

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

FORM 10-Q

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

For the quarterly period ended September 30, 1998

OR

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

Commission file number 0-15701

NATURAL ALTERNATIVES INTERNATIONAL, INC.
(Exact name of registrant as specified in its charter)

Delaware
(State of other jurisdiction of incorporation
or organization)

84-1007839
(I.R.S. Employer
Identification No.)

1185 LINDA VISTA DRIVE, SAN MARCOS, CALIFORNIA 92069
(Address of principal executive offices)
(Zip Code)

(760) 744-7340
(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 such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes No

5,887,375

(Number of shares of common stock of the registrant
outstanding as of October 30, 1998)

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NATURAL ALTERNATIVES INTERNATIONAL, INC.
PART I - FINANCIAL INFORMATION

BALANCE SHEETS

ASSETS

	September 30 1998 ----- (unaudited)	June 30 1998 -----
Current Assets:		
Cash and cash equivalents	\$ 5,282,807	\$ 4,714,212
Accounts receivable - less allowance for doubtful		

accounts of \$953,000 at September 30, 1998 and \$1,073,000 at June 30, 1998		
Inventories	7,687,744	12,558,731
Notes receivable - current portion	11,956,080	11,504,936
Prepaid expenses	398,199	399,307
Deferred income taxes	1,035,652	594,054
Deposits	745,000	854,000
Other current assets	571,338	641,573
	567,985	229,308
	-----	-----
Total Current Assets	28,244,805	31,496,121
	-----	-----
Property and equipment, net	11,640,666	10,531,865
	-----	-----
Other Assets:		
Investments	54,224	61,971
Notes receivable, less current portion	177,179	160,273
Other noncurrent assets, net	740,499	737,049
	-----	-----
Total Other Assets	971,902	959,293
	-----	-----
TOTAL ASSETS	\$40,857,373	\$42,987,279
	=====	=====

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NATURAL ALTERNATIVES INTERNATIONAL, INC.
PART I - FINANCIAL INFORMATION

BALANCE SHEETS (continued)

LIABILITIES AND STOCKHOLDERS' EQUITY

	September 30 1998	June 30 1998
	-----	-----
	(unaudited)	
Current Liabilities:		
Accounts payable	\$ 7,508,166	\$ 12,301,859
Current installments of long-term debt	47,465	46,501
Current installments of capital lease obligation	16,650	23,542
Income taxes payable	808,539	378,055
Accrued compensation and employee benefits	312,018	438,242
	-----	-----
Total Current Liabilities	8,692,838	13,188,199
Deferred income taxes	391,000	500,000
Long-term debt, less current installments	965,147	977,375
Long-term pension liability	662,564	662,564
	-----	-----
Total Liabilities	10,711,549	15,328,138
	-----	-----
Stockholders' Equity:		
Preferred stock; \$.01 par value; 500,000 shares authorized; none issued or outstanding	--	--
Common stock; \$.01 par value; 8,000,000 shares authorized; issued and outstanding 5,887,375 at September 30, 1998 and 5,768,209 at June 30, 1998	58,874	57,682
Additional paid-in capital	10,730,289	9,756,822
Retained earnings	19,412,549	17,892,778
Accumulated other comprehensive income	(55,888)	(48,141)
	-----	-----

Total Stockholders' Equity	30,145,824	27,659,141
	-----	-----
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	\$ 40,857,373	\$ 42,987,279
	=====	=====

See accompanying notes to unaudited financial statements.

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NATURAL ALTERNATIVES INTERNATIONAL, INC.
PART I - FINANCIAL INFORMATION

STATEMENTS OF EARNINGS
(Unaudited)

	For the Three Months Ended September 30	
	1998	1997
	-----	-----
Net sales	\$ 16,985,802	\$ 12,032,576
Cost of goods sold	12,331,693	8,871,222
	-----	-----
GROSS PROFIT	4,654,109	3,161,354
Selling, general & administrative expenses	2,173,115	2,206,644
	-----	-----
INCOME FROM OPERATIONS	2,480,994	954,710
	-----	-----
Other income (expense):		
Interest income	59,677	35,800
Interest expense	(21,900)	(30,090)
	-----	-----
	37,777	5,710
	-----	-----
EARNINGS BEFORE INCOME TAXES	2,518,771	960,420
Income taxes	999,000	362,000
	-----	-----
NET EARNINGS	\$ 1,519,771	\$ 598,420
	=====	=====
NET EARNINGS PER COMMON SHARE:		
Basic	\$ 0.26	\$ 0.11
	=====	=====
Diluted	\$ 0.25	\$ 0.11
	=====	=====

See accompanying notes to unaudited financial statements.

NATURAL ALTERNATIVES INTERNATIONAL, INC.
PART I - FINANCIAL INFORMATION

STATEMENT OF STOCKHOLDERS' EQUITY
(Unaudited)

	Common Stock		Additional Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Income	Total
	Shares	Amount				
Balance, June 30, 1998	5,768,209	\$57,682	\$ 9,756,822	\$17,892,778	\$ (48,141)	\$27,659,141
Issuance of common stock upon exercise of employee stock options	119,166	1,192	574,951	--	--	576,143
Income tax benefit from stock options exercised	--	--	398,516	--	--	398,516
Net unrealized loss on investments	--	--	--	--	(7,747)	(7,747)
Net earnings	--	--	--	1,519,771	--	1,519,771
Balance, September 30, 1998	5,887,375	\$58,874	\$10,730,289	\$19,412,549	\$ (55,888)	\$30,145,824

See accompanying notes to unaudited financial statements.

NATURAL ALTERNATIVES INTERNATIONAL, INC.
PART I - FINANCIAL INFORMATION

STATEMENTS OF CASH FLOWS
(Unaudited)

	For the Three Months Ended September 30	
	1998	1997
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net earnings	\$ 1,519,771	\$ 598,420
Adjustments to reconcile net earnings to net cash provided by (used in) operating activities:		
Bad debt provision	65,000	90,000
Tax benefit on option exercise	398,516	--
Depreciation and amortization	475,275	346,234

Other	--	(5,585)
Changes in operating assets and liabilities:		
(Increase) decrease in:		
Accounts receivable	4,805,987	1,237,199
Inventories	(451,144)	(1,380,232)
Prepaid expenses	(441,598)	(293,254)
Deposits	70,235	103,180
Tax refund receivable	--	797,000
Other assets	--	(51,790)
(Decrease) increase in:		
Accounts payable	(4,978,702)	(1,604,113)
Accrued compensation and employee benefits	(126,224)	(66,092)
Income taxes payable	430,824	--
	-----	-----
Net Cash Provided by (Used in) Operating Activities	\$1,767,600	(\$ 229,033)

(continued)

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NATURAL ALTERNATIVES INTERNATIONAL, INC.
PART I - FINANCIAL INFORMATION

STATEMENTS OF CASH FLOWS (continued)
(Unaudited)

	For the Three Months Ended September 30	
	1998	1997
	-----	-----
CASH FLOWS FROM INVESTING ACTIVITIES:		
Capital expenditures	(\$1,397,876)	(\$1,206,991)
Issuance of notes receivable	(22,000)	(4,625)
Repayment of notes receivable	5,031	16,518
Other assets	(342,127)	--
	-----	-----
Net Cash Used in Investing Activities	(1,756,992)	(1,195,098)
	-----	-----
CASH FLOWS FROM FINANCING ACTIVITIES:		
Payments on long-term debt and capital leases	(18,156)	(49,209)
Issuance of common stock	576,143	9,750
	-----	-----
Net Cash Provided by (Used in) Financing Activities	557,987	(39,459)
	-----	-----
Net Increase (Decrease) in Cash and Cash Equivalents	568,595	(1,463,590)
Cash and Cash Equivalents at Beginning of Period	4,714,212	3,469,739
	-----	-----
Cash and Cash Equivalents at End of Period	\$ 5,282,807	\$ 2,006,149
	=====	=====
Supplemental Disclosures of Cash Flow Information:		
Cash paid during the quarter for:		
Interest	21,654	25,302
Income Taxes	493,000	--
Disclosure of non-cash activities:		
Fixed asset purchases in accounts payable	186,180	--

See accompanying notes to unaudited financial statements.

NATURAL ALTERNATIVES INTERNATIONAL, INC.
PART I - FINANCIAL INFORMATION

NOTES TO CONDENSED FINANCIAL STATEMENTS

NOTE 1 - BASIS OF PRESENTATION

The unaudited financial statements have been prepared in accordance with generally accepted accounting principles for interim financial information. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments, consisting of a normal recurring nature considered necessary for a fair presentation, have been included. It is suggested that these financial statements be read in conjunction with the financial statements and notes thereto included in the Company's annual report on Form 10-K for the year ended June 30, 1998. The results of operations for the periods ended September 30, 1998 and 1997 are not necessarily indicative of the operating results for the full year.

Certain amounts in prior period financial statements have been reclassified to conform to the current period financial statements.

NOTE 2 - INVENTORIES

Inventories are comprised of the following:

	September 30 1998 -----	June 30 1998 -----
Raw materials	\$7,189,624	\$7,049,954
Work in progress	4,449,735	3,971,315
Finished goods	316,721 -----	483,667 -----
	\$11,956,080 =====	\$11,504,936 =====

NOTE 3 - COMPREHENSIVE NET INCOME

The Company adopted Statement of Financial Accounting Standards No. 130, "Reporting Comprehensive Income" (SFAS 130) in the first quarter of fiscal year 1999. SFAS 130 establishes new standards for the reporting and presentation of comprehensive income and its components, however it has no impact on the Company's total net income or stockholders' equity. Comprehensive income includes a net unrealized loss of \$7,747 and zero for the quarters ended September 30, 1998 and 1997, respectively, and total comprehensive income was \$1,512,024 and \$598,420 for the quarters ended September 30, 1998 and 1997, respectively.

NATURAL ALTERNATIVES INTERNATIONAL, INC.
PART I - FINANCIAL INFORMATION

NOTES TO CONDENSED FINANCIAL STATEMENTS

NOTE 4 - NET EARNINGS PER SHARE

In 1998, the Company adopted Statement of Financial Accounting Standards No. 128, "Earnings Per Share" ("SFAS 128"). SFAS 128 requires the presentation of basic earnings per share, computed using the weighted average number of shares outstanding during the period, and diluted earnings per share, computed using the additional dilutive effect of all dilutive securities. The dilutive impact of stock options and warrants account for the additional weighted average shares of common stock outstanding for the Company's diluted earnings per share computation. Basic and diluted earnings per share have been calculated as follows:

	For the three months ended September 30	
	1998	1997
NUMERATOR:		
Net earnings - Numerator for basic and diluted earnings per share - income available to common shareholders	\$ 1,519,771	\$ 598,420
DENOMINATOR:		
Denominator for basic earnings per share - weighted average shares	5,831,891	5,430,916
Effect of dilutive securities - employee stock options	347,217	228,292
Denominator for diluted earnings per share - adjusted weighted average shares and assumed conversions	6,179,108	5,659,208
Basic earnings per share	\$ 0.26	\$ 0.11
Diluted earnings per share	\$ 0.25	\$ 0.11

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NATURAL ALTERNATIVES INTERNATIONAL, INC.
PART I - FINANCIAL INFORMATION

NOTES TO CONDENSED FINANCIAL STATEMENTS

NOTE 5 - MAJOR CUSTOMERS

The Company had substantial sales to five separate customers during one or more of the periods shown in the following table. The loss of any of these customers could have an adverse impact on the Company's revenues and earnings in the short-term. Sales by customer, representing 10% or more of the respective period's total sales, are shown below by industry segment.

Industry Segment	Three Months Ended		September 30, 1997	
	Sales by Customer	% (a)	Sales by Customer	% (a)
Multi-level Distribution:				
Customer 1	\$4,966,503	29%	\$4,763,331	40%
Customer 2	3,463,488	20%	2,023,937	17%
Customer 3	(b)		1,370,156	11%
Customer 4	(b)		1,253,346	10%

	-----	-----	-----	-----
Retail Distribution:	8,429,991	49%	9,410,770	78%
Customer 5	2,922,709	17%	(b)	
	-----	-----	-----	-----
	\$11,352,700	67%	\$9,410,770	78%
	=====	=====	=====	=====

(a) Percent of total sales

(b) Sales for the period were less than 10% of total sales.

(c) Total does not foot due to rounding.

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NATURAL ALTERNATIVES INTERNATIONAL, INC.
PART I - FINANCIAL INFORMATION

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION
AND RESULTS OF OPERATIONS

Except for the historical information contained herein, the following discussion contains forward-looking statements that involve risks and uncertainties. The Company's actual results could differ materially from those projected in the forward-looking statements, including trends in financial performance (such as growth in sales and earnings) and financial condition (such as working capital, shareholders' equity, and total assets), the timely development and acceptance of new nutritional supplement formulations, trends in the nutritional and healthcare marketplace, anticipated costs and expenses associated with new facilities and additional equipment, availability of financing on reasonable terms, the maintenance and diversification of relationships with clients, the impact of competitive products and pricing, the impact of government regulations, and other risks including those detailed from time-to-time in the Company's SEC reports, including the report on Form 10-K for the year ended June 30, 1998.

Actual results may differ materially from those projected. These forward-looking statements represent the company's judgment as of the date of this release. The Company disclaims, however, any intent or obligation to update these forward-looking statements.

RESULTS OF OPERATIONS

FIRST QUARTER OF FISCAL 1998 AND 1997

Net sales increased 41.2% or approximately \$5.0 million to approximately \$17.0 million for the quarter ended September 30, 1998, from approximately \$12.0 million for the quarter ended September 30, 1997. The Company added several new customers subsequent to the first quarter of fiscal 1998 and sales to these customers was the primary reason for the increase. In addition, an increase in sales to certain existing customers through their international distribution channels was partially offset by a decrease in sales to other existing customers.

Sales of products into international markets increased 23.9% to approximately \$4.5 million for the quarter ended September 30, 1998, from approximately \$3.6 million for the quarter ended September 30, 1997. The increase is primarily the result of existing customers expanding into Asian and European markets.

Income from operations increased 159.9% to approximately \$2.5 million for the quarter ended September 30, 1998, from approximately \$1.0 million for the quarter ended September 30, 1997. This was primarily due to a \$1.5 million increase in gross profit.

Gross profit margins were 27.4% for the quarter ended September 30, 1998, compared to 26.3% for the quarter ended September 30, 1997. The increase in margins was primarily due to purchasing cost efficiencies and efficiencies

gained through higher production volume.

Selling, general and administrative expenses decreased as a percentage of revenues to 12.8% for the quarter ended September 30, 1998 from 18.3% for the quarter ended September 30, 1997. The decrease is due to the increase in sales noted above while selling, general and administrative expenses remained consistent in absolute dollars at approximately \$2.2 million.

Net earnings increased 154% or \$.9 million to approximately \$1.5 million for the quarter ended September 30, 1998 from approximately \$.6 for the quarter ended September 30, 1997. The increase in net earnings was due primarily to increased sales and improved gross profit margins.

Diluted earnings per share increased 127% for the quarter ended September 30, 1998 to \$.25 from \$.11 for the quarter ended September 30, 1997.

YEAR 2000 ISSUES

Most computer databases, as well as embedded microprocessors in computer systems and industrial equipment, have been programmed to use a two-digit number to represent the year. Computer programs that recognize a date using "00" as the year 1900 rather than the year 2000 could result in errors or system failures. Accordingly, all companies must analyze their systems and make the necessary changes to ensure that automated processes will correctly distinguish between years before and after the year 2000.

NATURAL ALTERNATIVES INTERNATIONAL, INC. PART I - FINANCIAL INFORMATION

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (CONTINUED)

During the quarter ended September 30, 1998, the Company purchased a new financial and manufacturing software system which, in management's judgment, will support the Company's continued growth and expansion. The Company expects to implement its new computer systems by March 31, 1999; the Company has also begun an assessment of the potential for Year 2000 problems with embedded microprocessors in its production equipment. The Company estimates that it will have incurred approximately \$1 million in costs, of which approximately \$100,000 will be charged directly to expense, by the end of its 1999 fiscal year to replace its financial and manufacturing software systems and to remediate or replace embedded microprocessors in its production equipment. This amount will be funded from internally generated cash flows.

The Company has received some preliminary information concerning the Year 2000 readiness of some of its vendors of goods and services. It expects to engage in discussions with its most significant vendors during the balance of 1998 and 1999 in an attempt to determine the extent to which the Company is vulnerable to those vendors' possible failure to become Year 2000 ready. Furthermore, a reasonably likely worse case scenario would be if one or more of the Company's most significant vendors of goods and services, or the suppliers of the Company's necessary energy, telecommunications and transportation needs, experienced a material disruption in business and this caused the Company to experience a material disruption in business. Such a disruption could have a material adverse effect on the results of operations, liquidity and financial condition of the Company. The Company is currently developing contingency plans to address unavoided or unavoidable Year 2000 risks and expects to create such a plan during the balance of 1998 and 1999.

If some or all of the Company's remediated or replaced internal computer systems fail to correctly distinguish between years before and after the year 2000, or if any software applications or embedded microprocessors critical to the Company's operations are overlooked in the assessment or implementation phases, there could be a material adverse effect on the Company's results of operations, liquidity and financial condition of a magnitude which the Company has not yet fully analyzed.

LIQUIDITY AND CAPITAL RESOURCES

At September 30, 1998, the Company had working capital of approximately \$19.7 million and borrowings available under revolving lines of credit of \$3.0 million. As of September 30, 1998, there were no borrowings under these lines.

For the quarter ended September 30, 1998, net cash provided by operating activities was approximately \$1.8 million compared to net cash used in operating activities of approximately \$.2 million for the quarter ended September 30, 1997. This increase of approximately \$2.0 million was due primarily to an increase in net earnings, a decrease in accounts receivable, and an increase in income taxes payable partially offset by decreases in accounts payable and the increase in inventory. Current maturities of long-term debt and capital leases amounted to approximately \$64,000 which the Company expects to pay out of working capital.

The Company has revolving line of credit agreements permitting borrowings up to \$3.0 million, which are secured by the Company's receivables, inventory, equipment, and vehicles and bear interest at the bank's prime rate. The present loan agreement with the bank contains financial covenants concerning limitations on maintenance of debt, certain financial ratio's and other matters, for all of which the Company is in full compliance as of November 13, 1998. The lines of credit expire on January 19, 1999; management expects such lines to be renewed in the normal course of business.

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NATURAL ALTERNATIVES INTERNATIONAL, INC. PART I - FINANCIAL INFORMATION

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (CONTINUED)

Capital expenditures for the quarter ended September 30, 1998 amounted to approximately \$1.6 million primarily in connection with the building improvements in progress at the Company's new headquarters building and the purchases of additional encapsulation and other production equipment to expand the Company's output capacity. The Company anticipates capital expenditures of approximately \$12.0 million during fiscal 1999. These planned expenditures relate primarily to building improvements for the Company's new headquarters building, which is expected to be occupied in early 1999, and a warehouse and blending facility, which was leased in August 1998. These expenditures are expected to be paid from a combination of cash holdings, net cash provided by operating activities in fiscal 1999, borrowings under the Company's lines of credit with its bank, and anticipated long term debt or equity financing. If these financing alternatives become unavailable, the Company may be required to defer or restrict certain commercial activities or delay or eliminate expenditures for certain of its potential products and/or markets.

New Accounting Pronouncements

In February 1998, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards No. 132, "Employers' Disclosures about Pensions and Other Postretirement Benefits." This Statement standardizes the disclosure requirements for pensions and other postretirement benefits, requires additional information on changes in the benefit obligations and fair values of plan assets and eliminates certain disclosures. Restatement of disclosures for earlier periods is required. The Company will adopt this Statement in its financial statements for the year ending June 30, 1999.

In June 1997, the FASB issued Statement of Financial Accounting Standards No. 131, Disclosures about Segments of an Enterprise and Related Information" ("SFAS 131"). SFAS 131 establishes standards for the manner in which public business enterprises report information about operating segments and also establishes standards for related disclosures about products and services, geographic areas, and major customers. These statements are effective for years beginning after December 15, 1997. The Company does not expect that the adoption of SFAS Nos. 131 and 132 will result in disclosures that will be materially different from those previously included in its financial statements.

QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The Company is exposed to risks relating to changes in interest rates and stock market fluctuations.

At September 30, 1998, the Company maintains a portion of its cash and cash equivalents in financial instruments with original maturities of three months or less. These financial instruments, principally comprised of government backed money market funds, are subject to interest rate risk and will decline in value if interest rates increase. The Company also maintains a short-term investment portfolio containing common stocks that are subject to market risk. The Company has not used derivative financial instruments in its investment portfolio.

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NATURAL ALTERNATIVES INTERNATIONAL, INC.
PART II - OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

The Company is involved in various claims and legal actions arising in the ordinary course of business. In the opinion of management, based in part on the advice of counsel, the ultimate disposition of these matters will not have a material adverse impact on the Company's consolidated financial position, operations or cash flows.

ITEM 2. CHANGES IN SECURITIES

During the quarter ending September 30, 1998, 38,390, 61,610, and 19,166 common shares were issued pursuant to employee stock option exercises under the 1992 Incentive Stock Option Plan, the 1992 Nonqualified Stock Option Plan and the 1994 Nonqualified Stock Option Plan, respectively. These shares were issued pursuant to an effective registration statement.

ITEM 3. DEFAULTS BY THE COMPANY ON ITS 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: The following exhibits are filed herewith:

27.0. Financial Data Schedule

27.1 Restated - Financial Data Schedule for the Three Months Ended September 30, 1997.

(b) No reports on Form 8-K were filed during the quarter ended September 30, 1998.

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.

NATURAL ALTERNATIVES INTERNATIONAL, INC.

MARK A. LE DOUX

Date: November 13, 1998

Mark A. Le Doux
Chief Executive Officer
Assistant Treasurer

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