues: | | |
| Product sales, net | $ 10,291,000 | $ 7,381,000 |
| Development and licensing revenue | 35,000 | 35,000 |
| Total revenues | 10,326,000 | 7,416,000 |
| Costs and operating expenses: | | |
| Cost of product sales | 5,220,000 | 3,719,000 |
| Selling, general and administrative | 3,217,000 | 2,386,000 |
| Research and development | 1,032,000 | 1,005,000 |
| Total costs and operating expenses | 9,469,000 | 7,110,000 |
| Income from operations | 857,000 | 306,000 |
| Interest and other income | 48,000 | 63,000 |
| Interest and other expense | (18,000) | (54,000) |
| Net income before income taxes | 887,000 | 315,000 |
| Income tax provision | 24,000 | 10,000 |
| Net income | 863,000 | 305,000 |
| Preferred dividends and accretion (a) | (204,000) | (595,000) |
| Net income (loss) attributable to common shareholders | $ 659,000 | $ (290,000) |
| Basic and diluted net income (loss) per share | $ 0.04 | $ (0.02) |
| Shares used in computing basic per share amounts | 16,921,000 | 16,392,000 |
| Shares used in computing diluted per share amounts | 17,480,000 | 16,392,000 |

(a) For the three months ended June 30, 2003, includes dividends of $204,000. For the three months ended June 30, 2002, includes dividends of $225,000 and a non-cash dividend charge of $370,000 related to the beneficial conversion feature contained in the Company's Series E Preferred Stock issued in April 2002. See note 3 to condensed financial statements.

See notes to condensed financial statements.

**Abaxis, Inc.**
**Condensed Balance Sheets**
**(unaudited and in rounded thousands)**

| | June 30, 2003 | March 31, 2003 |
|---|---|---|
| **ASSETS** | | |
| Current assets: | | |
| Cash and cash equivalents | $ 11,598,000 | $ 10,430,000 |
| Trade receivables (net of allow ances of $257,000 at June 30, 2003 and $267,000 at March 31, 2003) | 7,055,000 | 7,482,000 |
| Inventories | 5,612,000 | 4,982,000 |
| Prepaid expenses | 464,000 | 667,000 |
| Total current assets | 24,729,000 | 23,561,000 |
| Property and equipment - net | 8,340,000 | 8,580,000 |
| Deposits and other assets | 195,000 | 227,000 |
| Total assets | $ 33,264,000 | $ 32,368,000 |
| **LIABILITIES, CONVERTIBLE PREFERRED STOCK AND SHAREHOLDERS' EQUITY** | | |
| Current liabilities: | | |
| Accounts payable | $ 1,808,000 | $ 2,084,000 |
| Dividends payable | 204,000 | 408,000 |
| Accrued payroll and related expenses | 2,121,000 | 1,811,000 |
| Other accrued liabilities | 353,000 | 377,000 |
| Warranty reserve | 145,000 | 123,000 |
| Deferred revenue | 358,000 | 378,000 |
| Current portion of capital lease obligations | 46,000 | 58,000 |
| Current portion of long-term debt | 467,000 | 467,000 |
| Total current liabilities | 5,502,000 | 5,706,000 |
| Capital lease obligations, less current portion | 32,000 | 38,000 |
| Long-term debt, less current portion | 350,000 | 466,000 |
| Deferred rent | 345,000 | 321,000 |
| Deferred revenue, less current portion | 336,000 | 318,000 |
| Commission obligation, less current portion | 75,000 | 75,000 |
| Total non-current liabilities | 1,138,000 | 1,218,000 |
| Commitments and contingencies | | |
| Redeemable convertible preferred stock, Series E, no par value: issued and outstanding shares - 5,570 at June 30, 2003 and March 31, 2003 (liquidation preference of $5,570,000 at June 30, 2003 and March 31, 2003) | 3,176,000 | 3,176,000 |
| Shareholders' equity: | | |
| Convertible preferred stock, Series D, no par value: authorized shares - 5,000,000; issued and outstanding shares - 6,508 at June 30, 2003 and March 31, 2003 | 3,143,000 | 3,143,000 |
| Common stock, no par value: authorized shares - 35,000,000; issued and outstanding shares - 16,959,330 at June 30, 2003 and 16,816,095 at March 31, 2003 | 81,130,000 | 80,608,000 |
| Accumulated deficit | (60,825,000) | (61,483,000) |
| Total shareholders' equity | 23,448,000 | 22,268,000 |
| Total liabilities, convertible preferred stock and shareholders' equity | $ 33,264,000 | $ 32,368,000 |

See notes to condensed financial statements.

**Abaxis, Inc.**
**Condensed Statements of Cash Flows**
**(unaudited and in rounded thousands)**

| | Three Months Ended June 30, | |
|---|---|---|
| | **2003** | **2002** |
| **Operating activities:** | | |
| Net income | $ 863,000 | $ 305,000 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Depreciation and amortization | 377,000 | 357,000 |
| Common stock issued for employee benefit plans | 38,000 | 104,000 |
| Stock based compensation (reversal), including amortization of deferred stock compensation | 8,000 | (22,000) |
| Changes in operating assets and liabilities: | | |
| Trade receivables | 427,000 | (263,000) |
| Interest receivable | -- | (11,000) |
| Inventories | (628,000) | (40,000) |
| Prepaid expenses | 203,000 | 205,000 |
| Deposits and other assets | 32,000 | (117,000) |
| Accounts payable | (276,000) | 12,000 |
| Accrued payroll and related expenses | 310,000 | (68,000) |
| Warranty reserve and other accrued liabilities | (2,000) | (73,000) |
| Deferred rent | 24,000 | 32,000 |
| Deferred revenue | (2,000) | (28,000) |
| Long-term commission obligation | -- | (14,000) |
| Net cash provided by operating activities | 1,374,000 | 379,000 |
| **Investing activities:** | | |
| Purchase of property and equipment | (140,000) | (400,000) |
| **Financing activities:** | | |
| Repayment of line of credit | -- | (1,000,000) |
| Repayment of equipment financing | (116,000) | (116,000) |
| Repayment of capital lease obligations | (18,000) | (37,000) |
| Net cash proceeds from issuance of preferred stock | -- | 6,812,000 |
| Exercise of warrants and common stock options | 68,000 | 27,000 |
| Net cash provided by (used in) financing activities | (66,000) | 5,686,000 |
| Net increase in cash and cash equivalents | 1,168,000 | 5,665,000 |
| Cash and cash equivalents at beginning of period | 10,430,000 | 4,098,000 |
| Cash and cash equivalents at end of period | $ 11,598,000 | $ 9,763,000 |
| **Supplemental disclosures of cash flow information:** | | |
| Cash paid for interest | $ 18,000 | $ 48,000 |
| Cash paid for taxes | $ 14,000 | -- |
| **Noncash financing activities:** | | |
| Preferred stock dividends and accretion | $ 204,000 | $ 595,000 |
| Issuance of common stock for conversion of preferred stock and payment of dividends payable | $ 408,000 | $ 280,000 |
| Warrants and options issued for services and issuance costs | $ -- | $ 361,000 |

See notes to condensed financial statements.

**ABAXIS, INC.**
**NOTES TO CONDENSED FINANCIAL STATEMENTS**

**(Unaudited)**

## 1. BASIS OF PRESENTATION

The condensed unaudited financial statements included herein have been prepared by the Company pursuant to the rules and regulations of the Securities and Exchange Commission. These condensed unaudited financial statements should be read in conjunction with the audited financial statements and notes thereto included in the Company's Annual Report on Form 10-K/A for the fiscal year ended March 31, 2003. The unaudited condensed financial statements included herein reflect all normal recurring adjustments, which are, in the opinion of management, necessary to state fairly the results of operations and financial position for the periods presented. Certain amounts as presented in the financial statements for the previous periods have been reclassified to conform to the fiscal year ending March 31, 2004 financial statement presentation. The results for the period ended June 30, 2003 are not necessarily indicative of the results to be expected for the entire fiscal year ending March 31, 2004 or for any future period.

## 2. SIGNIFICANT ACCOUNTING POLICIES

***Comprehensive Income*** - Comprehensive income was the same as net income for the three months ended June 30, 2003 and 2002.

***New Accounting Pronouncements*** - In December 2002, the FASB issued SFAS No. 148, "Accounting for Stock-Based Compensation - Transition and Disclosure." SFAS No. 148 amends FASB Statement No. 123, "Accounting for Stock-Based Compensation," to provide alternative methods of transition for a voluntary change to the fair value based method of accounting for stock-based employee compensation. In addition, SFAS No. 148 amends the disclosure requirements of SFAS No. 123 to require prominent disclosures in both annual and interim financial statements of the method of accounting for stock-based employee compensation and the effect of the method used on reported results. SFAS No. 148 is effective for fiscal years beginning after December 15, 2002. The Company adopted the disclosure provisions of SFAS No. 148 on January 1, 2003. The Company does not expect to change to using the fair value based method of accounting for stock-based employee compensation; and therefore, adoption of SFAS No. 148 is not expected to have an impact on the financial position, results of operations or cash flows of the Company.

Had compensation cost been recognized based on the fair value at the date of grant for options during the three months ended June 30, 2003 and 2002, the pro forma amounts of the Company's net income and basic and diluted net income (loss) per share would have been as follows (in rounded thousands, except per share amounts):

| | Three Months Ended June 30, | |
|---|---|---|
| | **2003** | **2002** |
| Net income: | | |
| As reported | $ 863,000 | $ 305,000 |
| | | |
| Less stock-based compensation expense determined under the fair value method for all awards, net of related tax effects | (347,000) | (349,000) |
| | | |
| Pro forma net income (loss) | $ 516,000 | $ (44,000) |
| | | |
| Basic and diluted net income (loss) per share: | | |
| As reported | $ 0.04 | $ (0.02) |
| Pro forma | $ 0.03 | $ (0.00) |

The Company's calculations were made using the Black-Scholes option pricing model, based on a multiple option valuation approach, and forfeitures were recognized as they occurred. The following are the weighted average assumptions:

| | Three Months Ended June 30, | |
|---|---|---|
| | 2003 | 2002 |
| Expected life of option | 6 years | 6 years |
| Risk-free interest rate | 2.78 % | 3.17 % |
| Dividend yield | 0.00% | 0.00% |
| Volatility | 61 % | 62 % |

In April 2003, the FASB issued SFAS No. 149, “Amendment of Statement 133 on Derivative Instruments and Hedging Activities. ” This statement amends and clarifies financial accounting and reporting for derivative instruments, including certain derivative instruments embedded in other contracts (collectively referred to as derivatives) and for hedging activities under FASB Statement No. 133, “Accounting for Derivative Instruments and Hedging Activities. ” This statement is effective for contracts entered into or modified after June 30, 2003. The adoption of this statement is not expected to have an impact on the Company's financial position, results of operations or cash flows.

In May 2003, the FASB issued SFAS No. 150, “Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity. ” This statement establishes standards for how an issuer classifies and measures certain financial instruments with characteristics of both liabilities and equity. This statement is effective for financial instruments entered into or modified after May 31, 2003 and otherwise is effective at the beginning of the first interim period beginning after June 15, 2003. The adoption of this statement is not expected to have an impact on the Company's financial position, results of operations or cash flows.

**3. NET INCOME (LOSS) PER SHARE INFORMATION**

Basic net income (loss) per share is computed based upon the weighted average number of shares of common stock outstanding and the net income attributable to common shareholders. Diluted net income (loss) per share is computed by dividing net income attributable to common shareholders by the weighted average number of common shares that would have been outstanding during the period assuming the issuance of common shares for all potential dilutive common shares outstanding. Shares used in the calculation of diluted net income (loss) per share for the three months ended June 30, 2003 exclude an aggregate of 4,355,000 common equivalent shares and for the three months ended June 30, 2002 exclude an aggregate of 5,145,000 common equivalent shares related to outstanding options and warrants, using the treasury stock method and related to preferred shares issuable upon conversion of preferred stock, as their effect would be antidilutive.

The reconciliation of the weighted average number of common shares outstanding used in calculating basic net income (loss) per share and in calculating diluted net income (loss) per share is as follows (in rounded thousands):

| | Three Months Ended June 30 | |
|---|---|---|
| | 2003 | 2002 |
| Weighted average number of common shares outstanding used in calculating basic net income (loss) per share..... | 16,921,000 | 16,392,000 |
| Weighted average number of dilutive stock options and w arrants outstanding using the treasury stock method..... | 559,000 | -- |
| Weighted average number of shares outstanding used in calculating diluted net income (loss) per share..... | 17,480,000 | 16,392,000 |

**4. INVENTORY**

Inventories are stated at the lower of cost (first-in, first-out method) or market and consist of the following (in rounded thousands):

| | June 30, 2003 | March 31, 2003 |
|---|---|---|
| Raw materials | $ 2,802,000 | $ 2,317,000 |
| Work-in-process | 1,915,000 | 2,071,000 |
| Finished goods | 895,000 | 594,000 |
| | $ 5,612,000 | $ 4,982,000 |

**5. WARRANTY RESERVES**

The Company provides for provisions for the estimated future costs to be incurred under the Company's standard warranty obligations of one year. Estimated contractual warranty obligations are recorded when related sales are recognized and any additional amounts are recorded when such costs are probable and can be reasonably estimated.

The warranty reserve activity is summarized as follows for the three-month periods ended June 30, 2003 and 2002 (in rounded thousands):

| | Three Months Ended June 30 | |
|---|---|---|
| | 2003 | 2002 |
| Balance Beginning of Period | $ 123,000 | $ 192,000 |
| Provision for warranty expense | 162,000 | 85,000 |
| Warranty costs incurred | (140,000) | (85,000) |
| Balance End of Period | $ 145,000 | $ 192,000 |

**6. LINE OF CREDIT AND LONG-TERM DEBT**

In March 2002, the Company terminated certain line of credit and equipment financing loans and entered into new line of credit and equipment financing loans with Comerica Bank-California. The new line of credit provides for borrowings of up to $5,250,000, based on the Company's outstanding accounts receivables and inventory, as defined by the bank: up to $4,000,000 is collateralized by domestic receivables and up to $1,250,000 is collateralized by foreign receivables. This new line of credit bears interest at the prime rate, which was 4.00% at June 30, 2003, and is payable monthly. Of the $4,000,000 domestic line of credit, $820,000 was committed to secure a letter of credit for the Company’s facilities lease. The domestic line of credit terminates upon notification by either party and the outstanding balance is payable upon demand. The foreign line of credit expired in September 2002 and was renewed until September 2003. The Company’s weighted average interest rate on borrowings under its line of credit facilities during the three months ended June 30, 2003 and 2002 was 4.24% and 4.75%, respectively. At June 30, 2003, there was no amount outstanding under the Company’s line of credit. At June 30, 2003, $3,950,000 was available for borrowing.

The balance of the new equipment financing loan at June 30, 2003 was $817,000. The equipment loan bears interest at the prime rate plus 1%, which totaled 5.00% at June 30, 2003 and is payable in monthly installments of principal and interest totaling approximately $42,000 over a period of two years. The weighted average interest rate on equipment financing loans during the three months ended June 30, 2003 and 2002 was 5.24% and 5.75%, respectively.

The line of credit and equipment financing agreements contain certain financial covenants, which are evaluated on a quarterly basis. Included in these financial covenants, among other stipulations, is a requirement that the Company have a minimum net income of $25,000 before preferred stock dividends and accretion in any three quarters of a fiscal year, provided that any loss before preferred stock dividends and accretion incurred in the remaining quarter is not to exceed $250,000. The Company is also required to be profitable, as defined, on a fiscal year to date basis beginning with the six month period ending September 30 and to have net income before preferred stock dividends and accretion on preferred stock of $1,150,000 for the fiscal year ending March 31, 2004. In addition, the Company is required to have a minimum liquidity coverage, as defined, of not less than 1.25 to 1.00, cash flow coverage, as defined, of not less than 1.20 to 1.00, debt to net worth ratio, as defined, not greater than 1.00 to 1.00 and to maintain a tangible effective net worth, as defined, of not less than $15,000,000 to be increased by 100% of any net equity capital raised and a minimum of 50% of net income. At June 30, 2003, the Company was in compliance with these covenants.

Borrowings under the line of credit and equipment financing loans are secured by a pledge of the Company's net book value of assets of $26.6 million at June 30, 2003 including its intellectual property.

**7. CUSTOMER AND GEOGRAPHIC INFORMATION**

The Company currently operates in one segment and develops, manufactures and markets portable blood analysis systems for use in any veterinary or human patient-care setting to clinicians with rapid blood constituent measurements. The following is a summary of revenues from external customers for each group of products and services provided by the Company (in rounded thousands):

| | Three Months Ended June 30, | |
|---|---|---|
| | 2003 | 2002 |
| Blood chemistry analyzers | $ 3,152,000 | $ 1,998,000 |
| Reagent discs and kits | 6,478,000 | 4,846,000 |
| Other | 661,000 | 537,000 |
| Product sales, net | 10,291,000 | 7,381,000 |
| Development and licensing revenue | 35,000 | 35,000 |
| Total revenues | $ 10,326,000 | $ 7,416,000 |

The following is a summary of revenues by customer group (in rounded thousands):

| | Three Months Ended June 30, | |
|---|---|---|
| | 2003 | 2002 |
| Medical Market | $ 1,596,000 | $ 793,000 |
| Veterinary Market | 8,192,000 | 6,324,000 |
| Other | 538,000 | 299,000 |
| Total revenues | $ 10,326,000 | $ 7,416,000 |

Two distributors, Vedco Inc. and DVM Resources accounted for 26% and 16%, respectively, of total revenues for the three-month period ended June 30, 2003, and 38% and 7%, respectively, of total revenues for the three-month period ended June 30, 2002. The following is a summary of revenues by geographic region based on customer location (in rounded thousands):

| | Three Months Ended June 30 | |
|---|---|---|
| | 2003 | 2002 |
| United States | $ 8,962,000 | $ 6,280,000 |
| Europe | 1,114,000 | 815,000 |
| Asia and Latin America | 250,000 | 321,000 |
| Total revenues | $ 10,326,000 | $ 7,416,000 |

Substantially all of the Company's long-lived assets are located in the United States.

**8. REDEEMABLE CONVERTIBLE PREFERRED STOCK - SERIES E**

*Series E Convertible Preferred Stock* – In March 2002 and April 2002, the Company sold 3,750 and 3,620 shares, respectively, of Series E convertible preferred stock (the "Series E Preferred") at a per share price of $1,000, resulting in net cash proceeds to the Company aggregating $6,812,000. The Company recorded stock offering proceeds receivable of $3,446,000 for the first closing of Series E Preferred at March 31, 2002. The proceeds were

received by the Company on April 3, 2002. The Series E Preferred is non-voting and pays an annual cumulative dividend of 6.5% of the original issue price per share, payable semiannually in cash or shares of common stock at the Company's election. Upon the liquidation of, dissolution of, winding-up of, or change of control in Abaxis, holders of the Series E Preferred are entitled to receive $1,000 per share, the original issue price, plus any accrued but unpaid dividends, as a liquidation preference prior to Abaxis making any distributions to holders of common stock. Accordingly, the Series E preferred stock is classified as a redeemable convertible preferred stock and is included outside of shareholders' equity in the accompanying condensed balance sheets.

At June 30, 2003, the outstanding shares of Series E Preferred were convertible into 856,924 shares of common stock. The Series E Preferred automatically converts into shares of common stock upon the earlier of: (i) the first date following March 28, 2003 on which the closing per share price of Abaxis common stock exceeds $12.00 for twenty consecutive trading days (the "Automatic Price Conversion Date"), or (ii) March 28, 2007; provided, however, that if the closing sales price of the common stock as reported on Nasdaq National Market System is less than $6.50 for each of the twenty (20) consecutive trading days immediately prior to and including March 28, 2007, then the Series E preferred stock will convert into common stock automatically upon the earlier to occur of (A) March 28, 2008, or (B) the Automatic Price Conversion Date. The shares may also be converted at the option of the holder at any time. The number of common shares into which the Series E convertible preferred stock is convertible is subject to adjustment for anti-dilution, stock splits, and other certain events.

Each Series E Preferred investor received a warrant to purchase 50 shares of common stock for each preferred share acquired. The common stock warrants are valid for five years and exercisable at $7.00 per share. Approximately $1,235,000 of the aggregate proceeds were attributed to the value of the warrants and allocated to common stock. The fair value of the warrants was determined using the Black-Scholes option-pricing model with the following assumptions: contractual life of five years, volatility of 78.6%, risk free interest rate of 4.57%-4.92% and no dividends during the contractual term. In connection with the sale of the Series E convertible preferred stock the Company issued to advisors for services a fully-vested warrant to purchase 113,385 shares of its common stock at an exercise price of $6.50 per share and 25,000 shares of its common stock. The aggregate value of these warrants and shares of common stock of $601,000 was recorded as a stock issuance cost. The value of the warrants was determined using the Black-Scholes option pricing model with assumptions substantially consistent with those used for valuing the warrants issued to the investors.

In accordance with the provisions of Emerging Issues Task Force (EITF) Issue 00-27, "Application of EITF Issue No. 98-5, 'Accounting for Convertible Securities with Beneficial Conversion Features of Contingently Adjustable Conversion Ratios,' to Certain Convertible Securities," which became effective in November 2000, the allocated value of the Series E convertible preferred stock contained a beneficial conversion feature calculated based on the difference between the effective conversion price of the proceeds allocated to the Series E convertible preferred stock and the fair market value of the common stock at the date of issuance. The Company determined an aggregate dividend charge of $957,000 representing the value of the beneficial conversion feature.

The amounts recorded in the Company's financial statements for the fiscal year ended March 31, 2003, representing the amounts attributed to the closings in April 2002, were as follows: net cash proceeds - $3,366,000 ($254,000 of issuance costs incurred), allocation to warrants issued to investors - $590,000, warrants issued to advisors for services - $361,000, and the amount of the dividend charge related to the value of beneficial conversion feature - $370,000.

**9. SHAREHOLDERS' EQUITY**

*Stock Purchase Rights* - On April 22, 2003, the Board of Directors of the Company approved the adoption of a Shareholder Rights Plan. Under the terms of the plan, shareholders of record on May 8, 2003, received one preferred stock purchase right for each outstanding share of Common Stock held. Each right entitles the registered holder to purchase from the Company one one-thousandth of a share of the Company's Series RP Preferred Stock, $0.001 par value, at a price of $24.00 per share and becomes exercisable when a person or group acquires 15% or more of the Company's Common Stock without prior approval by the Board of Directors.

**Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations**

Overview

*This Management's Discussion and Analysis of Financial Condition and Results of Operations includes a number of forward-looking statements which reflect Abaxis' current views with respect to future events and financial performance. In this report, the words "will", "anticipates", "believes", "expects", "future", "intends", "plans", and similar expressions identify forward-looking statements. These forward-looking statements are subject to certain risks and uncertainties, including but not limited to those discussed below, that could cause actual results to differ materially from historical results or those anticipated. Such risks and uncertainties include market acceptance of Abaxis' products and continuing development of its products, obtaining required Food and Drug Administration ("FDA") clearance and other government approvals, risks associated with manufacturing and distributing products on a commercial scale, including complying with Federal and state food and drug regulations, and general market conditions and competition. Readers are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date hereof. Abaxis assumes no obligation to update any forward-looking statements as circumstances change.*

Abaxis, Inc. ("us" or "we"), incorporated in California in 1989, develops, manufactures and markets portable blood analysis systems for use in any veterinary or human patient-care setting to provide clinicians with rapid blood constituent measurements. Our principal offices are located at 3240 Whipple Road, Union City, California 94587, and our telephone number at that location is (510) 675-6500. We maintain a website at *www.abaxis.com*. Investors can obtain copies of our filings with the Securities and Exchange Commission from this site free of charge, as well as from the Securities and Exchange Commission website at *www.sec.gov*.

Our primary product is a system consisting of a compact 6.9 kilogram analyzer and a series of single-use plastic discs, called reagent discs, containing all the chemicals required to perform a panel of up to 12 tests. The system can be operated with minimal training and performs multiple routine tests on whole blood, serum or plasma samples. The system provides test results in less than 15 minutes with the precision and accuracy equivalent to a clinical laboratory analyzer. We currently market this system for veterinary use under the name VetScan® and in the human medical market under the name Piccolo®. We also market a hematology analyzer under the name VetScan HMT, which provides a complete blood count ("CBC") including three-part white blood cell ("WBC") differential in less than 2 minutes and requires only 12 µL (microliter) of whole blood. It provides results for eight selectable species, plus two user configurable programs. We market one type of reagent kit with this analyzer. We purchase the hematology analyzer and reagent kits from Melet Schloesing Laboratories of France. We are not obligated to purchase a minimum amount of analyzers or reagent kits. We market the combination of the VetScan and the VetScan HMT under the name VetScan DXS.

In the three months ended June 30, 2003, our domestic revenues accounted for 87% of our total revenues versus 85% in the three months ended June 30, 2002. International revenues accounted for 13% of total revenues in the three months ended June 30, 2003 versus 15% in the three months ended June 30, 2002. The primary reason for the increase in domestic revenues and commensurate decrease in international revenues as a percentage of total revenues in the three months ended June 30, 2003 was an increase of $439,000 in total sales to the U.S. military.

During the three months ended June 30, 2003, we sold 356 instruments worldwide, which includes both blood chemistry and hematology analyzers, a 51% increase from 235 instruments sold in the three months ended June 30, 2002. The increase in instrument sales was primarily in the United States.

Reagent discs and kits sold during the three months ended June 30, 2003 were 536,000, an increase of 30% compared to sales of 412,000 reagent discs and kits during the three months ended June 30, 2002. The increase in reagent discs and kits sold is consistent with our belief that there will be increasing recurring reagent disc revenue as our product lines achieve greater market penetration and more consistent utilization. This growth is mainly attributable to the expanded installed base of VetScan DXS systems and higher consumption rates of institutional users.

Sales for any future periods are not predictable with a significant degree of certainty. We generally operate with limited order backlog because our products typically are shipped shortly after orders are received. As a result, product sales in any quarter are generally dependent on orders booked and shipped in that quarter. Our expense levels, which are to a large extent fixed, are based in part on our expectations of future revenues. Accordingly, we may be unable to adjust spending in a timely manner to compensate for any unexpected revenue shortfall. As a result, any such shortfall would negatively affect our operating results and financial condition. Our sales may be adversely impacted by pricing pressure from competitors. Our ability to be consistently profitable will depend, in

part, on our ability to increase our sales volumes of our VetScan DXS and Piccolo products and to compete with other competitors successfully. We believe that period to period comparisons of our results of operations are not necessarily meaningful.

We introduced our VetScan Canine Heartworm Antigen Test in December 2001. The test is a stand-alone lateral flow device similar in format to simple pregnancy tests. Results are available in a maximum of 10 minutes. We purchased the Vetscan Canine Heartworm Antigen Test from S.A. Scientific, Inc., of San Antonio, Texas, a privately-held leader in the development and manufacturing of a wide-range of one-step rapid tests for various diseases. The addition of the VetScan Canine Heartworm Antigen Test expanded our product lines in the veterinary market. However, in March 2002, Idexx Laboratories, Inc., our principal competitor in the veterinary market, filed a patent infringement lawsuit against both S.A. Scientific and us. On December 6, 2002, we and S.A. Scientific entered into a settlement agreement with Idexx under which, among other terms, Abaxis paid Idexx $249,500 in cash damages and ceased the selling of the particular canine heartworm antigen test referenced in the complaint. We are exploring whether or not we will introduce another canine heartworm antigen test in the near future, although there can be no assurance that we would be successful in any such efforts or that any party will not claim patent infringement on us or file suit upon other grounds.

We continue to explore the application of our proprietary technology used to produce the dry reagents used in the reagent discs, called the Orbos Discrete Lyophilization Process, to other companies' products. This process allows the production of an accurate, precise amount of active chemical ingredients in the form of a soluble bead. We believe that the Orbos process has broad applications in products where delivery of active ingredients in a stable, pre-metered format is desired. We have contracts with Becton Dickinson Immunocytometry Systems and Amersham Biosciences Corp. (formerly Pharmacia Biotech, Inc.) to either supply products or license Orbos technology. Revenues from these agreements, however, is unpredictable. We are currently working with other companies to determine the potential suitability of the Orbos technology to these companies' products. As resources permit, we will pursue other development, licensing or manufacturing agreement opportunities for our Orbos technology with other companies. There can be no assurances, however, that other applications will be identified or that additional agreements with us will result.

**Results of Operations**

*Total Revenues*

During the three months ended June 30, 2003, we reported total revenues of $10,326,000, a $2,910,000 or 39% increase from total revenues of $7,416,000 for the three months ended June 30, 2002. The revenue increase was due to an increase of $1,154,000 in instrument sales, an increase of $1,632,000 in reagent sales and an increase of $124,000 in other sales. Our instrument and reagent sales accounted for 31% and 63%, respectively, of our product sales in the three months ended June 30, 2003 compared to 27% and 66%, respectively, of our product sales in the three months ended June 30, 2002.

We receive royalty payments from Amersham Biosciences (formerly Pharmacia Biotech) equal to 5% of net sales, as defined in our agreement, of Amersham's products that use our technology. During the three months ended June 30, 2003 and 2002, we reported development and licensing revenues of $35,000.

Total revenues in the U.S. for the three months ended June 30, 2003 were $8,962,000, a $2,682,000 or 43% increase from total U.S. revenues of $6,280,000 for the three months ended June 30, 2002. The net increase in the U.S. in the three months ended June 30, 2003 compared to the three months ended June 30, 2002 was attributed to increases of $439,000 in total instrument placements and reagent discs sold to the U.S. military, $1,027,000 in instrument placements to all other customers (excluding the U.S. military), $1,102,000 of reagent discs sold to all other customers (excluding the U.S. military) and $114,000 in other sales.

Total revenues in Europe for the three months ended June 30, 2003 were $1,114,000, a $299,000 or 37% increase from revenues of $815,000 for the three months ended June 30, 2002. The increase in revenues primarily reflects both an increase in instrument sales of $52,000 and reagent sales of $243,000.

Total revenues in Asia and Latin America for the three months ended June 30, 2003 were $250,000, a $71,000 or 22% decrease from revenues of $321,000 for the three months ended June 30, 2002. The decrease in revenues in Asia and Latin America primarily reflects an increase in instrument sales of $11,000 offset by a decrease in reagent sales of $88,000.

*Cost of Product Sales*

Cost of product sales during the three months ended June 30, 2003 was $5,220,000, or 51% of product sales, as compared to $3,719,000, or 50% of product sales, in the three months ended June 30, 2002. The dollar increase in cost of product sales was primarily attributable to continued increases in sales volume of instruments and reagent discs.

*Selling, General and Administrative Expense*

Selling, general and administrative expenses were $3,217,000, or 31% of total revenues, in the three months ended June 30, 2003 compared to $2,386,000, or 32% of total revenues, in the three months ended June 30, 2002. The increase in selling, general and administrative expenses was due primarily to our strategy to expand in the human medical market.

*Research and Development Expense*

Research and development expenses were $1,032,000, or 10% of total revenues, in the three months ended June 30, 2003, compared to $1,005,000, or 14% of total revenues, in the three months ended June 30, 2002. We expect the dollar amount of research and development expenses to slightly increase as we complete development and clinical trials of the Renal Function, Hepatic Function and Comprehensive Metabolic tests in the human medical market. There can be no assurance, however, that we will undertake such research and development activities in future periods or, if we do, that such activities will be successful.

*Interest and Other Income*

Our interest income was $43,000 for the three months ended June 30, 2003, compared to $63,000 for the three months ended June 30, 2002. In the three months period ended June 30, 2003, interest income included $30,000 earned on cash and cash equivalents and $13,000 from our reagent rental program.

*Interest and Other (Expense)*

Our interest expense was $18,000 for the three months ended June 30, 2003, compared to $54,000 for the three months ended June 30, 2002. During the three months ended June 30, 2003, interest expense primarily consisted of $14,000 on our capital equipment loan and capital leases for equipment. During the three months ended June 30, 2002, interest expense primarily consisted of $32,000 on our capital equipment loan and line of credit and $20,000 on capital leases for equipment. No interest was capitalized during the periods.

*Income Taxes*

Income tax expense totaled $24,000 for the three months ended June 30, 2003 compared to income tax expense of $10,000 for the three months ended June 30, 2002. Income tax expense in these two periods primarily relate to taxes for various state tax jurisdictions.

**Liquidity and Capital Resources**

As of June 30, 2003, we had $11,598,000 in cash and cash equivalents. We anticipate to incur incremental additional costs to support our future operations, including further commercialization of our products and development of new test methods that will allow us to expand our veterinary market and further penetrate the human diagnostic market; acquisition of capital equipment for our manufacturing facility, which includes the ongoing costs related to continuing development of our current and future products; and additional pre-clinical testing and clinical trials for our current and future products.

We anticipate that our existing capital resources, debt financing, and anticipated revenue from the sales of our products will be adequate to satisfy our currently planned operating and financial requirements through the next twelve months. Our future capital requirements will largely depend upon the increased market acceptance of our point-of-care blood analyzer products. However, our sales for any future periods are not predictable with a significant degree of certainty.

Net cash provided by operating activities during the three months ended June 30, 2003 was $1,374,000 compared to net cash provided by operating activities of $379,000 in the three months ended June 30, 2002. Net cash provided by operating activities was due primarily to net income of $863,000 plus depreciation and amortization of $377,000, a decrease of $662,000 in trade receivables, prepaid expenses, deposits and other assets and increases totaling $280,000 in accounts payable, warranty reserve and other accrued liabilities and deferred revenue. These sources of cash were partially offset by increase of $628,000 in inventories and decreases in accrued payroll and related

expenses and deferred rent totaling $334,000.

Net cash used in investing activities for the three months ended June 30, 2003 was $140,000 as compared to net cash used of $400,000 for the three months ended June 30, 2002. The increase in net cash used is due to an increase in the purchases of property and equipment.

Net cash used in financing activities for the three months ended June 30, 2003 was $66,000 as compared to net cash provided of $5,686,000 for the three months ended June 30, 2002. Net cash used in financing activities for the three months ended June 30, 2003 was primarily the result of the exercise of common stock options of $68,000 offset by repayments on a capital equipment loan and capital lease obligations totaling $134,000. Net cash provided by financing activities for the three months ended June 30, 2002 was primarily the result of net cash proceeds from issuance of Series E preferred stock of $6,812,000 offset by the exercise of common stock options of $27,000, repayments on the line of credit of $1,000,000, and repayments totaling $153,000 on the equipment financing loan and capital lease obligations.

*Series E Convertible Preferred Stock* – In March 2002 and April 2002, we sold 3,750 and 3,620 shares, respectively, of Series E convertible preferred stock (the "Series E Preferred") at a per share price of $1,000, resulting in aggregate net cash proceeds to us of $6,812,000. We recorded stock offering proceeds receivable of $3,446,000 for the first closing of Series E Preferred at March 31, 2002. The proceeds were received by us on April 3, 2002. The Series E Preferred is non-voting and pays an annual cumulative dividend of 6.5% of the original issue price per share, payable semiannually either in cash or shares of common stock at our election. Upon the liquidation of, dissolution of, winding-up of, or change of control in Abaxis, holders of the Series E Preferred are entitled to receive $1,000 per share, the original issue price, plus any accrued but unpaid dividends, as a liquidation preference prior to our making any distributions to holders of our common stock.

At June 30, 2003, the outstanding shares of Series E Preferred were convertible into 856,924 shares of common stock. The Series E Preferred automatically converts into shares of common stock upon the earlier of: (i) the first date following March 28, 2003 on which the closing per share price of our common stock exceeds $12.00 for twenty consecutive trading days (the "Automatic Price Conversion Date"), or (ii) March 28, 2007; provided, however, that if the closing sales price of our common stock as reported on Nasdaq National Market System is less than $6.50 for each of the twenty (20) consecutive trading days immediately prior to and including March 28, 2007, then the Series E preferred stock will convert into common stock automatically upon the earlier to occur of (A) March 28, 2008, or (B) the Automatic Price Conversion Date. The shares may also be converted at the option of the holder at any time. The number of common shares into which the Series E convertible preferred stock is convertible is subject to adjustment for anti-dilution, stock splits, and other certain events.

Each Series E Preferred investor received a warrant to purchase 50 shares of common stock for each preferred share acquired. The common stock warrants are valid for five years and exercisable at $7.00 per share. Approximately $1,235,000 of the aggregate proceeds were attributed to the value of the warrants and allocated to common stock. The fair value of the warrants was determined using the Black-Scholes option-pricing model with the following assumptions: contractual life of five years, volatility of 78.6%, risk free interest rate of 4.57%-4.92% and no dividends during the contractual term. In connection with the sale of the Series E Preferred we issued to advisors for services a fully-vested warrant to purchase 113,385 shares of our common stock at an exercise price of $6.50 per share and 25,000 shares of common stock. The aggregate value of the warrant and shares of our common stock of $601,000 was recorded as a stock issuance cost. The value of the warrants was determined using the Black-Scholes option pricing model with assumptions substantially consistent with those used for valuing the warrants issued to the investors.

In accordance with the provisions of Emerging Issues Task Force (EITF) Issue 00-27, "Application of EITF Issue No. 98-5, 'Accounting for Convertible Securities with Beneficial Conversion Features of Contingently Adjustable Conversion Ratios,' to Certain Convertible Securities," the allocated value of the Series E convertible preferred stock contained a beneficial conversion feature calculated based on the difference between the effective conversion price of the proceeds allocated to the Series E convertible preferred stock and the fair market value of the common stock at the date of issuance. Accordingly, we determined an aggregate dividend charge of $957,000 representing the value of the beneficial conversion feature.

The amounts recorded in our financial statements for the fiscal year ended March 31, 2003, representing the amounts attributed to the closings in April 2002, were as follows: net cash proceeds - $3,366,000 ($254,000 of issuance costs incurred), allocation to warrants issued to investors - $590,000, warrants issued to advisors for services - $361,000, and the amount of the dividend charge related to the beneficial conversion feature - $370,000.

*Line of Credit and Long-Term Debt* – In March 2002, we terminated certain line of credit and equipment financing loans and entered into new line of credit and equipment financing loans with Comerica Bank-California. The new line of credit provides for borrowings of up to $5,250,000, based on our outstanding accounts receivables and inventory, as defined by the bank: up to $4,000,000 is collateralized by domestic receivables and up to $1,250,000 is collateralized by foreign receivables. This new line of credit bears interest at the prime rate, which was 4.00% at June 30, 2003, and is payable monthly. Of the $4,000,000 domestic line of credit, $820,000 was committed to secure a letter of credit for our facilities lease. The domestic line of credit terminates upon notification by either party and the outstanding balance is payable upon demand. The foreign line of credit expired in September 2002 and was renewed until September 2003. The weighted average interest rate on borrowings under our line of credit facilities during the three months ended June 30, 2003 and 2002 was 4.24% and 4.75%, respectively. At June 30, 2003, there was no amount outstanding under our line of credit. At June 30, 2003, $3,950,000 was available for borrowing.

The balance of the new equipment financing loan at June 30, 2003 was $817,000. The equipment loan bears interest at the prime rate plus 1%, which totaled 5.00% at June 30, 2003, and is payable in monthly installments of principal and interest totaling approximately $42,000 over a period of two years. The weighted average interest rate on equipment financing loans during the three months ended June 30, 2003 and 2002 was 5.24% and 5.75%, respectively.

The line of credit and equipment financing agreements contain certain financial covenants, which are evaluated on a quarterly basis. Included in these financial covenants, among other stipulations, is a requirement that we have a minimum net income of $25,000 before preferred stock dividends and accretion in any three quarters of a fiscal year, provided that any loss before preferred stock dividends and accretion incurred in the remaining quarter is not to exceed $250,000. We are also required to be profitable, as defined, on a fiscal year to date basis beginning with the six month period ending September 30 and to have net income before preferred stock dividends and accretion on preferred stock of $1,150,000 for the fiscal year ending March 31, 2004. In addition, we are required to have a minimum liquidity coverage, as defined, of not less than 1.25 to 1.00, cash flow coverage, as defined, of not less than 1.20 to 1.00, debt to net worth ratio, as defined, not greater than 1.00 to 1.00 and to maintain a tangible effective net worth, as defined, of not less than $15,000,000 to be increased by 100% of any net equity capital raised and a minimum of 50% of net income. At June 30, 2003, we were in compliance with these covenants.

Borrowings under the line of credit and equipment financing loans are secured by a pledge of our net book value of assets of $26.6 million at June 30, 2003 including our intellectual property.

**Critical Accounting Policies** – We have identified certain accounting policies as critical to our business operations and the understanding of our results of operations. The impact and any associated risks related to the identified critical accounting policies on our business operations are discussed in our amended Annual Report on Form 10-K/A for the fiscal year ended March 31, 2003 filed with the Securities and Exchange Commission.

**Contingencies** – We are involved in various litigation matters in the normal course of business. We believe that the ultimate resolution of these matters will not have a material effect on our financial position or results of operations.

On March 28, 2002, Idexx Laboratories, Inc., our principal competitor in the veterinary diagnostic market, filed a complaint in the United States District Court for the District of Maine (Civil Action Docket No. 02-69-P-H) alleging that a canine heartworm test produced for us by a third party, S.A. Scientific, Inc., and sold using the Abaxis brand infringed on U.S. Patents Nos. 4,965,187 and 4,939,096 held by Idexx. On December 6, 2002, we and S.A. Scientific entered into a settlement agreement with Idexx under which, among other terms, we paid Idexx $249,500 in cash damages and ceased selling the particular canine heartworm antigen test referenced in the complaint. We are exploring whether or not we will introduce another canine heartworm antigen test in the near future and there can be no assurance that any party will not claim patent infringement or file suit upon other grounds. We would incur expenses in the defense of such claims and our attention could be diverted from our operations.

**New Accounting Pronouncements** – In December 2002, the FASB issued SFAS No. 148, "Accounting for Stock-Based Compensation - Transition and Disclosure." SFAS No. 148 amends FASB Statement No. 123, "Accounting for Stock-Based Compensation," to provide alternative methods of transition for a voluntary change to the fair value based method of accounting for stock-based employee compensation. In addition, SFAS No. 148 amends the disclosure requirements of SFAS No. 123 to require prominent disclosures in both annual and interim financial statements of the method of accounting for stock-based employee compensation and the effect of the method used on reported results. SFAS No. 148 is effective for fiscal years beginning after December 15, 2002. We adopted the disclosure provisions of SFAS No. 148 on January 1, 2003. We do not expect to change to using the fair value based method of accounting for stock-based employee compensation; and therefore, adoption of SFAS No. 148 is

not expected to have an impact on our financial position, results of operations or cash flows in the financial statements.

In April 2003, the FASB issued SFAS No. 149, "Amendment of Statement 133 on Derivative Instruments and Hedging Activities. " This statement amends and clarifies financial accounting and reporting for derivative instruments, including certain derivative instruments embedded in other contracts (collectively referred to as derivatives) and for hedging activities under FASB Statement No. 133, "Accounting for Derivative Instruments and Hedging Activities. " This statement is effective for contracts entered into or modified after June 30, 2003. The adoption of this statement is not expected to have an impact on our financial position, results of operations or cash flows.

In May 2003, the FASB issued SFAS No. 150, "Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity. " This statement establishes standards for how an issuer classifies and measures certain financial instruments with characteristics of both liabilities and equity. This statement is effective for financial instruments entered into or modified after May 31, 2003 and otherwise is effective at the beginning of the first interim period beginning after June 15, 2003. The adoption of this statement is not expected to have an impact on our financial position, results of operations or cash flows.

## RISK FACTORS THAT MAY AFFECT OUR PERFORMANCE

Our future performance is subject to a number of risks. If any of the following risks actually occur, our business could be harmed and the trading price of our common stock could decline. You should also refer to other information contained in our annual report for the fiscal year ended March 31, 2003, as filed on Form 10-K/A, including the financial statements included therein and the notes related thereto.

When used in these risk factors, the words "anticipates," "believes," "expects," "intends," "plans," "future," and similar expressions identify forward-looking statements. Our actual results could differ materially from those that we project in the forward-looking statements as a result of factors that we have set forth throughout this document as well as factors of which we are currently not aware.

### We Are Not Consistently Profitable; We Must Increase Sales Of Our Piccolo And Vetscan DXS Products To Maintain Consistent Profitability

We recognized a net loss in two of the last twelve fiscal quarters ended March 31, 2003. After accounting for dividend charges associated with the issuance of our preferred stock and non-cash charges related to the beneficial conversion feature contained in the preferred stock, we recognized a net loss in six of those quarters. There can be no assurance that we will experience profitability in the future. As of June 30, 2003, we have incurred cumulative net losses of approximately $61 million. Our ability to be consistently profitable will depend, in part, on our ability to increase our sales volumes of our VetScan DXS and Piccolo products. Increasing our sales volume of our products will depend upon our ability to:

- continue to develop our products;
- increase our sales and marketing activities;
- increase our manufacturing activities; and
- effectively compete against current and future competitors.

We cannot assure you that we will be able to successfully increase our sales volumes of our products to achieve sustained profitability.

### We Are Not Able To Predict Sales In Future Quarters And A Number Of Factors Affect Our Periodic Results

We are not able to accurately predict our sales in future quarters. In any quarter, we derive almost half of our revenues from two distributors who resell our products to the ultimate user. While we are better able to predict sales of our reagent discs, as we sell these discs primarily for use with analyzers that we sold in prior periods, we generally are unable to predict with much certainty sales of our analyzers, as we typically sell our analyzers to new users. Accordingly, our sales in any one quarter are not indicative of our sales in any future period. In addition, we

generally operate with limited order backlog, because we ship our products shortly after we receive the orders from our customers. As a result, our product sales in any quarter are generally dependent on orders that we receive and ship in that quarter. We base our expense levels, which are to a large extent fixed, in part on our expectations as to future revenues. We may be unable to reduce our spending in a timely manner to compensate for any unexpected revenue shortfall. As a result, any such shortfall would immediately materially and adversely impact our operating results and financial condition. In addition, we have historically experienced a decrease in our sales, especially in Europe, in our second and third quarters, ending in September and December of each year, which we believe is due to seasonal patterns in the decision making processes to acquire our products. Accordingly, we believe that period to period comparisons of our results of operations are not necessarily meaningful.

Our periodic operating results have varied in the past. In the future, we anticipate our periodic operating results to vary significantly depending on, but not limited to, a number of factors, including, in addition to those factors discussed elsewhere in this section:

- new product announcements made by us or our competitors;
- changes in our pricing structures or the pricing structures of our competitors;
- our ability to develop, introduce and market new products on a timely basis;
- our manufacturing capacities and our ability to increase the scale of these capacities;
- the mix of product sales between our analyzer and our reagent disc products;
- the amount we spend on research and development; and
- changes in our strategy.

**We Could Fail to Achieve Anticipated Revenue If The Market Does Not Accept Our Products**

Our core compact blood analyzer product differs substantially from current blood analyzers on the market. Our primary competition is from centralized laboratories that offer a greater number of tests than our products, but do so at greater cost and requiring more time. We also compete with other point-of-care analyzers that cost more, require more maintenance and offer a narrower range of tests. However, these point-of-care analyzers are generally marketed by larger companies which have greater resources for sales and marketing, in addition to a recognized brand name and established relationships.

Historically we have marketed our VetScan analyzer to veterinarians and we have limited experience in large scale sales of our Piccolo analyzer into the human medical market. We continue to develop new animal blood tests that we cannot be assured will be accepted by the veterinary market. Although we believe that our blood analyzers offer consumers many advantages, including according to our analyses substantial cost savings, in terms of the actual product and implementation of it procedurally, these advantages involve changes to current standard practices, such as using large clinical laboratories, that will require changes in both the procedures and mindset of care providers. The human medical market in particular is highly regulated, structured and often slow to change. If we are unable to convince large numbers of medical clinics, hospitals and other points-of-care of the benefits of our products, we will suffer lost sales and could fail to achieve anticipated revenue.

**We are Dependent Upon Our Profitability, and If We Cannot Remain Profitable We May Need Additional Funding In The Future And These Funds May Not Be Available To Us**

We believe that our existing capital resources, bank and equipment financing loans and anticipated revenue from the sales of our products will be adequate to satisfy our currently planned operating and financial requirements through March 31, 2004, although no assurances can be given. Our bank financing documents contain a number of covenants concerning financial tests that we must meet that are more fully detailed in the agreements that we have filed with the SEC as exhibits to our periodic reports. We may need additional funds if we are unable to meet requirements for continuing access to bank financing or if we do not achieve anticipated revenues from the sale of our Piccolo and VetScan DXS products.

Further, we expect to incur incremental additional costs to support our future operations, including:

- further commercialization of our products and development of new test methods to allow us to further

penetrate the human diagnostic market and the veterinary diagnostic market;

- our need to acquire capital equipment for our manufacturing facilities, which includes the ongoing implementation of our semi-automated manufacturing lines to provide capacity for the production of commercial volumes of our products;

- research and design costs related to the continuing development of our current and future products; and

- additional pre-clinical testing and clinical trials for our current and future products.

To the extent that our existing resources and anticipated revenue from the sale of our products are insufficient to fund our activities or if we are unable to meet the financial tests contained in our bank financing documents, we may have to raise additional funds from the issuance of public or private securities. In the event that we cannot maintain compliance with the financial covenants of our bank financing agreements, we may also be subject to increased interest rate expenses. We may not be able to raise additional funding, or if we are able to, we may not be able to raise funding on acceptable terms. We may also dilute then-existing shareholders if we raise additional funds by issuing new equity securities. Alternately, we may have to relinquish rights to certain of our technologies, products and/or sales territories if we are required to obtain funds through arrangements with collaborative partners. If we are unable to raise needed funds, we may be required to curtail our operations significantly. This would materially adversely affect our operating results and financial condition.

**We Recently Settled a Patent Infringement Lawsuit And We Could Be the Subject of Similar Legal Action in the Future**

On March 28, 2002, Idexx Laboratories, Inc., our principal competitor in the veterinary diagnostic market, filed a complaint in the United States District Court for the District of Maine (Civil Action Docket No. 02-69-P-H) alleging that a canine heartworm test produced for us by a third party, S.A. Scientific, Inc., and sold using the Abaxis brand infringed on U.S. Patents Nos. 4,965,187 and 4,939,096 held by Idexx. On December 6, 2002, the parties entered into a settlement agreement under which, among other terms, we paid Idexx $249,500 in cash damages and we ceased the selling the particular canine heartworm antigen test referenced in the complaint. We are exploring whether we will introduce another canine heartworm antigen test in the near future and there can be no assurance that any party will not claim patent infringement or file suit upon other grounds. We would incur expenses in the defense of such claims and our attention could be diverted from our operations.

**We Rely On Patents And Other Proprietary Information, The Loss Of Any Of Which Would Negatively Affect Our Business**

As of June 30, 2003, we have filed 26 patent applications in the United States, of which 23 have been issued. Additionally, we have filed several international patent applications covering the same subject matter as our domestic applications. The patent position of any medical device manufacturer, including Abaxis, is uncertain and may involve complex legal and factual issues. Consequently, we may not be issued any additional patents, either domestically or internationally. Furthermore, our patents may not provide significant proprietary protection because there is a chance that they will be circumvented or invalidated. We cannot be certain that we were the first creator of the inventions covered by our issued patents or pending patent applications, or that we were the first to file patent applications for these inventions, because (1) the United States Patent and Trademark Office maintains all patent applications in secrecy until it issues the patents and (2) publications of discoveries in the scientific or patent literature tend to lag behind actual discoveries by several months. We may have to participate in interference proceedings, which are proceedings in front of the U.S. Patent and Trademark Office, to determine who will be issued a patent. These proceedings could be costly and could be decided against us.

We also rely upon copyrights, trademarks and unpatented trade secrets. Others may independently develop substantially equivalent proprietary information and techniques that would undermine our proprietary technologies. Further, others may gain access to our trade secrets or disclose such technology. Although we require our employees, consultants and advisors to execute agreements that require that our corporate information be kept confidential and that any inventions by these individuals are property of Abaxis, there can be no assurance that these agreements will provide meaningful protection or adequate remedies for our trade secrets in the event of unauthorized use or disclosure of such information. The unauthorized dissemination of our confidential information would negatively impact our business.

**We Continue to Develop Our Marketing And Distribution Experience In the Human Diagnostic Market And Have Limited Resources To Devote To Such Efforts**

Although we have gained experience marketing our VetScan System products for the past seven years in the veterinary diagnostic market, we have much less experience in marketing the Piccolo System in the human diagnostic market. Accordingly, we have limited sales, marketing and distribution experience, especially in the human diagnostic market. We cannot assure you that:

- we will be able to establish and maintain effective distribution arrangements in the human medical market;
- any distribution arrangements that we are able to establish will be successful in marketing our products; or
- the costs associated with marketing and distributing our products will not be excessive.

Should we fail to effectively develop our marketing and distribution efforts, our growth will be limited and our results of operations will be adversely affected.

**Many of Our Sales Force Have Been Employed by Us for Less Than One Year And We Must Effectively Train And Integrate Our Sales Team In Order To Achieve Our Anticipated Revenue**

We have thirty-two full-time sales personnel involved in our sales and marketing activities, many of whom have been employed by us for a limited period of time. While these individuals work with our distribution partners both domestically and internationally to extend our market reach, the primary selling activities are often done by these individuals. If we are to increase our sales, we will need to train our new salespeople and supervise them closely. We also will continue hiring additional sales personnel. If we are unable to retain our existing personnel, or attract and train additional qualified personnel, our growth may be limited due to our lack of capacity to market our products.

**We Need to Successfully Manufacture and Market Additional, Recently Approved Reagent Discs For The Human Diagnostic Market If We Are To Compete In That Market**

We have developed a blood analysis system that consists of a portable blood analyzer and single-use reagent discs. Each reagent disc performs a series of standard blood tests. We believe that it is necessary to develop additional series of reagent discs with various tests for use with the Piccolo and VetScan DXS. Historically, we primarily developed reagent discs suitable for the veterinary diagnostic market. We recently received approval from the U.S. Food and Drug Administration to begin selling additional tests, namely HDL and triglycerides, for the more lucrative human diagnostic market. These tests are included in standard tests for which the medical community receives reimbursements from third party payors such as HMOs and Medicare. We may not be able to successfully manufacture or market these newly developed reagent discs. Our failure to meet these challenges will materially adversely affect our operating results and financial condition.

**We Rely On Distributors To Sell Our Products; We Rely On Sole Distributor Arrangements In A Number Of Countries**

We distribute our products primarily through distributors. As a result, we are dependent upon these distributors to sell our products and to assist us in promoting and creating a demand for our products. We have a number of distributors in the United States who distribute our VetScan DXS products. Two distributors, Vedco Inc. and DVM Resources accounted for 26% and 16%, respectively, of total revenues for the three-month period ended June 30, 2003. Vedco Inc. and DVM Resources accounted for 38% and 7%, respectively, of total revenues for the three-month period ended June 30, 2002. We believe that our future growth depends on the efforts of these distributors. If one of our distributors, particularly Vedco, Inc., were to stop selling our products we may not be able to replace such lost revenue. We operate on a purchase order basis with Vedco, Inc. and DVM Resources and each of these distributors is under no contractual obligation to continue carrying our products. Further, many of our distributors may carry our competitors' products, and may promote our competitors' products over our own products. Finally, we do not have at this time distribution partners in the United States or overseas who distribute our products for the human diagnostic market.

We currently have exclusive distribution agreements for our VetScan DSX products in Argentina, Australia, Austria, Bahrain, China, Greece, Japan, Korea, Mexico, New Zealand, Portugal, South Africa, Spain, Switzerland, United Arab Emirates and the United Kingdom. Our distributor in each of these countries is responsible for obtaining the necessary approvals to sell our products. These distributors may not be successful in obtaining proper approvals for our products in their respective countries, and they may not be successful in marketing our products. We plan to enter into additional distribution agreements to expand our international distribution base and solidify our international presence. However, we may not be successful in entering into additional distributor agreements. Our

distributors may terminate their relationship with us at any time. Historically, we have experienced a high degree of turnover among our international distributors. This high degree of turnover makes it difficult for us to establish a steady distribution network overseas. Consequently, we may not be successful in marketing our Piccolo System and VetScan DXS products internationally.

**We Depend On Sole Suppliers For Several Key Components To Our Products, Many of Whom We Have Not Entered Into Contractual Relationships With**

We use several key components that are currently available from limited or sole sources as discussed below:

- *Reagent Discs:* Two injection molding manufacturers, C. Brewer & Co. and Nypro Oregon, Inc., currently make the molded plastic discs which, when loaded with reagents and welded together, form our reagent disc products. We believe that only a few manufacturers are capable of producing these discs to the narrow tolerances that we require; to date, we have only qualified these two manufacturers, with Nypro Oregon, Inc. being qualified at two separate facilities, to manufacture the molded plastic discs.

- *Reagent Chemicals:* We currently depend on the following single source vendors for some of the chemicals that we use to produce the dry reagent chemistry beads that are either inserted in our reagent discs or sold as a stand-alone product: Amano Enzyme USA Co., Ltd., Genzyme Corporation, Kikkoman Corporation Biochemical Division, Lee Biosolutions, Inc., the Diagnostic Systems and Molecular Biochemicals divisions of F. Hoffman-La Roche, Ltd., Shinko American Inc., Sigma Aldrich Inc. and Worthington Biochemical Corporation.

- *Blood Analyzer Components:* Our analyzer products use several technologically advanced components that we currently purchase from two single source vendors, PerkinElmer, Inc. and Electro-Alliance, Inc. Our analyzers use a printer that is only made by Seiko North America Corporation. The loss of the supply of any of these components could force us to redesign our analyzers.

- *Hematology Instrument and Reagents:* We currently purchase HMT instruments and reagents from MELET SCHLOESING Laboratories (MELET) of France.

We operate on a purchase order basis with all of the suppliers of our molded plastic reagent disks, reagent chemicals, and blood analyzer components and thus these suppliers are under no contractual obligation to supply us with their products or to do so at specified prices. Although we believe that there are potential alternate suppliers available for these critical components, to date we have not qualified additional vendors beyond those referenced above.

Because we are dependent on a limited number of suppliers and manufacturers for critical components to our products, we are particularly susceptible to any interruption in the supply of these products or the viability of our assembly arrangements. The loss of any one of these suppliers or a disruption in our manufacturing arrangements could materially adversely affect our business and financial condition.

**We Compete With Larger, Better Established Entities Such As Hospitals And Commercial Laboratories**

Blood analysis is a well established field in which there are a number of competitors that have substantially greater financial resources and larger, more established marketing, sales and service organizations than we do. We compete with the following organizations:

- commercial clinical laboratories;

- hospitals' clinical laboratories; and

- manufacturers of bench top multi-test blood analyzers and other testing systems that health care providers can use "on-site."

**We May Not Be Able To Compete With These Organizations Or Their Products Or With Future Organizations Or Future Products**

Historically, hospitals and commercial laboratories perform the most human medical testing, and commercial laboratories perform the most veterinary medical testing. We have identified five principal factors that customers typically use to evaluate our products and those of our competitors. These factors are:

- range of tests offered;
- the immediacy of results;
- cost effectiveness;
- ease of use; and
- reliability of results.

We believe that we compete effectively on each of these factors except for the range of tests offered. Clinical laboratories are effective at processing large panels of tests using skilled technicians and complex equipment. While our current offering of reagent discs cannot provide the same broad range of tests, we believe that in certain limited markets our products provide a sufficient breadth of test menus to compete successfully with clinical laboratories given the advantages of our products with respect to the other four factors. However, we cannot assure you that we will continue to be able to compete effectively on cost effectiveness, ease of use, immediacy of results or reliability of results. We also cannot assure you that we will ever be able to compete effectively solely on the basis of range of tests offered.

Competition in the human and veterinary diagnostic markets is intense. Our principal competitors in the human blood-analyzer market are Alfa Wassermann S.P.A., Hemagen Diagnostics, Inc., i-STAT Corporation, Johnson & Johnson (including its subsidiary, Ortho-Clinical Diagnostics, Inc.), Novitron International, Inc. and Roche. Our principal competitors in the veterinary blood-analyzer market are Idexx Laboratories, Inc. and Heska Corporation. Most of our competitors have significantly greater financial and other resources than we do. In particular, many of our competitors have large sales forces and well-established distribution channels. Consequently, we must develop our distribution channels and improve our direct sales force in order to compete in these markets.

**Changes In Third Party Payor Reimbursement Regulations Can Negatively Affect Our Business**

By regulating the maximum amount of reimbursement they will provide for blood testing services, third party payors, such as HMOs, pay-per-service insurance plans, Medicare and Medicaid, can indirectly affect the pricing or the relative attractiveness of our human testing products. For example, the Health Care Financing Administration sets the level of reimbursement of fees for blood testing services for Medicare beneficiaries. If third party payors decrease the reimbursement amounts for blood testing services, it may decrease the amount that physicians and hospitals are able to charge patients for such services. Consequently, we will need to charge less for our products. If the government and third party payors do not provide for adequate coverage and reimbursement levels to allow health care providers to use our products, the demand for our products will decrease.

**We Are Subject To Numerous Governmental Regulations**

- ***Need for FDA Certification for Our Medical Device Products***

Our Piccolo products are regulated under the 1976 Medical Device Amendments to the Food, Drug and Cosmetic Act, which is administered by the Food and Drug Administration. The FDA has classified our Piccolo products as "Class I" and "Class II" devices. These classifications require us to submit to the FDA a pre-market notification form or 510(k). The FDA uses the 510(k) to substantiate product claims that are made by medical device manufacturers prior to marketing. In our 510(k) notification, we must, among other things, establish that the product we plan to market is "substantially equivalent" to (1) a product that was on the market prior to the adoption of the 1976 Medical Device Amendment or (2) to a product that the FDA has previously cleared under the 510(k) process. The FDA review process of a 510(k) notification can last anywhere from three to six months, and the FDA must issue a written order finding "substantial equivalence" before a company can market a medical device. To date, we have received market clearance from the FDA for our Piccolo System and 26 reagent tests that we have on eight reagent discs. We are currently developing additional tests that the FDA will have to clear through the 510(k) notification procedures. These new test products are crucial for our success in the human diagnostic market. If we do not receive 510(k) clearance for a particular product, we will not be able to sell that product in the United States.

- ***Need to Comply with Manufacturing Regulations***

The 1976 Medical Device Amendment also requires us to manufacture our Piccolo products in accordance with Good Manufacturing Practices guidelines. Current Good Manufacturing Practice requirements are set forth in

the quality system regulation. These requirements regulate the methods used in, and the facilities and controls used for, the design, manufacture, packaging, storage, installation and servicing of our medical devices intended for human use. Our manufacturing facility is subject to periodic audits. In addition, various state regulatory agencies may regulate the manufacture of our products. For example, we have obtained a license from the State of California to manufacture our products. In September 1996, the FDA granted our manufacturing facility "in compliance" status, based on the regulations for Good Manufacturing Practices for medical devices. We are scheduled for inspection by the FDA and the State of California on a routine basis, typically once every 24 months. In April 2001, the State of California granted licensing for the new Union City facility in early May 2001. The most recent inspection was in March 2003 when the FDA conducted a facilities inspection and verified our compliance with the 21 CFR 820 Regulation. We cannot assure you that we will successfully pass a re-inspection by the FDA or the State of California. In addition, we cannot assure you that we can comply with all current or future government manufacturing requirements and regulations. If we are unable to comply with the regulations, or if we do not pass routine inspections, our business and results of operations will be materially adversely affected.

- ***Effects of the Clinical Laboratory Improvement Amendments on Our Products***

Our Piccolo products are affected by the Clinical Laboratory Improvement Amendments of 1988. The Clinical Laboratory Improvement Amendments are intended to insure the quality and reliability of all medical testing in the United States regardless of where tests are performed. The current Clinical Laboratory Improvement Amendments divide laboratory tests into three categories: "simple," "moderately complex" and "highly complex." Tests performed using the Piccolo system are in the "moderately complex" category. This category requires that any location in which testing is performed be certified as a laboratory. Hence, we can only sell our Piccolo products to customers who meet the standards of a laboratory. To receive "laboratory" certification, a testing facility must be certified by the Health Care Financing Administration. After the testing facility receives a "laboratory" certification, it must then meet the Clinical Laboratory Improvement Amendments regulations. Because we can only sell our Piccolo products to testing facilities that are certified "laboratories," the market for our products is correspondingly constrained. Consequently, the market for our Piccolo products will be confined to those testing facilities that are certified as "laboratories" and our growth will be limited accordingly.

- ***We Are Subject to Various Federal, State and Local Regulations***

Federal and state regulations regarding the manufacture and sale of health care products and diagnostic devices may change. We cannot predict what impact, if any, such changes would have on our business. In addition, as we continue to sell in foreign markets, we may have to obtain additional governmental clearances in those markets. We may not be able to obtain regulatory clearances for our products in the United States or in foreign markets, and the failure to obtain these regulatory clearances will materially adversely affect our business and results of operations.

Although we believe that we will be able to comply with all applicable regulations of the Food and Drug Administration and of the State of California, including Quality System Regulations, current regulations depend on administrative interpretations. Future interpretations made by the Food and Drug Administration, the Centers for Medicare and Medicaid Services (CMS) or other regulatory bodies may adversely affect our business.

**We Depend On Key Members Of Our Management And Scientific Staff, And We Must Retain And Recruit Qualified Individuals If We Are To Be Competitive**

We are highly dependent on the principal members of our management and scientific staff. The loss of any of these key personnel, including in particular Clinton H. Severson, our President, Chief Executive Officer and Chairman of our Board of Directors, might impede the achievement of our business objectives. Mr. Severson's amended and restated employment agreement with us was filed with the SEC on August 14, 2001 as an exhibit to our quarterly report for the quarter ended June 30, 2001. We are not aware of any member of our executive management team who intends to retire within one year of the date of this filing. We currently do not maintain key man life insurance on any of our employees. Although historically we have been relatively successful both in retaining our current management and scientific staff and attracting and retaining skilled and experienced marketing, sales and manufacturing personnel, we may not be able to employ such personnel on acceptable terms in the future because numerous medical products and other high technology companies compete for the services of these qualified individuals.

**We May Inadvertently Produce Defective Products, Which May Subject Us to Significant Warranty Liabilities or Product Liability Claims And We May Have Insufficient Product Liability Insurance**

Our business involves applying sophisticated methods to raw materials and producing defect-free medical test equipment. Although we have established procedures for quality control on both the raw materials that we receive from suppliers and our manufactured final products, these procedures may prove inadequate to detect a defect that either occurs in limited quantities or that we have not anticipated. Should we inadvertently ship defective products, we may be subject to substantial claims under our warranty policy. Further, our business exposes us to potential product liability risks, which are inherent in the testing, manufacturing and marketing of human and veterinary medical products. We currently maintain product liability insurance. We believe that this insurance is adequate for our needs, taking into account the risks involved and cost of coverage. However, our product liability insurance may be insufficient to cover potential liabilities. In addition, in the future the coverage that we require may be unavailable on commercially reasonable terms, if at all. Even with our current insurance coverage, a mass product defect, product liability claim or recall could materially adversely affect our business or our financial condition.

**Legislative Actions, Higher Insurance Cost And Potential New Accounting Pronouncements Are Likely To Cause Our General And Administrative Expenses To Increase And Impact Our Future Financial Position And Results Of Operations**

In order to comply with the newly adopted Sarbanes-Oxley Act of 2002, as well as proposed changes to listing standards by Nasdaq, and proposed accounting changes by the Securities and Exchange Commission, we may be required to enhance our internal controls, hire additional personnel and utilize additional outside legal, accounting and advisory services, all of which will cause our general and administrative costs to increase. Insurers are also likely to increase premiums as a result of the high claims rates incurred over the past year, and so our premiums for our various insurance policies, including our directors' and officers' insurance policies, are likely to increase. Proposed changes in the accounting rules, including legislative and other proposals to account for employee stock options as a compensation expense among others, could materially increase the expenses that we report under generally accepted accounting principles and adversely affect our operating results.

**We Must Comply With Strict And Costly Environmental Regulations**

We are subject to stringent federal, state and local laws, rules, regulations and policies that govern the use, generation, manufacture, storage, air emission, effluent discharge, handling and disposal of certain materials and wastes. In particular, we are subject to laws, rules and regulations governing the handling and disposal of biohazardous materials used in the development and testing of our products. We handle and dispose of human and veterinary blood samples for testing (whole blood, plasma, serum) and we pay approximately $48,000 per year to comply with applicable environmental regulations. Although we believe that we have complied with applicable laws and regulations in all material respects and have not been required to take any action to correct any noncompliance, we may have to incur significant costs to comply with environmental regulations if our manufacturing to commercial levels continues to increase. In addition, if a government agency determines that we have not complied with these laws, rules and regulations, we may have to pay significant fines and/or take remedial action that would be expensive and we do not carry environmental-related insurance coverage.

**System Failures Or Delays May Harm Our Business And Our Facilities And Manufacturing Operations Are Vulnerable To Natural Disasters And Other Unexpected Losses**

Our success depends on the efficient and uninterrupted operation of our manufacturing operations, which are co-located with our corporate headquarters in Union City, California. A failure of manufacturing operations, be it in the development and manufacturing of our VetScan or Piccolo analyzers or the reagent discs used in the analyzers could result in our inability to supply customer demand.

We do not have a backup facility to provide redundant manufacturing capacity in the event of a system failure. Accordingly, if our Union City location experienced a system failure, or regulatory problem that temporarily shut-down our manufacturing facility, our manufacturing ability would become unavailable until we were able to bring an alternative facility online, a process which could take several weeks or even months. These manufacturing operations are also vulnerable to damage from earthquakes, fire, floods, power loss, telecommunications failures, break-ins and similar events. Although we carry property and business interruption insurance, our coverage may not be adequate to compensate us for all losses that may occur. Additionally, our computer servers may be vulnerable to computer viruses, physical or electronic break-ins and similar disruptions.

**Fluctuations In Foreign Exchange Rates And The Possible Lack Of Financial Stability In Foreign Countries Could Prevent Overseas Sales Growth**

Our international sales are overwhelmingly currently U.S. dollar-denominated. As a result, an increase in the value of the U.S. dollar relative to foreign currencies could make our products less competitive in international markets. For the limited amount of our sales denominated in local currencies, we are subject to fluctuations in exchange rates between the U.S. dollar and the particular local currency. Our operating results could also be adversely affected by the seasonality of international sales and the economic conditions of our overseas markets.

**Our Stock Price Is Highly Volatile And Investing In Our Stock Involves A High Degree Of Risk**

The market price of our common stock, like the securities of many other medical products companies, fluctuates over a wide range, and will continue to be highly volatile in the future. During the past two fiscal years, our stock price traded at a high of $6.99 on January 25, 2002 and a low of $2.69 on April 5, 2001. The following factors may affect the market price of our common stock:

- fluctuation in our operating results;
- announcements of technological innovations or new commercial products by us or our competitors;
- changes in governmental regulation;
- prospects and proposals for health care reform;
- governmental or third party payors' controls on prices that our customers may pay for our products;
- developments or disputes concerning patent or our other proprietary rights;
- public concern as to the safety of our devices or similar devices developed by our competitors; and
- general market conditions.

Because our stock price is so volatile, investing in our common stock is highly risky. A potential investor must be able to withstand the loss of his entire investment in our common stock.

**Our Recently Adopted Shareholders Rights Plan And Our Ability To Issue Preferred Stock May Delay Or Prevent A Change Of Control Of Abaxis**

Our Shareholder Rights Plan, adopted by our board of directors on April 22, 2003 may make it more difficult for a third party to acquire, or discourage a third party from attempting to acquire, control of Abaxis. The Shareholder Rights Plan could limit the price that investors might be willing to pay in the future for shares of our common stock.

In addition, our board of directors has the authority to issue up to 5,000,000 shares of preferred stock and to determine the price, rights, preferences, privileges and restrictions, including voting rights, of those shares without any further vote or action by the stockholders, except to the extent required by NASDAQ rules. The issuance of preferred stock, while providing flexibility in connection with possible financings or acquisitions or other corporate purposes, could have the effect of making it more difficult for a third party to acquire a majority of our outstanding voting stock.

**Item 3. Quantitative and Qualitative Disclosures About Market Risk**

We are exposed to financial market risks with respect to interest rates on our accounts receivable line of credit, long-term debt and cash equivalent investments.

For our accounts receivable line of credit, the interest rate is equal to the prime rate. Consequently, an increase in the prime rate would expose us to higher interest expenses. There was no outstanding balance on our accounts receivable line of credit at June 30, 2003.

For our long-term debt, which is our equipment loan, the interest rate is equal to 1.0% over the prime rate. As with our accounts receivable credit facility, any increase in interest rates would expose us to higher interest expenses. The balance on our long-term debt was $817,000 as of June 30, 2003. Based on this balance, for each 1% increase in the prime rate, we would pay a total of approximately $2,000 of additional interest each quarter.

All of our sales are denominated in U.S. dollars, except for sales under our OEM agreement to provide VetScan systems to MELET which are denominated in Euros. Sales to MELET during the three months ended June 30, 2003 were 1% of our total revenues. At June 30, 2003, the net receivable from Melet was $104,000.

As a matter of management policy, we do not currently enter into transactions involving derivative financial instruments. In the event we do enter into such transactions in the future, such items will be accounted for in accordance with Statement of Financial Accounting Standards No. 133, "Accounting for Derivative Instruments and Hedging Activities," in which case we will formally document all relationships between hedging instruments and hedged items, as well as our risk management objective and strategy for undertaking such hedge transactions.

**Item 4. Controls and Procedures**

(a) Under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, we evaluated the effectiveness of our disclosure controls and procedures, as such term is defined under Rule 13a-15(e) promulgated under the Securities Exchange Act of 1934, as amended. Based on this evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective as of the end of the period covered by this quarterly report.

(b) There have been no significant changes in our internal controls or in other factors that could significantly affect internal controls subsequent to the date of the evaluation referenced in paragraph (a) above.

## PART II -- OTHER INFORMATION

**Item 1. Legal Proceedings**

We are involved in various litigation matters in the normal course of business. Except for the lawsuit discussed below and for which a settlement agreement was reached in December 2002, we believe that the ultimate resolution of these matters will not have a material effect on our financial position or results of operations.

On March 28, 2002, Idexx Laboratories, Inc., our principal competitor in the veterinary diagnostic market, filed a complaint in the United States District Court for the District of Maine (Civil Action Docket No. 02-69-P-H) alleging that a canine heartworm test produced for us by a third party, S.A. Scientific, Inc., and sold using the Abaxis brand infringes on U.S. Patents Nos. 4,965,187 and 4,939,096 held by Idexx. On December 6, 2002, the parties entered into a settlement agreement under which, among other terms, we paid Idexx $249,500 in cash damages and we have ceased the selling of the particular canine heartworm antigen test referenced in the complaint. We are exploring whether or not we will introduce another canine heartworm antigen test in the future and there can be no assurance that any party will not claim patent infringement against us or file suit upon other grounds.

**Item 2. Changes in Securities and Use of Proceeds**

None

**Item 3. Defaults Upon Senior Securities**

None

**Item 4. Submission of Matters to a Vote of Security Holders**

None

**Item 5. Other Information**

None

**Item 6. Exhibits And Reports On Form 8-K**

(a) Exhibits included herein

| Exhibit Number | Description |
|---|---|

| | |
|---|---|
| 31.1 | Certification of President and Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. |
| 31.2 | Certification of Chief Financial Officer and Vice President of Finance pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. |
| 32.1 | Certification of President and Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. |
| 32.2 | Certification of Chief Financial Officer and Vice President of Finance pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. |

(b) Reports on Form 8-K

On April 25, 2003, we filed a Current Report on Form 8-K to release our quarterly earnings announcement.

On May 16, 2003, we filed a report on Form 8-K (File No. 000-19720) relating to the approval by our Board of Directors of a Stock Purchase Rights Plan and amendment to our Bylaws regarding the notice periods for stockholder proposals for stockholder meetings. Our Board of Directors declared a dividend distribution of one Preferred Stock Purchase Right (each a "Right" and collectively the "Rights") for each outstanding share of Common Stock, $0.001 par value ("Common Stock"), of the Company.

On August 1, 2003, we filed a Current Report on Form 8-K to release our quarterly earnings announcement.

**SIGNATURES**

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

ABAXIS, INC.
*(Registrant)*

Date: August 13, 2003

BY: /s/ Clinton H. Severson

Clinton H. Severson

President, Chief Executive Officer and Director
(Principal Executive Officer)

Date: August 13, 2003

BY: /s/ Alberto R. Santa Ines

Alberto R. Santa Ines

Chief Financial Officer and Vice President of Finance (Principal Financial and Accounting Officer)

**Exhibit 31.1**

**Sarbanes-Oxley Section 302(a) Certification**

I, Clinton H. Severson, certify that:

1. I have reviewed this quarterly report on Form10-Q of Abaxis, Inc.;

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

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

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

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

b) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

c) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: August 13, 2003

/s/ Clinton H. Severson

Clinton H. Severson
President and Chief Executive Officer

**Exhibit 31.2**

**Sarbanes-Oxley Section 302(a) Certification**

I, Alberto R. Santa Ines, certify that:

1. I have reviewed this quarterly report on Form10-Q of Abaxis, Inc.;

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

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

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

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

b) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

c) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: August 13, 2003

/s/ Alberto R. Santa Ines
Alberto R. Santa Ines
Chief Financial Officer and
Vice President, Finance

**Exhibit 32.1**

**Certification of Chief ExecutiveOfficer**

I, Clinton H. Severson, Chief Executive Officer of Abaxis, Inc. (the "Registrant"), do hereby certify in accordance with 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

(1) the Quarterly Report on Form 10-Q of the Registrant, to which this certification is attached as an exhibit (the "Report"), fully complies with the requirements of section 13(a) of the Securities Exchange Act of 1934 (15 U.S.C. 78m); and

(2) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Registrant.

Dated: August 13, 2003

By: /s/ Clinton H. Severson
Clinton H. Severson
President and
Chief Executive Officer

**Exhibit 32.2**

**Certification of Chief Financial Officer**

I, Alberto R. Santa Ines, Chief Financial Officer of Abaxis, Inc. (the "Registrant"), do hereby certify in accordance with 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

(1) the Quarterly Report on Form 10-Q of the Registrant, to which this certification is attached as an exhibit (the "Report"), fully complies with the requirements of section 13(a) of the Securities Exchange Act of 1934 (15 U.S.C. 78m); and

(2) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Registrant.

Dated: August 13, 2003

By: /s/ Alberto R. Santa Ines
Alberto R. Santa Ines
Vice President, Finance and
Chief Financial Officer