

Edgar Filing: FRIEDMANS INC - Form 10-Q

FRIEDMANS INC  
Form 10-Q  
August 13, 2002

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

FORM 10-Q

(MARK ONE)

Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the Quarterly Period Ended June 29, 2002

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 0-22356

FRIEDMAN'S INC.

-----  
(Exact name of registrant as specified in its charter)

Delaware

58-2058362

-----  
(State or other jurisdiction of incorporation or organization)

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

4 West State Street  
Savannah, Georgia 31401

31401

-----  
(Address of principal executive offices)

-----  
(Zip Code)

(912) 233-9333

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

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

Indicate the number of shares outstanding of each of the issuer's classes of

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common stock, as of the latest practical date.

The number of shares of Registrant's Class A Common Stock \$.01 par value per share, outstanding at August 12, 2002 was 17,423,706.

The number of shares of Registrant's Class B Common Stock \$.01 par value per share, outstanding at August 12, 2002 was 1,196,283.

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#### Part I. Financial Information

##### Item 1.

#### FRIEDMAN'S INC.

#### CONSOLIDATED INCOME STATEMENTS

(Unaudited)

(In thousands, except per share and number of store data)

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|   | Three months ended |                  |
|---|--------------------|------------------|
|   | June 29,<br>2002   | June 30,<br>2001 |
|   | -----              | -----            |
| Net sales .....   | \$ 91,112          | \$ 85,236        |
| Operating Costs and Expenses:   |                    |                  |
| Cost of goods sold, including occupancy,<br>distribution and buying ..... | 48,212             | 46,427           |
| Selling, general and administrative .....                                 | 37,159             | 44,924           |
| Depreciation, amortization and impairment charges .....                   | 2,845              | 5,079            |
|   | -----              | -----            |
| Income (loss) from operations .....                                       | 2,896              | (11,194)         |
| Interest and other income from related party .....                        | (657)              | (625)            |
| Interest expense .....  | 505                | 1,243            |
|   | -----              | -----            |
| Income (loss) before income taxes .....                                   | 3,048              | (11,812)         |
| Income tax expense (benefit) .....  | 1,085              | (3,793)          |
| Minority interest .....   | (52)               | (974)            |
|   | -----              | -----            |
| Net income (loss) .....   | \$ 2,015           | \$ (7,045)       |
|   | =====              | =====            |
| Earnings (loss) per share - basic .....                                   | \$ 0.11            | \$ (0.49)        |
|   | =====              | =====            |
| Earnings (loss) per share - diluted .....                                 | \$ 0.11            | \$ (0.49)        |
|   | =====              | =====            |
| Weighted average shares - basic .....                                     | 18,620             | 14,517           |
| Weighted average shares - diluted .....                                   | 19,050             | 14,517           |
| Number of stores open .....   | 650                | 635              |

See notes to consolidated financial statements.

FRIEDMAN'S INC.  
CONSOLIDATED BALANCE SHEETS  
(In thousands, except per share and share amounts)

June 2  
2002  
-----

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### ASSETS

#### Current Assets:

|  |  |          |
|--|--|----------|
| Cash .....   |  | \$ 31    |
| Accounts receivable, net of allowance for doubtful accounts of \$23,400<br>at June 29, 2002, \$21,563 at June 30, 2001 and \$14,745 at<br>September 29, 2001 ..... |  | 153,1    |
| Inventories .....  |  | 144,4    |
| Deferred income taxes .....  |  | 3,0      |
| Other current assets .....   |  | 7,5      |
| Total current assets .....   |  | 308,4    |
| Equipment and improvements, net .....  |  | 51,4     |
| Tradename rights, net .....  |  | 5,0      |
| Receivable from Crescent Jewelers .....  |  | 108,8    |
| Other assets .....   |  | 3,3      |
| Total assets .....   |  | \$ 477,1 |

### LIABILITIES AND STOCKHOLDERS' EQUITY

#### Current Liabilities:

|   |  |          |
|---|--|----------|
| Accounts payable .....  |  | \$ 27,4  |
| Accrued liabilities and other .....   |  | 19,0     |
| Bank debt, Crescent Jewelers .....  |  | 108,8    |
| Bank debt, Friedman's and capital lease obligation .....  |  | 39,5     |
| Total current liabilities .....   |  | 194,9    |
| Long term bank debt, Friedman's .....   |  | 6        |
| Long term capital lease obligation .....  |  | 1,2      |
| Deferred income taxes and other .....   |  | 1,2      |
| Minority interest in equity of subsidiary .....   |  |          |
| <br>Stockholders' Equity:   |  |          |
| Preferred stock, par value \$.01, 10,000,000 shares authorized<br>and none issued .....   |  | 1        |
| Class A common stock, par value \$.01, 25,000,000 shares<br>authorized, 17,423,706, 13,321,655 and 13,322,655 issued and<br>outstanding at June 29, 2002, June 30, 2001 and<br>September 29, 2001, respectively ..... |  | 154,0    |
| Class B common stock, par value \$.01, 7,000,000 shares<br>authorized, 1,196,283 issued and outstanding .....   |  | 126,9    |
| Additional paid-in-capital .....  |  | (9)      |
| Retained earnings .....   |  |          |
| Stock purchase loans .....  |  |          |
| Total stockholders' equity .....  |  | 280,2    |
| Total liabilities and stockholders' equity .....  |  | \$ 477,1 |

Note: The balance sheet at September 29, 2001 has been derived from the audited financial statements at that date but does not include all the information and footnotes required by generally accepted accounting principles for complete financial statements.

See notes to consolidated financial statements.

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FRIEDMAN'S INC.  
CONSOLIDATED STATEMENTS OF CASH FLOWS  
(Unaudited)  
(In thousands)

|   | Nine<br>-----<br>June 2<br>2002<br>----- |
|---|--|
| Operating Activities:   |  |
| Net income .....  | \$ 23,4                                  |
| Adjustments to reconcile net income to net cash used in operating activities: |  |
| Depreciation, amortization and impairment charges .....                       | 8,4                                      |
| Provision for doubtful accounts .....   | 43,9                                     |
| Minority interest in loss of consolidated subsidiary .....                    | (1                                       |
| Changes in assets and liabilities:  |  |
| Increase in accounts receivable .....   | (64,4                                    |
| Increase in inventories .....   | (7,8                                     |
| Decrease (increase) in other assets .....                                     |  |
| (Decrease) increase in accounts payable and accrued liabilities .....         | (10,4                                    |
|   | -----                                    |
| Net cash used in operating activities .....                                   | (7,0                                     |
| Investing Activities:   |  |
| Additions to equipment and improvements .....                                 | (5,7                                     |
| Repayments of employee stock purchase loans .....                             | 1  |
|   | -----                                    |
| Net cash used in investing activities .....                                   | (5,5                                     |
| Financing Activities:   |  |
| (Repayments of) proceeds from bank borrowings .....                           | (21,6                                    |
| Proceeds from stock issuance, net .....                                       | 34,9                                     |
| Proceeds from employee stock purchases and options exercised .....            |  |
| Payment of cash dividend .....  | (8                                       |
|   | -----                                    |
| Net cash provided by financing activities .....                               | 12,5                                     |
|   | -----                                    |
| Decrease in cash .....  | (1                                       |
| Cash, beginning of period .....   | 4  |
|   | -----                                    |
| Cash, end of period .....   | \$ 3                                     |
|   | =====                                    |

See notes to consolidated financial statements.

FRIEDMAN'S INC.

Notes to Consolidated Financial Statements

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(Unaudited)

June 29, 2002

## NOTE A - BASIS OF PRESENTATION

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for the three month and nine month periods ended June 29, 2002 are not necessarily indicative of the results that may be expected for the year ending September 28, 2002. For further information, refer to the financial statements and footnotes thereto included in the Friedman's Inc. Annual Report on Form 10-K for the year ended September 29, 2001. Certain reclassifications have been made to prior year amounts to conform with current year presentation.

## NOTE B - NEW ACCOUNTING STANDARD

The Company adopted Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets" ("FAS 142"), on September 30, 2001. Under FAS 142, intangible assets deemed to have indefinite lives are no longer amortized but are subject to impairment tests in accordance with the new standard. Other intangible assets continue to be amortized over their useful lives. Application of the non-amortization provisions of FAS 142 to the Company's tradename rights, which had previously been amortized over fifteen years, resulted in an increase in net earnings of approximately \$77,000 and \$230,000 (\$0.004 and \$0.014 per fully diluted share) for the three months and nine months ended June 29, 2002, respectively.

## NOTE C - STORE CLOSINGS

During fiscal 2001, the Company recorded store closing expenses, principally for lease obligations, of \$4.2 million for the closure or planned closure of 33 stores. All 33 stores were closed by December 29, 2001. In connection with these closings, the Company made payments of \$0.5 million and \$1.1 million during the three months and nine months ended June 29, 2002, respectively. The Company had a remaining liability for lease obligations of approximately \$0.4 million at June 29, 2002.

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

The following discussion and other sections of this Form 10-Q may constitute forward-looking statements for purposes of the Securities Act of 1933, as amended, and the Securities Exchange Act of 1934, as amended, and as such may involve known and unknown risks, uncertainties and other factors that may cause our actual results, performance or achievements to be materially different from future results, performance or achievements expressed or implied

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by such forward-looking statements. For these statements, we claim the protection of the safe harbor for forward-looking statements contained in the Private Securities Litigation Reform Act of 1995. These statements are made based on management's current expectations or beliefs as well as assumptions made by, and information currently available to, management. The words "expect," "anticipate," "intend," "plan," "believe," "seek," "estimate," and similar expressions are intended to identify such forward-looking statements. Our actual results may differ materially from the results anticipated in these forward-looking statements due to a variety of factors, including without limitation those discussed under the section titled "Risk Factors" in the reports that we file with the SEC from time to time, including our Annual Report on Form 10-K for our fiscal year ended September 29, 2001. All written or oral forward-looking statements attributable to us are expressly qualified in their entirety by these cautionary statements.

### APPLICATION OF CRITICAL ACCOUNTING POLICIES

**Revenue Recognition.** We recognize revenue related to our merchandise sales at the time of sale, reduced by a provision for returns. We estimate this returns provision principally based on prior year return rates. We recognize finance charges, product warranties and credit insurance revenue ratably over the term or estimated term of the related contracts. We periodically review the estimated term of product warranties and may adjust the estimated term over which our product warranty revenue is recognized based on actual trends and experience. The effect of our estimation may be an increase or decrease in our warranty revenue and, as a result, a corresponding increase or decrease in our net sales. We classify finance charges, credit insurance and other credit service revenues as a reduction in selling, general and administrative expenses in the accompanying income statements.

**Accounts Receivable.** Approximately 50% of our merchandise sales are made under installment contracts due in periodic payments over periods typically ranging from three to 24 months. The accounts are stated net of unearned finance charges, product warranties, credit insurance and our allowance for doubtful accounts. We follow industry practice and include amounts due after one year in current assets.

We conduct credit approval and collection procedures at each store and follow internal company guidelines to evaluate the credit worthiness of our customers and to manage the collection process. In order to minimize our credit risk, we generally require down payments on credit sales and offer credit insurance to our customers. We believe that we are not dependent on a given industry or business for our customer base, and, therefore, have no significant concentration of credit risk.

We maintain an allowance for uncollectible accounts. We estimate the reserve each quarter based on historical experience, the composition of outstanding balances, trends at specific stores and other relevant information. The application of this methodology may result in increases or decreases in our provision for uncollectible accounts from quarter to quarter. Our policy is generally to write off in full any credit account receivable if no payments have been received for 120 days and any other credit accounts receivable, regardless of payment history, if judged uncollectible (for example, in the event of fraud in the credit application or bankruptcy).

We do not require separate collateral to secure credit purchases made by our customers, but we do retain a security interest in the purchased item.

**Store Opening and Closing Costs.** We expense store opening costs when incurred. We determine our store closing costs, consisting of fixed asset impairment charges and accruals for remaining lease obligations, and recognize these costs in the period in which we make the decision that a store will be

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closed. We then close the store shortly thereafter. Indicators of impairment generally do not exist with respect to our property and equipment except in circumstances of store closings.

Our senior management and our independent accountants have discussed each of the above accounting policies and the selection of the various accounting estimates used with the Audit Committee of our Board of Directors. The Audit Committee has reviewed the results of operations for the three months and nine months ended June 29, 2002.

THREE MONTHS ENDED JUNE 29, 2002 COMPARED TO THREE MONTHS ENDED JUNE 30, 2001

### RESULTS OF OPERATIONS

Net sales increased 6.9% to \$91.1 million for the three months ended June 29, 2002, from \$85.2 million for the three months ended June 30, 2001. The increase in sales was attributable to a comparable store sales increase of 4.0% and the addition of 15 net new stores since June 30, 2001.

Cost of goods sold, including occupancy, distribution and buying costs, increased 3.8% to \$48.2 million, or 52.9% of net sales, for the three months ended June 29, 2002, versus \$46.4 million, or 54.5% of net sales, for the three months ended June 30, 2001. The decline in cost of goods sold as a percentage of net sales was primarily the result of improved merchandise gross margins, particularly in the bridal and diamond solitaire category. The improvement in gross margin was also impacted by an increase in reserves for inventory disposition costs in the prior year.

Selling, general and administrative expenses decreased 17.3% to \$37.2 million for the three months ended June 29, 2002, from \$44.9 million for the three months ended June 30, 2001. As a percentage of net sales, selling, general and administrative expenses decreased to 40.8% for the three months ended June 29, 2002 as compared to 52.7% for the comparable period last year. For the three months ended June 30, 2001, selling, general and administrative expenses included a non-comparable charge of \$3.7 million related to the closing of 23 stores and operating expenses of \$1.2 million related to the Company's internet joint venture. Excluding the store closing charge and the consolidation of internet operations, selling, general and administrative expenses were \$40.0 million for the three months ended June 30, 2001, or 46.9% of net sales. This decrease of selling, general and administrative expenses in total and as a percentage of net sales was primarily the result of decreases in the provision for bad debts, direct operating expenses and an increase in receivable revenues. The improvement in the provision for bad debts as a percentage of net sales was primarily the result of a lower than expected charge-off performance during the quarter. Direct operating expenses decreased in total and as a percentage of net sales primarily due to the leveraging effect of the increase in comparable store sales. Receivable revenues increased in total and as a percentage of net sales primarily due to the increase in gross accounts receivable.

Depreciation, amortization and impairment charges decreased 44.0% to \$2.8 million for the three months ended June 29, 2002, from \$5.1 million for the three months ended June 30, 2001. Depreciation, amortization and impairment charges as a percentage of net sales was 3.1% for the three months ended June 29, 2002 compared to 6.0% in the comparable period in the prior year. The three months ended June 30, 2001 included non-comparable charges of \$0.6 million related to store closings and \$1.6 million related to the write-down of impaired assets used in the Company's internet joint venture. Excluding these non-comparable charges, depreciation, amortization and impairment charges for the three months ended June 30, 2001 was \$2.9 million, or 3.3% of net sales. The comparable decrease in depreciation, amortization and impairment expense was



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primarily due to our adoption of a new accounting standard. Effective September 30, 2001, we adopted Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets" ("FAS 142"). In accordance with FAS 142, we discontinued amortization of our tradename rights beginning September 30, 2001, resulting in an increase in net earnings of approximately \$77,000 (\$.004 per fully diluted share) for the three months ended June 29, 2002. The increase in net earnings for fiscal year 2002 due to adoption of FAS 142 is expected to be approximately \$301,000 (\$.02 per share). The decrease in depreciation, amortization and impairment charges resulting from the application of FAS 142 was somewhat offset by increased depreciation expense related to the increased store count versus the comparable period in the prior year.

Interest and other income from a related party was up slightly to \$0.7 million for the three months ended June 29, 2002 compared to \$0.6 million for the three months ended June 30, 2001. Interest expense decreased to \$0.5 million for the three months ended June 29, 2002 compared to \$1.2 million for the three months ended June 30, 2001. The decrease in interest expense was due to lower average borrowings levels, primarily due to net cash proceeds of \$35.0 million from the sale of our common stock, and a decrease in our effective interest rate. See "Liquidity and Capital Resources."

Net income increased by \$9.1 million to \$2.0 million for the three months ended June 29, 2002 compared to a net loss of \$7.0 million for the three months ended June 30, 2001. Basic and diluted earnings per share increased to \$0.11 for the three months ended June 29, 2002 from a loss per share of \$0.49 for the three months ended June 30, 2001. Basic weighted average common shares outstanding increased 28.3% to 18,620,000 for the three months ended June 29, 2002 from 14,517,000 for the comparable period in the prior year. Diluted weighted average

common shares outstanding increased 30.3% to 19,050,000 for the three months ended June 29, 2002 from 14,517,000 for the comparable period in the prior year. The increase in basic and diluted weighted average shares outstanding was primarily due to our issuance of 4.1 million shares of common stock in an offering completed on February 11, 2002.

NINE MONTHS ENDED JUNE 29, 2002 COMPARED TO NINE MONTHS ENDED JUNE 30, 2001

### RESULTS OF OPERATIONS

Net sales increased 6.0% to \$366.8 million for the nine months ended June 29, 2002, from \$346.2 million for the nine months ended June 30, 2001. The increase in sales was attributable to a comparable store sales increase of 3.3% and the addition of 15 net new stores since June 30, 2001.

Cost of goods sold, including occupancy, distribution and buying costs, increased 4.6% to \$188.9 million, or 51.5% of net sales, for the nine months ended June 29, 2002, versus \$180.7 million, or 52.2% of net sales, for the nine months ended June 30, 2001. The decline in cost of goods sold as a percentage of net sales was primarily the result of improved merchandise gross margins particularly in the bridal and diamond solitaire category. The improvement in gross margin was also impacted by an increase in reserves for inventory disposition costs in the prior year.

Selling, general and administrative expenses decreased 0.8% to \$133.3 million for the nine months ended June 29, 2002, from \$134.3 million for the nine months ended June 30, 2001. As a percentage of net sales, selling, general and administrative expenses decreased to 36.3% for the nine months ended June 29, 2002 as compared to 38.8% for the comparable period last year. Selling,

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general and administrative expenses for the nine months ended June 30, 2001 included a non-comparable charge of \$4.2 million related to the closing of 33 stores and operating expenses of \$2.2 million related to the Company's internet joint venture. Excluding the store closing charge and the consolidation of internet operations, selling, general and administrative expenses for the nine months ended June 30, 2001 was \$127.9 million or 36.9% of net sales. The decrease as a percentage of net sales was primarily the result of improved expense controls slightly offset by an increase in provision for bad debts.

Depreciation, amortization and impairment charges decreased 22.9% to \$8.5 million for the nine months ended June 29, 2002, from \$11.0 million for the nine months ended June 30, 2001. Depreciation, amortization and impairment charges as a percentage of net sales was 2.3% for the nine months ended June 29, 2002 compared to 3.2% in the comparable period in the prior year. The nine months ended June 30, 2001 included non-comparable charges of \$0.7 million related to store closings and \$1.9 million related to the depreciation and write-down of impaired assets used in the Company's internet joint venture. Excluding these non-comparable charges, depreciation, amortization and impairment charges for the nine months ended June 30, 2001 was \$8.4 million, or 2.4% of net sales. The decrease in depreciation expense as a percentage to net sales was primarily the result of the leveraging effect of the increase in comparable store sales and our adoption of FAS 142. Our adoption of FAS 142 resulted in an increase in net earnings of approximately \$230,000 (\$.014 per fully diluted share) for the nine months ended June 29, 2002.

Interest and other income from a related party increased to \$2.0 million for the nine months ended June 29, 2002 compared to \$1.9 million for the nine months ended and June 30, 2001. Interest expense decreased to \$2.2 million for the nine months ended June 29, 2002 compared to \$3.9 million for the nine months ended June 30, 2001. The decrease in interest expense was primarily due to a decrease in our effective interest rate and lower average borrowing levels. The decrease in average borrowing levels is primarily due to net cash proceeds of \$35.0 million from the sale of our common stock. See "Liquidity and Capital Resources."

Net income increased by 84.1% to \$23.4 million for the nine months ended June 29, 2002 compared to \$12.7 million for the nine months ended June 30, 2001. Basic earnings per share was \$1.41 for the nine months ended June 29, 2002 compared to \$0.88 for the nine months ended June 30, 2001. Basic weighted average common shares outstanding increased 14.5% to 16,604,000 for the nine months ended June 29, 2002 from 14,495,000 for the comparable period in the prior year. Diluted earnings per share was \$1.39 for the nine months ended June 29, 2002 compared to \$0.88 for the nine months ended June 30, 2001. Diluted weighted average common shares outstanding increased 16.4% to 16,867,000 for the nine months ended June 29, 2002 from 14,495,000 for the comparable period in the prior year. The increase in basic and diluted weighted average shares outstanding was primarily due to our issuance of 4.1 million shares of common stock in an offering completed on February 11, 2002.

### LIQUIDITY AND CAPITAL RESOURCES

For the nine months ended June 29, 2002, net cash used in our operating activities was \$7.1 million compared to \$2.1 million for the nine months ended June 30, 2001. During the nine months ended June 29, 2002, the Company used its increased cash flow to reduce accounts payable and accrued liabilities from \$67.9 million to \$46.5 million, resulting in reduced financial leverage.

Investing activities, principally capital expenditures associated with new and renovated stores, used cash of \$5.6 million for the nine months ended June 29, 2002 compared to \$9.8 million during the nine months ended June 30,

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2001. The decrease was due primarily to the opening of fewer stores than in the comparable period in the prior year.

Financing activities provided \$12.5 million of cash for the nine months ended June 29, 2002 compared to \$11.8 million for the nine months ended June 30, 2001. In February 2002, we completed the issuance of 4.1 million shares of our Class A common stock at a price of \$9.50 per share. Cash proceeds from the stock sale, net of related expenses, were \$35.0 million and were mostly used to repay bank debt.

On September 15, 1999, we entered into a three year \$67.5 million senior secured revolving credit facility. Borrowings under the credit facility bear interest at either the federal funds rate plus 0.5%, the prime rate or, at our option, the eurodollar rate plus applicable margin ranging from 1.00% to 1.75%. The applicable margin is determined based on a calculation of the combined leverage ratio of Friedman's and our affiliate, Crescent Jewelers. The facility is secured by certain of our assets. The credit facility also contains the following financial covenants:

- o measured as of the end of each fiscal quarter, Friedman's trailing twelve-month Consolidated Leverage Ratio must not be greater than 3.0:1.0;
- o at all times, Friedman's Consolidated Net Worth must not be less than the sum of (i) \$180 million, plus (ii) as of the end of each fiscal quarter, an amount equal to 50% of Consolidated Net Income (but not less than zero) for that fiscal quarter, which increases will be cumulative, plus (iii) an amount equal to 75% of net proceeds from certain equity transactions; and
- o measured as of the end of each fiscal quarter, Friedman's trailing twelve-month Consolidated Fixed Charge Ratio must not be less than 2.0:1.0.

For further information about the terms of these financial covenants, we refer you to our credit agreement and its amendments that we have filed as exhibits to our reports with the SEC.

At June 29, 2002, \$39.0 million was outstanding under the facility, with interest accruing on such borrowings in a range from 3.6% to 4.8%. Therefore, we had \$28.5 million of available borrowings under our credit facility at June 29, 2002. We were in compliance with our debt covenants as of June 29, 2002. Amounts available under our credit facility are subject to adjustment based on our accounts receivable balances and inventory levels.

Our credit facility matures on September 15, 2002. We believe that we will be able to replace this facility on terms similar to the current facility, and that we will have sufficient capital to fund our operations through the upcoming year.

In connection with our credit facility, we agreed to provide certain credit enhancements, including the support of \$60 million of our eligible receivables and inventories, and to guarantee the obligations of Crescent under its \$112.5 million senior secured revolving credit facility, provided by the same bank group as our credit facility. The level of support was recently increased to \$80 million of our eligible receivables and inventories. In consideration for these credit enhancements, Crescent makes quarterly payments to us in an amount equal to 2% per annum of the outstanding obligations of Crescent under its credit facility during the preceding fiscal quarter. In further consideration of these credit enhancements, Crescent issued us a warrant to purchase 7,942,904 shares of Crescent's non-voting Class A common stock, or approximately 50% of the capital stock of Crescent on a fully diluted basis, for

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an exercise price of \$500,000.

Crescent's bank facility limits certain capital and other nonrecurring expenditures. From the period beginning April 1, 2002 through the last day of the fiscal month June 2002, Crescent's Consolidated Capital Expenditures may not exceed \$750,000. Crescent must also have a minimum Consolidated EBITDA measured on a cumulative three-month basis at the end of each fiscal month. For the three months ended May 2002, the Consolidated EBITDA is \$1,950,000, and for the three months ended June 2002, the Consolidated EBITDA is \$1,775,000.

During our fiscal year 2001, Crescent violated two covenants under its credit facility as a result of its settlement of litigation in September 2001 and our third quarter loss. The lenders under the Crescent credit facility waived these violations, but the maturity of Crescent's debt was advanced to March 31, 2002 from September 15, 2002. This date was subsequently extended in several amendments in April 2002. These amendments, among other things, set the maturity date of Crescent's credit facility to July 12, 2002. On July 11, 2002 an additional amendment extended the maturity date to August 28, 2002.

We have selected the agents to lead the financing to replace the credit facilities of both Friedmans and Crescent. We anticipate that the financing will be in place by August 28, 2002. In conjunction with the new credit facilities for both companies, Friedman's will terminate its guarantee and provision of credit enhancement relating to Crescent's current credit facility, and will instead make a direct investment in Crescent. The final terms of the direct investment in Crescent by Friedman's will be approved by a committee of our independent directors. Pending completion of the financings by us and by Crescent, Crescent's entire liability under its credit facility, \$108.9 million as of June 29, 2002, has been recorded in our Consolidated Balance Sheet along with a corresponding asset of equal amount.

On June 1, 2002, our Board of Directors declared a quarterly dividend of \$0.02, payable on July 15, 2002, to stockholders of record as of June 28, 2002.

### ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.

Our market risk is limited to fluctuations in interest rates as it pertains to our borrowings under the credit facility. We pay interest on borrowings at either the federal funds rate plus 0.5%, the prime rate or, at our option, the eurodollar rate plus applicable margin ranging from 1.00% to 1.75%. If the interest rates on our borrowings average 100 basis points more in fiscal 2002 than they did in fiscal 2001, then our interest expense would increase and income before income taxes would decrease by \$656,000. This amount is determined solely by considering the impact of the hypothetical change in the interest rate on our borrowing cost without consideration for other factors such as actions management might take to mitigate its exposure to interest rate changes.

## Part II. Other Information

### Item 6. Exhibits and Reports on Form 8-K

The Company did not file a Current Report on Form 8-K during the three month period ended June 29, 2002.

## Edgar Filing: FRIEDMANS INC - Form 10-Q

The exhibits to this report on Form 10-Q are listed on the Exhibit Index which immediately follows the signature page hereto.

### EXHIBIT INDEX

Exhibit  
Number  
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- 3.1 Registrant's Certificate of Incorporation, as amended (incorporated by reference from Exhibit 4(a) to the Registrant's Registration Statement on Form S-8 (File No. 333-17755) dated March 21, 1997).
- 3.2 Bylaws of the Registrant (incorporated by reference from Exhibit 3.2 to the Registrant's Registration Statement on Form S-1 (File No. 33-67662), and amendments thereto, originally filed on August 19, 1993).
- 4.1 See Exhibits 3.1 and 3.2 for provisions of the Certificate of Incorporation and Bylaws of the Registrant defining rights of holders of Class A and Class B Common Stock of the Registrant.
- 4.2 Form of Class A Common Stock certificate of the Registrant (incorporated by reference from Exhibit 4.2 to the Registrant's Registration Statement on Form S-1 (File No. 33-67662), and amendments thereto, originally filed on August 19, 1993).
- 10.1 Amendment Number Six, dated July 11, 2002 to Credit Agreement dated September 15, 1999, by and between Crescent Jeweler's Inc., as Borrower, certain subsidiaries and affiliates of Crescent, as guarantors, the lenders named therein, Bank of America, N.A., as Administrative Agent, and General Electric Capital Corp., as Documentation Agent.

### SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) 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 on August 13, 2002.

FRIEDMAN'S INC.

By: /s/ Victor M. Suglia

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Victor M. Suglia  
Senior Vice President and  
Chief Financial Officer