

**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, 2004

OR

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_.

Commission File Number: 0-25238

**NATURAL HEALTH TRENDS CORP.**

Incorporated in Florida

I.R.S. Employer Identification No.  
59-2705336

12901 Hutton Drive  
Dallas, Texas 75234  
(972) 241-4080

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

Indicate by check mark whether the registrant is an accelerated filer (as defined by Rule 12b-2 of the Exchange Act). Yes  No

As of November 1, 2004, the number of shares outstanding of the registrant's class of common stock, par value \$0.001 per share, was 6,819,573.

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**NATURAL HEALTH TRENDS CORP. AND SUBSIDIARIES**  
**Quarterly Report on Form 10-Q**  
**September 30, 2004**

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**PART I. FINANCIAL INFORMATION**

**Item 1. Financial Statements**

**NATURAL HEALTH TRENDS CORP. AND SUBSIDIARIES**

**CONSOLIDATED BALANCE SHEETS**

(In Thousands, Except Share Data)

	September 30, 2004	December 31, 2003
	(Unaudited)	
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$ 5,419	\$ 11,133
Restricted cash	2,321	1,363
Accounts receivable	433	239
Inventories, net	11,793	3,580
Prepaid expenses and other current assets	1,031	1,646
Total current assets	20,997	17,961
Property and equipment, net	658	883
Software, net	5,200	—
Database, net	514	509
Goodwill	13,971	208
Deferred tax asset	1,649	—
Deposits and other assets	801	779
Total assets	\$ 43,790	\$ 20,340
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Current liabilities:		
Accounts payable	\$ 3,869	\$ 3,820
Income taxes payable	2,421	1,443
Accrued distributor commissions	1,669	568
Other accrued expenses	3,310	831
Deferred revenue	6,592	6,634
Deferred tax liability	196	—
Current portion of debt	2,641	314
Other current liabilities	329	513
Total current liabilities	21,027	14,123
Debt	15	31
Total liabilities	21,042	14,154
Commitments and contingencies		
Minority interest	449	711
Mezzanine common stock	960	—
Stockholders' equity:		
Preferred stock, \$1,000 par value; 1,500,000 shares authorized; none issued and outstanding	—	—
Common stock, \$0.001 par value; 500,000,000 shares authorized; 5,449,869 and 4,656,409 shares issued and outstanding at September 30, 2004 and December 31, 2003, respectively	5	4
Additional paid-in capital	48,835	34,007
Accumulated deficit	(26,997)	(28,389)
Accumulated other comprehensive loss	(504)	(147)
Total stockholders' equity	21,339	5,475
Total liabilities and stockholders' equity	\$ 43,790	\$ 20,340

The accompanying notes are an integral part of these unaudited interim consolidated financial statements.

**NATURAL HEALTH TRENDS CORP. AND SUBSIDIARIES**  
**UNAUDITED INTERIM CONSOLIDATED STATEMENTS OF OPERATIONS**  
(In Thousands, Except Per Share Data)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2004	2003 As Restated	2004	2003 As Restated
Net sales	\$40,482	\$ 16,740	\$96,604	\$ 39,964
Cost of sales	8,323	3,671	19,539	7,450
Gross profit	32,159	13,069	77,065	32,514
Operating expenses:				
Distributor commissions	17,421	6,988	50,205	16,498
Selling, general and administrative expenses	8,836	4,133	25,078	10,983
Total operating expenses	26,257	11,121	75,283	27,481
Income from operations	5,902	1,948	1,782	5,033
Other expense:				
Loss on foreign exchange	(6)	(88)	(22)	(99)
Other expense, net	(56)	(27)	(11)	(38)
Interest expense, net	(29)	(35)	(89)	(55)
Total other expense, net	(91)	(150)	(122)	(192)
Income before income taxes and minority interest	5,811	1,798	1,660	4,841
Income tax expense	(857)	(500)	(109)	(1,200)
Minority interest benefit (expense)	74	(22)	(159)	(45)
Net income	5,028	1,276	1,392	3,596
Preferred stock dividends	—	—	—	1
Income available to common stockholders	\$ 5,028	\$ 1,276	\$ 1,392	\$ 3,595
Basic income per common share	\$ 0.92	\$ 0.27	\$ 0.27	\$ 0.78
Diluted income per common share	\$ 0.75	\$ 0.22	\$ 0.22	\$ 0.63
Weighted-average number of shares outstanding:				
Basic	5,450	4,656	5,189	4,626
Diluted	6,692	5,821	6,439	5,663

The accompanying notes are an integral part of these unaudited interim consolidated financial statements.

**NATURAL HEALTH TRENDS CORP. AND SUBSIDIARIES**  
**UNAUDITED INTERIM CONSOLIDATED STATEMENTS OF CASH FLOWS**  
(In Thousands)

	Nine Months Ended September 30,	
	2004	2003 As Restated
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>		
Net income	\$ 1,392	\$ 3,596
Adjustments to reconcile net income to net cash (used in) provided by operating activities:		
Depreciation and amortization	871	467
Stock issued for services	13	50
Minority interest expense	159	45
Imputed compensation	99	—
Deferred income taxes	(1,453)	—
Changes in assets and liabilities, excluding acquisitions:		
Accounts receivable	(194)	(563)
Inventories, net	(8,213)	(949)
Prepaid expenses and other current assets	(656)	849
Deposits and other assets	(47)	(597)
Accounts payable	1,864	(939)
Income taxes payable	1,029	1,200
Accrued distributor commissions	1,101	(523)
Other accrued expenses	2,401	868
Deferred revenue	(42)	(1,450)
Other current liabilities	(184)	(146)
Net cash (used in) provided by operating activities	<u>(1,860)</u>	<u>1,908</u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>		
Business acquired	(1,337)	—
Purchase of minority interest	(142)	—
Database purchase	—	(163)
Purchases of property and equipment	(180)	(449)
Increase in restricted cash	(958)	(852)
Net cash used in investing activities	<u>(2,617)</u>	<u>(1,464)</u>
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>		
Payments on debt	(892)	(279)
Proceeds from issuance of common stock	12	—
Net cash used in financing activities	<u>(880)</u>	<u>(279)</u>
EFFECT OF EXCHANGE RATES ON CASH AND CASH EQUIVALENTS	<u>(357)</u>	<u>57</u>
NET (DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS	<u>(5,714)</u>	<u>222</u>
CASH AND CASH EQUIVALENTS, beginning of period	11,133	3,864
CASH AND CASH EQUIVALENTS, end of period	<u>\$ 5,419</u>	<u>\$ 4,086</u>
<b>SUPPLEMENTAL CASH FLOW INFORMATION:</b>		
Non-cash investing and financing activities:		
Common stock issued for acquisitions	\$15,498	\$ 433
Debt issued for acquisitions	3,203	—

The accompanying notes are an integral part of these unaudited interim consolidated financial statements.

## NATURAL HEALTH TRENDS CORP. AND SUBSIDIARIES

### NOTES TO UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS

#### 1. OVERVIEW AND BASIS OF PRESENTATION

##### *Overview*

Natural Health Trends Corp. (“NHTC” or the “Company”) is a Florida corporation incorporated in 1988. NHTC is an international direct-selling company which operates through subsidiaries that distribute products to promote health, wellness and vitality. Lexxus International, Inc., a wholly-owned subsidiary, and other Lexxus subsidiaries, sell certain cosmetic products as well as “quality of life” products. eKaire.com, Inc., a wholly-owned subsidiary, distributes nutritional supplements aimed at general health and wellness. Other active wholly or majority owned subsidiaries of NHTC and their countries of incorporation include:

- Lexxus International (SW Pacific) Pty. Ltd. (Australia)
- Kaire Nutraceuticals Australia Pty. Ltd. (Australia)
- Lexxus International (NZ) Ltd. (New Zealand)
- Kaire Nutraceuticals New Zealand Ltd. (New Zealand)
- Lexxus International Co., Ltd. (Taiwan)
- MyLexxus Europe AG (Switzerland)
- KGC Networks Pte. Ltd. (Singapore)
- Lexxus International Co., Ltd. (Hong Kong)
- Lexxus International Marketing, Pte. Ltd. (Singapore)
- Lexxus International Network Marketing, Inc. (the Philippines)
- LXX Ltd. (South Korea)
- I Luv My Pet, Inc. (U.S.)
- Marketvision Communications Corp. (Delaware)
- Lexxus Korea, Inc. (Delaware)
- MyLexxus Personal Care International (India) Pvt. Ltd.

NHTC’s common stock, par value, \$0.001 per share, is listed on the NASD OTC Bulletin Board. In March 2003, NHTC effected a 1-for-100 reverse stock split with respect to its outstanding shares of common stock. In addition, the trading symbol for the shares of its common stock changed from “NHTC” to “NHLC”. All share references will give effect to the reverse stock split. On May 27, 2004, the Company filed a listing application with The NASDAQ Stock Market (“NASDAQ”) for quotation of its shares of common stock. No assurance can be given that the Company will be approved by NASDAQ, or if approved, when the Company’s shares will be quoted thereon.

##### *Basis of Presentation*

The unaudited interim consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. As a result, certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States have been condensed or omitted. In the opinion of management, the accompanying unaudited interim consolidated financial statements contain all adjustments, consisting of normal recurring adjustments, considered necessary for a fair statement of the Company’s financial information as of September 30, 2004, and for the nine months and

three months ended September 30, 2004 and 2003. The results of operations of any interim period are not necessarily indicative of the results of operations to be expected for the fiscal year. These consolidated financial statements should be read in conjunction with the consolidated financial statements and related notes included in our 2003 Annual Report on Form 10-KSB.

Certain prior period amounts have been reclassified to conform to the current period presentation. These reclassifications had no effect on previously reported net income or stockholders' equity.

## **2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

### *Principles of Consolidation*

The accompanying interim consolidated financial statements include the accounts of NHTC and all of its wholly and majority-owned subsidiaries. All intercompany accounts and transactions have been eliminated in consolidation.

### *Use of Estimates*

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities, and the reported amounts of revenues and expenses, including the recoverability of inventory. The Company's estimates and assumptions are continually evaluated based on available information and experience. Because the use of estimates is inherent in the financial reporting process, actual results could differ from estimates. If there is a significant unfavorable change to current conditions, it would likely result in a material adverse impact to the Company's business, operating results and financial condition.

### *Revenue Recognition*

The Company's revenues are primarily derived from sales of products, sales of starter and renewal administrative enrollment packs and shipping fees. Product sales and direct expenses are recognized when the products are shipped. The Company defers revenue from the sale of its starter and renewal administrative enrollment packs and recognizes the revenue and its associated direct costs over the term of the membership, generally twelve months. As of September 30, 2004, the Company had deferred revenue of approximately \$6,592,000, of which approximately \$2,441,000 pertained to goods ordered that will be shipped in the fourth quarter of 2004 and approximately \$4,151,000 pertained to unamortized administrative enrollment packs.

The Company also estimates and records a sale return allowance for possible sales refunds based on its historical experience on a country-by-country basis.

### *Shipping and Handling Cost*

The Company records freight and shipping revenue collected from distributors as revenue. The Company records shipping and handling costs associated with customer shipments as cost of sales.

### *Distributor Commissions*

Distributors are paid commissions based on their direct and indirect commissionable net sales and downline growth. Commissions are earned over 52 business periods and are paid three weeks in arrears. Commissions are accrued when earned.

### Accounting for Stock-Based Compensation

Currently, NHTC follows Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees" ("APB 25") and its related interpretations for stock options granted to employees and members of its board of directors. Under the recognition and measurement principles of APB 25, NHTC is not required to recognize any compensation expense unless the market price of the stock exceeds the exercise price on the date of grant, the terms of the grant are subsequently modified or in the case of variable options. The Financial Accounting Standards Board ("FASB") has recently issued a proposal to change the recognition and measurement principles for equity-based compensation granted to employees and board members. Under the proposed rules, NHTC would be required to recognize compensation expense related to stock options granted to employees and board members effective for periods beginning after June 15, 2005. The compensation expense would be calculated based on the expected number of options expected to vest and would be recognized over the stock options' vesting period. If this proposal is passed, NHTC would be required to recognize compensation expense related to stock options granted to its employees or board members, which could have a material effect on its consolidated financial condition and results of operations.

For disclosure purposes in accordance with Statement of Financial Accounting Standards 123 ("SFAS 123"), the fair value of options is estimated on the date of grant using the Black-Scholes option pricing model. If NHTC had recognized compensation cost in accordance with SFAS 123, NHTC's income available to common stockholders and income per common share would have been as follows (in thousands, except per share data):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2004	2003 As Restated	2004	2003 As Restated
Income available to common stockholders	\$5,028	\$ 1,276	\$ 1,392	\$ 3,595
Add: Stock-based employee compensation expense included in reported net income, net of tax effect	—	—	—	—
Deduct: Stock-based employee compensation expense determined under fair value based method, net of tax effect	(19)	(10)	(3,848)	(29)
Pro forma income available to common stockholders	\$5,009	\$ 1,266	\$(2,456)	\$ 3,566
Basic income per common share:				
As reported	\$ 0.92	\$ 0.27	\$ 0.27	\$ 0.78
Pro forma	\$ 0.92	\$ 0.27	\$ (0.47)	\$ 0.77
Diluted income per common share:				
As reported	\$ 0.75	\$ 0.22	\$ 0.22	\$ 0.63
Pro forma	\$ 0.75	\$ 0.22	\$ (0.47)	\$ 0.63

### Earnings Per Share

Basic income per common share is computed based on the weighted-average number of common shares outstanding during the periods presented. Diluted income per common share data gives effect to all potentially dilutive common shares that were outstanding during the periods presented. Income per



common share for the three and nine months ended September 30, 2004 and 2003 are as follows (in thousands, except per share data):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2004	2003 As Restated	2004	2003 As Restated
<b>Basic Calculation:</b>				
Income available to common stockholders	\$5,028	\$ 1,276	\$1,392	\$ 3,595
Weighted-average number of shares outstanding	5,450	4,656	5,189	4,626
Basic income per common share	\$ 0.92	\$ 0.27	\$ 0.27	\$ 0.78
<b>Diluted Calculation:</b>				
Income available to common stockholders	\$5,028	\$ 1,276	\$1,392	\$ 3,595
Weighted-average number of shares outstanding	5,450	4,656	5,189	4,626
Net effect of dilutive stock options and warrants based upon treasury stock method	1,242	1,165	1,250	1,037
Weighted-average number of shares outstanding assuming full conversion of all potentially dilutive securities	6,692	5,821	6,439	5,663
Diluted income per common share	\$ 0.75	\$ 0.22	\$ 0.22	\$ 0.63

#### *Accounting for Software*

As part of the Marketvision Communications Corp. acquisition (see Note 4), the Company acquired approximately \$5,600,000 of computer software and programs. The valuation of the software was determined by a third party appraisal firm. The software is classified as a non-current asset in the balance sheet and is being amortized over a seven-year period beginning April 1, 2004.

#### *Recently Issued Accounting Standards*

During the first quarter of 2004, the Company adopted FASB Interpretation No. 46R, "Consolidation of Variable Interest Entities — An Interpretation of ARB No. 51." The adoption of this accounting standard did not have a material effect on the Company'.

### **3. COMPREHENSIVE INCOME (In Thousands)**

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2004	2003 As Restated	2004	2003 As Restated
Net income	\$5,028	\$ 1,276	\$1,392	\$ 3,596
Other comprehensive income (loss), net of tax:				
Foreign currency translation adjustment	51	42	(357)	57
Comprehensive income	\$5,079	\$ 1,318	\$1,035	\$ 3,653

#### 4. BUSINESS COMBINATIONS

The Company entered into the following business combinations during the nine months ended September 30, 2004:

*Purchase of the Minority Interest of Lexus International, Inc.*

On March 29, 2004, the Company purchased 4,900 shares of common stock owned by the minority stockholders of Lexus International, Inc., a Delaware corporation ("Lexus"), (representing the 49% interest in Lexus not owned by the Company) in exchange for 100,000 shares of restricted NHTC common stock. The total purchase price, including acquisition related costs of approximately \$7,000, was approximately \$1,969,000 based upon the average closing price of NHTC common stock of \$23.08 discounted by 15% due to the restrictions contained in the purchase agreement. The average closing price of \$23.08 was calculated based on the closing price of NHTC common stock a few days before and after the acquisition was announced. The purchase price was allocated between the additional net assets acquired of approximately \$164,000 and goodwill.

*Purchase of Marketvision Communications Corp.*

On March 31, 2004, the Company entered into a merger agreement with Marketvision Communications Corp. ("Marketvision"), pursuant to which the Company acquired all of the outstanding capital stock of Marketvision in exchange for the issuance of 690,000 shares of NHTC restricted common stock (the "Issued Shares"), promissory notes in the aggregate principle amount of approximately \$3,203,000, a cash payment of approximately \$1,337,000 in April 2004, less pre-acquisition net payables due to Marketvision of approximately \$646,000, for a total purchase price of approximately \$17,583,000, including acquisition costs of approximately \$153,000. The Issued Shares were valued at the average closing price of NHTC common stock of \$23.08 discounted by 15% due to certain restrictions contained in the purchase agreement. The average closing price of \$23.08 was calculated based on the closing price of NHTC common stock a few days before and after the acquisition was announced. Marketvision is the exclusive developer and service provider of direct selling internet technology used by the Company since 2001. Marketvision hosts and maintains the internet technology for the Company and charges an annual fee for this service based upon the number of enrolled distributors of the Company's products. Marketvision earned revenues for this service of approximately \$1,839,000 and \$579,000 for the year ended December 31, 2003 and three months ended March 31, 2004, respectively.

Management believes that this transaction was in the best interests of the Company because (i) the success of the Company's business is dependent upon Marketvision's direct selling software and (ii) the Company projects enrolling a significant number of new distributors in the future, which would be very expensive under the former compensation agreement between the Company and Marketvision. Since the former owners of Marketvision include Terry LaCore, a member of the Company's Board of Directors and the Chief Executive Officer of Lexus International, Inc., a wholly owned subsidiary of NHTC, the Board of Directors hired the independent appraisal firm of Bernstein, Conklin & Balcombe to assess the fairness of the transaction with Marketvision from a financial point of view. In March 2004, Bernstein, Conklin & Balcombe delivered its opinion to the Company's Board of Directors that the Marketvision transaction is fair to the Company from a financial point of view.

In addition, the Company entered into a Shareholder's Agreement with the former stockholders of Marketvision. Such agreement contained customary terms and conditions, including restrictions on transfers of the Issued Shares, rights of first refusal and indemnification. Further, the Shareholder's Agreement contains a one time put right related to 240,000 Issued Shares for the benefit of the former stockholders of Marketvision (other than Mr. LaCore) that requires NHTC, during the six month period commencing eighteen months following the earlier of (i) the first anniversary of the closing date, or (ii)

the date on which the Issued Shares are registered with the Securities and Exchange Commission (the “SEC”) for resale to the public, to repurchase all or part of such shares still owned by the such stockholders for \$4.00 per share less any amount previously received by such stockholders from the sale of their shares of the Issued Shares. The Company has recorded this obligation of \$960,000 as mezzanine common stock in the consolidated balance sheet. The agreement also provided the former stockholders of Marketvision with piggyback registration rights in the event NHTC files a registration statement with the SEC, other than on Forms S-4 or S-8, stock option grants for the former stockholders (other than Mr. LaCore) as well as three-year employment agreements for the former stockholders, other than Mr. LaCore. In the event that the Company defaults on its payment obligations under the notes or the employment agreements, an entity owned by the former stockholders of Marketvision (other than Mr. LaCore) has certain rights to use, develop, modify, market, distribute and sublicense the Marketvision software to third parties.

Operations of Marketvision subsequent to March 31, 2004 have been included in the Company’s consolidated financial statements. The transaction was accounted for using the purchase method of accounting and the purchase price was allocated among the assets acquired based on their estimated fair market values. The assets of Marketvision included certain computer equipment and developed software.

The purchase price was calculated as follows (in thousands):

690,000 shares of NHTC Common Stock valued at \$23.08 per share less 15% discount for restrictions associated with the stock issued	\$13,536
Cash paid in April 2004	1,337
Promissory notes issued at closing	3,203
Preacquisition net payables due to Marketvision	(646)
Acquisition costs	153
Total purchase price	<u>\$17,583</u>

The purchase price was allocated among assets acquired based on their estimated fair market values as follows (in thousands):

Property and equipment	\$ 25
Amortizable intangible assets	5,600
Goodwill	11,958
Deferred taxes	(1,904)
Deferred tax asset recognized for the Company’s loss carry forward based upon offset against Marketvision’s deferred tax liabilities	<u>1,904</u>
Total purchase price allocation	<u>\$17,583</u>

Amortizable intangibles acquired will be amortized over their estimated life of seven years. The purchase price allocation is based on preliminary estimates, including estimates of federal tax contingencies, which are subject to change once additional information becomes available. Changes to these estimates could result in changes to the purchase price allocation.

*Purchase of the Minority Interest of Lexxus International Co., Ltd. (Taiwan)*

On April 19, 2004, the Company purchased 510,000 shares of common stock owned by the minority stockholders of Lexxus International Co., Ltd. (Taiwan), a Taiwan limited liability corporation (“Lexxus Taiwan”), (representing the 30% interest in Lexxus Taiwan not owned by the Company or Lexxus) in exchange for approximately \$136,000 in cash. The cash consideration given approximated the

book value of the shares acquired and no goodwill resulted from the transaction. All Lexxus Taiwan minority shareholders were unrelated to the Company.

## **5. CONTINGENCIES**

During the fall of 2003, the customs agency of the government of South Korea brought a charge against LXX, Ltd., the Company's wholly owned subsidiary operating in South Korea ("LXX"), with respect to the importation of the Company's Alura product. The customs agency alleges that Alura is not a cosmetic product, but rather should be categorized and imported as a pharmaceutical product. The matter is currently being considered in the courts. During the ongoing hearings, LXX intends to present expert testimony that Alura is not a pharmaceutical product, and therefore, LXX should be permitted to sell and distribute Alura in South Korea. The failure to sell Alura in South Korea is not anticipated to have a material adverse effect on the financial condition, results of operations, cash flow or business prospects of LXX.

On or around March 31, 2004, Lexxus International, Inc. ("Lexxus") received a letter from John Loghry, a former Lexxus distributor, alleging that Lexxus had wrongfully terminated an alleged oral distributorship agreement with Mr. Loghry and that the Company had breached an alleged oral agreement to issue shares of the Company's common stock to Mr. Loghry. The letter demanded a settlement payment of \$35 million without any explanation as to the amount of the claim. After Mr. Loghry threatened to commence suit against Lexxus and the Company in Nebraska, on May 13, 2004, Lexxus and the Company filed an action for declaratory relief against Mr. Loghry in the United States District Court for the Northern District of Texas seeking, inter alia, a declaration that Mr. Loghry was not wrongfully terminated and is not entitled to recover anything from Lexxus or the Company. Mr. Loghry has filed counterclaims against the Company and Lexxus asserting his previously articulated claims. Discovery has commenced and the Company intends to vigorously defend itself in this case.

In September 2004, Mr. Loghry filed third party claims against certain officers of the Company and Lexxus, including against Terry LaCore and Mark Woodburn for fraud, LaCore, Woodburn, and Lisa Grossman for conspiracy to commit the same, and Grossman for tortious interference. A motion to dismiss this action has been filed.

On November 1, 2004, Toyota Jidosha Kabushiki Kaisha (d/b/a Toyota Motor Corporation) and Toyota Motor Sales, U.S.A. (collectively, "Toyota") filed a complaint against the Company and Lexxus International, Inc. ("Lexxus") in United States District Court for the Central District of California (CV04-9028). The complaint alleges trademark and service mark dilution, unfair competition, trademark and service mark infringement, and trade name infringement, each with respect to Toyota's Lexus trademark. Toyota seeks to enjoin the Company and Lexxus from using the Lexxus mark and otherwise competing unfairly with Toyota, to transfer the ownership of the mylexxus.com and lexxusinternational.com Internet sites to Toyota, and reimbursement of costs and reasonable attorney fees incurred by Toyota in connection with this matter. The Company denies the allegations contained in the complaint and intends to vigorously defend this action. In the event that the Company is unsuccessful in defending this action, the Company may be required to change the name of some or all of its Lexxus subsidiaries and domain names which could have a material adverse effect on the financial condition, results of operations, cash flow or business prospects of the Company.

From time to time, the Company is involved in legal proceedings incidental to the course of its business. The Company believes that all pending actions, individually and in the aggregate, will not have a material adverse effect on the financial condition, results of operations, cash flows or business prospects.

## **6. RELATED PARTY TRANSACTIONS**

In August 2001, the Company entered into an agreement with S&B Partnership, an affiliate of Brad LaCore, the brother of Terry LaCore. Under the terms of the agreement, S&B Partnership provides warehouse facilities, manages and ships inventory, and disburses payments to independent distributors. The Company paid approximately \$116,500 and \$112,300 for such services during the nine months ended September 30, 2004 and 2003, respectively.

In September 2001, the Company entered into an oral consulting agreement with William Woodburn, the father of Mark Woodburn, the Company's president, pursuant to which William Woodburn provided the Company with management advice and other advisory assistance. The Company paid \$118,750 and \$125,000 for such services during the nine months ended September 30, 2004 and 2003, respectively. The consulting agreement between the Company and Mr. Woodburn was terminated as of September 30, 2004.

The Company's former controller is married to Mark Woodburn. Her employment ended in August 2004. The Company paid her approximately \$75,000 for the nine month periods ended September 30, 2004 and 2003.

## **7. SUBSEQUENT EVENTS**

On October 6, 2004, the Company entered into a securities purchase agreement with certain institutional and accredited investors as well as certain officers and directors of the Company. Pursuant to the agreement, the Company agreed to sell 1,369,704 units at a price of \$12.595 per unit. Each unit consist of one share of the Company's common stock and one stock purchase warrant exercisable for one share of the Company's common stock at any time through October 6, 2009 at an exercise price of \$12.47 per share. Proceeds are approximately \$15.9 million, net of transaction fees.

In connection with the Marketvision acquisition, the Company issued three different promissory notes in the aggregate principal amount of approximately \$3,203,000 (see Note 4). As of September 30, 2004, two of these promissory notes in the aggregate amount of \$1.5 million became due and payable. On October 12, 2004, the Company repaid approximately \$1.6 million and the notes due on September 30, 2004 have been paid in full.

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

The following Management's Discussion and Analysis should be read in conjunction with Management's Discussion and Analysis included in our Annual Report on Form 10-KSB for the year ended December 31, 2003, filed with the Securities and Exchange Commission ("SEC"), and our other filings, including Current Reports on Form 8-K, filed with the SEC through the date of this Report.

### Company Overview

NHTC is an international direct-selling organization. NHTC controls subsidiaries that distribute products through three separate direct selling networks that promote health, wellness and vitality. Lexxus International, Inc. and other Lexxus subsidiaries (collectively, "Lexxus") sell certain cosmetic products as well as "quality of life" products. eKaire.com, Inc., ("eKaire"), a wholly-owned subsidiary, distributes nutritional supplements aimed at general health and wellness. I Luv My Pet, Inc., ("ILMP"), a wholly-owned subsidiary, distributes nutritional supplements for dogs and cats. NHTC operates its Lexxus, eKaire and ILMP direct selling operations as a single segment and primarily sells its products through a network of commissioned distributors. NHTC aggregates the Lexxus and eKaire operating segments because it believes it operates as a single reportable segment selling its products in similar distribution channels in each of its operations. Operations of ILMP are not material for the nine months ended September 30, 2004 and are under evaluation for potential change in strategies.

*Net Sales.* NHTC derives its revenue from sales of its products, sales of its starter and renewal administrative enrollment packs, and from shipping fees. Substantially all of its product sales are to independent distributors at published wholesale prices. NHTC believes the vast majority of its product sales are for personal consumption; however, NHTC cannot distinguish its personal consumption sales from its other sales because it has no involvement in its products after delivery other than usual and customary product returns.

*Cost of sales.* Cost of sales of products purchased from third-party manufacturers, costs of promotional materials sold to NHTC's distributors, freight, provisions for slow moving or obsolete inventories and, prior to the closing of the merger with Marketvision as of March 31, 2004, the cost of NHTC's third party software service provider.

*Distributor commissions.* Distributor commissions are dependent on the sales mix and, for 2004, typically range between 42% and 55% of net sales. Commissions are paid to NHTC's independent distributors in accordance with its global compensation plan based on commissionable net sales, which consist of finished products.

*Foreign exchange.* NHTC is exposed to certain market risks, including changes in currency exchange rates as measured against the United States dollar. The value of the United States dollar may affect NHTC's financial results. Changes in exchange rates could positively or negatively affect its financial results, as expressed in United States dollars. The effect of the translation of the Company's foreign operations are included in accumulated other comprehensive income within stockholders' equity and such do not impact the statement of operations.

*Effect of inflation.* NHTC believes inflation has not had a material impact on its operations or profitability.

## **Critical Accounting Policies and Estimates**

For a complete review of NHTC's critical accounting policies and new accounting pronouncements that may impact NHTC's operations, refer to the Annual Report on Form 10-KSB for the year ended December 31, 2003. In response to SEC Release No. 33-8040, "Cautionary Advice Regarding Disclosure About Critical Accounting Policies" and SEC Release Number 33-8056, "Commission Statement about Management's Discussion and Analysis of Financial Condition and Results of Operations," NHTC has identified certain policies that are important to the portrayal of its consolidated financial condition and consolidated results of operations. These policies require the application of significant judgment by NHTC's management. NHTC periodically analyzes the need for certain estimates, including the need for such items as reserves for inventory valuation, impairment of long-lived assets, revenue recognition, sales returns, and contingencies. NHTC bases any estimates needed on its historical experience, industry standards, and various other assumptions that may be reasonable under the circumstances. NHTC cautions its readers that actual results could differ from its estimates under different assumptions or conditions. If circumstances change relating to the various assumptions or conditions used in such estimates NHTC could experience an adverse effect on its consolidated financial condition, changes in financial condition, and results of operations. NHTC's critical accounting policies at September 30, 2004 include the following:

### *Inventory Valuation*

NHTC's inventory carrying value is reviewed and compared to the net realizable value of its inventory and any inventory value in excess of net realizable value is written down. In addition, NHTC reviews its inventory for obsolescence and any inventory identified as obsolete is reserved or written off. NHTC's determination of obsolescence is based on assumptions about the demand for its products, product expiration dates, estimated future sales, and management's future plans.

### *Asset Impairment*

NHTC reviews the book value of its property and equipment and other long-term assets whenever an event or change in circumstances indicates that the net book value of an asset or group of assets may be unrecoverable. NHTC's impairment review includes a comparison of future projected cash flows (undiscounted and without interest charges) generated by the asset or group of assets with its associated carrying value. NHTC believes its expected future cash flows approximate or exceed its net book value. However, if circumstances change and the net book value of the asset or group of assets exceeds expected cash flows, NHTC would have to recognize an impairment loss to the extent the net book value of an asset exceeds its fair value.

### *Allowance for Sales Returns*

The Company maintains an allowance for sales returns and refunds based on the return practices and policies by country and our historical experience. The allowance for sales returns may need to be adjusted if actual sales returns differ from estimates.

### *Revenue Recognition*

Product sales are recognized when shipped. NHTC defers revenue received from the sale of its starter and renewal administrative packs due to the term of the membership, generally twelve months. Such fees are recognized as revenue on a straight-line basis over the term of the membership. Although NHTC has no immediate plans to significantly change the terms or conditions of the starter or renewal

memberships, any changes in the future could result in additional revenue deferrals or could cause NHTC to recognize its deferred revenue over a longer period of time.

#### *Tax Valuation Allowances*

The Company evaluates the probability of realizing the future benefits of any of its deferred tax assets and records a valuation allowance when it believes a portion or all of its deferred tax assets may not be realized. If the Company is unable to realize the expected future benefits of its deferred tax assets, it would be required to provide an additional valuation allowance.

#### **Results of Operations**

##### *Three Months Ended September 30, 2004 Compared to the Three Months Ended September 30, 2003*

The following table summarizes NHTC's consolidated operating results as a percentage of net sales for each of the years indicated:

	<b>Three Months Ended September 30,</b>	
	<b>2004</b>	<b>2003</b>
Net sales	100.0%	100.0%
Cost of sales	20.6%	21.9%
Gross profit	79.4%	78.1%
Operating expenses:		
Distributor commissions	43.0%	41.8%
Selling, general and administrative expenses	21.8%	24.7%
Total operating expenses	64.8%	66.5%
Income from operations	14.6%	11.6%
Other expense, net	(0.2%)	(0.9%)
Income before income taxes and minority interest	14.4%	10.7%
Income taxes and minority interest	(2.0%)	(3.1%)
Net income	12.4%	7.6%

##### **Overview of the Results of Operations for the Three Months ended September 30, 2004**

On April 12, 2004, an investigative television program was aired nationwide in the People's Republic of China with respect to the operations of the Company's Lexus Hong Kong subsidiary and the Lexus representative office located in Beijing. The television program alleged that the Company engaged in a pyramid scheme and sold products without proper permits.

After a thorough internal investigation of the issues raised in the television program, the Company concluded that additional training and development of certain Lexus independent distributors located in Hong Kong was warranted. Accordingly, the Company began intensive training of its independent distributors with respect to (i) applicable Chinese legal requirements, and (ii) the need for distributors to accurately and fairly describe business opportunities available to potential distributors. In May 2004, the Company elected to suspend shipment of product to certain Hong Kong distributors until

they had completed the required training. This resulted in an unshipped sales backlog of orders to be shipped of approximately \$6,598,000 as of June 30, 2004. As of September 30, 2004, training of the distributors has been substantially completed.

Furthermore, in order to accommodate the concerns of many independent distributors, Lexxus extended its existing 14-day return policy in Hong Kong to 180 days to allow distributors and customers who purchased products during the two-week period prior to, and the two-week period after, the airing of the television program to return purchased merchandise for a full refund. In accordance with Statement of Financial Accounting Standards No. 48 "Revenue Recognition when Right of Return Exists", the Company was unable to estimate the sales returns that would result from this change in policy and accordingly deferred revenue recognition on sales orders of approximately \$5,404,000 as of June 30, 2004 until the 180-day return period has expired. During the third quarter, the Company reversed the entire deferral and recognized approximately \$5,284,000 in revenue, net of approximately \$120,000 in sales returns.

Further, the Company decided not to seek recovery for any commissions already paid to its distributors related to product sales recorded during this period that were subsequently returned. In addition, the Company incurred approximately \$1,030,000 additional costs during the second quarter to conduct the training efforts and to further remediate the adverse publicity in the Hong Kong region.

Due to the adverse publicity caused by the airing of the television program, gross sales (before returns and refunds) for the Lexxus Hong Kong operations declined from an average of approximately \$285,000 per day during the quarter ended March 31, 2004 to an average of approximately \$170,000 and \$155,000 per day during the quarters ended June 30, 2004 and September 30, 2004, respectively. The Company cannot predict when, if ever, sales from the Lexxus Hong Kong operations will increase to levels comparable to that of the first quarter.

A summary of the net impact to the Company's results of operations for the three months ended September 30, 2004 due to the deferred revenue is as follows (in thousands):

Item	Amount (Unaudited)
Hong Kong Deferred Revenue:	
Orders entered in Q2 but shipped in Q3	\$ 6,598
Less: estimated cost of sales	(1,188)
Less: estimated distributor commissions	(3,299)
	<u>2,111</u>
Revenue deferred to Q3 under SFAS No. 48	5,404
Less: estimated cost of sales	(973)
	<u>4,431</u>
Hong Kong Training and Remediation Costs:	
Incremental sales returns under the special extended return privilege	(120)
Estimated cost of sale on sales returns	22
	<u>(98)</u>
<b>Total</b>	<b>\$ <u>6,444</u></b>



A summary of the net impact to the Company's results of operations for the nine months ended September 30, 2004 is as follows (in thousands):

Item	Amount
	<b>(Unaudited)</b>
Incremental sales returns under the special extended return privilege	\$ 2,083
Less: estimated cost of sales on incremental sales returns	(375)
Additional fees paid for retention of distributors	360
Facilities and related costs to conduct distributor training	590
Advertising, legal and media related costs	80
	<u>\$ 2,738</u>

#### Net Sales

Net sales were approximately \$40,482,000 for the three months ended September 30, 2004 compared to \$16,740,000 for the three months ended September 30, 2003. This net increase of approximately \$23,742,000 or 141.8% was primarily attributable to the increase in the number of active Lexxus distributors, re-orders and sales of new products. Excluding the \$11.9 million revenue deferred from the second quarter (\$6.6 million orders entered but not shipped until the third quarter and \$5.4 million shipped in the second quarter but not recognized until the third quarter, offset by \$0.1 million incremental special product returns), net sales for the quarter were \$28.6 million, not including approximately \$2.4 million orders taken but shipped during the third quarter.

#### Cost of Sales

Cost of sales was approximately \$8,323,000 or 20.6% of net sales for the three months ended September 30, 2004 compared with approximately \$3,671,000 or 21.9% of net sales for the three months ended September 30, 2003. This increase of approximately \$4,652,000 or 126.7% was primarily attributable to increased net sales. Cost of sales as a percentage of net sales decreased due to the elimination of commissions paid to Marketvision, which was acquired by the Company on March 31, 2004.

#### Gross Profit

Gross profit was approximately \$32,159,000 or 79.4% of net sales for the three months ended September 30, 2004 compared with approximately \$13,069,000 or 78.1% of net sales for the three months ended September 30, 2003. This increase of approximately \$19,090,000 or 146.1% was attributable to the increase in sales overall.

#### Distributor Commissions

Distributor commissions were approximately \$17,421,000 or 43.0% of net sales for the three months ended September 30, 2004 compared with approximately \$6,988,000 or 41.8% of net sales for the three months ended September 30, 2003. This increase of approximately \$10,433,000 or 149.3% was driven by the increase in net sales, the terms of the compensation plans, and promotions held during the third quarter of 2004. Commissions paid of approximately \$2.7 million, related to the \$5.4 million revenue deferred from the second quarter to the third quarter were already recorded in the second quarter of 2004.

#### Selling, General and Administrative Expenses

Selling, general and administrative expenses were approximately \$8,836,000 or 21.8% of net sales for the three months ended September 30, 2004 compared with approximately \$4,133,000 or 24.7% of net sales for the three months ended September 30, 2003. The decrease in selling, general and administrative costs as a percentage of net sales was due to greater revenue. The increase in selling,

general and administrative expenses of approximately \$4,703,000 or 113.8% was mainly attributable to the more marketing and promotional activities world-wide.

#### Other Expenses, Net

Other expenses, net were approximately \$91,000 for the three months ended September 30, 2004 compared with approximately \$150,000 for the three months ended September 30, 2003. This decrease of approximately \$59,000 was due to a decrease in currency-related losses.

#### Income Taxes

Income tax expense was approximately \$857,000 or 14.7% of income before income taxes and minority interest for the three months ended September 30, 2004 compared with income tax expense of \$500,000 or 27.8% of income before income taxes and minority interest for the three months ended September 30, 2003. The decrease in effective tax rate was attributable to use of net operating losses in the U.S. and lower effective tax rates on foreign earnings in 2004.

#### Minority Interest,

Minority interest benefit was approximately \$74,000 for the three months ended September 30, 2004, as compared to minority interest expense of approximately \$22,000 for the three months ended September 30, 2003. The change was driven mainly by the change in profitability of KGC Networks Pte. Ltd.

#### Net Income

Net income was approximately \$5,028,000 or 12.4% of net sales for the three months ended September 30, 2004 compared to net income of approximately \$1,276,000 or 7.6% of net sales for the three months ended September 30, 2003. The increase in net income was mainly attributable to increased revenue.

#### *Nine Months Ended September 30, 2004 Compared to the Nine Months Ended September 30, 2003*

The following table summarizes NHTC's consolidated operating results as a percentage of net sales for each of the years indicated:

	Nine Months Ended September 30,	
	2004	2003
Net sales	100.0%	100.0%
Cost of sales	20.2%	18.6%
Gross profit	79.8%	81.4%
Operating expenses:		
Distributor commissions	52.0%	41.3%
Selling, general and administrative expenses	26.0%	27.5%
Total operating expenses	78.0%	68.8%
Income from operations	1.8%	12.6%
Other expense, net	(0.1%)	(0.5%)
Income before income taxes and minority interest	1.7%	12.1%
Income taxes and minority interest	(0.3%)	(3.1%)
Net income	1.4%	9.0%

## Overview of the Results of Operations for the Nine Months ended September 30, 2004

### Net Sales

Net sales were approximately \$96,604,000 for the nine months ended September 30, 2004 compared to \$39,964,000 for the nine months ended September 30, 2003. This net increase of approximately \$56,640,000 or 141.7% was primarily attributable to the increased number of active Lexxus distributors, Lexxus's expansion into new markets, including South Korea in the second quarter of 2003 and sales of new products.

### Cost of Sales

Cost of sales was approximately \$19,539,000 or 20.2% of net sales for the nine months ended September 30, 2004 compared with approximately \$7,450,000 or 18.6% of net sales for the nine months ended September 30, 2003. This increase of approximately \$12,089,000 or 162.3% was primarily driven by increased sales. Cost of sales as a percentage of net sales increased primarily due to greater air freight costs to ship product from the US to Asia and Europe in 2004, partly offset by the elimination of the commissions paid to Marketvision after its acquisition by the Company on March 31, 2004.

### Gross Profit

Gross profit was approximately \$77,065,000 or 79.8% of net sales for the nine months ended September 30, 2004 compared with approximately \$32,514,000 or 81.4% of net sales for the nine months ended September 30, 2003. This increase of approximately \$44,551,000 or 137.0% was attributable to the increase in sales.

### Distributor Commissions

Distributor commissions were approximately \$50,205,000 or 52.0% of net sales for the nine months ended September 30, 2004 compared with approximately \$16,498,000 or 41.3% of net sales for the nine months ended September 30, 2003. This increase of approximately \$33,707,000 or 204.3% and as a percentage of sales was related to the increase in sales, the terms of the compensation plans, and promotions held during the nine months ended September 30, 2004. Commissions of approximately \$1.1 million paid on returns and refunds pertaining to the special product return privilege granted to certain Hong Kong distributors in the second quarter also increased commissions as a percentage of sales in 2004.

### Selling, General and Administrative Expenses

Selling, general and administrative costs were approximately \$25,078,000 or 26.0% of net sales for the nine months ended September 30, 2004 compared with approximately \$10,983,000 or 27.5% of net sales for the nine months ended September 30, 2003. This increase of approximately \$14,095,000 or 128.3% was mainly attributable to the increased marketing and promotional activities world-wide, special expenses the Company incurred as a result of the negative television program aired on CCTV and the administrative expenses associated with the new office in Seoul, South Korea, which was opened in the second quarter of 2003. The 2004 selling, general and administrative costs as a percentage of net sales was less than a year ago over the comparable period, mainly due to much higher revenue.

### Other Expense, Net

Other expense, net was approximately \$122,000 for the nine months ended September 30, 2004 compared with expense of approximately \$192,000 for the nine months ended September 30, 2003. This decrease of approximately \$70,000 was mainly due to less currency-related losses.

## Income Taxes

Income tax expense was approximately \$109,000 or 6.6% of income before income taxes and minority interest for the nine months ended September 30, 2004 compared with \$1,200,000 or 24.8% of income before income taxes and minority interest for the nine months ended September 30, 2003. The decrease in effective tax rate was attributable to use of net operating losses in the U.S. and lower effective tax rates on foreign earnings in 2004.

## Minority Interest

Minority interest expense was approximately \$159,000 for the nine months ended September 30, 2004, compared to approximately \$45,000 of expense for the nine months ended September 30, 2003. The increase in the expense relates primarily to the improved profitability of our subsidiary, KGC Networks Pte. Ltd.

## Net Income

Net income was approximately \$1,392,000 or 1.4% of net sales for the nine months ended September 30, 2004 compared to net income of approximately \$3,596,000 or 9.0% of net sales for the nine months ended September 30, 2003. The decrease in net income was due to higher commissions paid to distributors and marketing expenses, partly offset by higher volume.

## Liquidity and Capital Resources

Cash generated from operations is the main funding source for the Company's working capital and capital expenditure. In the past, NHTC also borrowed from institutions and individuals and issued preferred stock. In October 2004, the Company raised approximately \$15.9 million net of transaction fees through a private equity placement.

At September 30, 2004, the ratio of current assets to current liabilities was 1.00 to 1.00 and NHTC had working capital deficit of approximately \$30,000. Working capital as of September 30, 2004 increased since June 30, 2004 mainly due to a decrease in deferred revenue, and declined from the December 31, 2003 mainly because of increased accrued expenses and the issuance of promissory notes in connection with the Marketvision acquisition.

Cash used in operations for the nine months ended September 30, 2004 was approximately \$1,860,000. Cash used in investing activities during the period was approximately \$2,617,000, which primarily relates to the cash payment made to Marketvision as part of the acquisition together with an increase of restricted cash related to the credit card reserve, purchase of minority interest and capital expenditures. Cash used in financing activities during the period was approximately \$880,000 utilized for the repayment of Marketvision-related notes payable and long-term debt. Total cash decreased by approximately \$5,714,000 during the period.

With cash generated from profitable business operations and the net proceeds from the private placement closed in October 2004, NHTC believes that its existing liquidity and cash flows from operations, including its cash and cash equivalents, should be adequate to fund normal business operations expected in the future.

NHTC intends to continue to open additional operations in new foreign markets in coming years. The Company is in the process of planning for its entry into the Mexican and Japanese markets. The estimated initial cost for entering into the Mexican market is \$2 million to \$3 million, and \$5 million to \$7 million for the Japanese market.

China is currently the Company's most important business development project. Direct selling, or multi-level marketing, is currently prohibited in China. The Chinese government is committed to opening the direct selling market and has published drafts of pertinent legislation, which is expected to be formally adopted some time next year. Before the formal adoption of direct selling laws, many of the international direct selling companies have started to operate in China in a retail format. In June 2004, Lexxus obtained a license to engage in retail business in China. The license stipulates a capital requirement of \$12 million over a three-year period. As of November 2, 2004, the Company has not funded this capital requirement for the retail license. In planning for a retail operation, the Company estimates that each retail store will cost approximately \$50,000 to \$100,000 and is evaluating the number, location, timing and format of store openings.

Since the airing of a negative program on Chinese television on April 12, 2004, the Company has been unable to determine whether any governmental investigations have been initiated or are under consideration by the Chinese government as a result of such adverse publicity. The Company is also unable to predict whether it will be successful in obtaining a direct selling license to operate in China, and if it is successful, when it will be permitted to commence direct selling operations there. Further, even if the Company is successful in obtaining a direct selling license to do business in China, it is uncertain as to whether the Company will generate profits from such operations.

In connection with the Marketvision acquisition, the Company issued three different promissory notes in the aggregate principal amount of approximately \$3.2 million. As of September 30, 2004, two of these promissory notes in the aggregate amount of \$1.5 million became due and payable. On October 12, 2004, the Company repaid approximately \$1.6 million and the notes due on September 30, 2004 have been paid in full.

#### **Off – Balance Sheet Arrangements**

NHTC does not utilize off-balance sheet financing arrangements other than in the normal course of business. NHTC finances the use of certain facilities, office and computer equipment, and automobiles under various operating lease agreements.

#### **Forward Looking Statements**

Certain statements contained in this Quarterly Report on Form 10-Q constitute "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. All statements included in this Quarterly Report, other than statements of historical facts, regarding our strategy, future operations, financial position, estimated revenues, projected costs, prospects, plans and objectives are forward-looking statements. When used in this Quarterly Report, the words "will," "believe," "anticipate," "intend," "estimate," "expect," "project" and similar expressions are intended to identify forward-looking statements, although not all forward-looking statements contain these identifying words. We cannot guarantee future results, levels of activity, performance or achievements, and you should not place undue reliance on our forward-looking statements. Our actual results could differ materially from those anticipated in these forward-looking statements as a result of various factors. Our forward-looking statements do not reflect the potential impact of any future acquisitions, mergers, dispositions, joint ventures or strategic investments. In addition, any forward-looking statements represent our expectation only as of the day this Quarterly Report was first filed with the SEC and should not be relied on as representing our expectations as of any subsequent date. While we may elect to update forward-looking statements at some point in the future, we specifically disclaim any obligation to do so, even if our expectations change.

Although we believe that the expectations reflected in any of our forward-looking statements are reasonable, actual results could differ materially from those projected or assumed in any of our forward-looking statements. Our future financial condition and results of operations, as well as any forward-looking statements, are subject to change and to inherent risks and uncertainties, such as those disclosed in this Quarterly Report. Important factors that could cause our actual results, performance and achievements, or industry results to differ materially from estimates or projections contained in forward-looking statements include, among others, the following:

- our relationship with our distributors;
- our need to continually recruit new distributors;
- our internal controls and accounting methods may require further modification;
- regulatory matters governing our products and network marketing system;
- adverse publicity associated with our products or network marketing organizations;
- our relationship with minority interest partners;
- product liability claims;
- our reliance on outside manufacturers;
- risks associated with operating internationally, including foreign exchange risks;
- product concentration;
- dependence on increased penetration of existing markets;
- the competitive nature of our business; and
- our ability to generate sufficient cash to operate and expand our business.

Market data and other statistical information used throughout this report is based on independent industry publications, government publications, reports by market research firms or other published independent sources and on our good faith estimates, which are derived from our review of internal surveys and independent sources. Although we believe that these sources are reliable, we have not independently verified the information and cannot guarantee its accuracy or completeness.

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

NHTC does not engage in trading market risk sensitive instruments and does not purchase investments as hedges or for purposes “other than trading” that are likely to expose it to certain types of market risk, including interest rate, commodity price or equity price risk. NHTC has not issued any debt instruments, entered into any forward or future contracts, purchased any options or entered into any swaps.

#### *Currency Risk and Exchange Rate Information*

Some of NHTC’s revenue and some of their expenses are recognized outside of the United States, except for inventory purchases, which are primarily transacted in U.S. dollars from vendors in the United States. The local currency of each subsidiary’s primary markets is considered the functional currency. Revenue and expenses are translated at the weighted average exchange rates for the periods reported. Therefore, the reported revenue and earnings will be positively impacted by a weakening of the U.S. dollar and will be negatively impacted by a strengthening of the U.S. dollar. Given the uncertainty of exchange rate fluctuations, we cannot estimate the effect of these fluctuations on our future business, product pricing, and results of operations or financial condition.

#### *Seasonality*

In addition to general economic factors, NHTC is impacted by seasonal factors and trends such as major cultural events and vacation patterns. For example, most Asian markets celebrate their respective local New Year in the first quarter, which generally has a negative impact on that quarter. We believe

that direct selling in the United States and Europe is also generally negatively impacted during the month of August, which is in our third quarter, when many individuals, including our distributors, traditionally take time off for vacations.

#### **Item 4. Controls and Procedures**

We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed in our Exchange Act reports is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms and that such information is accumulated and communicated to our management, including our President and Chief Financial Officer, as appropriate, to allow for timely decisions regarding required disclosure. In designing and evaluating the disclosure controls and procedures, management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, and management is required to apply its judgment in evaluating the cost-benefit relationship of possible controls and procedures.

During the quarters ended September 30 and December 31, 2003, the Company re-evaluated its financial statements for the years ended December 31, 2002 and 2001, the quarterly periods included in such years and the quarterly periods ended March 31, June 30 and September 30, 2003. As a result of such review, the Company determined that it inadvertently applied the incorrect accounting treatment with respect to the following items:

- (i) revenue recognition with respect to administrative enrollment fees;
- (ii) revenue cut-off between 2002 and 2003;
- (iii) accounts receivable reconciliation to supporting documents;
- (iv) reserves established for product returns and refunds;
- (v) the gain recorded in connection with the sale of a subsidiary in 2001;
- (vi) income tax provisions; and
- (vii) stock option based compensation.

Consequently, the Company amended and restated its financial statements for each quarter in 2001, 2002 and 2003 as well as for the years ended December 31, 2001 and 2002 with respect to each of the foregoing items (collectively, the "Restatement Items").

An evaluation of the Company's disclosure controls and procedures (as defined in Section 13(a)-14(c) of the Exchange Act) as of September 30, 2004 was carried out under the supervision and with the participation of the Company's President and Chief Financial Officer and other members of the Company's senior management. The Company's President and Chief Financial Officer concluded that the Company's disclosure controls and procedures as currently in effect are effective in ensuring that the information required to be disclosed by the Company in the reports it files or submits under the Exchange Act is (i) accumulated and communicated to the Company's management (including the President and Chief Financial Officer) in a timely manner, and (ii) recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms. During the nine months ended September 30, 2004, the Company made changes to improve its internal controls over financial reporting with respect to (i) each of the Restatement Items, and (ii) monthly financial reports provided to the Company by its subsidiaries. The Company hired a new Chief Financial Officer in August 2004 and a new Chief Accounting Officer in September 2004 and is still hiring additional accounting staff to supplement existing personnel. In addition, the Company has commenced its documentation required under the Sarbanes-Oxley Act of 2002 and is developing additional policies and procedures to further strengthen its international reporting, including the areas of revenue recognition, sales and expense cut-off and sales returns. The Company hired a reporting specialist in November 2004 to coordinate the world-wide Sarbanes-Oxley compliance work. The Company plans to implement additional controls and procedures sufficient to accurately report their financial performance on a timely basis. A regional Chief

Financial Officer was recruited to improve financial reporting and operational efficiency in the region of Greater China and Southeast Asia. There have been no other changes in the Company's internal control over financial reporting (as defined in Rule 13a-15(f) of the Exchange Act) that occurred during the quarter ended September 30, 2004, that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

The Company intends to continually review and evaluate the design and effectiveness of its disclosure controls and procedures and to improve its controls and procedures over time and to correct any deficiencies that it may discover in the future. The goal is to ensure that senior management has timely access to all material financial and non-financial information concerning the Company's business. While the Company believes the present design of its disclosure controls and procedures is effective to achieve its goal, future events affecting its business may cause the Company to modify its disclosure controls and procedures.

## **PART II — OTHER INFORMATION**

### **Item 1. Legal Proceedings**

During the fall of 2003, the customs agency of the government of South Korea brought a charge against LXX, Ltd., the Company's wholly owned subsidiary operating in South Korea ("LXX"), with respect to the importation of the Company's Alura product. The customs agency alleges that Alura is not a cosmetic product, but rather should be categorized and imported as a pharmaceutical product. The matter is currently being considered in the courts. During the ongoing hearings, LXX intends to present expert testimony that Alura is not a pharmaceutical product, and therefore, LXX should be permitted to sell and distribute Alura in South Korea. The failure to sell Alura in South Korea is not anticipated to have a material adverse effect on the financial condition, results of operations, cash flow or business prospects of LXX.

On or around March 31, 2004, Lexxus International, Inc. ("Lexxus") received a letter from John Loghry, a former Lexxus distributor, alleging that Lexxus had wrongfully terminated an alleged oral distributorship agreement with Mr. Loghry and that the Company had breached an alleged oral agreement to issue shares of the Company's common stock to Mr. Loghry. The letter demanded a settlement payment of \$35 million without any explanation as to the amount of the claim. After Mr. Loghry threatened to commence suit against Lexxus and the Company in Nebraska, on May 13, 2004, Lexxus and the Company filed an action for declaratory relief against Mr. Loghry in the United States District Court for the Northern District of Texas seeking, inter alia, a declaration that Mr. Loghry was not wrongfully terminated and is not entitled to recover anything from Lexxus or the Company. Mr. Loghry has filed counterclaims against the Company and Lexxus asserting his previously articulated claims. Discovery has commenced and the Company intends to vigorously defend itself in this case.

In September 2004, Mr. Loghry filed third party claims against certain officers of the Company and Lexxus, including against Terry LaCore and Mark Woodburn for fraud, LaCore, Woodburn, and Lisa Grossman for conspiracy to commit the same, and Grossman for tortious interference. A motion to dismiss this action has been filed.

On November 1, 2004, Toyota Jidosha Kabushiki Kaisha (d/b/a Toyota Motor Corporation) and Toyota Motor Sales, U.S.A. (collectively, "Toyota") filed a complaint against the Company and Lexxus International, Inc. ("Lexxus") in United States District Court for the Central District of California (CV04-9028). The complaint alleges trademark and service mark dilution, unfair competition, trademark and service mark infringement, and trade name infringement, each with respect to Toyota's Lexus trademark. Toyota seeks to enjoin the Company and Lexxus from using the Lexxus mark and otherwise competing unfairly with Toyota, to transfer the ownership of the mylexxus.com and lexxusinternational.com Internet sites to Toyota, and reimbursement of costs and reasonable attorney fees incurred by Toyota in



connection with this matter. The Company denies the allegations contained in the complaint and intends to vigorously defend this action. In the event that the Company is unsuccessful in defending this action, the Company may be required to change the name of some or all of its Lexus subsidiaries and domain names which could have a material adverse effect on the financial condition, results of operations, cash flow or business prospects of the Company.

From time to time, the Company is involved in legal proceedings incidental to the course of its business. The Company believes that all pending actions, individually and in the aggregate, will not have a material adverse effect on the financial condition, results of operations, cash flows or business prospects.

**Item 2. Unregistered Sales of Equity Securities and Use of Proceeds**

Not applicable.

**Item 3. Defaults upon Senior Securities**

Not applicable.

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

Not applicable.

**Item 5. Other Information**

Not applicable.

**Item 6. Exhibits**

4.1 Form of Common Stock Purchase Warrant issued to investors in private placement in October 2004.

10.1 Employment Agreement dated as of August 1, 2004 between the Company and Chris Sharnq.

10.2 Form of Registration Rights Agreement between the Company and the investors in the Company's private placement in October 2004.

31.1 Certification of President required by Section 302 of the Sarbanes-Oxley Act of 2002.

31.2 Certification of Chief Financial Officer required by Section 302 of the Sarbanes-Oxley Act of 2002.

32.1 Certification of President required by Section 906 of the Sarbanes-Oxley Act of 2002.

32.2 Certification of Chief Financial Officer required by 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.

**NATURAL HEALTH TRENDS CORP.**

By: /s/ Mark D. Woodburn

\_\_\_\_\_  
Mark D. Woodburn

President

By: /s/ Chris Sharng

\_\_\_\_\_  
Chris Sharng

Executive Vice President and Chief Financial Officer

Date: November 11, 2004

**CERTIFICATION PURSUANT TO SECTION 302  
OF THE SARBANES-OXLEY ACT**

I, Mark Woodburn, the President of Natural Health Trends Corp., do certify that:

1. I have reviewed this quarterly report on Form 10-Q of Natural Health Trends Corp.;
2. Based on my knowledge, this 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 report;
3. Based on my knowledge, the financial statements, and other financial information included in this 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 report;
4. I am responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e))-and have:
  - a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under my supervision to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to me by others within those entities, particularly during the period in which this report is being prepared;
  - b. Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report my 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 that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting.
5. 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 registrant's board of directors (or persons performing the equivalent function):
  - a. All significant deficiencies 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.

/s/ Mark Woodburn \_\_\_\_\_

Mark Woodburn  
President

Date: November 11, 2004

**CERTIFICATION PURSUANT TO SECTION 302  
OF THE SARBANES-OXLEY ACT**

I, Chris Sharng, the Chief Financial Officer of Natural Health Trends Corp., do certify that:

1. I have reviewed this quarterly report on Form 10-Q of Natural Health Trends Corp.;
2. Based on my knowledge, this 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 report;
3. Based on my knowledge, the financial statements, and other financial information included in this 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 report;
4. I am responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e))-and have:
  - a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under my supervision to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to me by others within those entities, particularly during the period in which this report is being prepared;
  - b. Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report my 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 that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting.
5. 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 registrant's board of directors (or persons performing the equivalent function):
  - a. All significant deficiencies 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.

/s/ Chris Sharng \_\_\_\_\_

Chris Sharng  
Executive Vice President and  
Chief Financial Officer

Date: November 11, 2004

**CERTIFICATION PURSUANT TO  
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report of Natural Health Trends Corp. (the "Company") on Form 10-Q for the three and nine months ending September 30, 2004 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Mark Woodburn, President of the Company, certify, to the best of my knowledge that:

- (1) The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and result of operations of the Company.

Date: November 11, 2004

/s/ Mark Woodburn \_\_\_\_\_  
Mark Woodburn  
President

**CERTIFICATION PURSUANT TO  
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report of Natural Health Trends Corp. (the "Company") on Form 10-Q for the three and nine months ending September 30, 2004 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Chris Sharng, Chief Financial Officer of the Company, certify, to the best of my knowledge that:

- (1) The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and result of operations of the Company.

Date: November 11, 2004

/s/ Chris Sharng \_\_\_\_\_  
Chris Sharng  
Executive Vice President and  
Chief Financial Officer

EXHIBIT 4.1

[EXECUTION COPY]

NEITHER THE ISSUANCE AND SALE OF THE SECURITIES REPRESENTED BY THIS CERTIFICATE NOR THE SECURITIES INTO WHICH THESE SECURITIES ARE EXERCISABLE HAVE BEEN REGISTERED UNDER THE SECURITIES ACT OF 1933, AS AMENDED. NO SALE OR DISTRIBUTION MAY BE EFFECTED WITHOUT AN EFFECTIVE REGISTRATION STATEMENT RELATED THERETO OR AN OPINION OF COUNSEL IN A FORM REASONABLY SATISFACTORY TO THE COMPANY THAT SUCH REGISTRATION IS NOT REQUIRED UNDER THE SECURITIES ACT OF 1933, AS AMENDED, OR UNLESS SOLD PURSUANT TO RULE 144 OF SUCH ACT. NOTWITHSTANDING THE FOREGOING, THE SECURITIES MAY BE PLEDGED IN CONNECTION WITH A BONA FIDE MARGIN ACCOUNT OR OTHER LOAN OR FINANCING ARRANGEMENT SECURED BY THE SECURITIES.

NATURAL HEALTH TRENDS CORP.

FORM OF COMMON STOCK PURCHASE WARRANT

Warrant No. : \_\_\_\_\_

Number of Shares: \_\_\_\_\_

Date of Issuance: October 6, 2004 ("Issuance Date")

Natural Health Trends Corp., a Florida corporation (the "Company"), hereby certifies that, for good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, [INSERT NAME OF BUYER], the registered holder hereof or its permitted assigns (the "Holder"), is entitled, subject to the terms set forth below, to purchase from the Company, at the Exercise Price (as defined below) then in effect, upon surrender of this Common Stock Purchase Warrant (including all Common Stock Purchase Warrants issued in exchange, transfer or replacement hereof, the "Warrant"), at any time or times on or after the date hereof, but not after 11:59 P.M., New York Time, on the Expiration Date (as defined below), \_\_\_\_\_ (\_\_\_\_) fully paid nonassessable shares of Common Stock (as defined below) (the "Warrant Shares"). Except as otherwise defined herein, capitalized terms in this Warrant shall have the meanings set forth in Section 13. This Warrant is one of the Common Stock Purchase Warrants (the "SPA Warrants") issued pursuant to (i) Section 1 of that certain Securities Purchase Agreement, or (ii) Article 3 of that certain Subscription Agreement, each dated as of October 6, 2004 (the "Subscription Date"), among the Company and the investors (the "Buyers") referred to therein (the "Purchase Agreements").

1. EXERCISE OF WARRANT.

(a) MECHANICS OF EXERCISE. Subject to the terms and conditions hereof, this Warrant may be exercised by the Holder on any day on or after the date hereof, in whole or in part, by (i) delivery of a written notice, in the form attached hereto as EXHIBIT A (the "Exercise Notice"), of the Holder's election to exercise this Warrant and (ii) payment to the Company of an amount equal to the applicable Exercise Price multiplied by the number of Warrant Shares as to which this Warrant is being exercised (the "Aggregate Exercise Price") in cash or by wire transfer of immediately available funds. The Holder shall not be required to deliver the original Warrant in order to effect an exercise hereunder. Execution and delivery of the Exercise Notice with respect to less than all of the Warrant Shares shall have the same effect as cancellation of

the original Warrant and issuance of a new Warrant evidencing the right to purchase the remaining number of Warrant Shares. On or before the first Business Day following the date on which the Company has received each of the Exercise Notice and the Aggregate Exercise Price (the "Exercise Delivery Documents"), the Company shall transmit by facsimile an acknowledgment of confirmation of receipt of the Exercise Delivery Documents to the Holder and the Company's transfer agent (the "Transfer Agent"). On or before the tenth Business Day following the date on which the Company has received all of the Exercise Delivery Documents (the "Share Delivery Date"), the Company shall (X) provided that the Transfer Agent is participating in The Depository Trust Company ("DTC") Fast Automated Securities Transfer Program, upon the request of the Holder, credit such aggregate number of shares of Common Stock to which the Holder is entitled pursuant to such exercise to the Holder's or its designee's balance account with DTC through its Deposit Withdrawal Agent Commission system, or (Y) if the Transfer Agent is not participating in the DTC Fast Automated Securities Transfer Program, issue and dispatch by overnight courier to the address as

specified in the Exercise Notice, a certificate, registered in the name of the Holder or its designee, for the number of shares of Common Stock to which the Holder is entitled pursuant to such exercise. Upon delivery of the Exercise Notice and Aggregate Exercise Price referred to in clause (ii) above, the Holder shall be deemed for all corporate purposes to have become the holder of record of the Warrant Shares with respect to which this Warrant has been exercised, irrespective of the date of delivery of the certificates evidencing such Warrant Shares. If this Warrant is submitted in connection with any exercise pursuant to this Section 1(a) and the number of Warrant Shares represented by this Warrant submitted for exercise is greater than the number of Warrant Shares being acquired upon an exercise, then the Company shall as soon as practicable and in no event later than three Business Days after any exercise and at its own expense, issue a new Warrant (in accordance with Section 6(d)) representing the right to purchase the number of Warrant Shares purchasable immediately prior to such exercise under this Warrant, less the number of Warrant Shares with respect to which this Warrant is exercised. No fractional shares of Common Stock are to be issued upon the exercise of this Warrant, but rather the number of shares of Common Stock to be issued shall be rounded up to the nearest whole number.

(b) EXERCISE PRICE. For purposes of this Warrant, "Exercise Price" means \$12.47, subject to adjustment as provided herein.

2. ADJUSTMENT OF EXERCISE PRICE AND NUMBER OF WARRANT SHARES. The Exercise Price and the number of Warrant Shares shall be adjusted from time to time as follows:

(a) ADJUSTMENT UPON SUBDIVISION OR COMBINATION OF COMMON STOCK. If the Company at any time on or after the Issuance Date subdivides (by any stock split, stock dividend, recapitalization or otherwise) one or more classes of its outstanding shares of Common Stock into a greater number of shares, the Exercise Price in effect immediately prior to such subdivision will be proportionately reduced and the number of Warrant Shares will be proportionately increased. If the Company at any time on or after the Issuance Date combines (by combination, reverse stock split or otherwise) one or more classes of its outstanding shares of Common Stock into a smaller number of shares, the Exercise Price in effect immediately prior to such combination will be proportionately increased and the number

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of Warrant Shares will be proportionately decreased. Any adjustment under this Section 2(a) shall become effective at the close of business on the date the subdivision or combination becomes effective.

3. PURCHASE RIGHTS; FUNDAMENTAL TRANSACTION.

(a) PURCHASE RIGHTS. In addition to any adjustments pursuant to Section 2 above, if at any time the Company grants, issues or sells any Options, Convertible Securities or rights to purchase stock, warrants, securities or other property pro rata to the record holders of any class of Common Stock (the "Purchase Rights"), then the Holder will be entitled to acquire, upon the terms applicable to such Purchase Rights, the aggregate Purchase Rights which such holder could have acquired if such holder had held the number of shares of Common Stock acquirable upon complete exercise of this Warrant (without regard to any limitations on the exercise of this Warrant) immediately before the date on which a record is taken for the grant, issuance or sale of such Purchase Rights, or, if no such record is taken, the date as of which the record holders of Common Stock are to be determined for the grant, issue or sale of such Purchase Rights.

(b) FUNDAMENTAL TRANSACTIONS. The Company shall not enter into or be party to a Fundamental Transaction unless the Successor Entity assumes in writing all of the obligations of the Company under this Warrant and the other Transaction Documents in accordance with the provisions of this Section 3(b) pursuant to written agreements in form and substance reasonably satisfactory to the Required Holders and approved by the Required Holders prior to such Fundamental Transaction. Upon consummation of the Fundamental Transaction, the Successor Entity shall deliver to the holder of this Warrant in exchange therefor, a warrant substantially identical in form and substance to this Warrant, except that there shall be issuable upon exercise of such warrant at any time after the consummation of the Fundamental Transaction but prior to the Expiration Date, in lieu of the shares of the Company's Common Stock (or other securities, cash, assets or other property) purchasable upon the exercise of the



Warrant prior to such Fundamental Transaction, such shares of stock, securities, cash, assets or any other property whatsoever (including warrants or other purchase or subscription rights) which the Holder would have been entitled to receive upon the happening of such Fundamental Transaction had the Warrant been exercised immediately prior to such Fundamental Transaction, as adjusted in accordance with the provisions of this Warrant. Provisions made pursuant to this Section shall be in a form and substance reasonably satisfactory to the Required Holders. The provisions of this Section shall apply similarly and equally to successive Fundamental Transactions and shall be applied without regard to any limitations on the exercise of this Warrant.

4. **NONCIRCUMVENTION.** The Company hereby covenants and agrees that the Company will not, by amendment of its Articles of Incorporation, as amended or through any reorganization, transfer of assets, consolidation, merger, dissolution, issue or sale of securities, or any other voluntary action, avoid or seek to avoid the observance or performance of any of the terms of this Warrant, and will at all times in good faith carry out all the provisions of this Warrant and take all action as may be required to protect the rights of the Holder. Without limiting the generality of the foregoing, the Company (i) will not increase the par value of any

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shares of Common Stock receivable upon the exercise of this Warrant above the Exercise Price then in effect, (ii) will take all such actions as may be necessary or appropriate in order that the Company may validly and legally issue fully paid and nonassessable shares of Common Stock upon the exercise of this Warrant, and (iii) will, so long as any of the SPA Warrants are outstanding, take all action necessary to reserve and keep available out of its authorized and unissued Common Stock, solely for the purpose of effecting the exercise of the SPA Warrants, the number of shares of Common Stock as shall from time to time be necessary to effect the exercise of the SPA Warrants then outstanding (without regard to any limitations on exercise).

5. **WARRANT HOLDER NOT DEEMED A STOCKHOLDER.** Except as otherwise specifically provided herein, the Holder, solely in such Person's capacity as a holder, of this Warrant shall not be entitled to vote or receive dividends or be deemed the holder of shares of the Company for any purpose, nor shall anything contained in this Warrant be construed to confer upon the Holder, solely in such Person's capacity as a holder of this Warrant, any of the rights of a stockholder of the Company or any right to vote, give or withhold consent to any corporate action (whether any reorganization, issue of stock, reclassification of stock, consolidation, merger, conveyance or otherwise), receive notice of meetings, receive dividends or subscription rights, or otherwise, prior to the issuance to the Holder of the Warrant Shares which such Person is then entitled to receive upon the due exercise of this Warrant. In addition, nothing contained in this Warrant shall be construed as imposing any liabilities on such Holder to purchase any securities (upon exercise of this Warrant or otherwise) or as a stockholder of the Company, whether such liabilities are asserted by the Company or by creditors of the Company. Notwithstanding this Section 5, the Company will provide the Holder with copies of the same notices and other information given to the stockholders of the Company generally, contemporaneously with the giving thereof to the stockholders.

#### 6. REISSUANCE OF WARRANTS.

(a) **TRANSFER OF WARRANT.** The Holder may transfer this Warrant and the rights hereunder only in accordance with applicable securities laws. If this Warrant is to be transferred, the Holder shall surrender this Warrant to the Company, whereupon the Company will forthwith issue and deliver upon the order of the Holder a new Warrant (in accordance with Section 6(d)), registered as the Holder may request, representing the right to purchase the number of Warrant Shares being transferred by the Holder and, if less than the total number of Warrant Shares then underlying this Warrant is being transferred, a new Warrant (in accordance with Section 6(d)) to the Holder representing the right to purchase the number of Warrant Shares not being transferred.

(b) **LOST, STOLEN OR MUTILATED WARRANT.** Upon receipt by the Company of evidence reasonably satisfactory to the Company of the loss, theft, destruction or mutilation of this Warrant, and, in the case of loss, theft or destruction, of any indemnification undertaking by the Holder to the Company in customary form, in the case of mutilation, upon surrender and cancellation of this Warrant, the Company shall execute and deliver to the Holder a new Warrant (in

accordance with Section 6(d)) representing the right to purchase the Warrant Shares then underlying this Warrant.

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(c) WARRANT EXCHANGEABLE FOR MULTIPLE WARRANTS. This Warrant is exchangeable, upon the surrender hereof by the Holder at the principal office of the Company, for a new Warrant or Warrants (in accordance with Section 6(d)) representing in the aggregate the right to purchase the number of Warrant Shares then underlying this Warrant, and each such new Warrant will represent the right to purchase such portion of such Warrant Shares as is designated by the Holder at the time of such surrender; provided, however, that no Warrants for fractional shares of Common Stock shall be given.

(d) ISSUANCE OF NEW WARRANTS. Whenever the Company is required to issue a new Warrant pursuant to the terms of this Warrant, such new Warrant (i) shall be of like tenor with this Warrant, (ii) shall represent, as indicated on the face of such new Warrant, the right to purchase the Warrant Shares then underlying this Warrant (or in the case of a new Warrant being issued pursuant to Section 6(a) or Section 6(c), the Warrant Shares designated by the Holder which, when added to the number of shares of Common Stock underlying the other new Warrants issued in connection with such issuance, does not exceed the number of Warrant Shares then underlying this Warrant), (iii) shall have an issuance date, as indicated on the face of such new Warrant which is the same as the Issuance Date, and (iv) shall have the same rights and conditions as this Warrant.

7. NOTICES. Whenever notice is required to be given under this Warrant, unless otherwise provided herein, such notice shall be given in accordance with Section 9(f) of the Securities Purchase Agreement. The Company shall provide the Holder with prompt written notice of all actions taken pursuant to this Warrant, including in reasonable detail a description of such action and the reason therefore. Without limiting the generality of the foregoing, the Company will give written notice to the Holder (i) promptly upon any adjustment of the Exercise Price or number of Warrant Shares or number or kind of securities purchasable upon exercise of this Warrant, setting forth in reasonable detail, and certifying, the facts requiring such adjustment and the calculation of such adjustment and (ii) prior to the date on which the Company closes its books or takes a record (A) with respect to any dividend or distribution upon the Common Stock, (B) with respect to any grants, issues or sales of any Options, Convertible Securities or rights to purchase stock, warrants, securities or other property to holders of Common Stock or (C) for determining rights to vote with respect to any Fundamental Transaction, dissolution or liquidation, provided in each case that such information shall be made known to the public prior to or in conjunction with such notice being provided to the Holder.

8. AMENDMENT AND WAIVER. Except as otherwise provided herein, the provisions of this Warrant may be amended and the Company may take any action herein prohibited, or omit to perform any act herein required to be performed by it, only if the Company has obtained the written consent of the Required Holders; provided that no such action may increase the exercise price of any SPA Warrant or decrease the number of shares or class of stock obtainable upon exercise of any SPA Warrant without the written consent of the Holder. No such amendment shall be effective to the extent that it applies to less than all of the holders of the SPA Warrants then outstanding.

9. GOVERNING LAW. This Warrant shall be construed and enforced in accordance with, and all questions concerning the construction, validity, interpretation and

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performance of this Warrant shall be governed by, the internal laws of the State of New York, without giving effect to any choice of law or conflict of law provision or rule (whether of the State of New York or any other jurisdictions) that would cause the application of the laws of any jurisdictions other than the State of New York.

10. CONSTRUCTION; HEADINGS. This Warrant shall be deemed to be jointly drafted by the Company and all the Buyers and shall not be construed against any person as the drafter hereof. The headings of this Warrant are for convenience of reference and shall not form part of, or affect the interpretation of, this Warrant.

11. REMEDIES, OTHER OBLIGATIONS, BREACHES AND INJUNCTIVE RELIEF. The remedies provided in this Warrant shall be cumulative and in addition to all other remedies available under this Warrant or any other Transaction Document (as defined in the Purchase Agreements), at law or in equity (including a decree of specific performance and/or other injunctive relief), and nothing herein shall limit the right of the holder of this Warrant right to pursue actual damages for any failure by the Company to comply with the terms of this Warrant. The Company acknowledges that a breach by it of its obligations hereunder will cause irreparable harm to the Holder and that the remedy at law for any such breach may be inadequate. The Company therefore agrees that, in the event of any such breach or threatened breach, the holder of this Warrant shall be entitled, in addition to all other available remedies, to an injunction restraining any breach, without the necessity of showing economic loss and without any bond or other security being required.

12. TRANSFER. This Warrant may be offered for sale, sold, transferred or assigned without the consent of the Company, subject to applicable securities laws; provided however, in no event shall the Holder effect a public distribution of this Warrant without the prior written consent of the Company which consent maybe withheld in the Company's sole discretion.

13. CERTAIN DEFINITIONS. For purposes of this Warrant, the following terms shall have the following meanings:

(a) "COMMON STOCK" means (i) the Company's common stock, par value \$.001 per share, and (ii) any capital stock into which such Common Stock shall have been changed or any capital stock resulting from a reclassification of such Common Stock.

(b) "CONVERTIBLE SECURITIES" means any stock or securities (other than Options) directly or indirectly convertible into or exercisable or exchangeable for Common Stock.

(c) "EXPIRATION DATE" means the date sixty months after the Issuance Date or, if such date falls on a day other than a Business Day or on which trading does not take place on the Principal Market (a "Holiday"), the next date that is not a Holiday.

(d) "FUNDAMENTAL TRANSACTION" means that the Company shall, directly or indirectly, in one or more related transactions, (i) consolidate or merge with or into (whether or not the Company is the surviving corporation) another Person (except for a migratory merger

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pursuant to which the Company changes its state of incorporation), or (ii) sell, assign, transfer, convey or otherwise dispose of all or substantially all of the properties or assets of the Company to another Person, or (iii) allow another Person to make a purchase, tender or exchange offer that is accepted by the holders of more than the 50% of the outstanding shares of Common Stock (not including any shares of Common Stock held by the Person or Persons making or party to, or associated or affiliated with the Persons making or party to, such purchase, tender or exchange offer), or (iv) consummate a stock purchase agreement or other business combination (including, without limitation, a reorganization, recapitalization, or spin-off) with another Person whereby such other Person acquires more than the 50% of the outstanding shares of Common Stock (not including any shares of Common Stock held by the other Person or other Persons making or party to, or associated or affiliated with the other Persons making or party to, such stock purchase agreement or other business combination).

(e) "OPTIONS" means any rights, warrants or options to subscribe for or purchase Common Stock or Convertible Securities.

(f) "PARENT ENTITY" of a Person means an entity that, directly or indirectly, controls the applicable Person and whose common stock or equivalent equity security is quoted or listed on an Eligible Market, or, if there is more than one such Person or Parent Entity, the Person or Parent Entity with the largest public market capitalization as of the date of consummation of the Fundamental Transaction.

(g) "PERSON" means an individual, a limited liability company, a

partnership, a joint venture, a corporation, a trust, an unincorporated organization, any other entity and a government or any department or agency thereof.

(h) "PRINCIPAL MARKET" means the principal exchange or market on which the Common Stock is listed and trades, which initially is the OTC Bulletin Board.

(i) "REGISTRATION RIGHTS AGREEMENT" means that certain registration rights agreement by and among the Company and the Buyers.

(j) "REQUIRED HOLDERS" means the holders of the SPA Warrants representing at least a majority of the shares of Common Stock underlying the SPA Warrants then outstanding.

(k) "SUCCESSOR ENTITY" means the Person, which may be the Company, formed by, resulting from or surviving any Fundamental Transaction or the Person with which such Fundamental Transaction shall have been made, provided that if such Person is not a publicly traded entity whose common stock or equivalent equity security is quoted or listed for trading on an Eligible Market, Successor Entity shall mean such Person's Parent Entity.

IN WITNESS WHEREOF, the Company has caused this Warrant to Purchase Common Stock to be duly executed as of the Issuance Date set out above.

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NATURAL HEALTH TRENDS CORP.

By: \_\_\_\_\_  
Name: Mark D. Woodburn  
Title: President

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EXHIBIT A

EXERCISE NOTICE

TO BE EXECUTED BY THE REGISTERED HOLDER TO EXERCISE THIS  
WARRANT TO PURCHASE COMMON STOCK

NATURAL HEALTH TRENDS CORP.

The undersigned holder hereby exercises the right to purchase \_\_\_\_\_ of the shares of Common Stock ("Warrant Shares") of Natural Health Trends Corp., a Florida corporation (the "Company"), evidenced by the attached Warrant to Purchase Common Stock (the "Warrant"). Capitalized terms used herein and not otherwise defined shall have the respective meanings set forth in the Warrant.

1. PAYMENT OF EXERCISE PRICE. The holder shall pay the Aggregate Exercise Price in the sum of \$\_\_\_\_\_ in immediately available funds to the Company in accordance with the terms of the Warrant.

2. ACCREDITED INVESTOR. The Holder is an "accredited investor" as defined in Rule 501(c) under the Securities Act of 1933, as amended.

3. DELIVERY OF WARRANT SHARES. The Company shall deliver to the holder \_\_\_\_\_ Warrant Shares in accordance with the terms of the Warrant.

Date: \_\_\_\_\_, \_\_\_\_\_

Name of Registered Holder

By: \_\_\_\_\_  
Name:  
Title:

ACKNOWLEDGMENT

The Company hereby acknowledges this Exercise Notice and hereby directs Continental Stock Transfer and Trust Company to issue the above indicated number

of shares of Common Stock in accordance with the Transfer Agent Instructions dated October 6, 2004 from the Company and acknowledged and agreed to by Continental Stock Transfer and Trust Company.

NATURAL HEALTH TRENDS CORP.

By: \_\_\_\_\_

Name: Mark D. Woodburn

Title: President

EXHIBIT 10.1

EMPLOYMENT AGREEMENT

EMPLOYMENT AGREEMENT, dated as of June 24, 2004 and effective as of August 1, 2004, by and between Natural Health Trends Corp., a Florida corporation (the "Company"), of 12901 Hutton Drive, Dallas, Texas 75234 and Chris Sharnq, an individual residing at 1352 Saddlebrook Court, Bartonville, Texas 76226 (the "Executive").

WITNESSETH:

WHEREAS, the Company desires to employ the Executive, and the Executive desires to be employed by the Company, upon the terms and conditions hereinafter set forth.

NOW, THEREFORE, for good and valuable consideration, the receipt and sufficiency of which is hereby acknowledged, the parties mutually agree as follows:

SECTION 1. EMPLOYMENT. The Company agrees to employ Executive and the Executive hereby accepts such employment, as the Company's Executive Vice President and Chief Financial Officer, subject to the terms and conditions set forth in this Agreement.

SECTION 2. DUTIES; EXCLUSIVE SERVICES; BEST EFFORTS. The Executive shall perform all duties incident to the position of Executive Vice President and Chief Financial Officer as well as any other duties as may from time to time be assigned by the President of the Company or his designee, and agrees to abide by all By-laws, policies, practices, procedures or rules of the Company. The Executive agrees to devote his best efforts, energies and skill to the discharge of the duties and responsibilities attributable to his position, and to this end, he will devote his full time and attention exclusively to the business and affairs of the Company. The Executive also agrees that he shall not take personal advantage of any business opportunities which arise during his employment and which may benefit the Company. All material facts regarding such opportunities must be promptly

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reported to the President for consideration by the Company. Notwithstanding the foregoing, the Executive may donate his time and efforts to charitable causes so long as such endeavors do not effect his ability to perform his duties under this Agreement. If requested by the Company, the Executive shall serve on the Board of Directors or any committee thereof without additional compensation.

SECTION 3. TERM OF EMPLOYMENT; VACATION.

(a) Unless extended in writing by both the Company and the Executive, the term of this Agreement shall commence on the effective date hereof and terminate on December 31, 2007, subject to earlier termination by the parties pursuant to Sections 5 and 6 hereof (the "Term").

(b) The Executive shall be entitled to two (2) weeks vacation during each year of the Term.

SECTION 4. COMPENSATION OF EXECUTIVE.

4.1 SALARY. The Company shall pay to Executive a base salary of two hundred thirty thousand (\$230,000) dollars for the twelve-month period commencing August 1st, 2004 (the "Base Salary"), less such deductions as shall be required to be withheld by applicable law and regulations. The Base Salary payable to Executive shall be paid at such regular weekly, biweekly or semi-monthly time or times as the Company makes payment of its regular payroll in the regular course of business. Commencing on the first anniversary of the date hereof, the Base Salary shall be increased to two hundred and fifty thousand (\$250,000) and be effective for the rest of the Term.

4.2 STOCK OPTIONS. On the date hereof and upon the execution of this Agreement by the parties, the Executive shall receive non-qualified stock options exercisable for an aggregate of 34,124 shares of the Company's common stock ("Common Stock") at an exercise price equal to the closing price of

the Company's common stock on the date hereof, as reported on the OTC Bulletin Board. An equal number of Options (or approximately 832 Options) shall vest monthly during the Term; provided however, that no Options shall vest

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during the six (6) month period commencing on the date hereof and ending on January 31st, 2005, and on January 31st, 2005, 4,992 Options shall vest. The Options shall be granted pursuant to the Company's 2002 Stock Plan (the "Plan") and subject to the terms and conditions thereof.

4.3 PERFORMANCE BONUSES. During the term of this Agreement, the Executive shall be entitled to receive an annual cash performance bonus (the "Annual Bonus") for each year during the Term commencing on January 1st and ending on the following December 31st based upon (i) the Executive's performance of his duties, and (ii) the Company's financial performance, each as determined by the Company's Compensation Committee (or lieu thereof, the Company's Board of Directors) in its reasonable discretion. The Executive and the Company shall agree on certain minimum and maximum annual performance criteria. If (i) the minimum target is not achieved, the Executive will not be entitled to any Annual Bonus, (ii) the minimum target is achieved, the Executive will be entitled to an Annual Bonus equal to 25% of his Base Salary in effect on January 1st of the applicable year, or (iii) the maximum target is achieved, the Executive will be entitled to an Annual Bonus equal to 50% of his Base Salary in effect on January 1st of the applicable year. Such Annual Bonus, if any, shall be paid within forty five (45) days following the end of such yearly bonus period. Notwithstanding the foregoing, the Executive shall receive a cash bonus of no less than \$50,000 for each of the calendar years ending December 31, 2004 and 2005.

4.4 EXPENSES. During the Term, the Company shall promptly reimburse the Executive for all reasonable and necessary travel expenses (including business class on all international flights over 5 hours in duration) and other disbursements incurred by the Executive on behalf of the Company, in performance of the Executive's duties hereunder, assuming Executive has received prior approval for such travel expenses and disbursements by the Company to the extent possible consistent with corporate practices with respect to the reimbursement of expenses incurred by the Company's senior executives. In addition, the

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Company shall pay or reimburse Executive for any membership fees and dues for various professional organizations in an amount not to exceed \$2,000.00.

4.5 BENEFITS. The Executive shall be permitted during the Term to participate in any hospitalization or disability insurance plans, health programs, pension plans, bonus plans or similar benefits that may be available to other executives of the Company (including coverage under any officers and directors liability insurance policy), subject to such eligibility rules as are applied to senior managers generally. The Company shall, if possible, waive any waiting period applicable to the Executive under any benefit plan.

SECTION 5. DISABILITY OF THE EXECUTIVE. If the Executive is incapacitated or disabled by accident, sickness or otherwise so as to render the Executive mentally or physically incapable of performing the services required to be performed under this Agreement for a period of 90 consecutive days or 120 days in any period of 360 consecutive days (a "Disability"), the Company may, at the time or during the period of such Disability, at its option, terminate the employment of the Executive under this Agreement immediately upon giving the Executive written notice to that effect.

#### SECTION 6. TERMINATION.

6.1 WITH CAUSE. The Company may terminate the employment of the Executive and all of the Company's obligations under this Agreement at any time for Cause (as hereinafter defined) by giving the Executive notice of such termination, with reasonable specificity of the details thereof. "Cause" shall include, without limitation, the following:

(i) failure or neglect, by the Executive to perform the duties of the Executive's position;

(ii) failure of the Executive to obey orders given by the Company or his supervisors;

(iii) misconduct by the Executive in connection with the performance of any of his duties, including, without limitation, misappropriation of funds or property of the

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Company, securing or attempting to secure personally any profit in connection with any transaction entered into on behalf of the Company, misrepresentation to the Company, or any violation of law or regulations on Company premises or to which the Company is subject;

(iv) commission by the Executive of an act involving moral turpitude, dishonesty, theft or unethical business conduct, or conduct which impairs or injures the reputation of, or harms, the Company;

(v) disloyalty by the Executive, including without limitation, aiding a competitor;

(vi) failure by the Executive to devote his full time and best efforts to the Company's business and affairs;

(vii) failure by the Executive to work exclusively for the Company;

(viii) failure to fully cooperate in any investigation by the Company;

(ix) any breach of this Agreement or Company rules;

(x) any other act of misconduct by the Executive;

(xi) the Executive's abuse of alcohol or other drugs or controlled substances; or

(xii) the Executive's death or resignation hereunder; provided however, that if the Executive resigned for Good Reason (as hereinafter defined) or in connection with a Change of Control (as hereinafter defined) in accordance with Section 6.3, such resignation shall not be considered "Cause" hereunder. A termination pursuant to this Section 6.1 shall take effect 10 days after the giving of written notice to the Executive unless the Executive shall, during such 10-day period, remedy to the reasonable satisfaction of the Board of Directors of the Company the misconduct, disregard, abuse or breach specified in such notice; provided, however, that such termination shall take effect immediately upon the giving of such notice if the Board of Directors of the Company shall, in its reasonable discretion, have determined that such misconduct, disregard, abuse or breach is not remediable (which determination shall be stated in such notice).

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6.2 WITHOUT CAUSE. The Company may terminate the employment of the Executive and all of the Company's obligations under this Agreement (except as hereinafter provided) at any time during the Term without Cause by giving the Executive written notice of such termination, to be effective 10 days following the giving of such written notice.

6.3 CHANGE OF CONTROL. The Executive may terminate this Agreement by delivering written notice to the Company within six (6) months following the effective date of a Change of Control. As used herein, the term "Change of Control" shall mean: (i) when any "person" as defined in Section 3(a)(9) of the Securities and Exchange Act of 1934, as amended (the "Exchange Act"), and as used in Section 13(d) and 14(d) thereof, including a "group" as defined in Section 13(d) of the Exchange Act, but excluding the Company or any subsidiary or any affiliate of the Company or any employee benefit plan sponsored or maintained by the Company or any subsidiary of the Company (including any trustee of such plan acting as trustee), becomes the "beneficial owner" (as defined in Rule 13d-3 under the Exchange Act) of securities of the Company representing more than 50% of the combined voting power of the Company's then outstanding securities; or (ii) when, during any period of twenty-four (24) consecutive months, the individuals who, at the beginning of such period,



constitute the Board of Directors (the "Incumbent Directors") cease for any reason other than death to constitute at least a majority thereof, provided, however, that a director who was not a director at the beginning of such 24-month period shall be deemed to have satisfied such 24-month requirement (and be an Incumbent Director) if such director was elected by, or on the recommendation of or with the approval of, at least two-thirds of the directors who then qualified as Incumbent Directors either actually (because they were directors at the beginning of such 24-month period) or through the operation of this proviso; or (iii) the occurrence of a transaction requiring stockholder approval under applicable state law for the acquisition of the Company by an entity other than the Company or a subsidiary or an affiliated company of the Company through purchase of assets, or by merger, or otherwise.

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6.4 WITH GOOD REASON. The Executive may terminate his employment hereunder (and the Term) for Good Reason after the occurrence of such event constituting a material breach of this Agreement by the Company that has not been fully cured within ten (10) days after written notice thereof has been given by the Executive to the Company. "Good Reason" shall mean the occurrence of any of the following without the written consent of the Executive of his approval: (i) the assignment to Executive of duties inconsistent with the Agreement or a change in his title or authority; (ii) any change in reporting responsibility so that Executive reports to any person other than the President of the Company; (iii) the requirement of the Executive to relocate to a location outside the Dallas/Forth Worth metropolitan area; or (iv) any material breach of the Agreement by the Company.

For convenience of reference, the date upon which any termination of the employment of the Executive pursuant to Sections 5 or 6 shall be effective shall be hereinafter referred to as the "Termination Date".

#### SECTION 7. EFFECT OF TERMINATION OF EMPLOYMENT.

7.1 WITH CAUSE. Upon the termination of the Executive's employment for Cause, neither the Executive nor the Executive's beneficiaries or estate shall have any further rights to compensation under this Agreement or any claims against the Company arising out of this Agreement, except the right to receive (i) the unpaid portion of the Base Salary provided for in Section 4.1, earned through the Termination Date (the "Unpaid Salary Amount"), (ii) reimbursement for any expenses for which the Executive shall not have theretofore been reimbursed, as provided in Section 4.6 (the "Expense Reimbursement Amount") and (iii) payment for accrued and unused vacation time (the "Vacation Amount"). All options granted to the Executive shall terminate on the Termination Date, except in the event that the Executive has been terminated for Cause due to Executive's death or resignation, in which case the Executive's right to exercise his vested options shall expire ninety (90) days after the Termination Date.

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7.2. FOR DISABILITY. Upon the termination of the Executive's employment as a result of a Disability, neither the Executive nor the Executive's beneficiaries or estate shall have any further rights to compensation under this Agreement or any claims against the Company arising out of this Agreement, except the right to receive (i) the Unpaid Salary Amount, (ii) the Expense Reimbursement Amount and (iii) the Vacation Amount. Following a termination for a Disability, the Executive's right to exercise his vested options shall not expire until ninety (90) days after the Termination Date.

7.3 WITHOUT CAUSE OR FOR GOOD REASON. Upon the termination of the Executive's employment by the Company without Cause (and not as a result of a Disability) or by the Executive for Good Reason, neither the Executive nor the Executive's beneficiaries or estate shall have any further rights to compensation under this Agreement or any claims against the Company arising out of this Agreement, except the Executive shall have the right to receive (i) the Unpaid Salary Amount, (ii) the Expense Reimbursement Amount, and (iii) the Vacation Amount, and (iv) severance compensation equal to the then Base Salary for six (6) months if such Termination Date is on or before January 31, 2005, or twelve (12) months if such Termination Date is on or after February 1, 2005, all of which is payable within thirty (30) days following the Termination Date. The Executive shall not be entitled to receive any severance payment until and after (i) he has consulted with qualified independent legal counsel regarding

his employment and termination with the Company, (ii) he has executed a full general release of all claims against the Company, its affiliates, officers, directors, employees, agents and representatives, in form and substance satisfactory to the Company, and delivered such general release to the Company, and (iii) all applicable waiting periods, if any, with respect to the irrevocable nature of the general release has have elapsed. Following a termination not for Cause or by the Executive for Good Reason, the Executive's right to exercise his vested options shall not expire until ninety (90) days after the Termination Date (collectively, the "General Release Requirement").

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7.4 CHANGE OF CONTROL. Upon the termination of this Agreement by the Executive in connection with a Change of Control and in accordance with Section 6.3, neither the Executive nor the Executive's beneficiaries or estate shall have any further rights to compensation under this Agreement or any claims against the Company arising out of this Agreement, except the Executive shall have the right to receive (i) the Unpaid Salary Amount, (ii) the Expense Reimbursement Amount, (iii) the Vacation Amount, and (iv) severance compensation equal to the Base Salary for the greater of (x) the remaining term of this Agreement (as if this Agreement was not terminated) and (y) two (2) years. The Executive shall not be entitled to receive any severance payment until and after he has complied with the General Release Requirement. For the purpose of defining the Executive's right to stock options, the Executive's termination of employment for a Change of Control shall be equivalent to an involuntary termination of employment. The Executive's right to his vested options shall not expire until ninety (90) days after the Termination Date.

#### SECTION 8. RESTRICTIVE COVENANTS.

8.1 CERTAIN DEFINITIONS. For purposes of this Section 8, the following terms shall have the following meanings:

"COMPETITIVE ACTIVITY" means any activity conducted in the Restricted Area which competes with any substantial aspect or part of Employer's business whether as a proprietor, partner, shareholder, owner, member, employer, employee, independent contractor, venturer or otherwise.

"COMPETITOR" means any Person, other than Employer or its successor, which at any time during the Restriction Period engages in any Competitive Activity.

"CONFIDENTIAL INFORMATION" means all information of or relating to Employer, its business or practice, which is not generally known or available to the public (whether or not in written or tangible form) including, without limitation, customer lists,

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supplier lists, processes, know-how, trade secrets, pricing policies and other confidential business information.

"CONFIDENTIAL MATERIALS" means any and all documents, records, reports, lists, notes, plans, materials, customer lists, distributor lists, programs, software, disks, recordings, manuals, correspondence, memoranda, magnetic media or any other tangible media (including, without limitation, copies or reproductions of any of the foregoing) in which any Confidential Information may be contained.

"EMPLOYER" means Parent, Employer and its Subsidiaries, whether now or in the future.

"PERSON" means an individual, proprietorship, partnership, joint venture, corporation, limited liability company, association, trust, estate, unincorporated organization, a government or any branch, subdivision, department or agency thereof, or any other entity.

"PERSONNEL" means any and all employees, contractors, agents, consultants or other Persons rendering services to Employer for compensation in any form, whether employed by or independent of Employer.

"RESTRICTED AREA" means the United States, Canada and Asia and their respective territories and possessions, and worldwide with respect to any

Competitive Activity involving the Internet, World Wide Web, telemarketing or other electronic or similar media.

"RESTRICTION PERIOD" means the period of time, commencing on the date hereof and expiring two (2) years after the termination of Executive's employment with Employer pursuant to this Agreement, voluntarily or involuntarily, for any reason whatsoever, subject to extension pursuant to Section 8.6 below.

## 8.2 CONFIDENTIALITY.

(a) CONFIDENTIAL INFORMATION. Subject to Section 8.2(c):

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(1) DUTY TO MAINTAIN CONFIDENTIALITY. Executive shall maintain in strict confidence and duly safeguard to the best of his ability any and all Confidential Information in his possession or under his control.

(2) COVENANT NOT TO DISCLOSE, USE OR EXPLOIT. Except as reasonably necessary to perform his duties, Executive shall not, directly or indirectly, disclose, divulge or otherwise communicate to anyone or use or otherwise exploit for the benefit of anyone, other than Employer, any Confidential Information.

(3) CONFIDENTIAL MATERIALS. All Confidential Information and Confidential Materials are and shall remain the exclusive property of Employer and no Confidential Materials may be copied or otherwise reproduced, removed from the premises of Employer or entrusted to any Person (other than Employer or the Personnel entitled to such materials) by Executive, except as reasonably necessary to perform his duties, without prior written permission from Employer.

(b) SURVIVAL OF COVENANTS. Notwithstanding anything herein to the contrary, the covenants set forth in this Section 8.2 shall survive the termination of this Agreement and any other agreement among any or all of the parties hereto (regardless of the reason for such termination), unless terminated by a written instrument that expressly terminates by specific reference the covenants set forth in this Section 8.2.

(c) PERMITTED ACTIVITIES. If Executive receives a request or demand for Confidential Information (whether pursuant to a discovery request, subpoena or otherwise), Executive shall immediately give Employer written notice thereof and shall exert his best efforts to resist disclosure, within the limits of the law, including, without limitation, by fully cooperating and assisting Employer in whatever efforts it may make to resist or limit disclosure or to obtain a protective order or other appropriate remedy to limit or prohibit further disclosure or use of such Confidential Information. If Executive complies with the preceding sentence but nonetheless becomes legally compelled to disclose Confidential

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Information, Executive shall disclose only that portion of the Confidential Information that he is legally compelled to disclose.

8.3 COVENANT NOT TO COMPETE. During the Restriction Period, Executive shall not, directly or indirectly, whether as a sole practitioner, owner, partner, shareholder, investor, employee, employer, venturer, independent contractor, consultant or other participant, (i) own, manage, invest in or acquire any economic stake or interest in any Person involved in a Competitive Activity, (ii) derive economic benefit from or with respect to any Competitive Activity or (iii) otherwise engage or participate in any manner whatsoever in any Competitive Activity; provided, however, this Section 8.3 shall not restrict Executive from owning less than 2% of the publicly traded debt or equity securities issued by a corporation or other entity or from having any other passive investment that creates no conflict of loyalty or interest with any duty owed to Employer. Executive shall be deemed to have derived economic benefit in violation of this Section 8.3 if, among other things, any of his compensation or income is in any way related to any Competitive Activity conducted by any Person. Further, during the Restriction Period Executive shall not directly or indirectly advance, cooperate in or help or aid any Competitor in the conduct of any Competitive Activity.

8.4 COVENANT NOT TO INTERFERE. During the Restriction Period, Executive shall not, directly or indirectly, recruit, solicit or otherwise induce or influence any Personnel of Employer to discontinue, reduce the extent of, discourage the development of or otherwise harm such Personnel's relationship or commitment to Employer. Conduct prohibited under this Section 8.4 shall include, without limitation, seeking to employ or causing, aiding, inducing or influencing a Competitor to employ or seek to employ any Personnel of Employer.

8.5 EQUITABLE RELIEF. Each of the parties acknowledges that the provisions and restrictions of this Section 8 are reasonable and necessary for the protection of the legitimate interests of Employer. Each of the parties further acknowledges that the

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provisions and restrictions of this Section 6 are unique and that any breach or threatened breach of any of such provisions or restrictions will provide Employer with no adequate remedy at law, and the result will be irreparable harm to Employer. Therefore, the parties hereto agree that upon a breach or threatened breach of the provisions or restrictions of this Section 8, Employer shall be entitled, in addition to any other rights and remedies which may be available to it, to institute and maintain proceedings at law or in equity, to recover damages, to obtain an equitable accounting of all earnings, profits or other benefits resulting from such breach or threatened breach and to obtain specific performance or a temporary and permanent injunction.

8.6 FULL RESTRICTION PERIOD. If Executive violates any restrictive covenant contained herein and Employer institutes action for equitable relief, Employer, as a result of the time involved in obtaining such relief, shall not be deprived of the benefit of the full Restriction Period. Accordingly, the Restriction Period shall be deemed to have the duration specified in Section 8.1, computed from and commencing on the date on which relief is granted by a final order from which there is no appeal, but reduced, if applicable, by the length of time between the date the Restriction Period commenced and the date of the first violation of any restrictive covenant by Executive.

8.7 EQUITABLE ACCOUNTING. Employer shall have the right to demand and receive equitable accounting with respect to any consideration received by Executive in connection with activities in breach of the restrictive covenants herein, and Employer shall be entitled to payment from Executive of such consideration on demand.

8.8 PRIOR BREACHES. Neither the expiration of the Restriction Period nor the termination of the status of any Customer or Personnel as such (whether or not due to a breach hereof by Executive) shall preclude, limit or otherwise affect the rights and remedies of Employer against Executive based upon any breach hereof during the Restriction Period or before such status of Customer or Personnel terminated.

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8.9 NONCIRCUMVENTION OF COVENANTS. Executive acknowledges and agrees that, for purposes of this Agreement, an action shall be considered to have been taken by Executive "indirectly" if taken by or through, with Executive's knowledge, (a) any member of his immediate family, (b) any Person owned or controlled, solely or with others, directly or "indirectly" by Executive or a member of his family, (c) any Person of which he is an owner, partner, employer, employee, trustee, independent contractor or agent, (d) any employees, partners, owners or independent contractors of any such Person or (e) any other one or more representatives or intermediaries, it being the intention of the parties that Executive shall not directly or indirectly circumvent any restrictive covenant contained herein or the intent thereof.

8.10 NOTICE OF RESTRICTIONS. During the Restriction Period, Executive shall notify each prospective employer, partner or co-venturer of the restrictions contained in this Agreement. Employer is hereby authorized to contact any of such Persons for the purpose of providing notice of such restrictions.

8.11 REDUCTION OF RESTRICTIONS BY COURT ACTION. Each of the provisions hereof including, without limitation, the periods of time, geographic

areas and types and scopes of duties of, and restrictions on the activities of, the parties hereto specified herein are and are intended to be divisible, and if any portion thereof (including any sentence, clause or word) shall be held contrary to law or invalid or unenforceable in any respect in any jurisdiction, or as to one or more periods of time, areas or business activities or any part thereof, the remaining provisions shall not be affected but shall remain in full force and effect, and any such invalid or unenforceable provision shall be deemed, without further action on the part of any party hereto or other Person, modified and amended to the minimum extent necessary to render the same valid and enforceable in such jurisdiction.

8.12 FAIRNESS OF RESTRICTIONS. Executive acknowledges and agrees that (a) compliance with the restrictive covenants set forth herein would not prevent him from earning a living that involves his training and skills without relocating, but only from

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engaging in unfair competition with, misappropriating a corporate opportunity of, or otherwise unfairly harming Employer and (b) the restrictive covenants set forth herein are intended to provide a minimum level of protection necessary to protect the legitimate interests of Employer. In addition, the parties acknowledge that nothing herein is intended to or shall, limit, replace or otherwise affect any other rights or remedies at law or in equity for protection against unfair competition with, misappropriation of corporate opportunities of, disclosure of confidential and proprietary information of, or defamation of Employer, or for protection of any other rights or interest of Employer.

#### SECTION 9. MISCELLANEOUS.

9.1 GOVERNING LAW. THIS AGREEMENT SHALL BE DEEMED TO BE A CONTRACT MADE UNDER THE LAWS OF TEXAS AND FOR ALL PURPOSES SHALL BE CONSTRUED IN ACCORDANCE WITH THE LAWS OF SAID STATE APPLICABLE TO CONTRACTS MADE AND TO BE PERFORMED WITHIN SAID STATE.

9.2 ENTIRE AGREEMENT. This Agreement (together with the exhibits attached hereto, which hereby are incorporated by reference) contains the entire agreement of the parties hereto relating to the employment of Executive by the Company and the other matters discussed herein and supersedes all prior agreements and understandings with respect to such subject matter, and the parties hereto have made no agreements, representations or warranties relating to the subject matter of this Agreement which are not set forth herein.

9.3 WITHHOLDING TAXES. The Company may withhold from any compensation or other benefits payable under this Agreement all federal, state, city or other taxes as shall be required pursuant to any law or governmental regulation or ruling.

9.4 SUPPLEMENTS AND AMENDMENTS. This Agreement may be supplemented or amended only upon the written consent of each of the parties hereto.

9.5 ASSIGNMENT. Except as expressly provided below, this Agreement shall not be assignable, in whole or in part, by either party without the prior written consent

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of the other party. The Company may, without the prior written consent of Executive, assign its rights and obligations under this Agreement to any other corporation, firm or other business entity with or into which the Company may merge or consolidate, or to which the Company may sell or transfer all or substantially all of its assets, or of which 50% or more of the equity investment and of the voting control is owned, directly or indirectly, by, or is under common ownership with, the Company; provided, however, that such assignment may be made without Executive's prior written consent only if (a) such assignment has a valid business purpose and is not for the purpose of avoiding the Company's obligations hereunder or Executive's realization of the benefits of this Agreement and (b) the assignee expressly assumes in writing all obligations and liabilities to Executive hereunder. The Company will cause any purchaser of all or substantially all of the assets of the Company, by agreement in form and substance reasonably satisfactory to Executive, to expressly assume and agree to perform this Agreement in the same manner and to the same extent

that the Company would be required to perform it if no such purchase had taken place. This Agreement shall be binding upon and inure to the benefit of the Company and their respective successors and permitted assigns. This Agreement and all rights of Executive hereunder shall inure to the benefit of and be enforceable by Executive's heirs, personal or legal representatives and beneficiaries. If this Agreement is terminated pursuant to clause (a) of Section 8.1 hereof, all amounts payable pursuant to clause (a) of Section 8.2 hereof shall be paid to Executive's designated beneficiaries or, if no such beneficiaries have been designated, to Executive's estate.

9.6 NO WAIVER. No term or condition of this Agreement shall be deemed to have been waived, nor shall there be any estoppel to enforce any provisions of this Agreement, except by a statement in writing signed by the party against whom enforcement of the waiver or estoppel is sought. Any written waiver shall not be deemed a continuing waiver unless specifically stated, shall operate only as to the specific term or condition

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waived and shall not constitute a waiver of such term or condition for the future or as to any act other than that specifically waived.

9.7 SEVERABILITY. The provisions of this Agreement are severable, and if any one or more provisions may be determined to be judicially unenforceable and/or invalid by a court of competent jurisdiction, in whole or in part, the remaining provisions shall nevertheless be binding, enforceable and in full force and effect.

9.8 TITLES AND HEADINGS. The titles and headings of the various Sections of this Agreement are intended solely for convenience of reference and not intended for any purpose whatsoever to explain, modify or place any construction upon any of the provisions hereof.

9.9 ATTORNEYS' FEES. In the event that any party hereto brings suit against the other party, based upon or arising out of a breach or violation of this Agreement, each party hereto agrees that the party who is successful on the merits, upon final adjudication from which no further appeal can be taken or is taken within the time allowed by law, shall be entitled to recover his or its reasonable attorneys, fees and expenses from the party which is not successful.

9.10 INJUNCTIVE RELIEF. Executive agrees that it would be difficult to compensate the Company fully for damages for any violation of the provisions of Sections 6 and 8.3 hereof. Accordingly, Executive specifically agrees that the Company shall be entitled to temporary and permanent injunctive relief to enforce such provisions of this Agreement. This provision with respect to injunctive relief shall not, however, diminish the right of the Company to claim and recover damages in addition to injunctive relief.

9.11 NOTICES. For the purpose of this Agreement, notices and all other communications provided for in this Agreement shall be in writing and shall be deemed to have been duly given when hand delivered (which shall include personal delivery and delivery by courier, messenger or overnight delivery service) or mailed by certified mail, return receipt requested, postage prepaid, addressed as follows:

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If to Executive: At his home address in accordance with the Company's records.

If to the Company:

Natural Health Trends Corp.  
12901 Hutton Drive  
Dallas, Texas 75234  
Attention: President

If to the Executive:

Chris Sharn  
1352 Saddlebrook Court  
Bartonville, Texas 76226

or to such other address of which either party gives notice to the other party in accordance herewith, except that notices of change of address shall be effective only upon receipt.

9.12 COUNTERPARTS. This Agreement may be executed in any number of counterparts and each of such counterparts shall for all purposes be deemed to be an original, and all such counterparts shall together constitute but one and the same instrument.

9.13 JURISDICTION. Each of the parties hereto hereby irrevocably consents and submits to the exclusive jurisdiction of the courts of the State of Texas, located in Dallas County, and of the United States District Court for the Northern District of Texas in connection with any suit, action or other proceeding concerning the interpretation of this Agreement or enforcement of Sections 8 or 9 of this Agreement. The Executive waives and agrees not to assert any defense that the court lacks jurisdiction, venue is improper, inconvenient forum or otherwise. The Executive waives the right to a jury trial and agrees to accept service of process by certified mail at the Executive's last known address.

9.14 POST EMPLOYMENT OBLIGATIONS. (a) All records, files, lists, including computer generated lists, drawings, documents, equipment and similar items relating to the Company's business which the Executive shall prepare or receive from the Company shall remain the Company's sole and exclusive property. Upon termination of this Agreement, the

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Executive shall promptly return to the Company all property of the Company in his possession. The Executive further represents that he will not copy or cause to be copied, print out or cause to be printed out any software, documents or other materials originating with or belonging to the Company. The Executive additionally represents that, upon termination of his employment with the Company, he will not retain in his possession any such software, documents or other materials.

(b) The Executive agrees that both during and after his employment he shall, at the request of the Company, render all assistance and perform all lawful acts that the Company considers necessary or advisable in connection with any litigation involving the Company or any director, officer, employee, shareholder, agent, representative, consultant, client or vendor of the Company.

IN WITNESS WHEREOF, the parties hereto have executed this Agreement as of the date set forth above.

NATURAL HEALTH TRENDS CORP.

By: \_\_\_\_\_  
Name:  
Title:

\_\_\_\_\_  
Chris Sharng

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EXHIBIT 10.2

[EXECUTION COPY]

FORM OF REGISTRATION RIGHTS AGREEMENT

REGISTRATION RIGHTS AGREEMENT (this "AGREEMENT"), dated as of October 6, 2004, by and among Natural Health Trends Corp. a Florida corporation, with headquarters located at 1201 Hutton Drive, Dallas, Texas 75234 (the "COMPANY"), and the undersigned buyers (each, a "BUYER" and collectively, the "BUYERS").

WHEREAS:

A. In connection with (i) the Securities Purchase Agreement and (ii) the Subscription Agreements, by and among the Company and the parties hereto of even date herewith (the "PURCHASE AGREEMENTS"), the Company has agreed, upon the terms and subject to the conditions of the Purchase Agreements, to issue and sell to each Buyer units ("UNITS") consisting of (i) shares (the "COMMON SHARES") of the Company's common stock, par value \$0.001 per share (the "COMMON STOCK"), and (ii) common stock purchase warrants (the "WARRANTS") exercisable for shares of Common Stock (the "WARRANT SHARES");

B. To induce the Buyers to execute and deliver the Purchase Agreements, the Company has agreed to provide certain registration rights under the Securities Act of 1933, as amended, and the rules and regulations thereunder, or any similar successor statute (collectively, the "1933 ACT"), and applicable state securities laws.

NOW, THEREFORE, in consideration of the premises and the mutual covenants contained herein and other good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, the Company and each of the Buyers hereby agree as follows:

1. Definitions.

As used in this Agreement, the following terms shall have the following meanings:

a. "BUSINESS DAY" means any day other than Saturday, Sunday or any other day on which commercial banks in The City of New York are authorized or required by law to remain closed.

b. "INVESTOR" means a Buyer, any transferee or assignee thereof to whom a Buyer assigns its rights under this Agreement and who agrees to become bound by the provisions of this Agreement in accordance with Section 9 and any transferee or assignee thereof to whom a transferee or assignee assigns its rights under this Agreement and who agrees to become bound by the provisions of this Agreement in accordance with Section 9.

c. "PERSON" means an individual, a limited liability company, a partnership, a joint venture, a corporation, a trust, an unincorporated organization and governmental or any department or agency thereof. a.

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d. "REGISTER," "REGISTERED," and "REGISTRATION" refer to a registration effected by preparing and filing one or more Registration Statements (as defined below) in compliance with the 1933 Act and pursuant to Rule 415 and the declaration or ordering of effectiveness of such Registration Statement(s) by the SEC.

e. "REGISTRABLE SECURITIES" means (i) the Common Shares included in the Units, (ii) the Warrant Shares issued or issuable upon exercise of the Warrants, and (iii) any shares of capital stock issued or issuable with respect to the Common Shares, the Warrant Shares or the Warrants as a result of any stock split, stock dividend, recapitalization, exchange or similar event or otherwise.

f. "REGISTRATION STATEMENT" means a registration statement or registration statements of the Company filed under the 1933 Act



covering the Registrable Securities.

g. "RULE 415" means Rule 415 under the 1933 Act or any successor rule providing for offering securities on a continuous or delayed basis.

h. "SEC" means the United States Securities and Exchange Commission.

Capitalized terms used herein and not otherwise defined herein shall have the respective meanings set forth in the Purchase Agreements.

## 2. Registration.

a. Initial Mandatory Registration. The Company shall prepare, and, as soon as practicable but in no event later than 60 days after the Closing Date (as defined in the Purchase Agreements) (the "FILING DEADLINE"), file with the SEC the Registration Statement on Form S-1 covering the resale of all Registrable Securities. The Registration Statement shall contain (except if otherwise directed by the holders of at least a majority of the Registrable Securities) the "Selling Stockholders" section in substantially the form attached hereto as Exhibit B and the "Plan of Distribution" section attached hereto as Exhibit B. The Company shall use its best efforts to have the Registration Statement declared effective by the SEC as soon as practicable, but in no event later than the date which is 180 days after the Closing Date (the "EFFECTIVENESS DEADLINE").

b. Allocation of Registrable Securities. The initial number of Registrable Securities included in any Registration Statement and each increase in the number of Registrable Securities included therein shall be allocated pro rata among the Investors based on the number of Registrable Securities held by each Investor at the time the Registration Statement covering such initial number of Registrable Securities or increase thereof is declared effective by the SEC. In the event that an Investor sells or otherwise transfers any of such Investor's Registrable Securities, each transferee shall be allocated a pro rata portion of the then remaining number of Registrable Securities included in such Registration Statement for such transferor. Any shares of Common Stock included in a Registration Statement and which remain allocated to any Person which ceases to hold any Registrable Securities covered by such Registration Statement shall be allocated to the remaining Investors, pro rata based on the number of

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Registrable Securities then held by such Investors which are covered by such Registration Statement. The Company may include Company securities held by other security holders on any Registration Statement without the prior written consent of Buyers.

c. Legal Counsel. Subject to Section 5 hereof, the Buyers holding at least a majority of the Registrable Securities shall have the right to select one legal counsel to review and oversee any registration pursuant to this Section 2 ("LEGAL COUNSEL"), which shall be Bass Berry & Sims PLC, or such other counsel as thereafter designated by the holders of at least a majority of the Registrable Securities. The Company and Legal Counsel shall reasonably cooperate with each other in performing the Company's obligations under this Agreement.

d. Effect of Failure to File and Obtain and Maintain Effectiveness of Registration Statement. If (i) a Registration Statement covering all the Registrable Securities required to be covered thereby and required to be filed by the Company pursuant to this Agreement is not declared effective by the SEC on or before the Effectiveness Deadline or (ii) on any day after such Registration Statement has been declared effective by the SEC sales of all the Registrable Securities required to be included on such Registration Statement cannot be made (other than during an Allowable Grace Period (as defined in Section 3(l)) pursuant to such Registration Statement (including, without limitation, because of a failure to keep such Registration Statement effective, to disclose such information as is necessary for sales to be made pursuant to such Registration Statement or to register sufficient shares of Common Stock), then, as full and entire relief for any damages to any holder by reason of any such delay in or reduction of its ability to sell any Registrable Securities, the Company shall pay to each holder of Registrable Securities an

amount in cash equal to the product of (i) the Purchase Price paid by such Buyer (as such term is defined in the Purchase Agreements) multiplied by (ii) 0.005. The payment to which a holder shall be entitled pursuant to this Section 2(d) is referred to herein as a "REGISTRATION DELAY PAYMENT." A Registration Delay Payment shall be paid on the last day of the calendar quarter during which such Registration Delay Payment is incurred. In the event the Company fails to make a Registration Delay Payment in a timely manner, such Registration Delay Payment shall bear interest at the rate of 10% per annum until paid in full. A Registration Delay Payment due and owing by the Company to an Investor shall be Investor's sole remedy for a breach by the Company of its obligations under Section 2 of this Agreement.

### 3. Related Obligations.

At such time as the Company is obligated to file a Registration Statement with the SEC pursuant to Section 2(a), the Company will use commercially reasonable efforts to effect the registration of the Registrable Securities in accordance with the intended method of disposition thereof and, pursuant thereto, the Company shall have the following obligations:

a. The Company shall submit to the SEC, within ten (10) Business Days after the Company learns that no review of the Registration Statement will be made by the staff of the SEC or that the staff has no further comments on the Registration Statement, as the case may be, a request for acceleration of effectiveness of such Registration Statement to a time and date not later than 48 hours after the submission of such request. The Company shall keep the Registration Statement effective pursuant to Rule 415 at all times until the earlier of (i) the date as of which the Investors may sell all of the Registrable Securities covered by such

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Registration Statement without restriction pursuant to Rule 144(k) (or successor thereto) promulgated under the 1933 Act or (ii) the date on which the Investors shall have sold all the Registrable Securities covered by such Registration Statement (the "REGISTRATION PERIOD").

b. The Company shall prepare and file with the SEC such amendments (including post-effective amendments) and supplements to a Registration Statement and the prospectus used in connection with such Registration Statement, which prospectus is to be filed pursuant to Rule 424 promulgated under the 1933 Act, as may be necessary to keep such Registration Statement effective at all times during the Registration Period, and, during such period, comply with the provisions of the 1933 Act with respect to the disposition of all Registrable Securities of the Company covered by such Registration Statement until such time as all of such Registrable Securities shall have been disposed of in accordance with the intended methods of disposition by the seller or sellers thereof as set forth in such Registration Statement. In the case of amendments and supplements to a Registration Statement which are required to be filed pursuant to this Agreement (including pursuant to this Section 3(b)) by reason of the Company filing a report on Form 10-K, Form 10-Q or Form 8-K or any analogous report under the Securities Exchange Act of 1934, as amended (the "1934 ACT"), the Company shall have incorporated such report by reference into such Registration Statement, if applicable, or shall file such amendments or supplements with the SEC on the same day on which the 1934 Act report is filed which created the requirement for the Company to amend or supplement such Registration Statement.

c. The Company shall (A) permit Legal Counsel to review and comment upon (i) a Registration Statement at least five (5) days prior to its filing with the SEC and (ii) all amendments and supplements to all Registration Statements (except for Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q and Current Reports on Form 8-K and any similar or successor reports) within a reasonable number of days prior to their filing with the SEC, and (B) not file any Registration Statement or amendment or supplement thereto in a form to which Legal Counsel reasonably objects. The Company shall not submit a request for acceleration of the effectiveness of a Registration Statement or any amendment or supplement thereto without the prior approval of Legal Counsel, which consent shall not be unreasonably withheld. The Company shall furnish to Legal Counsel, without charge, (i) copies of any correspondence from the SEC or the staff of the SEC to the Company or its representatives relating to any Registration Statement, (ii) promptly after the same is prepared and filed with the SEC, one copy of any Registration Statement and any

amendment(s) thereto, including financial statements and schedules, all documents incorporated therein by reference, if requested by an Investor, and all exhibits and (iii) upon the effectiveness of any Registration Statement, one copy of the prospectus included in such Registration Statement and all amendments and supplements thereto. The Company shall reasonably cooperate with Legal Counsel in performing the Company's obligations pursuant to this Section 3.

d. The Company shall furnish to each Investor whose Registrable Securities are included in any Registration Statement, without charge, (i) upon the effectiveness of any Registration Statement, five (5) copies of the prospectus included in such Registration Statement and all amendments and supplements thereto (or such other number of copies as such Investor may reasonably request) and (ii) such other documents, including copies of any

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preliminary or final prospectus, as such Investor may reasonably request from time to time in order to facilitate the disposition of the Registrable Securities owned by such Investor.

e. The Company shall use its best efforts to (i) register and qualify, unless an exemption from registration and qualification applies, the resale by Investors of the Registrable Securities covered by a Registration Statement under such other securities or "blue sky" laws of all applicable jurisdictions in the United States, (ii) prepare and file in those jurisdictions, such amendments (including post-effective amendments) and supplements to such registrations and qualifications as may be necessary to maintain the effectiveness thereof during the Registration Period, (iii) take such other actions as may be necessary to maintain such registrations and qualifications in effect at all times during the Registration Period, and (iv) take all other actions reasonably necessary or advisable to qualify the Registrable Securities for sale in such jurisdictions; provided, however, that the Company shall not be required in connection therewith or as a condition thereto to (x) qualify to do business in any jurisdiction where it would not otherwise be required to qualify but for this Section 3(e), (y) subject itself to general taxation in any such jurisdiction, or (z) file a general consent to service of process in any such jurisdiction. The Company shall promptly notify Legal Counsel and each Investor who holds Registrable Securities of the receipt by the Company of any notification with respect to the suspension of the registration or qualification of any of the Registrable Securities for sale under the securities or "blue sky" laws of any jurisdiction in the United States or its receipt of actual notice of the initiation or threatening of any proceeding for such purpose.

f. The Company shall notify Legal Counsel and each Investor in writing of the happening of any event, as promptly as practicable after becoming aware of such event, as a result of which the prospectus included in a Registration Statement, as then in effect, includes an untrue statement of a material fact or omission to state a material fact required to be stated therein or necessary to make the statements therein, in the light of the circumstances under which they were made, not misleading (provided that in no event shall such notice contain any material, nonpublic information), and, subject to Section 3(l), promptly prepare a supplement or amendment to such Registration Statement to correct such untrue statement or omission, and deliver ten (10) copies of such supplement or amendment to Legal Counsel and each Investor (or such other number of copies as Legal Counsel or such Investor may reasonably request). The Company shall also promptly notify Legal Counsel and each Investor in writing (i) when a prospectus or any prospectus supplement or post-effective amendment has been filed, and when a Registration Statement or any post-effective amendment has become effective (notification of such effectiveness shall be delivered to Legal Counsel and each Investor by facsimile on the same day of such effectiveness and by overnight mail), (ii) of any request by the SEC for amendments or supplements to a Registration Statement or related prospectus or related information, and (iii) of the Company's reasonable determination that a post-effective amendment to a Registration Statement would be appropriate.

g. The Company shall use its best efforts to prevent the issuance of any stop order or other suspension of effectiveness of a Registration Statement, or the suspension of the qualification of any of the Registrable Securities for sale in any jurisdiction and, if such an order or

suspension is issued, to obtain the withdrawal of such order or suspension at the earliest possible moment and to notify Legal Counsel and each Investor who holds Registrable Securities

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being sold of the issuance of such order and the resolution thereof or its receipt of actual notice of the initiation or threat of any proceeding for such purpose.

h. The Company shall hold in confidence and not make any disclosure of information concerning an Investor provided to the Company unless (i) disclosure of such information is necessary to comply with federal or state securities laws, (ii) the disclosure of such information is necessary to avoid or correct a misstatement or omission in any Registration Statement, (iii) the release of such information is ordered pursuant to a subpoena or other final, non-appealable order from a court or governmental body of competent jurisdiction, or (iv) such information has been made generally available to the public other than by disclosure in violation of this Agreement or any other agreement. The Company agrees that it shall, upon learning that disclosure of such information concerning an Investor is sought in or by a court or governmental body of competent jurisdiction or through other means, give prompt written notice to such Investor and allow such Investor, at the Investor's expense, to undertake appropriate action to prevent disclosure of, or to obtain a protective order for, such information.

i. The Company shall cooperate with the Investors who hold Registrable Securities being offered and, to the extent applicable, facilitate the timely preparation and delivery of certificates (not bearing any restrictive legend) representing the Registrable Securities to be offered pursuant to a Registration Statement and enable such certificates to be in such denominations or amounts, as the case may be, as the Investors may reasonably request and registered in such names as the Investors may request.

j. The Company shall use its best efforts to comply with all applicable rules and regulations of the SEC in connection with any registration hereunder.

k. Within five (5) Business Days after a Registration Statement which covers Registrable Securities is ordered effective by the SEC, the Company shall deliver, and shall cause legal counsel for the Company to deliver, to the transfer agent for such Registrable Securities (with copies to the Investors whose Registrable Securities are included in such Registration Statement) confirmation that such Registration Statement has been declared effective by the SEC in the form attached hereto as Exhibit A.

l. Notwithstanding anything to the contrary herein, at any time after the Registration Statement has been declared effective by the SEC, the Company may delay the disclosure of material, non-public information concerning the Company the disclosure of which at the time is not, in the good faith opinion of the Board of Directors of the Company and its counsel, in the best interest of the Company and, in the opinion of counsel to the Company, otherwise required (a "GRACE PERIOD"); provided, that the Company shall promptly (i) notify the Investors in writing of the existence of material, non-public information giving rise to a Grace Period (provided that in each notice the Company will not disclose the content of such material, non-public information to the Investors) and the date on which the Grace Period will begin, and (ii) notify the Investors in writing of the date on which the Grace Period ends; and, provided further, that no Grace Period shall exceed forty-five (45) consecutive days (an "ALLOWABLE GRACE PERIOD") and during any three hundred sixty-five (365) day period there shall be no more than two (2) Allowable Grace Periods.

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#### 4. Obligations of the Investors.

a. At least seven (7) Business Days prior to the first anticipated filing date of a Registration Statement, the Company shall notify each Investor in writing of the information the Company requires from each such Investor if such Investor elects to have any of such Investor's Registrable Securities included in such Registration Statement. It shall be a condition precedent to the obligations of the Company to complete the registration pursuant to this Agreement with respect to the Registrable

Securities of a particular Investor that such Investor shall furnish to the Company such information regarding itself, the Registrable Securities held by it and the intended method of disposition of the Registrable Securities held by it as shall be reasonably required to effect the effectiveness of the registration of such Registrable Securities and shall execute such documents in connection with such registration as the Company may reasonably request.

b. Each Investor, by such Investor's acceptance of the Registrable Securities, agrees to cooperate with the Company as reasonably requested by the Company in connection with the preparation and filing of any Registration Statement hereunder, unless such Investor has notified the Company in writing of such Investor's election to exclude all of such Investor's Registrable Securities from such Registration Statement.

c. Each Investor agrees that, upon receipt of any notice from the Company of the happening of any event of the kind described in Section 3(g) or the first sentence of 3(f), such Investor will immediately discontinue disposition of Registrable Securities pursuant to any Registration Statement(s) covering such Registrable Securities until such Investor's receipt of the copies of the supplemented or amended prospectus contemplated by Section 3(g) or the first sentence of 3(f) or receipt of notice that no supplement or amendment is required. Notwithstanding anything to the contrary, the Company shall cause its transfer agent to deliver unlegended shares of Common Stock to a transferee of an Investor in accordance with the terms of the Purchase Agreements in connection with any sale of Registrable Securities with respect to which an Investor has entered into a contract for sale prior to the Investor's receipt of a notice from the Company of the happening of any event of the kind described in Section 3(g) or the first sentence of 3(f) and for which the Investor has not yet settled.

#### 5. Expenses of Registration.

All reasonable expenses, other than underwriting discounts and commissions, incurred in connection with registrations, filings or qualifications pursuant to Sections 2 and 3, including, without limitation, all registration, listing and qualifications fees, printers and accounting fees, and fees and disbursements of counsel for the Company shall be paid by the Company. The Company shall also reimburse the Investors for the fees and disbursements of Legal Counsel in connection with registration, filing or qualification pursuant to Sections 2 and 3 of this Agreement which amount shall be limited to \$5,000 for the Registration Statement.

#### 6. Indemnification.

In the event any Registrable Securities are included in a Registration Statement under this Agreement:

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a. To the fullest extent permitted by law, the Company will, and hereby does, indemnify, hold harmless and defend each Investor, the directors, officers, members, partners, employees, agents, representatives of, and each Person, if any, who controls any Investor within the meaning of the 1933 Act or the 1934 Act (each, an "INDEMNIFIED PERSON"), against any losses, claims, damages, liabilities, judgments, fines, penalties, charges, costs, reasonable attorneys' fees, amounts paid in settlement or expenses, joint or several, (collectively, "CLAIMS") incurred in investigating, preparing or defending any action, claim, suit, inquiry, proceeding, investigation or appeal taken from the foregoing by or before any court or governmental, administrative or other regulatory agency, body or the SEC, whether pending or threatened, whether or not an indemnified party is or may be a party thereto ("INDEMNIFIED DAMAGES"), to which any of them may become subject insofar as such Claims (or actions or proceedings, whether commenced or threatened, in respect thereof) arise out of or are based upon: (i) any untrue statement or alleged untrue statement of a material fact in a Registration Statement or any post-effective amendment thereto or in any filing made in connection with the qualification of the offering under the securities or other "blue sky" laws of any jurisdiction in which Registrable Securities are offered ("BLUE SKY FILING"), or the omission or alleged omission to state a material fact required to be stated therein or necessary to make the statements therein not misleading, (ii) any untrue statement or alleged untrue statement of a material fact contained in any preliminary prospectus if used prior to the effective date of such Registration Statement, or contained in the final

prospectus (as amended or supplemented, if the Company files any amendment thereof or supplement thereto with the SEC) or the omission or alleged omission to state therein any material fact necessary to make the statements made therein, in the light of the circumstances under which the statements therein were made, not misleading, (iii) any violation or alleged violation by the Company of the 1933 Act, the 1934 Act, any other law, including, without limitation, any state securities law, or any rule or regulation thereunder relating to the offer or sale of the Registrable Securities pursuant to a Registration Statement or (iv) any material violation of this Agreement (the matters in the foregoing clauses (i) through (iv) being, collectively, "VIOLATIONS"). Subject to Section 6(c), the Company shall reimburse the Indemnified Persons, promptly as such expenses are incurred and are due and payable, for any legal fees or other reasonable expenses incurred by them in connection with investigating or defending any such Claim. Notwithstanding anything to the contrary contained herein, the indemnification agreement contained in this Section 6(a): (i) shall not apply to a Claim by an Indemnified Person arising out of or based upon a Violation which occurs in reliance upon and in conformity with information furnished in writing to the Company by such Indemnified Person for such Indemnified Person expressly for use in connection with the preparation of the Registration Statement or any such amendment thereof or supplement thereto, if such prospectus was timely made available by the Company pursuant to Section 3(d); (ii) with respect to any preliminary prospectus, shall not inure to the benefit of any such Person from whom the Person asserting any such Claim purchased the Registrable Securities that are the subject thereof (or to the benefit of any Person controlling such Person) if the untrue statement or omission of material fact contained in the preliminary prospectus was corrected in the prospectus, as then amended or supplemented, if such prospectus was timely made available by the Company pursuant to Section 3(d), and the Indemnified Person was promptly advised in writing not to use the incorrect prospectus prior to the use giving rise to a violation and such Indemnified Person, notwithstanding such advice, used it or failed to deliver the correct prospectus as required by the 1933 Act and such correct prospectus was timely made available pursuant to Section 3(d); (iii)

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shall not be available to the extent such Claim is based on a failure of the Investor to deliver or to cause to be delivered the prospectus made available by the Company, including a corrected prospectus, if such prospectus or corrected prospectus was timely made available by the Company pursuant to Section 3(d); and (iv) shall not apply to amounts paid in settlement of any Claim if such settlement is effected without the prior written consent of the Company, which consent shall not be unreasonably withheld or delayed. Such indemnity shall remain in full force and effect regardless of any investigation made by or on behalf of the Indemnified Person and shall survive the transfer of the Registrable Securities by the Investors pursuant to Section 9.

b. In connection with any Registration Statement in which an Investor is participating, each such Investor agrees to severally and not jointly indemnify, hold harmless and defend, to the same extent and in the same manner as is set forth in Section 6(a), the Company, each of its directors, each of its officers who signs the Registration Statement and each Person, if any, who controls the Company within the meaning of the 1933 Act or the 1934 Act (each, an "INDEMNIFIED PARTY"), against any Claim or Indemnified Damages to which any of them may become subject, under the 1933 Act, the 1934 Act or otherwise, insofar as such Claim or Indemnified Damages arise out of or are based upon any Violation, in each case to the extent, and only to the extent, that such Violation occurs in reliance upon and in conformity with written information furnished to the Company by such Investor expressly for use in connection with such Registration Statement; and, subject to Section 6(c), such Investor will reimburse any legal or other expenses reasonably incurred by an Indemnified Party in connection with investigating or defending any such Claim; provided, however, that the indemnity agreement contained in this Section 6(b) and the agreement with respect to contribution contained in Section 7 shall not apply to amounts paid in settlement of any Claim if such settlement is effected without the prior written consent of such Investor, which consent shall not be unreasonably withheld or delayed; provided, further, however, that the Investor shall be liable under this Section 6(b) for only that amount of a Claim or Indemnified Damages as does not exceed the net proceeds to such Investor as a result of the sale of Registrable Securities pursuant to such Registration Statement. Such indemnity shall remain in full force and effect regardless of any investigation made by or on behalf of such Indemnified Party and shall survive the transfer of the Registrable Securities by the Investors pursuant to

Section 9. Notwithstanding anything to the contrary contained herein, the indemnification agreement contained in this Section 6(b) with respect to any preliminary prospectus shall not inure to the benefit of any Indemnified Party if the untrue statement or omission of material fact contained in the preliminary prospectus was corrected on a timely basis in the prospectus, as then amended or supplemented.

c. Promptly after receipt by an Indemnified Person or Indemnified Party under this Section 6 of notice of the commencement of any action or proceeding (including any governmental action or proceeding) involving a Claim, such Indemnified Person or Indemnified Party shall, if a Claim in respect thereof is to be made against any indemnifying party under this Section 6, deliver to the indemnifying party a written notice of the commencement thereof, and the indemnifying party shall have the right to participate in, and, to the extent the indemnifying party so desires, jointly with any other indemnifying party similarly noticed, to assume control of the defense thereof with counsel mutually satisfactory to the indemnifying party and the Indemnified Person or the Indemnified Party, as the case may be; provided, however, that an Indemnified Person or Indemnified Party shall have the right to retain its own counsel with the fees and expenses of not more than one counsel for such Indemnified

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Person or Indemnified Party to be paid by the indemnifying party, if, in the reasonable opinion of counsel retained by the indemnifying party, the representation by such counsel of the Indemnified Person or Indemnified Party and the indemnifying party would be inappropriate due to actual or potential differing interests between such Indemnified Person or Indemnified Party and any other party represented by such counsel in such proceeding. In the case of an Indemnified Person, legal counsel referred to in the immediately preceding sentence shall be selected by the Investors holding at least two-thirds in interest of the Registrable Securities included in the Registration Statement to which the Claim relates. The Indemnified Party or Indemnified Person shall cooperate fully with the indemnifying party in connection with any negotiation or defense of any such action or Claim by the indemnifying party and shall furnish to the indemnifying party all information reasonably available to the Indemnified Party or Indemnified Person which relates to such action or Claim. The indemnifying party shall keep the Indemnified Party or Indemnified Person reasonably apprised at all times as to the status of the defense or any settlement negotiations with respect thereto. No indemnifying party shall be liable for any settlement of any action, claim or proceeding effected without its prior written consent, provided, however, that the indemnifying party shall not unreasonably withhold, delay or condition its consent. No indemnifying party shall, without the prior written consent of the Indemnified Party or Indemnified Person, consent to entry of any judgment or enter into any settlement or other compromise which does not include as an unconditional term thereof the giving by the claimant or plaintiff to such Indemnified Party or Indemnified Person of a release from all liability in respect to such Claim or litigation. Following indemnification as provided for hereunder, the indemnifying party shall be subrogated to all rights of the Indemnified Party or Indemnified Person with respect to all third parties, firms or corporations relating to the matter for which indemnification has been made. The failure to deliver written notice to the indemnifying party within a reasonable time of the commencement of any such action shall not relieve such indemnifying party of any liability to the Indemnified Person or Indemnified Party under this Section 6, except to the extent that the indemnifying party is prejudiced in its ability to defend such action.

d. The indemnification required by this Section 6 shall be made by periodic payments of the amount thereof during the course of the investigation or defense, as and when bills are received or Indemnified Damages are incurred.

e. The indemnity agreements contained herein shall be in addition to (i) any cause of action or similar right of the Indemnified Party or Indemnified Person against the indemnifying party or others, and (ii) any liabilities the indemnifying party may be subject to pursuant to the law.

#### 7. Contribution.

To the extent any indemnification by an indemnifying party is prohibited or limited by law, the indemnifying party agrees to make the maximum

contribution with respect to any amounts for which it would otherwise be liable under Section 6 to the fullest extent permitted by law; provided, however, that: (i) no Person involved in the sale of Registrable Securities which Person is guilty of fraudulent misrepresentation (within the meaning of Section 11(f) of the 1933 Act) in connection with such sale shall be entitled to contribution from any Person involved in such sale of Registrable Securities who was not guilty of fraudulent

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misrepresentation; and (ii) contribution by any seller of Registrable Securities shall be limited in amount to the net amount of proceeds received by such seller from the sale of such Registrable Securities pursuant to such Registration Statement.

#### 8. Reports Under the 1934 Act.

With a view to making available to the Investors the benefits of Rule 144 promulgated under the 1933 Act or any other similar rule or regulation of the SEC that may at any time permit the Investors to sell securities of the Company to the public without registration ("RULE 144"), the Company agrees to:

a. make and keep public information available, as those terms are understood and defined in Rule 144;

b. file with the SEC in a timely manner all reports and other documents required of the Company under the 1933 Act and the 1934 Act so long as the Company remains subject to such requirements (it being understood that nothing herein shall limit the Company's obligations under Section 4(c) of the Securities Purchase Agreement) and the filing of such reports and other documents is required for the applicable provisions of Rule 144; and

c. furnish to each Investor so long as such Investor owns Registrable Securities, promptly upon request, (i) a written statement by the Company, if true, that it has complied with the reporting requirements of Rule 144, the 1933 Act and the 1934 Act, (ii) a copy of the most recent annual or quarterly report of the Company and such other reports and documents so filed by the Company, and (iii) such other information as may be reasonably requested to permit the Investors to sell such securities pursuant to Rule 144 without registration.

#### 9. Assignment of Registration Rights.

The rights under this Agreement shall be automatically assignable by the Investors to any transferee of all or any portion of such Investor's Registrable Securities if: (i) the Investor agrees in writing with the transferee or assignee to assign such rights, and a copy of such agreement is furnished to the Company within a reasonable time after such assignment; (ii) the Company is, within a reasonable time after such transfer or assignment, furnished with written notice of (a) the name and address of such transferee or assignee, and (b) the securities with respect to which such registration rights are being transferred or assigned; (iii) immediately following such transfer or assignment the further disposition of such securities by the transferee or assignee is restricted under the 1933 Act and applicable state securities laws; (iv) at or before the time the Company receives the written notice contemplated by clause (ii) of this sentence the transferee or assignee agrees in writing with the Company to be bound by all of the provisions contained herein; and (v) such transfer shall have been made in accordance with the applicable requirements of the Purchase Agreements, as applicable.

#### 10. Amendment of Registration Rights.

Provisions of this Agreement may be amended and the observance thereof may be waived (either generally or in a particular instance and either retroactively or prospectively), only

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with the written consent of the Company and Investors who then hold at least a majority of the Registrable Securities. Any amendment or waiver effected in accordance with this Section 10 shall be binding upon each Investor and the Company. No such amendment shall be effective to the extent that it applies to



less than all of the holders of the Registrable Securities. No consideration shall be offered or paid to any Person to amend or consent to a waiver or modification of any provision of any of this Agreement unless the same consideration also is offered to all of the parties to this Agreement.

11. Miscellaneous.

a. A Person is deemed to be a holder of Registrable Securities whenever such Person owns or is deemed to own of record such Registrable Securities. If the Company receives conflicting instructions, notices or elections from two or more Persons with respect to the same Registrable Securities, the Company shall act upon the basis of instructions, notice or election received from the such record owner of such Registrable Securities.

b. Any notices, consents, waivers or other communications required or permitted to be given under the terms of this Agreement must be in writing and will be deemed to have been delivered: (i) upon receipt, when delivered personally; (ii) upon receipt, when sent by facsimile (provided confirmation of transmission is mechanically or electronically generated and kept on file by the sending party); or (iii) one Business Day after deposit with a nationally recognized overnight delivery service, in each case properly addressed to the party to receive the same. The addresses and facsimile numbers for such communications shall be:

If to the Company:

Natural Health Trends Corp.  
12901 Hutton Drive  
Dallas, Texas 75234  
Telephone: (972) 241-6525  
Facsimile: (972)243-5430  
Attention: Chief Financial Officer

with a copy to:

Brown Rudnick Berlack Israels LLP  
120 West 45th Street  
New York, New York 10036  
Telephone: (212) 209-4812  
Facsimile: (212) 704-0196  
Attention: Alan N. Forman, Esq.

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If to Legal Counsel:

Bass Berry & Sims PLC  
315 Deaderick Street  
Nashville, TN 37238  
Telephone: (615) 742-6253  
Facsimile: (615) 742-2753  
Attention: J. Page Davidson, Esq.

If to a Buyer, to its address and facsimile number set forth on the Schedule of Buyers attached hereto, with copies to such Buyer's representatives as set forth on the Schedule of Buyers, or to such other address and/or facsimile number and/or to the attention of such other Person as the recipient party has specified by written notice given to each other party five (5) days prior to the effectiveness of such change. Written confirmation of receipt (A) given by the recipient of such notice, consent, waiver or other communication, (B) mechanically or electronically generated by the sender's facsimile machine containing the time, date, recipient facsimile number and an image of the first page of such transmission or (C) provided by a courier or overnight courier service shall be rebuttable evidence of personal service, receipt by facsimile or receipt from a nationally recognized overnight delivery service in accordance with clause (i), (ii) or (iii) above, respectively.

c. Failure of any party to exercise any right or remedy under this Agreement or otherwise, or delay by a party in exercising such right or remedy, shall not operate as a waiver thereof.

d. All questions concerning the construction,

validity, enforcement and interpretation of this Agreement shall be governed by the internal laws of the State of New York, without giving effect to any choice of law or conflict of law provision or rule (whether of the State of New York or any other jurisdictions) that would cause the application of the laws of any jurisdictions other than the State of New York. Each party hereby irrevocably submits to the non-exclusive jurisdiction of the state and federal courts sitting The City of New York, Borough of Manhattan, for the adjudication of any dispute hereunder or in connection herewith or with any transaction contemplated hereby or discussed herein, and hereby irrevocably waives, and agrees not to assert in any suit, action or proceeding, any claim that it is not personally subject to the jurisdiction of any such court, that such suit, action or proceeding is brought in an inconvenient forum or that the venue of such suit, action or proceeding is improper. Each party hereby irrevocably waives personal service of process and consents to process being served in any such suit, action or proceeding by mailing a copy thereof to such party at the address for such notices to it under this Agreement and agrees that such service shall constitute good and sufficient service of process and notice thereof. Nothing contained herein shall be deemed to limit in any way any right to serve process in any manner permitted by law. If any provision of this Agreement shall be invalid or unenforceable in any jurisdiction, such invalidity or unenforceability shall not affect the validity or enforceability of the remainder of this Agreement in that jurisdiction or the validity or enforceability of any provision of this Agreement in any other jurisdiction. EACH PARTY HEREBY IRREVOCABLY WAIVES ANY RIGHT IT MAY HAVE, AND AGREES NOT TO REQUEST, A JURY TRIAL FOR THE ADJUDICATION OF ANY DISPUTE HEREUNDER OR IN CONNECTION

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HEREWITH OR ARISING OUT OF THIS AGREEMENT OR ANY TRANSACTION CONTEMPLATED HEREBY.

e. This Agreement, the Purchase Agreements, the Warrant and the instruments referenced herein and therein constitute the entire agreement among the parties hereto with respect to the subject matter hereof and thereof. There are no restrictions, promises, warranties or undertakings, other than those set forth or referred to herein and therein. This Agreement, the Securities Purchase Agreement, the Warrant and the instruments referenced herein and therein supersede all prior agreements and understandings among the parties hereto with respect to the subject matter hereof and thereof.

f. Subject to the requirements of Section 9, this Agreement shall inure to the benefit of and be binding upon the permitted successors and assigns of each of the parties hereto.

g. The headings in this Agreement are for convenience of reference only and shall not limit or otherwise affect the meaning hereof.

h. This Agreement may be executed in identical counterparts, each of which shall be deemed an original but all of which shall constitute one and the same agreement. This Agreement, once executed by a party, may be delivered to the other party hereto by facsimile transmission of a copy of this Agreement bearing the signature of the party so delivering this Agreement.

i. Each party shall do and perform, or cause to be done and performed, all such further acts and things, and shall execute and deliver all such other agreements, certificates, instruments and documents, as any other party may reasonably request in order to carry out the intent and accomplish the purposes of this Agreement and the consummation of the transactions contemplated hereby.

j. All consents and other determinations required to be made by the Investors pursuant to this Agreement shall be made, unless otherwise specified in this Agreement, by Investors holding at least a majority of the Registrable Securities, determined as if all of the Warrants held by Investors then outstanding have been exercised for Registrable Securities.

k. The language used in this Agreement will be deemed to be the language chosen by the parties to express their mutual intent and no rules of strict construction will be applied against any party.

l. This Agreement is intended for the benefit of the parties hereto and their respective permitted successors and assigns, and is not

for the benefit of, nor may any provision hereof be enforced by, any other Person.

\* \* \* \* \*

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IN WITNESS WHEREOF, each Buyer and the Company have caused this Registration Rights Agreement to be duly executed as of the date first written above.

COMPANY: BUYERS:  
NATURAL HEALTH TRENDS CORP. [NAME]

By: \_\_\_\_\_ Name: \_\_\_\_\_  
Name: Mark D. Woodburn Title: \_\_\_\_\_  
Title: President

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SCHEDULE OF BUYERS

<TABLE>  
<CAPTION>

INVESTOR	INVESTOR ADDRESS AND FACSIMILE NUMBER	INVESTOR'S REPRESENTATIVE'S ADDRESS AND FACSIMILE NUMBER
-----	-----	-----
<S>	<C>	<C>

</TABLE>

EXHIBIT A

FORM OF NOTICE OF EFFECTIVENESS  
OF REGISTRATION STATEMENT

Continental Stock Transfer and Trust Company  
17 Battery Place  
New York, NY 10004  
Attn: Roger Bernhammer

Re: Natural Health Trends Corp.

Ladies and Gentlemen:

We are counsel to Natural Health Trends Corp., a Florida corporation (the "COMPANY"), and have represented the Company in connection with that certain Securities Purchase Agreement (the "SECURITIES PURCHASE AGREEMENT") entered into by and among the Company and the buyers named therein (collectively, the "HOLDERS") pursuant to which on October 6, 2004 the Company issued to the Holders units consisting of shares (the "COMMON SHARES") of the Company's Common Stock, par value \$0.001 per share (the "COMMON STOCK"), and common stock purchase warrants ("WARRANTS") exercisable for shares of Common Stock (the "WARRANT SHARES"). Pursuant to the Securities Purchase Agreement, the Company also has entered into a Registration Rights Agreement with the Holders (the "REGISTRATION RIGHTS AGREEMENT") pursuant to which the Company agreed, among other things, to register the Registrable Securities (as defined in the Registration Rights Agreement), including the Common Shares and Warrant Shares, as amended (the "1933 ACT"). In connection with the Company's obligations under the Registration Rights Agreement, on \_\_\_\_\_, 200\_, the Company filed a Registration Statement on Form S-1 (File No. 333-\_\_\_\_\_) (the "REGISTRATION STATEMENT") with the Securities and Exchange Commission (the "SEC") relating to the Registrable Securities which names each of the Holders as a selling stockholder thereunder.

In connection with the foregoing, we advise you that a member of the SEC's staff has advised us by telephone that the SEC has entered an order declaring the Registration Statement effective under the 1933 Act at [ENTER TIME OF EFFECTIVENESS] on [ENTER DATE OF EFFECTIVENESS] and we have no knowledge, after telephonic inquiry of a member of the SEC's staff, that any stop order suspending its effectiveness has been issued or that any proceedings for that

purpose are pending before, or threatened by, the SEC and the Registrable Securities are available for resale under the 1933 Act pursuant to the Registration Statement.

Very truly yours,

BROWN RUDNICK BERLACK ISRAELS LLP

By: \_\_\_\_\_  
Name:  
Title:

CC: [LIST NAMES OF HOLDERS]

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### EXHIBIT B

#### SELLING STOCKHOLDERS

The shares of common stock being offered by the selling stockholders are shares of common stock, and shares of common stock issuable upon exercise of the warrants which were sold by the Company in a private placement transaction. [Add description of sales by selling stockholders having piggyback registration rights from the MarketVision transaction] For additional information regarding the common shares and warrants, see "Private Placement of Units" above. We are registering the shares of common stock in order to permit the selling stockholders to offer the shares for resale from time to time. Except for the ownership of the shares and warrants, the selling stockholders have not had any material relationship with us within the past three years.

The table below lists the selling stockholders and other information regarding the beneficial ownership of the common stock by each of the selling stockholders. The second column lists the number of shares of common stock beneficially owned by each selling stockholder, based on its ownership of the common shares and warrants, as of \_\_\_\_\_, 200\_, assuming exercise of all warrants held by the selling stockholders on that date, without regard to any limitations on warrants exercise.

The third column lists the shares of common stock being offered by this prospectus by the selling stockholders.

In accordance with the terms of registration rights agreements with the holders of the Company's shares of common stock and warrants, this prospectus generally covers the resale of a number of shares of common stock equal to the number of shares of common stock issued to the selling stockholders plus the number of shares of common stock issuable upon exercise of the warrants, determined as if the outstanding warrants were exercised in full, as of the trading day immediately preceding the date this registration statement was initially filed with the SEC. Because the exercise price of the warrants may be adjusted for anti-dilution protection, the number of shares that will actually be issued may be more or less than the number of shares being offered by this prospectus. The fourth column assumes the sale of all of the shares offered by the selling stockholders pursuant to this prospectus.

The selling stockholders may sell all, some or none of their shares in this offering. See "Plan of Distribution."

<TABLE>  
<CAPTION>

NAME OF SELLING STOCKHOLDER	MAXIMUM NUMBER OF SHARES		NUMBER OF SHARES OWNED AFTER OFFERING
	NUMBER OF SHARES OWNED PRIOR TO OFFERING	TO BE SOLD PURSUANT TO THIS PROSPECTUS	
<S>	<C> [ ]	<C> [ ]	<C> [0]
[Other Buyers]	[ ]	[ ]	[0]

</TABLE>

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## PLAN OF DISTRIBUTION

We are registering the shares of common stock owned by the selling stockholders, and the shares of common stock issuable upon exercise of the warrants owned by the selling stockholders, to permit the resale of these shares of common stock by the holders from time to time after the date of this prospectus. We will not receive any of the proceeds from the sale by the selling stockholders of the shares of common stock. We will bear all fees and expenses incident to our obligation to register the shares of common stock.

The selling stockholders may sell all or a portion of the shares of common stock beneficially owned by them and offered hereby from time to time directly or through one or more underwriters, broker-dealers or agents. If the shares of common stock are sold through underwriters or broker-dealers, the selling stockholders will be responsible for underwriting discounts or commissions or agent's commissions. The shares of common stock may be sold in one or more transactions at fixed prices, at prevailing market prices at the time of the sale, at varying prices determined at the time of sale, or at negotiated prices. These sales may be effected in transactions, which may involve crosses or block transactions,

- on any national securities exchange or quotation service on which the securities may be listed or quoted at the time of sale,
- in the over-the-counter market,
- in transactions otherwise than on these exchanges or systems or in the over-the-counter market,
- through the writing of options, whether such options are listed on an options exchange or otherwise,
- ordinary brokerage transactions and transactions in which the broker-dealer solicits purchasers;
- block trades in which the broker-dealer will attempt to sell the shares as agent but may position and resell a portion of the block as principal to facilitate the transaction;
- purchases by a broker-dealer as principal and resale by the broker-dealer for its account;
- an exchange distribution in accordance with the rules of the applicable exchange;
- privately negotiated transactions;
- through the settlement of short sales
- pursuant to Rule 144 under the Securities Act;

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- broker-dealers may agree with the selling securityholders to sell a specified number of such shares at a stipulated price per share
- a combination of any such methods of sale; and
- any other method permitted pursuant to applicable law.

If the selling stockholders effect such transactions by selling shares of common stock to or through underwriters, broker-dealers or agents, such underwriters, broker-dealers or agents may receive commissions in the form of discounts, concessions or commissions from the selling stockholders or commissions from purchasers of the shares of common stock for whom they may act as agent or to whom they may sell as principal (which discounts, concessions or commissions as to particular underwriters, broker-dealers or agents may be in excess of those customary in the types of transactions involved). In connection with sales of the common stock or otherwise, the selling stockholders may enter

into hedging transactions with broker-dealers, which may in turn engage in short sales of the common stock in the course of hedging in positions they assume. The selling stockholders may also sell shares of common stock short and deliver shares of common stock covered by this prospectus to close out short positions. The selling stockholders may also loan or pledge shares of common stock to broker-dealers that in turn may sell such shares.

The selling stockholders may pledge or grant a security interest in some or all of the warrants or shares of common stock owned by them and, if they default in the performance of their secured obligations, the pledgees or secured parties may offer and sell the warrants or shares of common stock from time to time pursuant to this prospectus or any amendment to this prospectus under Rule 424(b)(3) or other applicable provision of the Securities Act of 1933, as amended, amending, if necessary, the list of selling stockholders to include the pledgee, transferee or other successors in interest as selling stockholders under this prospectus. The selling stockholders also may transfer and donate the shares of common stock in other circumstances in which case the transferees, donees, pledgees or other successors in interest will be the selling beneficial owners for purposes of this prospectus.

The selling stockholders and any broker-dealer participating in the distribution of the shares of common stock may be deemed to be "underwriters" within the meaning of the Securities Act, and any commission paid, or any discounts or concessions allowed to, any such broker-dealer may be deemed to be underwriting commissions or discounts under the Securities Act. At the time a particular offering of the shares of common stock is made, a prospectus supplement, if required, will be distributed which will set forth the aggregate amount of shares of common stock being offered and the terms of the offering, including the name or names of any broker-dealers or agents, any discounts, commissions and other terms constituting compensation from the selling stockholders and any discounts, commissions or concessions allowed or reallocated or paid to broker-dealers.

Under the securities laws of some states, the shares of common stock may be sold in such states only through registered or licensed brokers or dealers. In addition, in some states the shares of common stock may not be sold unless such shares have been registered or qualified for

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sale in such state or an exemption from registration or qualification is available and is complied with.

There can be no assurance that any selling stockholder will sell any or all of the shares of common stock registered pursuant to the shelf registration statement, of which this prospectus forms a part.

The selling stockholders and any other person participating in such distribution will be subject to applicable provisions of the Securities Exchange Act of 1934, as amended, and the rules and regulations thereunder, including, without limitation, Regulation M of the Exchange Act, which may limit the timing of purchases and sales of any of the shares of common stock by the selling stockholders and any other participating person. Regulation M may also restrict the ability of any person engaged in the distribution of the shares of common stock to engage in market-making activities with respect to the shares of common stock. All of the foregoing may affect the marketability of the shares of common stock and the ability of any person or entity to engage in market-making activities with respect to the shares of common stock.

We will pay all expenses of the registration of the shares of common stock pursuant to the registration rights agreement, estimated to be \$[ ] in total, including, without limitation, Securities and Exchange Commission filing fees and expenses of compliance with state securities or "blue sky" laws; provided, however, that a selling stockholder will pay all underwriting discounts and selling commissions, if any. We will indemnify the selling stockholders against liabilities, including some liabilities under the Securities Act, in accordance with the registration rights agreements, or the selling stockholders will be entitled to contribution. We may be indemnified by the selling stockholders against civil liabilities, including liabilities under the Securities Act, that may arise from any written information furnished to us by the selling stockholder specifically for use in this prospectus, in accordance with the related registration rights agreements, or we may be

entitled to contribution.

Once sold under the shelf registration statement, of which this prospectus forms a part, the shares of common stock will be freely tradable in the hands of persons other than our affiliates.

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