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REEDS JEWELERS INC  
Form 10-Q  
January 12, 2001

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SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON DC 20549

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FORM 10-Q

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

FOR THE QUARTER ENDED NOVEMBER 30, 2000  
COMMISSION FILE NUMBER 0-15247

REEDS JEWELERS, INC.  
(Exact name of registrant as specified in its charter)

NORTH CAROLINA  
(State or other jurisdiction of incorporation or  
organization)

56-1441702  
(I.R.S. Employer Identification No.)

2525 SOUTH SEVENTEENTH STREET  
WILMINGTON, NORTH CAROLINA  
(Address of principal executive offices)

28401  
(Zip code)

REGISTRANT'S TELEPHONE NUMBER, INCLUDING AREA CODE:  
(910) 350-3100

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes  No

Indicate the number of shares outstanding of each of the issuer's class of common stock, as of the latest practicable date.

The number of outstanding shares of Common Stock, par value \$0.10 per share, as of January 11, 2001 was 8,476,372.

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PART I

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ITEM 1. FINANCIAL STATEMENTS

The consolidated financial statements included herein have been prepared by Reeds Jewelers, Inc. (the "Company"), without audit, pursuant to the rules and regulations of the Securities and Exchange Commission. Certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted pursuant to such rules and regulations; however, the Company believes that the disclosures are adequate to make the information presented not misleading. It is suggested that these consolidated financial statements be read in conjunction with the financial statements and the notes thereto included in the Company's latest annual report on Form 10-K for the fiscal year ended February 29, 2000.

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REEDS JEWELERS, INC. AND SUBSIDIARIES  
CONSOLIDATED BALANCE SHEETS

	FEBRUARY 29 2000	NOVEMBER 30 2000	
	-----	-----	
ASSETS			
(UNAUDITED)			
Current assets:			
Cash and cash equivalents .....	\$ 895,000	\$ 919,000	\$
Accounts receivable:			
Customers, less allowance for doubtful accounts			
of \$4,060,000, \$3,937,000 and \$3,735,000 .....	48,897,000	47,525,000	
Other .....	758,000	3,549,000	
Merchandise inventories .....	46,253,000	59,977,000	
Deferred income taxes, net of valuation allowance of			
\$151,000, 142,000 and \$142,000 .....	2,249,000	2,023,000	
Other .....	486,000	1,414,000	
	-----	-----	
Total current assets .....	99,538,000	115,407,000	1
Property, furniture and equipment:			
Land and building .....	83,000	83,000	
Furniture and equipment .....	22,691,000	26,679,000	
Leasehold improvements .....	11,575,000	11,912,000	
	-----	-----	
	34,349,000	38,674,000	
Less accumulated depreciation and amortization .....	19,305,000	19,615,000	
	-----	-----	
Net property, furniture and equipment .....	15,044,000	19,059,000	
Other assets:			
Goodwill, net of accumulated amortization of			
\$2,547,000, \$2,882,000 and \$2,436,000 .....	5,849,000	5,514,000	
Deferred income taxes, net of valuation allowance of			
\$12,000, \$11,000 and \$11,000 .....	173,000	165,000	
Restricted investments (Note C) .....	--	2,628,000	
Miscellaneous .....	733,000	869,000	
	-----	-----	
	6,755,000	9,176,000	
	-----	-----	
TOTAL ASSETS .....	\$121,337,000	\$143,642,000	\$1

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	=====	=====	=====
LIABILITIES AND SHAREHOLDERS' EQUITY			
Current liabilities:			
Accounts payable .....	\$ 12,855,000	\$ 30,442,000	\$
Accrued compensation .....	3,569,000	1,901,000	
Accrued expenses .....	2,712,000	3,417,000	
Deferred revenue (Note D) .....	314,000	11,000	
Income taxes .....	2,233,000	--	
	-----	-----	-----
Total current liabilities .....	21,683,000	35,771,000	
Revolving credit note .....	52,359,000	62,689,000	
Subordinated notes payable to shareholders .....	845,000	845,000	
Deferred income taxes .....	1,267,000	1,823,000	
Deferred revenue (Note D) .....	--	--	
Other long-term liabilities .....	213,000	213,000	
	-----	-----	-----
Total liabilities .....	76,367,000	101,341,000	
Shareholders' equity:			
Common stock, par value \$0.10 per share; 25,000,000 shares authorized; 8,476,372 shares issued and outstanding in 2000 and 1999 .....	847,000	847,000	
Additional paid-in capital .....	10,560,000	10,560,000	
Retained earnings .....	33,563,000	30,894,000	
	-----	-----	-----
Total shareholders' equity .....	44,970,000	42,301,000	
	-----	-----	-----
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY .....	\$121,337,000	\$143,642,000	\$1
	=====	=====	=====

REEDS JEWELERS, INC. AND SUBSIDIARIES  
CONSOLIDATED STATEMENTS OF OPERATIONS

(UNAUDITED)

	THREE MONTHS ENDED		NINE
	NOVEMBER 30		MONTHS
	2000	1999	2000
	-----	-----	-----
Net sales .....	\$ 27,296,000	\$ 26,027,000	\$ 75,744,000
Cost of sales .....	14,168,000	13,045,000	38,119,000
	-----	-----	-----
Gross profit .....	13,128,000	12,982,000	37,625,000
Selling, general and administrative expenses	11,904,000	10,877,000	34,777,000
Depreciation and amortization .....	1,010,000	954,000	2,985,000
	-----	-----	-----
Operating earnings (loss) .....	214,000	1,151,000	(137,000)
Interest expense .....	1,359,000	1,079,000	3,847,000
	-----	-----	-----

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(Loss) income before income taxes .....	(1,145,000)	72,000	(3,984,000)
Income tax (benefit) expense .....	(378,000)	24,000	(1,315,000)
	-----	-----	-----
Net (loss) income .....	\$ (767,000)	\$ 48,000	\$ (2,669,000)
	=====	=====	=====
Basic and diluted net (loss) income per common share .....	\$ (0.09)	\$ 0.01	\$ (0.09)
	=====	=====	=====
Weighted average shares outstanding - diluted .....	8,476,372	8,476,372	8,476,372
	=====	=====	=====

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REEDS JEWELERS, INC. AND SUBSIDIARIES  
CONSOLIDATED STATEMENTS OF CASH FLOWS

(UNAUDITED)

	NINE MONTHS ENDED NOVEMBER 30, 2000	NINE MONTHS NOVEMBER 1999
	-----	-----
OPERATING ACTIVITIES		
Net (loss) income .....	\$ (2,669,000)	\$ 521,000
Adjustments to reconcile net (loss) income to net cash used in operating activities:		
Depreciation .....	2,591,000	2,322,000
Amortization .....	394,000	382,000
Loss on sale of property, furniture and equipment .....	278,000	24,000
Changes in operating assets and liabilities:		
Accounts receivable .....	(1,419,000)	340,000
Merchandise inventories .....	(13,724,000)	(11,699,000)
Other current assets and other assets .....	(1,123,000)	(580,000)
Accounts payable .....	17,587,000	(158,000)
Accrued compensation and expenses .....	(963,000)	(294,000)
Deferred revenue .....	(303,000)	(749,000)
Income taxes .....	(1,443,000)	(1,808,000)
Other long-term liabilities .....	--	5,000
	-----	-----
Net cash used in operating activities .....	(794,000)	(11,694,000)
INVESTING ACTIVITIES		
Purchases of property, furniture and equipment .....	(6,884,000)	(3,812,000)
Purchase of restricted investments .....	(2,628,000)	--
	-----	-----
Net cash used in investing activities .....	(9,512,000)	(3,812,000)
FINANCING ACTIVITIES		
Net proceeds from revolving credit note .....	10,330,000	15,514,000

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Net cash provided by financing activities .....	10,330,000	15,514,
Net increase in cash and cash equivalents .....	24,000	8,
Cash and cash equivalents at beginning of period .....	895,000	1,080,
Cash and cash equivalents at end of period .....	\$ 919,000	\$ 1,088,
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:		
Cash paid during the period for:		
Interest .....	\$ 3,718,000	\$ 2,757,
Income taxes .....	\$ 2,328,000	\$ 2,063,

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REEDS JEWELERS, INC. AND SUBSIDIARIES  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

A. MANAGEMENT'S OPINION

These consolidated financial statements should be read in conjunction with the audited consolidated financial statements and notes thereto included in the Company's Form 10-K for the fiscal year ended February 29, 2000.

Management of Reeds Jewelers, Inc. believes that the consolidated financial statements contained herein contain all adjustments necessary to present fairly the financial position, consolidated results of operations, and cash flows for the interim period. Management also believes that all adjustments so made are of a normal and recurring nature.

B. RECLASSIFICATIONS

Certain reclassifications were made to the 1999 financial statements to conform to the classifications used in 2000. The reclassifications had no effect on net income or shareholders' equity as previously reported.

C. RESTRICTED INVESTMENTS

	11/30/00	11/30/99
Cash .....	\$ 45,000	\$ --
Held-to-maturity investments ...	2,523,000	--
Equity investment .....	60,000	--
Total Restricted Investments	\$2,628,000	\$ --

Restricted Investments in the accompanying balance sheet represent cash, bonds and stock being held by the Company's subsidiary, First Retail Bank N.A., to comply with the Federal Banking Regulations.

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The Held-to-maturity investments consist of Federal Home Loan Bank bonds that mature in June 2001 and Atlanta Georgia Urban Housing bonds that mature in April 2019. These bonds are stated at amortized cost, as it is the intent of the Company to hold these securities until maturity.

The Company's equity investment, carried at cost, consists of 1,200 shares of Federal Reserve Bank stock with a \$50 par value at November 30, 2000.

### D. DEFERRED REVENUE

For the fiscal years ended prior to February 28, 1999, in accordance with FASB Technical Bulletin 90-1, "Accounting for Separately Priced Extended Warranty and Product Maintenance Contracts," revenue from these contracts was deferred and recognized in income on a straight-line basis over the contract period. This deferred revenue has been separated into its current and long-term portions on the balance sheet. Commission costs that were directly related to the acquisition of these contracts were deferred and charged to expense in proportion to the revenue recognized. All other costs, such as costs of services performed under the contracts, general and administrative expenses, and advertising expenses, were charged to expense as incurred. Previously deferred extended service contract revenue recognized for the quarters ended November 30, 2000 and 1999 of \$64,000 and \$198,000, respectively, has been reflected as a reduction of selling, general, and administrative expenses.

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During the first quarter of the fiscal year ended February 28, 1999, the Company stopped selling its own extended service contracts and began selling such contracts on behalf of unrelated third parties only. These contracts provided for warranty periods of 24 to 36 months. As a result of this change, the Company will continue to recognize existing deferred revenues from previously sold contracts through January 31, 2001 and now recognizes commission revenue for the unrelated third-party extended warranty plans at the time of sale.

### E. DEBT

In April 1999, the Company, its existing banks, and two additional banks entered into an amended revolving credit agreement whereby the Company may borrow up to \$65,000,000 through June 30, 2002 on terms similar to those of the previous agreement. Under this agreement, the Company pays interest monthly at an interest rate ranging from the 30-day LIBOR rate (6.83% at November 30, 2000) plus 125 basis points to 185 basis points or prime (9.50% at November 30, 2000) plus 25 basis points, depending upon the Company's debt-to-worth ratio. As of December 1, 2000, the Company's rate was 30-day LIBOR plus 165 basis points. The Company had \$62,689,000 outstanding on this revolver at November 30, 2000, which is classified as a long-term liability based on its expiration date. The revolving credit agreement is collateralized by substantially all of the Company's assets. The various loan agreements contain financial covenants including those that limit dividend payments and additional borrowings and prohibit new store openings if an event of default exists. The Company is in compliance with these covenants, as amended or waived.

### F. OPERATING SEGMENT INFORMATION

In June 1997, SFAS No. 131, "Disclosure about Segments of an Enterprise and Related Information," was issued effective for fiscal years ending after December 15, 1998. The Company now reports two segments, retail operations and credit operations. Separate financial information is produced internally and is regularly reviewed by the chief operating decision-maker ("CODM"). The retail

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operations segment consists of all store locations and corporate headquarters. The stores have all been combined into one segment because they have similar basic characteristics, such as the nature of products, and the class of customers for their products. Corporate headquarters is included in this same segment due to the fact that its revenues earned are incidental to the Company's activities and it serves as a support system to the stores. The credit operations segment is primarily engaged in providing and maintaining financing for the Company's customers. This operation is segregated since the CODM evaluates it separately. It also meets one of the three quantitative thresholds, the asset test, since it represents 10.0% or more of the combined assets of all operating segments.

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The following table summarizes the net sales, revenues, operating earnings, interest expense, assets, depreciation, and capital expenditures for each reportable segment for the quarters and nine-months ended November 30, 2000 and 1999. In the financial statements, other revenues are reflected as a reduction of selling, general, and administrative expenses and inter-segment revenue eliminates in consolidation.

	RETAIL OPERATIONS	CREDIT OPERATIONS	TOTAL
-----			
FOR THE QUARTER ENDED NOVEMBER 30, 2000			
NET SALES .....	\$ 27,296,000	\$ --	\$ 27,296,000
OTHER REVENUES .....	630,000	3,405,000	4,035,000
INTER-SEGMENT REVENUE .....	--	261,000	261,000
OPERATING (LOSS) EARNINGS .....	(1,279,000)	1,493,000	214,000
INTEREST EXPENSE .....	551,000	808,000	1,359,000
IDENTIFIABLE ASSETS .....	93,163,000	50,479,000	143,642,000
DEPRECIATION AND AMORTIZATION .....	960,000	50,000	1,010,000
CAPITAL EXPENDITURES .....	2,335,000	3,000	2,338,000
-----			
For the quarter ended November 30, 1999			
Net Sales .....	\$ 26,027,000	\$ --	\$ 26,027,000
Other revenues .....	778,000	2,834,000	3,612,000
Inter-segment revenue .....	--	256,000	256,000
Operating earnings .....	125,000	1,026,000	1,151,000
Interest expense .....	381,000	698,000	1,079,000
Identifiable assets .....	78,093,000	45,582,000	123,675,000
Depreciation and amortization .....	898,000	56,000	954,000
Capital expenditures .....	1,471,000	12,000	1,483,000
-----			
FOR THE NINE MONTHS ENDED NOVEMBER 30, 2000			
NET SALES .....	\$ 75,744,000	\$ --	\$ 75,744,000
OTHER REVENUES .....	1,905,000	9,556,000	11,461,000
INTER-SEGMENT REVENUE .....	--	714,000	714,000
OPERATING (LOSS) EARNINGS .....	(4,258,000)	4,121,000	(137,000)
INTEREST EXPENSE .....	1,415,000	2,432,000	3,847,000
IDENTIFIABLE ASSETS .....	93,163,000	50,479,000	143,642,000
DEPRECIATION AND AMORTIZATION .....	2,874,000	111,000	2,985,000
CAPITAL EXPENDITURES .....	6,816,000	68,000	6,884,000

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For the nine months ended November 30, 1999

Net Sales .....	\$ 72,177,000	\$ --	\$ 72,177
Other revenues .....	2,283,000	8,628,000	10,911
Inter-segment revenue .....	--	706,000	706
Operating (loss) earnings .....	(480,000)	4,141,000	3,661
Interest expense .....	826,000	2,058,000	2,884
Identifiable assets .....	78,093,000	45,582,000	123,675
Depreciation and amortization .....	2,549,000	155,000	2,704
Capital expenditures .....	3,638,000	174,000	3,812

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### ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

#### RESULTS OF OPERATIONS

##### Net Sales

Net sales for the third quarter ended November 30, 2000 were up 4.9% to \$27,296,000 from \$26,027,000 at the end of the third quarter last year. Same store sales, or stores open in comparable periods, rose 1.1% in the third quarter this year. For the nine months ended November 30, 2000, net sales increased 4.9% to \$75,744,000 from \$72,177,000 for the same period a year earlier. Comparable store sales rose 1.1% during the nine-month period. During the third quarter of fiscal 2001, the Company opened five stores in the Oxford AL, Fort Myers FL, Baltimore MD, Austin TX and Laredo TX markets. At November 30, 2000, the Company operated 120 stores in 19 states compared to 112 stores in 17 states at November 30, 1999.

The sales of a retail jeweler depend upon having the right mixture of merchandise available in its stores. Management has identified those inventory items that have the most favorable turnover and are the most profitable as core inventory items. The Company averaged 96.0% in-stock on its core items during third quarter fiscal 2001, compared to 97.2% last year; it averaged 94.1% in-stock on its entire basic merchandise mix compared to 87.3% during the same quarter a year ago. During the quarter ended November 30, 2000, core merchandise accounted for 54.8% of net sales, 82.4% of the items offered in the Company's basic merchandise mix, and 39.7% of its inventory investment. In the same quarter last year, core merchandise accounted for 49.5% of net sales, 61.1% of the items offered in the Company's basic merchandise mix, and 38.3% of its inventory investment. In the third quarter of fiscal 2001 and 2000, the average price of each piece of merchandise sold was \$249 and \$240, respectively.

Credit sales for the third quarter of fiscal 2001 accounted for 49.3% of net sales compared to 50.7% a year earlier. Although the total transactions during the quarter were down 1.0% compared to last year same quarter, the average transaction size increased 10.2% for credit sales and 7.4% for cash sales. Management believes that its proprietary financing program is a strategic competitive strength and seeks to optimize its risk-reward ratio by financing up to 55.0% of net sales.

##### Gross Profit

Gross margins were 48.1% of net sales for the third quarter of fiscal 2001, down from 49.9% for the same period a year earlier. Year-to-date, gross margins were 49.7%, down from 50.7% in the first nine months of the prior year. The decline



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is attributable to increased promotional activity. The Company has also been impacted by a decrease in the margins on special order transactions. Management plans to incorporate this merchandise into its basic inventory mix in order to mitigate the effect on margins. Management continued its aggressive advertising and promotion throughout the holiday season.

### Selling, General, and Administrative Expenses (SG&A)

Selling, general, and administrative expenses as a percentage of net sales were 43.6% and 41.8% for the quarters ended November 30, 2000 and 1999, respectively. Significant expense categories are reflected on a normalized basis for the third quarters of the last two fiscal years in the following table:

	Quarter Ended		Nine Mon
	11/30/00	11/30/99	11/30/00
Compensation - salaries & hourly wages .....	20.1 %	18.9 %	20.6 %
Compensation - bonuses & commissions .....	3.6 %	4.0 %	3.7 %
Compensation - benefits & other personnel costs	4.3 %	4.1 %	5.3 %
Rents for space .....	10.6 %	10.2 %	11.2 %
Advertising .....	4.7 %	3.4 %	4.2 %
Bad debt .....	5.6 %	5.2 %	5.3 %
Finance charges .....	(8.4)%	(8.1)%	(8.9)%
Late charge income .....	(2.8)%	(1.3)%	(2.2)%

The increase in selling, general, and administrative expenses is the result of higher compensation, occupancy, advertising, and bad debt expenses. Compensation from salaries and hourly wages increased at a faster rate than net sales. The increase was primarily a result of hiring additional staff for the twelve new stores and the internet site that opened since the third quarter of last year. An annual raise of approximately 5% also contributed to the increase. The increase in compensation from benefits and other personnel costs results from increased expenses from the Company's self-insured health insurance plan. The Company is also experiencing an increase in the negotiated base rents for new and remodeled stores. These increases are partially offset by the increased contribution from the Company's credit operations. The finance charges and late charge income increased as a direct result of the Company's nationally chartered credit card bank that opened during the second quarter.

Bad debt increased to \$1,522,000 from \$1,350,000 and rose to 5.6% of net sales for the quarter compared to 5.2% a year earlier. Gross write-offs for bad debts were \$1,879,000 versus \$1,681,000 in the same quarter last year. Net write-offs, after recovery of amounts previously written off, were \$1,658,000 and \$1,446,000 for the third quarter of the current and prior fiscal year, respectively. At the end of the third quarter of fiscal 2001 and 2000 the allowance for doubtful accounts was 7.65% of gross customer receivables. The average delinquent account (accounts more than 90 days past due) represented 11.1% and 10.6% of the Company's accounts receivable portfolio for the third quarter of fiscal 2001 and 2000, respectively. The Company's policies and procedures regarding credit authorization, collection, and write-offs have not changed significantly during each of the two periods. The approval rate on applications was 44.0% for the

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third quarter of the current year and 51.2% for the third quarter last year. During the first quarter ended May 31, 1999, the Company changed its portfolio mix to include young adults in a test program. Management made the decision in the third quarter of last year to end the test program. Although bad debt has increased quarter to quarter, management believes that over the next year the portfolio will return to historical levels of mix and approval rate.

In the first quarter of fiscal 1999 the Company began selling extended service agreements on behalf of an unrelated third party versus selling them in-house. The Company will continue to recognize deferred revenue from extended service agreements previously sold by the Company through January 31, 2001. The Company now recognizes commission revenue for the unrelated third-party extended service agreements at the time of sale. Previously deferred extended service agreements revenue recognized for the quarters ended November 30, 2000 and 1999 of \$64,000 and \$198,000, respectively, as well as commission revenues of \$566,000 and \$580,000, respectively, have been reflected as a reduction of selling, general, and administrative expenses. Extended service agreements equaled 2.3% and 3.0% of net sales during the quarters ended November 30, 2000 and 1999, respectively.

### Interest Expense

Interest expense increased \$280,000 over the prior year to \$1,359,000 for the quarter. Two-thirds of the additional interest is attributed to the higher interest rate and one-third is a result of increased average borrowings during the quarter. The effective pre-tax interest rate was 8.4%, up from 7.1% a year ago. Average total borrowings were 6.3% higher than during the third quarter of last year. Year to date, the expense was \$963,000 higher than the same period a year ago, and increased to 5.0% of net sales compared to 4.0% a year earlier.

### Income Taxes

The benefit for income taxes was \$378,000 during the third quarter ended November 30, 2000, compared to an expense of \$24,000 for the same period a year earlier. The Company's anticipated tax rate was 33.0% in the third quarter of both years.

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## LIQUIDITY AND CAPITAL RESOURCES

The Company requires cash for purchasing inventory, opening new stores, making leasehold improvements, enhancing technology, and acquiring equipment. Working capital needs normally peak in the fall as the Company increases inventories to meet anticipated demand during the all-important Christmas selling season. The Company's long-term growth strategy will require increasing working capital to fund capital expenditures, receivables, and inventories for new stores. Working capital requirements will be financed by funds generated from operations and bank lines described below. Cash used in operations for the nine months ending November 30, 2000 was \$794,000 compared to \$11,694,000 for the nine months ending November 30, 1999.

### Working Capital

Working capital decreased 0.8% at November 30, 2000 to \$79,636,000 from \$80,299,000 at November 30, 1999. The resulting ratio of current assets to current liabilities as of November 30, 2000 was 3.2 to 1, compared to 4.6 to 1 at November 30, 1999. Capital expenditures totaled \$6,884,000 and \$3,812,000 for the nine months ended November 30, 2000 and 1999, respectively. The Company opened three stores during the quarter ended May 31, 2000, four stores in the quarter ended August 31, 2000, and five stores in the quarter ended November 30,

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2000. Management does not intend to open any additional stores this fiscal year.

### Debt

In April 1999, the Company, its existing banks, and two additional banks entered into an amended revolving credit agreement whereby the Company may borrow up to \$65,000,000 through June 30, 2002 on terms similar to those of the previous agreement. Under this agreement, the Company pays interest monthly at an interest rate ranging from the 30-day LIBOR rate (6.83% at November 30, 2000) plus 125 basis points to 185 basis points or prime (9.50% at November 30, 2000) plus 25 basis points, depending upon the Company's debt-to-worth ratio. As of December 1, 2000, the Company's rate was 30-day LIBOR plus 165 basis points.

Borrowings under the Company's revolving credit facility averaged \$64.2 million during the third quarter of fiscal 2001 and \$60.3 million during the same quarter a year ago. The maximum borrowings outstanding under the facility at any time during each of the quarters were \$65.0 million and \$61.2 million, respectively. The Company had \$62,689,000 outstanding on this revolver at November 30, 2000, which is classified as a long-term liability based on its expiration date. The revolving credit agreement is collateralized by substantially all of the Company's assets. The various loan agreements contain financial covenants including those that limit dividend payments and additional borrowings and prohibit new store openings if an event of default exists. The Company is currently in compliance with these covenants, as amended or waived.

The Company also has subordinated notes totaling \$845,000 with three related parties, with interest payable monthly at the prime rate (9.50% at November 30, 2000) quoted in The Wall Street Journal. The notes are unsecured and are subordinate to the revolving bank note, which is collateralized by substantially all of the Company's assets.

### Disclosure Regarding Forward-Looking Statements

The Private Securities Litigation Reform Act of 1995 provides a "safe harbor" for forward-looking statements to encourage companies to provide prospective information about their companies without fear of litigation so long as those statements are identified as forward-looking and are accompanied by meaningful cautionary statements identifying important factors that could cause actual results to differ materially from those projected in the statement. Various forward-looking statements have been made throughout this discussion, including comments about:

- (i) planned store openings;
- (ii) goals for the mix of credit and cash sales;
- (iii) expected increases in gross margins; and
- (iv) expected increase in approval rates on credit applications.

Accordingly, Reeds Jewelers, Inc. hereby identifies the following important factors that could cause its actual financial results to differ materially from those projected by the Company in forward-looking statements:

- (i) availability of favorable locations on terms acceptable to the Company;
- (ii) unexpected changes in the marketing and pricing strategies of competitors;
- (iii) adverse changes in the political environments of countries providing raw materials for the jewelry industry;

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- (iv) adverse changes in consumer spending or consumer credit-worthiness;
- (v) significant changes in interest rates; or
- (vi) the loss of key executives.

### Impact of Inflation

In management's opinion, changes in net sales and net earnings that have resulted from inflation and changing prices have not been material during the periods presented. There is no assurance, however, that inflation will not materially affect Reeds Jewelers, Inc. in the future.

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## PART II. OTHER INFORMATION

### Item 1. Legal Proceedings.

The Company is from time to time involved in routine litigation incidental to the conduct of its business. The Company believes that no currently pending litigation to which it is a party will have a material adverse effect on its consolidated financial condition or results of operations.

### Item 2. Changes in Securities.

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 and Reports on Form 8-K.

#### (a) Exhibits.

None.

#### (b) Reports on Form 8-K.

Not applicable.

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## SIGNATURES

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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.

REEDS JEWELERS, INC.

January 12, 2001  
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/s/ James R. Rouse  
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James R. Rouse  
Treasurer and  
Chief Financial Officer