REEDS JEWELERS INC
Form 10-Q
January 14, 2002

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON DC 20549

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, 2001
COMMISSION FILE NUMBER 0-15247

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

NORTH CAROLINA	56-1441702
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
2525 SOUTH SEVENTEENTH STREET WILMINGTON, NORTH CAROLINA	28401
(Address of principal executive offices)	(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 [X]   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 14, 2002 was 8,476,372.

PART I

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 28, 2001.

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REEDS JEWELERS, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS

	FEBRUARY 28 2001	NOVEMBER 30 2001
ASSETS		(UNAUDITED)
Current assets:		
Cash and cash equivalents	$ 685,000	$ 1,015,000
Accounts receivable:		
Customers, less allowance for doubtful accounts of $4,262,000, $3,619,000 and $3,937,000	49,008,000	41,615,000
Other	1,191,000	1,374,000
Merchandise inventories	48,552,000	54,795,000
Income taxes receivable	604,000	5,472,000
Deferred income taxes, net of valuation allowance of $149,000, $109,000 and $142,000	2,194,000	1,912,000
Other	1,018,000	934,000
Total current assets	103,252,000	107,117,000
Property, furniture and equipment:		
Land and building	83,000	83,000
Furniture and equipment	25,421,000	24,893,000
Leasehold improvements	12,336,000	12,534,000
	37,840,000	37,510,000
Less accumulated depreciation and amortization	19,662,000	20,858,000
Net property, furniture and equipment	18,178,000	16,652,000
Other assets:		
Goodwill, net of accumulated amortization of $2,993,000, $0 and $2,882,000	5,403,000	-
Deferred income taxes, net of valuation allowance of $13,000, $39,000 and $11,000	195,000	676,000
Restricted investments (Note C)	2,580,000	-
Miscellaneous	829,000	973,000
	9,007,000	1,649,000
TOTAL ASSETS	$ 130,437,000	$ 125,418,000

LIABILITIES AND SHAREHOLDERS' EQUITY			
Current liabilities:			
Accounts payable....................................	$ 13,418,000	$ 24,509,000	$
Accrued compensation................................	2,305,000	1,808,000	
Accrued expenses....................................	2,348,000	5,180,000	
Deferred revenue (Note D)...........................	-	-	
Current portion of long-term debt (Note E)............	-	59,125,000	
Total current liabilities.......................	18,071,000	90,622,000	
Revolving credit note (Note E).........................	63,761,000	-	
Subordinated notes payable to shareholders.............	845,000	845,000	
Deferred income taxes..................................	2,517,000	1,268,000	
Other long-term liabilities............................	211,000	855,000	
Total liabilities...............................	85,405,000	93,590,000	
Shareholders' equity:			
Common stock, par value $0.10 per share; 25,000,000 shares authorized; 8,476,372 shares issued and outstanding in 2001 and 2000.............	847,000	847,000	
Additional paid-in capital.............................	10,560,000	10,560,000	
Retained earnings......................................	33,625,000	20,421,000	
Total shareholders' equity......................	45,032,000	31,828,000	
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY...	$ 130,437,000	$ 125,418,000	$

REEDS JEWELERS, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF OPERATIONS

(UNAUDITED)

	THREE MONTHS ENDED NOVEMBER 30		NINE MONTH NOVEMBE
	2001	2000	2001
Net sales......................................	$ 24,670,000	$ 27,296,000	$ 68,269,000
Cost of sales..................................	13,056,000	14,168,000	36,085,000
Gross profit........................	11,614,000	13,128,000	32,184,000
Selling, general and administrative expenses...	12,415,000	11,904,000	34,810,000
Depreciation and amortization..................	897,000	1,010,000	2,974,000
Restructuring charge (Note G)..................	4,864,000	-	4,864,000
Asset impairment charge (Note H)...............	5,983,000	-	5,983,000
Operating (loss) earnings............	(12,545,000)	214,000	(16,447,000)
Interest expense...............................	826,000	1,359,000	2,970,000
Loss before income taxes.......................	(13,371,000)	(1,145,000)	(19,417,000)

Income tax benefit...........................	(4,278,000)	(378,000)	(6,213,000)
Net loss.....................................	$ (9,093,000)	$ (767,000)	$ (13,204,000)
Basic and diluted net loss per common share....	$ (1.07)	$ (0.09)	$ (1.56)
Weighted average shares outstanding - diluted..	8,476,372	8,476,372	8,476,372

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

(UNAUDITED)

	NINE MONTHS ENDED NOVEMBER 30, 2001	NINE MONT NOVEMB 20
OPERATING ACTIVITIES		
Net loss..	$ (13,204,000)	$ (2,6
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:		
Asset impairment charge...........................	5,983,000	
Depreciation......................................	2,657,000	2,5
Amortization......................................	317,000	3
Loss on sale of property, furniture and equipment...	659,000	2
Changes in operating assets and liabilities:		
Accounts receivable...............................	7,210,000	(1,4
Merchandise inventories...........................	(6,243,000)	(13,7
Other current assets and other assets..............	(154,000)	(1,1
Accounts payable..................................	11,091,000	17,5
Accrued compensation and expenses..................	2,335,000	(9
Deferred revenue..................................	-	(3
Income taxes......................................	(6,316,000)	(1,4
Other long-term liabilities........................	644,000	
Net cash provided by (used in) operating activities..........	4,979,000	(7
INVESTING ACTIVITIES		
Proceeds from sale of property, furniture and equipment......	342,000	
Purchases of property, furniture and equipment..............	(2,935,000)	(6,8
Proceeds from sale of restricted investments................	2,580,000	
Purchase of restricted investments..........................	-	(2,6
Net cash used in investing activities.......................	(13,000)	(9,5
FINANCING ACTIVITIES		
Net (payments on) proceeds from revolving credit note........	(4,636,000)	10,3

Net cash (used in) provided by financing activities..........	(4,636,000)	10,3
Net increase in cash and cash equivalents....................	330,000	
Cash and cash equivalents at beginning of period.............	685,000	8
Cash and cash equivalents at end of period...................	$ 1,015,000	$ 9
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:		
Cash paid during the period for:		
Interest..	$ 3,070,000	$ 3,7
Income taxes..	$ 19,000	$ 2,3

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 28, 2001.

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 2000 financial statements to conform to the classifications used in 2001. The reclassifications had no effect on net loss or shareholders' equity as previously reported.

C. RESTRICTED INVESTMENTS

	11/30/01	11/30/00
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 held by the Company's subsidiary, First Retail Bank N.A., to comply with the Federal Banking Regulations.

The held-to-maturity investments consist of Federal Home Loan Bank bonds. These bonds are stated at cost at November 30, 2000, as the Company held these securities until maturity in June 2001.

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 as income on a straight-line basis over the contract period. This deferred revenue is classified as a current liability 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.

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. As a result of this change, the Company continued 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. Previously deferred extended service contract revenue recognized for the quarters ended November 30, 2001 and 2000 of $0 and $64,000, respectively, has been reflected as a reduction of selling, general, and administrative expenses.

E. DEBT

In April 1999, the Company, its existing banks, and three additional banks entered into an amended revolving credit agreement whereby the Company may borrow up to $65,000,000 through June 30, 2002. Under this agreement, the Company pays interest monthly at an interest rate ranging from the 30-day LIBOR rate (2.15% at November 30, 2001) plus 200 basis points to 260 basis points or the Prime Rate (5.00% at November 30, 2001), depending upon the Company's debt-to-worth ratio. As of December 1, 2001, the Company's rate was the Prime Rate. The Company had $59,125,000 outstanding on this revolver at November 30, 2001, which is classified as a current 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 accordance with SFAS No. 131, "Disclosure about Segments of an Enterprise and Related Information," the Company 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 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.

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, 2001 and 2000. 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, 2001			
NET SALES.........................	$ 24,670,000	$ -	$ 24,670,000
OTHER REVENUES....................	319,000	2,873,000	3,192,000
INTER-SEGMENT REVENUE.............	-	279,000	279,000
OPERATING (LOSS) EARNINGS.........	(13,159,000)	614,000	(12,545,000)
INTEREST EXPENSE..................	425,000	401,000	826,000
IDENTIFIABLE ASSETS...............	83,335,000	42,083,000	125,418,000
DEPRECIATION AND AMORTIZATION......	863,000	34,000	897,000
CAPITAL EXPENDITURES..............	205,000	-	205,000
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..............	2,339,000	3,000	2,342,000

FOR THE NINE MONTHS ENDED NOVEMBER 30, 2001			
NET SALES.........................	$ 68,269,000	$ -	$ 68,269,000
OTHER REVENUES....................	1,080,000	9,535,000	10,615,000
INTER-SEGMENT REVENUE.............	-	690,000	690,000
OPERATING (LOSS) EARNINGS.........	(20,057,000)	3,610,000	(16,447,000)
INTEREST EXPENSE..................	1,470,000	1,500,000	2,970,000
IDENTIFIABLE ASSETS...............	83,335,000	42,083,000	125,418,000
DEPRECIATION AND AMORTIZATION......	2,872,000	102,000	2,974,000
CAPITAL EXPENDITURES..............	2,935,000	-	2,935,000
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

G. RESTRUCTURING CHARGE

In November 2001, the Company recorded $4,864,000 in restructuring costs associated with the Company's exit from under-performing markets. These costs, in accordance with EITF 94-3, "Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity (including Certain Costs Incurred in a Restructuring)", represent the cost of closing stores in these markets. The amounts recorded consist of the costs associated with buying out store leases, inventory liquidation costs, and the loss on the sale or abandonment of leasehold improvements and furniture and fixtures. The charge also includes the severance costs associated with reducing its corporate office personnel by approximately 20% and its store personnel by approximately 17%. The Company expects the execution of its restructuring plan to be completed during fiscal year ended February 2003. The remaining liability as of November 30, 2001 was $2,763,000, which is included in accrued expenses on the balance sheet. As of November 30, 2001, the following amounts were recorded:

Activity For the Quarter Ended November 30, 2001

	ACCRUALS	WRITE-OFFS/ PAYMENTS	BALANCE AT NOVEMBER 30, 2001
Lease exit costs..................	$ 1,242,000	$ 807,000	$ 435,000
Sale/disposal of fixed assets......	1,966,000	608,000	1,358,000
Inventory liquidation costs........	1,338,000	483,000	855,000
Severance costs...................	318,000	203,000	115,000
Totals.......................	$ 4,864,000	$ 2,101,000	$ 2,763,000

H. ASSET IMPAIRMENT CHARGE

During the third quarter of fiscal year 2002, the Company recorded an asset impairment charge of $5,983,000. The charge includes a $5,180,000 write-down of goodwill due to the closing of a significant number of stores associated with the goodwill and the decrease in expected future cash flows from the remaining stores. The charge also includes an $803,000 reduction to fair value of the historical cost of assets associated with the Company's e-commerce initiative as a result of reduced revenues and earnings projections for Reeds.com.

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

RESULTS OF OPERATIONS

Net Sales

Net sales decreased 9.6% to $24,670,000 for the third quarter ended November 30, 2001, compared to $27,296,000 for the same quarter last year. Net sales for the nine months ended November 30, 2001 decreased 9.9% to $68,269,000 from $75,744,000 for the same period a year earlier. Same store sales, or stores open in comparable periods, declined 10.6% in the third quarter this year and 11.9% during the nine-month period this year. At November 30, 2001, the Company operated 115 stores in 21 states compared to 120 stores in 19 states at November 30, 2000. During the third quarter of fiscal 2001, the company closed four under performing stores in the Orlando FL, Tallahassee FL, Atlanta GA, and Nashville TN markets. The Company did not open any new stores during the third quarter this year and has no commitments to open stores in the remainder of this fiscal year. The Company is committed to opening one store in Durham NC in March 2002.

The sales of a retail jeweler depend upon having the right mixture of merchandise available in its stores. Core merchandise items are those that are the most profitable and have the highest turnover. The Company averaged 96.3% in-stock on its core items during third quarter fiscal 2002, compared to 96.0% last year; it averaged 93.3% in-stock on its entire basic merchandise mix compared to 94.1% during the same quarter a year ago. For the quarter ended November 30, 2001, core merchandise accounted for 51.4% of net sales, 56.3% of the items offered in the Company's basic merchandise mix, and 31.6% of its inventory investment. During the same quarter last year, 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. The average price of each piece of merchandise sold in the third quarter 2002 was $243, down from $249 a year earlier.

Credit sales for the third quarter of fiscal 2002 accounted for 41.8% of net sales compared to 49.3% a year earlier. Although the total transactions during the quarter were down 13.0% compared to last year same quarter, the average transaction size increased 5.8% for credit sales and 15.2% for cash sales.

Gross Profit

Gross margins were 47.1% during the quarter, down from 48.1% in the third quarter last year. Year-to-date, gross margins were 47.1%, down from 49.7% for the first nine months last year. The decrease in gross margins can be attributed to a higher level of promotional activity necessitated by the weak economy and the decrease in discretionary spending by consumers.

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

Selling, general, and administrative expenses as a percentage of net sales were 50.3% and 43.6% for the quarters ended November 30, 2001 and 2000, respectively. The increase as a percentage of net sales is attributable to the lower sales volume. Fixed costs, on a per store basis, including occupancy, base compensation, and benefits decreased 3.7% from the third quarter of the prior year, and year-to-date costs per store decreased 1.2%. 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 Months Ended	
	11/30/01	11/30/00	11/30/01	11/30/00

Compensation - salaries & hourly wages...	20.1 %	20.1 %	23.0 %	20.6 %
Compensation - bonuses & commissions.....	3.1 %	3.6 %	3.1 %	3.7 %
Compensation - benefits & other personnel costs.......................	4.2 %	4.3 %	4.8 %	5.3 %
Rents for space..........................	12.0 %	10.6 %	13.2 %	11.2 %
Advertising..............................	5.3 %	4.7 %	4.0 %	4.2 %
Bad debt.................................	7.6 %	5.6 %	6.6 %	5.3 %
Finance charges..........................	(8.4)%	(8.4)%	(9.9)%	(8.9)%
Late charge income.......................	(2.3)%	(2.8)%	(2.9)%	(2.2)%

Bad debt increased to $1,887,000 from $1,522,000 and rose to 7.6% of net sales for the quarter compared to 5.6% a year earlier. Gross write-offs for bad debts were $2,212,000 versus $1,607,000 in the same quarter last year. Net write-offs, after recovery of amounts previously written off, were $1,999,000 and $1,385,000 for the third quarter of the current and prior fiscal year, respectively. The allowance for doubtful accounts was 8.00% and 7.65% of gross customer receivables at the end of the third fiscal quarter of 2002 and 2001, respectively. The average delinquent account (accounts more than 90 days past due) represented 13.9% and 11.1% of the Company's accounts receivable portfolio for the third quarter of fiscal 2002 and 2001, respectively. The average approval rate on applications was 40.3% for the third quarter of the current year and 44.0% for the third quarter last year. The Company's policies and procedures regarding credit authorization, collection, and write-offs have not changed significantly during each of the two periods. The Company has entered into a purchase agreement to sell its proprietary credit card portfolio. The Company expects to close the sale before the end of this fiscal year and does not expect to record any write-down from the net stated value of the portfolio.

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 recognized 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, 2001 and 2000 of $0 and $64,000, respectively, as well as commission revenues of $319,000 and $566,000, respectively, have been reflected as a reduction of selling, general, and administrative expenses. Extended service agreements equaled 1.3% and 2.3% of net sales during the quarters ended November 30, 2001 and 2000, respectively.

Interest Expense

The average borrowings on the Company's line of credit dropped 5.8% over prior year. The Company continues to benefit from the general reduction of interest rates. The Company's effective pre-tax interest rate during the quarter dropped to 5.4% from 8.4% for the same period in the previous year. As a result, interest expense for the quarter was $826,000, 39.2% lower than the same quarter last year.

Income Taxes

The benefit for income taxes was $4,278,000 and $378,000 during the third quarters of fiscal 2002 and 2001, respectively. The Company's anticipated net effective tax rate was 32.0% during the third quarter ended November 30, 2001 and 33.0% in the third quarter of the previous year.

LIQUIDITY AND CAPITAL RESOURCES

The Company requires cash for purchasing inventory, opening new stores, remodeling existing stores, enhancing technology, and servicing debt. Working capital needs normally peak in the fall as the Company increases inventories to meet anticipated demand during the Christmas selling season. Working capital requirements will be financed by funds generated from operations, bank lines, and other steps described below. Cash provided by operations for the first nine months of the current year was $4,979,000 and cash used in operations was $794,000 for the first nine months of last year.

Decreased net sales have resulted in lower accounts receivables as customer payments are exceeding new charge sales. In addition, the Company has reduced inventory purchases because of the slowdown in consumer spending on discretionary items. The reductions in accounts receivable and inventories have reduced the amount of borrowings the Company can make under its revolving credit facility, so that only $58 - $60 million of its $65 million line is presently available.

As a result of the decreased profitability during the last eighteen months and the reduced liquidity that the Company has experienced, the Board of Directors and management have implemented a restructuring plan that involves: 1) closing a number of stores that are unprofitable and have a negative cash flow; 2) reducing personnel costs; and 3) restructuring its balance sheet.

The Company has entered into a purchase agreement to sell its proprietary credit card portfolio. The sale is contingent upon the Company having a $30 million two-year revolving bank facility in place by the date of the transaction. The Company expects to close the sale before the end of this fiscal year and does not expect to record any write-down from the net stated value of the portfolio. In anticipation of the sale of its proprietary credit card portfolio, the Company liquidated its subsidiary, First Retail Bank, NA on October 30, 2001, and, as a result, the $2.3 million of associated restricted investments, required to be maintained by banking regulations, became available for general corporate purposes. In conjunction with the sale of its receivables, the Company is negotiating with its lenders for an extension of its revolving bank facility through February 2004.

During the third quarter, Reeds closed four under-performing stores in the following locations: Orlando FL, Atlanta GA, Tallahassee FL, and Nashville TN. In the fourth quarter, the Company will be closing at least 15 additional locations via sales, lease terminations, and lease expirations. The Company recorded a $4.9 million restructuring charge in the third quarter, which included the associated lease termination fees, write-down of fixed assets, costs of closing 19 stores (including severance costs), as well as reducing the corporate headquarters personnel costs by 20%.

The impairment charge includes a $5.2 million write-down of goodwill due to the closing of a significant number of stores associated with the goodwill and the decrease in expected future cash flows from the remaining stores. The charge also includes an $800,000 reduction to fair value of the historical cost of assets associated with the Company's e-commerce initiative as a result of reduced revenues and earnings projections for Reeds.com. The non-recurring charges related to restructuring and impairment total $10.8 million.

Debt

Borrowings under the Company's revolving credit facility averaged $60.4 million during the third quarter of fiscal 2002 and $64.2 million during the same quarter a year ago. The maximum borrowings outstanding under the facility at any time during each of the quarters were $61.9 million and $65.0 million, respectively.

In April 1999, the Company, its existing banks, and three additional banks entered into an amended revolving credit agreement whereby the Company may borrow up to $65,000,000 through June 30, 2002. Under this agreement, the Company pays interest monthly at an interest rate ranging from the 30-day LIBOR rate (2.15% at November 30, 2001) plus 200 basis points to 260 basis points or the Prime Rate (5.00% at November 30, 2001), depending upon the Company's debt-to-worth ratio. As of December 1, 2001, the Company's rate was the Prime Rate.

The Company had $59,125,000 outstanding on this revolver at November 30, 2001, which is classified as a current 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.

The Company also has subordinated notes totaling $845,000 with three related parties, with interest payable monthly at the prime rate (5.00% at November 30, 2001) 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.

Working Capital

Working capital was $16,495,000 at November 30, 2001 compared to $79,636,000 at November 30, 2000 due to the reclassification of the revolving credit agreement to a current liability. The resulting ratio of current assets to current liabilities as of November 30, 2001 was 1.2 to 1, compared to 3.2 to 1 the same time last year. Capital expenditures totaled $2,935,000 and $6,884,000 for the nine months ended November 30, 2001 and 2000, respectively. The Company opened three stores during the quarter ended May 31, 2001; three stores in the quarter ended August 31, 2001 and no new stores were opened during the quarter ended November 30, 2001. The Company does not plan to open any additional stores during the remainder of this fiscal year.

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 and closings;

(ii) potential sale and any potential write-off of the Company's proprietary credit card portfolio;

(iii) potential financing arrangements with banks;

(iv) other elements of the Company's restructuring plans; and

(v) the future effects of these actions on cash flow and earnings.

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;

(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 the Company in the future.

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.

Not applicable.

(b) Reports on Form 8-K.

Not applicable.

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.

REEDS JEWELERS, INC.

January 14, 2002	/s/ James R. Rouse
	James R. Rouse Treasurer and Chief Financial Officer