

EDUCATIONAL DEVELOPMENT CORP

Form 10-Q

October 13, 2006

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**SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q**

(Mark One)

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

For the quarterly period ended August 31, 2006

**TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE
ACT OF 1934**

For the transition period from _____ to _____.

Commission file number: 0-4957

EDUCATIONAL DEVELOPMENT CORPORATION

(Exact name of registrant as specified in its charter)

Delaware

(State or other jurisdiction of
incorporation or organization)

73-0750007

(I.R.S. Employer
Identification No.)

10302 East 55th Place, Tulsa Oklahoma 74146-6515

(Address of principal executive offices)

Registrant's telephone number, including area code (918) 622-4522

Indicate by check mark whether the registrant (1) has filed all reports to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

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

Large accelerated filer Accelerated filer Non-accelerated filer

Indicate by check mark whether the Registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act)

Yes No

As of October 10, 2006 there were 3,758,989 shares of Educational Development Corporation Common Stock, \$0.20 par value outstanding.

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	August 31, 2006 (unaudited)	February 28, 2006
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	\$ 268,944	\$ 321,537
Accounts receivable (less allowances for doubtful accounts and returns: 08/31/06 - \$140,848; 2/28/06 - \$185,209)	3,246,915	2,946,462
Inventories Net	11,091,533	12,159,360
Prepaid expenses and other assets	74,711	119,508
Income taxes receivable	253,081	
Deferred income taxes	91,600	141,700
Total current assets	15,026,784	15,688,567
INVENTORIES Net	441,743	379,570
PROPERTY AND EQUIPMENT		
at cost (less accumulated depreciation: 08/31/06 - \$1,976,964 2/28/06 - \$1,904,934)	2,445,145	2,493,929
DEFERRED INCOME TAXES	92,000	81,900
	\$ 18,005,672	\$ 18,643,966
LIABILITIES AND SHAREHOLDERS EQUITY		
CURRENT LIABILITIES:		
Note payable to bank	\$	\$ 676,000
Accounts payable	2,671,879	3,042,937
Accrued salaries and commissions	587,354	566,379
Income taxes		71,749
Dividends payable		750,785
Other current liabilities	281,519	197,486
Total current liabilities	3,540,752	5,305,336
COMMITMENTS		
SHAREHOLDERS EQUITY:		
Common Stock, \$.20 par value (Authorized 8,000,000 shares; Issued 5,776,840 (8/31/06) and 5,771,840 shares (02/28/06); Outstanding	1,155,368	1,154,368

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3,759,239 (8/31/06) and 3,753,923 (2/28/06) shares)

Capital in excess of par value	7,603,328	7,577,495
Retained earnings	16,421,234	15,300,999
	25,179,930	24,032,862
Less treasury shares, at cost	(10,715,010)	(10,694,232)
	14,464,920	13,338,630
	\$ 18,005,672	\$ 18,643,966

See notes to condensed financial statements.

Table of Contents**EDUCATIONAL DEVELOPMENT CORPORATION**
CONDENSED STATEMENTS OF EARNINGS (UNAUDITED)

	Three Months Ended August 31,		Six Months Ended August 31,	
	2006	2005	2006	2005
REVENUES:				
Gross sales	\$ 9,059,937	\$ 9,548,491	\$ 19,803,315	\$ 20,542,895
Less discounts & allowances	(2,971,201)	(3,099,352)	(6,012,786)	(6,210,893)
Transportation revenue	395,634	345,013	800,818	688,829
Net revenues	6,484,370	6,794,152	14,591,347	15,020,831
COST OF SALES	2,516,500	2,739,220	5,395,870	5,743,996
Gross margin	3,967,870	4,054,932	9,195,477	9,276,835
OPERATING EXPENSES:				
Operating & selling	1,639,731	1,507,775	3,481,474	3,185,946
Sales commissions	1,403,759	1,476,698	3,276,919	3,393,832
General & administrative	484,618	411,930	909,639	829,239
Interest	4,919	28,256	7,577	42,948
	3,533,027	3,424,659	7,675,609	7,451,965
OTHER INCOME	266,046	8,174	271,569	16,077
EARNINGS BEFORE INCOME TAXES	700,889	638,447	1,791,437	1,840,947
INCOME TAXES	276,900	243,600	670,800	700,900
NET EARNINGS	\$ 423,989	\$ 394,847	\$ 1,120,637	\$ 1,140,047
BASIC AND DILUTED EARNINGS PER SHARE:				
Basic	\$ 0.11	\$ 0.11	\$ 0.30	\$ 0.30
Diluted	\$ 0.11	\$ 0.10	\$ 0.29	\$ 0.29
WEIGHTED AVERAGE NUMBER OF COMMON AND EQUIVALENT SHARES OUTSTANDING:				
Basic	3,756,042	3,745,057	3,756,251	3,741,595
Diluted	3,869,908	3,905,290	3,878,424	3,903,439

DIVIDENDS DECLARED PER COMMON SHARE	\$	\$	\$	\$	0.15
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See notes to condensed financial statements.

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	Common Stock (par value \$.20 per share)		Capital in Excess of Par Value	Retained Earnings	Treasury Stock		Shareholders Equity
	Number of Shares Issued	Amount			Number of Shares	Amount	
BALANCE, MAR. 1, 2006	5,771,840	\$ 1,154,368	\$ 7,577,495	\$ 15,300,999	2,017,917	\$ (10,694,232)	\$ 13,338,630
Purchases of treasury stock					10,991	(80,744)	(80,744)
Sales of treasury stock			5,196		(11,307)	59,966	65,162
Exercise of options at \$2.50/share	5,000	1,000	11,500				12,500
Tax benefit-stock options			9,137				9,137
Cash dividends net of accrual				(402)			(402)
Net earnings				1,120,637			1,120,637
BALANCE AUGUST 31, 2006	5,776,840	\$ 1,155,368	\$ 7,603,328	\$ 16,421,234	2,017,601	\$ (10,715,010)	\$ 14,464,920

See notes to condensed financial statements.

Table of Contents**EDUCATIONAL DEVELOPMENT CORPORATION**
CONDENSED STATEMENTS OF CASH FLOWS (UNAUDITED)

	Six Months Ended August 31,	
	2006	2005
CASH FLOWS FROM OPERATING ACTIVITIES	\$ 1,391,785	\$ (485,845)
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchases of property and equipment	(23,246)	(106,105)
Net cash used in investing activities	(23,246)	(106,105)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Borrowings under revolving credit agreement	3,278,000	7,932,000
Payments under revolving credit agreement	(3,954,000)	(6,869,000)
Cash received from exercise of stock options	12,500	49,375
Tax benefit of stock options exercised	9,137	12,240
Cash received from sale of treasury stock	65,162	78,263
Cash paid to acquire treasury stock	(80,744)	(77,250)
Dividends paid	(751,187)	(560,719)
Net cash provided by (used in) financing activities	(1,421,132)	564,909
Net Decrease in Cash and Cash Equivalents	(52,593)	(27,041)
Cash and Cash Equivalents, Beginning of Period	321,537	364,024
Cash and Cash Equivalents, End of Period	\$ 268,944	\$ 336,983
Supplemental Disclosure of Cash Flow Information:		
Cash paid for interest	\$ 9,919	\$ 36,688
Cash paid for income taxes	\$ 948,400	\$ 949,200

See notes to condensed financial statements.

Table of Contents**EDUCATIONAL DEVELOPMENT CORPORATION****NOTES TO CONDENSED FINANCIAL STATEMENTS**

Note 1 The information shown with respect to the three months and six months ended August 31, 2006 and 2005, which is unaudited, includes all adjustments which in the opinion of Management are considered to be necessary for a fair presentation of earnings for such periods. The adjustments reflected in the financial statements represent normal recurring adjustments. The results of operations for the three months and six months ended August 31, 2006 and 2005, respectively, are not necessarily indicative of the results to be expected at year end due to seasonality of the product sales.

These financial statements and notes are prepared pursuant to the rules and regulations of the Securities and Exchange Commission for interim reporting and should be read in conjunction with the Financial Statements and accompanying notes contained in the Company's Annual Report to Shareholders for the Fiscal Year ended February 28, 2006.

Note 2 Effective June 30, 2006 the Company signed an Eighth Amendment to the Credit and Security Agreement with Arvest Bank which provided a \$5,000,000 line of credit through June 30, 2007. Interest is payable monthly at the Wall Street Journal prime-floating rate minus 0.75% (7.50% at August 31, 2006) and borrowings are collateralized by substantially all the assets of the Company. At August 31, 2006 the Company had no debt outstanding under this agreement. Available credit under the revolving credit agreement was \$5,000,000 at August 31, 2006. Borrowings outstanding under the agreement ranged from \$0 to \$700,000 during the second quarter ended August 31, 2006.

Note 3 Inventories consist of the following:

	August 31, 2006	February 28, 2006
Current:		
Book inventory	\$ 11,121,993	\$ 12,186,820
Inventory valuation allowance	(30,460)	(27,460)
 Inventories net current	 \$ 11,091,533	 \$ 12,159,360
 Non-current:		
Book inventory	\$ 787,000	\$ 657,000
Inventory valuation allowance	(345,257)	(277,430)
 Inventories non-current	 \$ 441,743	 \$ 379,570

The Company occasionally purchases book inventory in quantities in excess of what will be sold within the normal operating cycle due to minimum order requirements of the Company's primary supplier. These amounts are included in non-current inventory.

Significant portions of inventory purchases by the Company are concentrated with an England based publishing company. Purchases from this England based publishing company were approximately \$2.3 million and \$2.7 million for the three months ended August 31, 2006 and 2005, respectively. Total inventory purchases from all suppliers were approximately \$3.1 million and \$3.1 million for the three months ended August 31, 2006 and 2005, respectively. Purchases from this England based publishing company were approximately \$4.1 million and \$5.7 million for the six months ended August 31, 2006 and 2005, respectively. Total inventory purchases from all suppliers were approximately \$5.1 million and \$6.7 million for the six months ended August 31, 2006 and 2005, respectively.

Note 4 Basic earnings per share (EPS) is computed by dividing net earnings by the weighted average number of common shares outstanding during the period. Diluted EPS is based on the combined weighted average number of common shares outstanding and dilutive potential common shares issuable which include, where appropriate, the

assumed exercise of options. In computing diluted EPS the Company has utilized the treasury stock method.

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The computation of weighted average common and common equivalent shares used in the calculation of basic and diluted earnings per share (EPS) is shown below.

	Three Months Ended August 31,		Six Months Ended August 31,	
	2006	2005	2006	2005
Net Earnings	\$ 423,989	\$ 394,847	\$ 1,120,637	\$ 1,140,047
Basic EPS:				
Weighted Average Shares Outstanding	3,756,042	3,745,057	3,756,251	3,741,595
Basic EPS	\$ 0.11	\$ 0.11	\$ 0.30	\$ 0.30
Diluted EPS:				
Weighted Average Shares Outstanding	3,756,042	3,745,057	3,756,251	3,741,595
Assumed Exercise of Options	113,866	160,233	122,173	161,844
Shares Applicable to Diluted Earnings	3,869,908	3,905,290	3,878,424	3,903,439
Diluted EPS	\$ 0.11	\$ 0.10	\$ 0.29	\$ 0.29

Since March 1, 1998, when the Company began its stock repurchase program, 2,339,427 shares of the Company's common stock at a total cost of \$11,886,681 have been acquired. The Board of Directors has authorized purchasing up to 2,500,000 shares as market conditions warrant.

Note 5 The Company accounts for stock-based compensation whereby share-based payment transactions with employees, such as stock options and restricted stock, are measured at estimated fair value at date of grant and recognized as compensation expense over the vesting period.

In the fourth quarter of fiscal year 2005, the Company early adopted Statement of Financial Accounting Standards No. 123 (revised 2004) Share Based Payment (SFAS No. 123R) which eliminates the alternative of applying the intrinsic value measurement provision of Accounting Principles Board Opinion No. 25 Accounting for Stock Issued to Employees to stock compensation awards and requires that share-based payment transactions with employees, such as stock options and restricted stock, be measured at fair value and recognized as compensation expense over the vesting period. The Company adopted SFAS No. 123R on the modified retrospective application method to all prior years for which SFAS No. 123R was effective. For the Company, this began with its fiscal year ended February 28, 1997.

There were no stock options granted during the quarter ended August 31, 2006.

Note 6 Freight costs and handling costs incurred are included in operating & selling expenses and were \$504,941 and \$512,092 for the three months ended August 31, 2006 and 2005, respectively. Freight costs and handling costs were \$1,063,969 and \$1,045,403 for the six months ended August 31, 2006 and 2005, respectively.

Note 7 The Company has two reportable segments: Publishing and Usborne Books at Home (UBAH). These reportable segments are business units that offer different methods of distribution to different types of customers. They are managed separately based on the fundamental differences in their operations. The Publishing Division markets its products to retail accounts, which include book, school supply, toy and gift stores and museums, through commissioned sales representatives, trade and specialty wholesalers and an internal telesales group. The UBAH Division markets its product line through a network of independent sales consultants through a combination of direct sales, home shows, book fairs and the Internet.

The accounting policies of the segments are the same as those of the Company. The Company evaluates segment performance based on earnings (loss) before income taxes of the segments, which is defined as segment net sales

reduced by direct cost of sales and direct expenses. Corporate expenses, depreciation, interest expense and income taxes are not allocated to the segments, but are listed in the other column. Corporate expenses include the executive department, accounting department, information services department, general office management and building facilities management. The Company's assets and liabilities are not allocated on a segment basis.

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Information by industry segment for the three months and six months ended August 31, 2006 and 2005 is set forth below:

	Publishing	UBAH	Other	Total
Three Months Ended August 31, 2006				
Net revenues from external customers	\$ 2,097,457	\$ 4,386,913	\$	\$ 6,484,370
Earnings before income taxes	\$ 585,378	\$ 879,895	\$ (764,384)	\$ 700,889

Three Months Ended August 31, 2005

Net revenues from external customers	\$ 2,264,964	\$ 4,529,188	\$	\$ 6,794,152
Earnings before income taxes	\$ 707,178	\$ 853,205	\$ (921,936)	\$ 638,447

Six Months Ended August 31, 2006

Net revenues from external customers	\$ 4,168,669	\$ 10,422,678	\$	\$ 14,591,347
Earnings before income taxes	\$ 1,243,800	\$ 2,204,995	\$ (1,657,358)	\$ 1,791,437

Six Months Ended August 31, 2005

Net revenues from external customers	\$ 4,425,072	\$ 10,595,759	\$	\$ 15,020,831
Earnings before income taxes	\$ 1,476,681	\$ 2,196,190	\$ (1,831,924)	\$ 1,840,947

ITEM 2 MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**Factors Affecting Forward Looking Statements**

This Quarterly Report on Form 10-Q, including the documents incorporated herein by reference, contains certain forward looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. These statements are not historical facts but are expectations or projections based on certain assumptions and analyses made by our senior management in light of their experience and perception of historical trends, current conditions, expected future developments and other factors. Actual events and results may be materially different from anticipated results described in such statements.

The Company's ability to achieve such results is subject to certain risks and uncertainties. Such risks and uncertainties include but are not limited to, product prices, continued availability of capital and financing, and other factors affecting the Company's business that may be beyond its control.

The words estimate, project, intend, expect, anticipate, believe and similar expressions are intended to identify forward-looking statements. These forward-looking statements are found at various places throughout this report and the documents incorporated in this report by reference as well as in other written materials, press releases and oral statements issued by us or on our behalf. We caution you not to place undue reliance on these forward-looking statements, which speak only as of the date that they are made. We do not undertake any obligation to publicly release any revisions to these forward-looking statements to reflect events or circumstances after the date of this report.

Overview

The Company operates two separate divisions, Publishing and Usborne Books at Home (UBAH), to sell the Usborne line of children's books. These two divisions each have their own customer base. The Publishing Division markets its products on a wholesale basis to various retail accounts. The UBAH Division markets its products to individual consumers as well as school and public libraries.

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The following table sets forth statement of earnings data as a percentage of net revenues.

	Three Months Ended August		Six Months Ended August	
	31, 2006	2005	31, 2006	2005
Net revenues	100.0%	100.0%	100.0%	100.0%
Cost of sales	38.8%	40.3%	37.0%	38.2%
Gross margin	61.2%	59.7%	63.0%	61.8%
Operating expenses:				
Operating & selling	25.3%	22.2%	23.9%	21.2%
Sales commissions	21.6%	21.7%	22.4%	22.6%
General & administrative	7.5%	6.1%	6.2%	5.5%
Interest	0.1%	0.4%	0.1%	0.3%
Total operating expenses	54.5%	50.4%	52.6%	49.6%
Other income	4.1%	0.1%	1.9%	0.1%
Earnings before income taxes	10.8%	9.4%	12.3%	12.3%
Income taxes	4.3%	3.6%	4.6%	4.7%
Net earnings	6.5%	5.8%	7.7%	7.6%

Operating Results for the Three Months Ended August 31, 2006

The Company had income before income taxes of \$700,889 for the three months ended August 31, 2006 compared with \$638,447 for the three months ended August 31, 2005

Revenues

	Three Months Ended August		\$ Increase/ (decrease)	% Increase/ (decrease)
	31, 2006	2005		
Gross sales	\$ 9,059,937	\$ 9,548,491	\$ (488,554)	(5.1%)
Less discounts & allowances	(2,971,201)	(3,099,352)	128,151	4.1%
Transportation revenue	395,634	345,013	50,621	14.7%
Net revenues	\$ 6,484,370	\$ 6,794,152	\$ (309,782)	(4.6%)

The UBAH Division's gross sales decreased 3.2% or \$155,475 during the three month period ending August 31, 2006 when compared with the same quarterly period a year ago. The Company attributes this decrease primarily to a 9.2% decrease in the number of consultants who made sales during the quarter ended August 31, 2006 when compared with the same period last year. This resulted in a 8.8% decrease in home party sales for the three months ended August 31, 2006 versus August 31, 2005. In addition, for these same two periods, direct sales declined 9.2%, school and library sales declined 36.1%, offset by a 30.3% increase in book fair sales and a 43.9% increase in web sales. The Publishing Division's gross sales decreased 7.2% or \$333,079, during the three month period ending August 31, 2005 when

compared with the same quarterly period a year ago. Sales to the national chains decreased 31% during the 2nd quarter when compared with last year. One of the national chains ran a special promotion in the 2nd quarter last year but did not run a similar one in the 2nd quarter this year, leading to the decline in sales to national chains. Sales to the smaller bookstores were up 5.2% in the second quarter this year.

The UBAH Division's discounts and allowances were \$734,084 and \$702,485 for the three months ended August 31, 2006 and 2005, respectively. The UBAH Division is a multi-level selling organization that markets its products through independent sales representatives (consultants). Sales are made to individual purchasers and school and public libraries. Most sales in the UBAH Division are at retail. As a part of the UBAH Division's marketing programs, discounts between 40% and 50% of retail are offered on selected items at various times throughout the year. The discounts and allowances in the UBAH Division will vary from year to year depending upon the marketing programs in place during any given year. The UBAH Division's discounts and allowances were 15.5% of UBAH's gross sales for the three months ended August 31, 2006 and 14.4% for the three months ended August 31, 2005.

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The Publishing Division's discounts and allowances are a much larger percentage of gross sales than discounts and allowances in the UBAH Division due to the different customer markets that each division targets. The Publishing Division's discounts and allowances were \$2,237,117 and \$2,396,867 for the three months ended August 31, 2006 and 2005, respectively. The Publishing Division sells to retail book chains, regional and local bookstores, toy and gift stores, school supply stores and museums. To be competitive with other wholesale book distributors, the Publishing Division sells at discounts between 48% and 55% of the retail price, based upon the quantity of books ordered and the dollar amount of the order. The Publishing Division's discounts and allowances were 51.8% of Publishing's gross sales for the three months ended August 31, 2006 and 51.5% for the three months ended August 31, 2005.

The increase in transportation revenues for the three months ended August 31, 2006 is the result of the January 2006 increase in the shipping rates charged in the UBAH Division.

Expenses

	Three Months Ended August			%
	31,		\$ Increase/ (decrease)	Increase/ (decrease)
	2006	2005		
Cost of sales	\$ 2,516,500	\$ 2,739,220	\$ (222,720)	(8.1%)
Operating & selling	1,639,731	1,507,775	131,956	8.8%
Sales commissions	1,403,759	1,476,698	(72,939)	(4.9%)
General & administrative	484,618	411,930	72,688	17.6%
Interest	4,919	28,256	(23,337)	(82.6%)
Total	\$ 6,049,527	\$ 6,163,879	\$ (114,352)	(1.9%)

Cost of sales decreased 8.1% or \$222,720 for the three months ended August 31, 2006 when compared with the three months ended August 31, 2005. In comparing the 8.1% decrease in cost of sales with the 5.1% decrease in gross sales, consideration must be given to the mix of products sold. The Company's cost of products it sells from inventory ranges from 25% to 34% of the gross sales price, depending upon the product sold. Cost of sales as a percentage of gross sales was 27.8% for the three months ended August 31, 2006 and for the three months ended August 31, 2005 was 28.7%. Cost of sales is the inventory cost of the product sold, which includes the cost of the product itself and inbound freight charges. Purchasing and receiving costs, inspection costs, warehousing costs, and other costs of our distribution network are included in operating and selling expenses. These costs totaled \$266,068 in the quarter ended August 31, 2006 and \$255,926 in the quarter ended August 31, 2005. Readers are advised to be cautious when comparing our gross margins with the gross margins of other companies, since some companies include the costs of their distribution networks in cost of sales.

In addition to costs associated with our distribution network (noted above), operating and selling costs include expenses of the Publishing Division, the UBAH Division and the order entry and customer service functions. Operating and selling expenses as a percentage of gross sales were 18.1% and 15.8% for the three months ended August 31, 2006 and 2005. Operating and selling expenses increased because of a \$90,000 increase in the estimated costs of travel contests held by the UBAH Division, an increase in promotional costs of \$37,290 in both divisions and an increase in payroll and benefit costs of \$20,260, necessary to keep the Company competitive in the local job market. Freight handling costs decreased \$12,137 due to decreased sales during the period.

Sales commissions in the Publishing Division increased 11.8% to \$30,986 for the three months ended August 31, 2006. Publishing Division sales commissions are paid on net sales and were 1.5% of net sales for the three months ended August 31, 2006 and 1.2% for the three months ended August 31, 2005. Sales commissions in the Publishing Division will fluctuate depending upon the amount of sales made to the Company's house accounts, which are the Publishing Division's largest customers and do not have any commission expense associated with them, and sales made by the Company's outside sales representatives. Sales commissions in the UBAH Division decreased 5.3% to \$1,372,773 for the three months ended August 31, 2006, the direct result of decreased sales in this division. UBAH

Division sales commissions are paid on retail sales and were 38.4% of retail sales for the three months ended August 31, 2006 and 40.3% of retail sales for the three months ended August 31, 2005. The fluctuation in the percentages of commission expense to retail sales is the result of the type of sale. Home shows, book fairs, school and library sales and direct sales have different commissions rates. Also contributing to the fluctuations in the percentages is the payment of overrides and bonuses, both dependent on consultants' monthly sales and downline sales. Other income increased \$257,872 for the quarter ended August 31, 2006. During the 2nd quarter the Company entered into a Plan of Reorganization and Dip Financing Agreement with a company in Chapter 11 bankruptcy as a prelude to acquiring that bankrupt company. The Company was not the successful bidder in an auction held by the U.S. Bankruptcy Court, but the Court awarded the Company a \$250,000 breakup fee. The Company's effective tax rate was 39.5% and 38.2% for the three months ended August 31, 2006 and 2005, respectively. These rates are higher than the federal statutory rate due to state income taxes.

Table of Contents**EDUCATIONAL DEVELOPMENT CORPORATION****Operating Results for the Six Months Ended August 31, 2006**

The Company had income before income taxes of \$1,791,437 for the six months ended August 31, 2006 compared with \$1,840,947 for the three months ended August 31, 2005.

Revenues

	Six Months Ended August 31,		\$ Increase/	%
	2006	2005	(decrease)	Increase/ (decrease)
Gross sales	\$ 19,803,315	\$ 20,542,895	\$ (739,580)	(3.6%)
Less discounts & allowances	(6,012,786)	(6,210,893)	198,107	3.2%
Transportation revenue	800,818	688,829	111,989	16.3%
Net revenues	\$ 14,591,347	\$ 15,020,831	\$ (429,484)	(2.9%)

The UBAH Division's gross sales decreased 2.1% or \$233,705 during the six month period ending August 31, 2006 when compared with the same six month period a year ago. The Company attributes this decrease primarily to a 7.8% decrease in the number of consultants who made sales during the six months ended August 31, 2006 when compared with the same six month period last year. This resulted in an 8.4% decrease in home party sales for the six months ended August 31, 2006 versus August 31, 2005. In addition, in comparing these same two six month periods, direct sales declined 16.8%, school and library sales declined 20.9%, offset by a 8.5% increase in book fair sales and a 44.6% increase in web sales. The Publishing Division's gross sales decreased 5.5% or \$505,875, during the six month period ending August 31, 2006 when compared with the same period a year ago. Sales to the national chains decreased 15% during the six months ended August 31, 2006 when compared with last year. One of the national chains ran a special promotion in the 2nd quarter last year but did not run a similar one in the 2nd quarter this year, leading to the decline in sales to national chains.

The UBAH Division's discounts and allowances were \$1,529,602 and \$1,487,085 for the six months ended August 31, 2006 and 2005, respectively. The UBAH Division is a multi-level selling organization that markets its products through independent sales representatives (consultants). Sales are made to individual purchasers and school and public libraries. Most sales in the UBAH Division are at retail. As a part of the UBAH Division's marketing programs, discounts between 40% and 50% of retail are offered on selected items at various times throughout the year. The discounts and allowances in the UBAH Division will vary from year to year depending upon the marketing programs in place during any given year. The UBAH Division's discounts and allowances were 13.7% of UBAH's gross sales for the six months ended August 31, 2006 and 13.0% for the six months ended August 31, 2005.

The Publishing Division's discounts and allowances are a much larger percentage of gross sales than discounts and allowances in the UBAH Division due to the different customer markets that each division targets. The Publishing Division's discounts and allowances were \$4,483,184 and \$4,723,808 for the six months ended August 31, 2006 and 2005, respectively. The Publishing Division sells to retail book chains, regional and local bookstores, toy and gift stores, school supply stores and museums. To be competitive with other wholesale book distributors, the Publishing Division sells at discounts between 48% and 55% of the retail price, based upon the quantity of books ordered and the dollar amount of the order. The Publishing Division's discounts and allowances were 51.9% of Publishing's gross sales for the six-month period ended August 31, 2006 and 51.7% for the six-month period ended August 31, 2005.

The increase in transportation revenues for the six months ended August 31, 2006 is the result of the January 2006 increase in the shipping rates charged in the UBAH Division.

Table of Contents**EDUCATIONAL DEVELOPMENT CORPORATION****Expenses**

	Six Months Ended August 31,		\$ Increase/ (decrease)	% Increase/ (decrease)
	2006	2005		
Cost of sales	\$ 5,395,870	\$ 5,743,996	\$ (348,126)	(6.1%)
Operating & selling	3,481,474	3,185,946	295,528	9.3%
Sales commissions	3,276,919	3,393,832	(116,913)	(3.4%)
General & administrative	909,639	829,239	80,400	9.7%
Interest	7,577	42,948	(35,371)	(82.4%)
Total	\$ 13,071,479	\$ 13,195,961	\$ (124,482)	(0.1%)

Cost of sales decreased 6.1% or \$348,126 for the six months ended August 31, 2006 when compared with the six months ended August 31, 2005. In comparing the 3.6% decrease in gross sales with the 6.1% decrease in cost of sales, consideration must be given to the mix of products sold. During the six months ended August 31, 2006, sales of consignment titles decreased 43% or \$261,551 over the same period last year. Consignment titles cost the Company 34% of gross sales price. The Company's cost of products it sells from inventory ranges from 25% to 34% of the gross sales price, depending upon the product. Cost of sales as a percentage of gross sales for the six months ended August 31, 2006 was 27.2% and for the six months ended August 31, 2005 was 28.0%. Cost of sales is the inventory cost of the product sold, which includes the cost of the product itself and inbound freight charges. Purchasing and receiving costs, inspection costs, warehousing costs, and other costs of our distribution network are included in operating and selling expenses. These costs totaled \$556,751 in the six months ended August 31, 2006 and \$523,366 in the six months ended August 31, 2005. Readers are advised to be cautious when comparing our gross margins with the gross margins of other companies, since some companies include the costs of their distribution networks in cost of sales.

In addition to costs associated with our distribution network (noted above), operating and selling costs include expenses of the Publishing Division, the UBAH Division and the order entry and customer service functions. Operating and selling expenses as a percentage of gross sales were 17.6% for the six months ended August 31, 2006 and 15.5% for the six months ended August 31, 2005. Operating and selling expenses increased because of an \$123,000 increase in the estimated costs of travel contests held by the UBAH Division, an increase in promotional costs of \$120,894 in both divisions and an increase in payroll and benefit costs of \$38,462, necessary to keep the Company competitive in the local job market.

Sales commissions in the Publishing Division increased 11.5% to \$58,873 for the six months ended August 31, 2006. Publishing Division sales commissions are paid on net sales and were 1.4% of net sales for the six months ended August 31, 2006 and 1.2% for the six months ended August 31, 2005. Sales commissions in the Publishing Division will fluctuate depending upon the amount of sales made to the Company's house accounts, which are the Publishing Division's largest customers and do not have any commission expense associated with them, and sales made by the Company's outside sales representatives. Sales commissions in the UBAH Division decreased 3.7% to \$3,218,046 for the six months ended August 31, 2005, the direct result of decreased sales in this division. UBAH Division sales commissions are paid on retail sales and were 36.1% of retail sales for the six months ended August 31, 2006 and 37.5% of retail sales for the six months ended August 31, 2005. The fluctuation in the percentages of commission expense to retail sales is the result of the type of sale. Home shows, book fairs, school and library sales and direct sales have different commissions rates. Also contributing to the fluctuations in the percentages is the payment of overrides and bonuses, both dependent on consultants' monthly sales and downline sales.

Other income increased \$255,492 for the six months ended August 31, 2006. During the 2nd quarter the Company entered into a Plan of Reorganization and Dip Financing Agreement with a company in Chapter 11 bankruptcy as a prelude to acquiring that bankrupt company. The Company was not the successful bidder in an auction held by the

U.S. Bankruptcy Court, but the Court awarded the Company a \$250,000 breakup fee that is recorded as other income. The Company's effective tax rate was 37.4% for the six months ended August 31, 2006 and 38.1% for the six months ended August 31, 2005, respectively. These rates are higher than the federal statutory rate due to state income taxes.

Liquidity and Capital Resources

The Company's primary uses of cash are for purchases of treasury stock under the stock buyback program and for working capital. The Company utilizes its bank credit facility to meet its short-term cash needs.

Table of Contents**EDUCATIONAL DEVELOPMENT CORPORATION**

The Company's Board of Directors has adopted a stock repurchase plan in which the Company may purchase up to 2,500,000 shares as market conditions warrant. Management believes the stock is undervalued and when stock becomes available at an attractive price, the Company will utilize free cash flow to repurchase shares. Management believes this enhances the value to the remaining stockholders and that these repurchases will have no adverse effect on the Company's short-term and long-term liquidity. The Company has a history of profitability and positive cash flow. The Company can sustain planned growth levels with minimal capital requirements. Consequently, cash generated from operations is used to liquidate any existing debt and then to repurchase shares outstanding or capital distributions through dividends. The Company expects its ongoing cash flow to exceed cash required to operate the business. During the first six months of fiscal year 2007 the Company repurchased 10,991 shares of its common stock under the stock repurchase program at a cost of \$80,744.

The Company's primary source of liquidity is cash generated from operations. During the first six months of fiscal year 2007 the Company experienced a positive cash flow from operating activities of \$1,391,785. Cash flows from operating activities increased due to a decrease in inventory of \$1,005,654 and a decrease in accounts payable and accrued expenses of \$266,050, offset by a net increase in accounts receivable and income taxes receivable of \$553,534. The Company believes that the inventory levels are at an adequate level to meet sales requirements and does not foresee increasing inventory significantly during the balance of fiscal year 2007. The increase in accounts receivable is due primarily to a special sales promotion in the Publishing Division which offered payment terms extended to mid-December. Fluctuations in accounts payable and accrued expenses involve timing of shipments received from the Company's principal supplier and the payments associated with these shipments.

The Company believes that in fiscal year 2007 it will experience a positive cash flow and that this positive cash flow along with the bank credit facility will be adequate to meet its liquidity requirements for the foreseeable future.

Cash used in investing activities was \$23,246. The principal uses of cash in investing activities were \$14,655 in property improvements, \$5,879 warehouse equipment and \$2,712 in computer equipment. The Company estimates that cash used in investing activities for fiscal year 2007 will be less than \$250,000. This would consist of software and hardware enhancements to the Company's existing data processing equipment, property improvements and additional warehouse equipment.

Cash used in financing activities was \$1,421,132, comprised of a net decrease of \$676,000 in borrowings under the bank credit agreement, \$12,500 received from the exercise of stock options, \$9,137 tax benefit of stock options exercised, \$65,162 received from the sale of treasury stock, \$80,744 paid to acquire treasury stock and a \$751,187 cash dividend payment.

As of August 31, 2006 the Company did not have any commitments in excess of one year.

Bank Credit Agreement

Effective June 30, 2006 the Company signed an Eighth Amendment to the Credit and Security Agreement with Arvest Bank which provided a \$5,000,000 line of credit through June 30, 2007. Interest is payable monthly at the Wall Street Journal prime-floating rate minus 0.75% (7.50% at August 31, 2006) and borrowings are collateralized by substantially all the assets of the Company. At August 31, 2006 the Company had no debt outstanding under this agreement. Available credit under the revolving credit agreement was \$5,000,000 at August 31, 2006. Borrowings outstanding under the agreement ranged from \$0 to \$700,000 during the six months ended August 31, 2006.

Critical Accounting Policies

Our discussion and analysis of our financial condition and results of operations are based upon our financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosures of contingent assets and liabilities. On an on-going basis, we evaluate our estimates, including those related to our valuation of inventory, allowance for uncollectible accounts receivable, allowance for sales returns, long-lived assets and deferred income taxes. We base our estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may materially differ

from these estimates under different assumptions or conditions. Historically, however, actual results have not differed materially from those determined using required estimates. The Company's significant accounting policies are described in the notes accompanying the financial statements included in the Company's Annual Report to Shareholders for the Fiscal Year ended February 28, 2006. However, the Company considers the following accounting policies to be more dependent on the use of estimates and assumptions.

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EDUCATIONAL DEVELOPMENT CORPORATION

Revenue Recognition

Sales are recognized and recorded when products are shipped. Products are shipped FOB shipping point. The UBAH Division's sales are paid before the product is shipped. These sales accounted for 71% of net revenues for the six months ended August 31, 2006 and August 31, 2005. The provisions of the SEC Staff Accounting Bulletin No.104,

Revenue Recognition in Financial Statements, have been applied, and as a result, a reserve is provided for estimated future sales returns. The Company's sales return policy allows the customer to return all purchases for an exchange or refund for up to 30 days after the customer receives the item. Estimated allowances for sales returns are recorded as sales are recognized and recorded. Management uses a moving average calculation to estimate the allowance for sales returns. The Company is not responsible for product damaged in transit. Damaged returns are primarily from the retail stores. The damages occur in the stores, not in shipping to the stores. It is industry practice to accept returns from wholesale customers. Transportation revenue, the amount billed to the customer for shipping the product, is recorded when products are shipped. Management has estimated and included a reserve for sales returns of \$70,000 as of August 31, 2006 and \$110,000 as of February 28, 2006.

Allowance for Doubtful Accounts

The Company maintains an allowance for estimated losses resulting from the inability of its customers to make required payments. An estimate of uncollectable amounts is made by management based upon historical bad debts, current customer receivable balances, age of customer receivable balances, the customer's financial condition and current economic trends. If the actual uncollected amounts significantly exceed the estimated allowance, then the Company's operating results would be significantly adversely affected. Management has estimated and included an allowance for doubtful accounts of \$70,848 and \$112,209 as of August 31, 2006 and February 28, 2006, respectively.

Inventory

Management continually estimates and calculates the amount of non-current inventory. Non-current inventory arises due to the Company occasionally purchasing book inventory in quantities in excess of what will be sold within the normal operating cycle due to minimum order requirements of the Company's primary supplier. Non-current inventory was estimated by management using the current year turnover ratio by title. All inventory in excess of 2 1/2 years of anticipated sales was classified as noncurrent inventory. Noncurrent inventory balances, before valuation allowance, were \$787,000 at August 31, 2006 and \$657,000 at February 28, 2006.

Inventories are presented net of a valuation allowance. Management has estimated and included a valuation allowance for both current and noncurrent inventory. This reserve is based on management's identification of slow moving inventory on hand at August 31, 2006 and February 28, 2006. Management has estimated a valuation allowance for both current and noncurrent inventory of \$375,717 and \$304,890 as of August 31, 2006 and February 28, 2006, respectively.

Deferred Tax Assets

The Company does not currently have a valuation allowance recorded against its deferred tax assets. If management determines it is more likely than not that its deferred tax assets would not be realizable in the future, a valuation allowance would be recorded to reduce the deferred tax asset to its net realizable value.

Long-lived Assets

In evaluating the fair value and future benefits of long-lived assets, we perform an analysis of the anticipated undiscounted future net cash flows of the related long-lived assets and reduce their carrying value by the excess, if any, of the result of such calculation. We believe at this time that the long-lived assets' carrying values and useful lives continue to be appropriate.

Stock- Based Compensation

The Company accounts for stock-based compensation whereby share-based payment transactions with employees, such as stock options and restricted stock, are measured at estimated fair value at date of grant and recognized as compensation expense over the vesting period.

Table of Contents**EDUCATIONAL DEVELOPMENT CORPORATION****Item 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

The Company does not have any material market risk.

Item 4 CONTROLS AND PROCEDURES

An evaluation was performed of the effectiveness of the design and operation of the Company's disclosure controls and procedures pursuant to Exchange Act Rule 13a-15(e) and 15d-15(e) as of August 31, 2006. This evaluation was conducted under the supervision and with the participation of the Company's management, including its Chief Executive Officer and its Controller and Corporate Secretary (Principal Financial and Accounting Officer). Based on that evaluation, the Company's Chief Executive Officer and its Controller and Corporate Secretary (Principal Financial and Accounting Officer) concluded that the Company's disclosure controls and procedures were effective to ensure that information required to be disclosed in reports that we file or submit under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported in accordance within the time periods specified in Securities and Exchange Commission rules and forms. It should be noted that the design of any system of controls is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions, regardless of how remote. There have been no changes in the Company's internal control over financial reporting that have materially affected or are reasonably likely to materially affect, its internal control over financial reporting, since the date these controls were evaluated.

PART II OTHER INFORMATION**Item 2 UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS**

The following table sets forth certain information concerning the repurchase of the Company's Common Stock made by the Company during the second quarter ended August 31, 2006.

ISSUER PURCHASES OF EQUITY SECURITIES

Period		(a) Total Number of Shares (or Units Purchased	(b) Average Price Paid per Share (or Unit)	(c) Total Number of Shares (or Units) Purchased as Part of Publicly Announced Plans or Programs (1)	(d) Maximum Number (or Approximate Dollar Value) of Shares (or Units) that May Yet Be Purchased Under the Plans or Programs
June 1, 2006	June 30, 2006	9,672	\$ 7.35	9,672	161,892
July 1, 2006	July 31, 2006	1,319	\$ 7.34	1,319	160,573
August 1, 2006	August 31, 2006				160,573
Total		10,991	\$ 7.35	10,991	

(1) In July 1998, the Board of Directors authorized the

Company to purchase up to 1,000,000 shares of the Company's common stock pursuant to a plan that was announced publicly on October 14, 1998. In May 1999, the Board of Directors authorized the Company to purchase up to an additional 1,000,000 shares of its common stock under this plan, which was announced publicly on May 19, 1999. In April 2004 the Board of Directors authorized the Company to purchase up to an additional 500,000 shares of its common stock under this plan. Pursuant to the plan, the Company may purchase such 2,500,000 shares of the Company's common stock until 2,500,000 shares have been repurchased. There is no expiration date

for the
repurchase plan.

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EDUCATIONAL DEVELOPMENT CORPORATION

Item 6 EXHIBITS

(a) Exhibits

- 10.1 Eighth Amendment dated June 30, 2006 to Restated Loan Agreement between the Company and Arvest Bank, Tulsa, OK

- 31.1 Certification of the Chief Executive Officer of Educational Development Corporation pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 furnished herewith.

- 31.2 Certification of Controller and Corporate Secretary (Principal Financial and Accounting Officer) of Educational Development Corporation pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 furnished herewith.

- 32.1 Certification pursuant to 18 U.S.C Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

SIGNATURES

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

EDUCATIONAL DEVELOPMENT CORPORATION

(Registrant)

Date October 13, 2006

By /s/ Randall W. White

Randall W. White
President

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EDUCATIONAL DEVELOPMENT CORPORATION
EXHIBIT INDEX

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