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RAYOVAC CORP
Form 10-Q
May 14, 2002

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

FORM 10Q

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

For the quarterly period ended March 31, 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 001-13615

Rayovac Corporation

(Exact name of registrant as specified in its charter)

Wisconsin 22-2423556

(State or other jurisdiction of (I.R.S. Employer
incorporation or organization) Identification Number)

601 Rayovac Drive, Madison, Wisconsin 53711

(Address of principal executive offices) (Zip Code)

(608) 275-3340

(Registrant's telephone number, including area code)

Not Applicable

(Former name, former address and former fiscal year, if changed since last report.)

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 (X) No ()

The number of shares outstanding of the Registrant's common stock, \$.01 par value, as of May 7, 2002, was 32,030,105.

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PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

RAYOVAC CORPORATION
 CONDENSED CONSOLIDATED BALANCE SHEETS
 March 31, 2002 and September 30, 2001
 (Unaudited)
 (In thousands)

-ASSETS-

| | MARCH 31 2002 ----- |
|------------------------------------|---------------------------|
| Current assets: | |
| Cash and cash equivalents | \$ 9,48 |
| Receivables | 116,30 |
| Inventories | 81,01 |
| Prepaid expenses and other | 32,92 |
| | ----- |
| Total current assets | 239,72 |
| Property, plant and equipment, net | 105,61 |
| Deferred charges and other, net | 43,39 |
| Intangible assets, net | 118,90 |
| | ----- |
| Total assets | \$ 507,63 ===== |

-LIABILITIES AND SHAREHOLDERS' EQUITY -

| | |
|--|----------|
| Current liabilities: | |
| Current maturities of long-term debt | \$ 25,46 |
| Accounts payable | 45,86 |
| Accrued liabilities: | |
| Wages and benefits and other | 29,69 |
| Other special charges | 2,79 |
| | ----- |
| Total current liabilities | 103,82 |
| Long-term debt, net of current maturities | 208,01 |
| Employee benefit obligations, net of current portion | 20,82 |
| Other | 12,58 |
| | ----- |
| Total liabilities | 345,24 |
| Shareholders' equity: | |
| Commonstock, \$.01 par value, authorized 150,000 shares; issued 61,564 and 61,579 shares, respectively; outstanding 32,028 and and 32,043 shares, respectively | 61 |
| Additional paid-in capital | 180,42 |
| Retained earnings | 125,76 |
| Accumulated other comprehensive loss | (8,31) |
| Notes receivable from officers/shareholders | (3,86) |
| | ----- |
| | 294,62 |

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| | |
|--|-----------|
| Less: Treasury stock, at cost, 29,536 shares | (130,07 |
| Less: Unearned restricted stock compensation | (2,16 |
| | ----- |
| Total shareholders' equity | 162,39 |
| | ----- |
| Total liabilities and shareholders' equity | \$ 507,63 |
| | ===== |

SEE ACCOMPANYING NOTES WHICH ARE AN INTEGRAL PART OF THESE STATEMENTS.

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RAYOVAC CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
For the three and six month periods ended March 31, 2002 and April 1, 2001
(Unaudited)
(In thousands)

| | THREE MONTHS | |
|--|--------------|------------|
| | 2002 | 2001 |
| | ----- | ----- |
| Net sales | \$ 121,153 | \$ 134,679 |
| Cost of goods sold | 71,203 | 78,507 |
| Special charges | 16 | 230 |
| | ----- | ----- |
| Gross profit | 49,934 | 55,942 |
| Selling | 24,612 | 28,011 |
| General and administrative | 9,067 | 11,117 |
| Research and development | 3,412 | 3,005 |
| | ----- | ----- |
| Total operating expenses | 37,091 | 42,133 |
| | | |
| Income from operations | 12,843 | 13,809 |
| Interest expense | 4,057 | 7,182 |
| Other expense (income), net | 397 | 181 |
| | ----- | ----- |
| Income before income taxes | 8,389 | 6,446 |
| Income tax expense | 3,009 | 2,321 |
| | ----- | ----- |
| Net income | \$ 5,380 | \$ 4,125 |
| | ===== | ===== |
| BASIC EARNINGS PER SHARE | | |
| Weighted average shares and equivalents outstanding | 31,767 | 27,578 |
| Net income | \$ 0.17 | \$ 0.15 |
| | ===== | ===== |
| DILUTED EARNINGS PER SHARE | | |
| Weighted average shares and equivalents outstanding | 32,344 | 28,719 |

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| | | |
|------------|---------|---------|
| Net income | \$ 0.17 | \$ 0.14 |
| | ===== | ===== |

SEE ACCOMPANYING NOTES WHICH ARE AN INTEGRAL PART OF THESE STATEMENTS.

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RAYOVAC CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
For the six month periods ended March 31, 2002 and April 1, 2001
(Unaudited)
(In thousands)

Cash flows from operating activities:
Net income
Non-cash adjustments to net income:
 Amortization
 Depreciation
 Other non-cash adjustments
Net changes in assets and liabilities

 Net cash provided by operating activities

Cash flows from investing activities:
Purchases of property, plant and equipment

 Net cash used by investing activities

Cash flows from financing activities:
Reduction of debt
Proceeds from debt financing
Issuance of common stock
Other

 Net cash used by financing activities

Effect of exchange rate changes on cash and cash equivalents

 Net (decrease) increase in cash and cash equivalents

Cash and cash equivalents, beginning of period

Cash and cash equivalents, end of period

SEE ACCOMPANYING NOTES WHICH ARE AN INTEGRAL PART OF THESE STATEMENTS.

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RAYOVAC CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)
(IN THOUSANDS, EXCEPT PER SHARE AMOUNTS)

1 SIGNIFICANT ACCOUNTING POLICIES

BASIS OF PRESENTATION: These financial statements have been prepared by Rayovac Corporation (the "Company"), without audit, pursuant to the rules and regulations of the Securities and Exchange Commission (the "SEC") and, in the opinion of the Company, include all adjustments (which are normal and recurring in nature) necessary to present fairly the financial position of the Company at March 31, 2002, results of operations and cash flows for the three and six month periods ended March 31, 2002, and April 1, 2001. Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted pursuant to such SEC rules and regulations. These condensed consolidated financial statements should be read in conjunction with the audited financial statements and notes thereto as of September 30, 2001. Certain prior year amounts have been reclassified to conform with the current year presentation.

SHIPPING AND HANDLING COSTS: The Company incurred shipping and handling costs of \$5,394 and \$6,612 and \$12,390 and \$13,931 for the three and six months ended March 31, 2002 and April 1, 2001, respectively, which are included in selling expense.

CONCENTRATION OF CREDIT RISK: Trade receivables potentially subject the Company to credit risk. The Company extends credit to its customers based upon an evaluation of the customer's financial condition and credit history and generally does not require collateral. The Company monitors its customer's credit and financial conditions based on changing economic conditions and will make adjustments to credit policies as required. The Company has historically incurred minimal credit losses but in the six months ending March 31, 2002 experienced a significant loss resulting from the bankruptcy filing of a major retailer in the United States.

The Company has a broad range of customers including many large retail outlet chains, one of which accounts for a significant percentage of our sales volume. This major customer represented approximately 22% and 20%, respectively, of receivables as of March 31, 2002 and September 30, 2001.

Approximately 25% of the Company's sales occur outside of North America, and these sales and related receivables are subject to varying degrees of credit, currency, political and economic risk. The Company monitors these risks and makes appropriate provisions for collectability based on an assessment of the risks present. The Argentine Peso and Venezuelan Bolivars devaluation did not have a significant impact on the Company's estimate of collectability.

ADOPTION OF NEW ACCOUNTING PRONOUNCEMENTS: In May 2000, the Emerging Issues Task Force (EITF) reached a consensus on Issue No. 00-14, "Accounting for Certain Sales Incentives". This Issue addresses the recognition, measurement, and income statement classification for various types of sales incentives including discounts, coupons, rebates and free products. In April 2001, the EITF reached a consensus on Issue

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No. 00-25, "Vendor Income Statement Characterization of Consideration to a Purchaser of the Vendor's Products or Services". This Issue addresses when consideration from a vendor to a retailer or distributor in connection with the purchase of the vendor's products to promote sales of the vendor's products should be classified in the vendor's income statement as a reduction of revenue or expense. The Company adopted EITF 00-14 and EITF 00-25 in the second fiscal quarter of 2002.

The adoption resulted in the following reclassifications for the three and six month periods ended March 31, 2002 and April 1, 2001 in the Company's results of operations. For the three months ended March 31, 2002 and April 1, 2001, net sales were reduced by \$8,823 and \$10,513, respectively; cost of sales were increased by \$2,705 and \$2,415, respectively; and selling expenses were reduced by \$11,528 and \$12,928, respectively. For the six months ended March 31, 2002 and April 1, 2001, net sales were reduced by \$29,290 and \$29,765, respectively;

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cost of sales were increased by \$7,947 and \$6,969, respectively; and selling expenses were reduced by \$37,237 and \$36,734, respectively.

Concurrent with the adoption of EITF 00-25, the Company reclassified certain accrued trade incentives as a contra receivable versus the Company's previous presentation as a component of accounts payable. Historically, customers offset earned trade incentives when making payments on account. Therefore, the Company believes the reclassification of these accrued trade incentives as a contra receivable better reflects the underlying economics of the Company's net receivable due from trade customers.

The reclassification results in a reduction in accounts receivable and accounts payable in our Consolidated Balance Sheets of \$22,163 and \$21,383 at March 31, 2002 and September 30, 2001, respectively.

Effective October 1, 2001, the Company adopted Statement of Financial Accounting Standards (SFAS) 141, BUSINESS COMBINATIONS, and SFAS 142, GOODWILL AND OTHER INTANGIBLE ASSETS.

Statement 141 requires that the purchase method of accounting be used for all business combinations initiated or completed after June 30, 2001. Statement 141 also specifies criteria that intangible assets acquired in a purchase method business combination must meet to be recognized and reported apart from goodwill. Statement 142 requires that goodwill and intangible assets with indefinite useful lives no longer be amortized, but instead tested for impairment at least annually in accordance with the provisions of Statement 142. Statement 142 also requires that intangible assets with estimable useful lives be amortized over their respective estimated useful lives to their estimated residual values, and reviewed for impairment in accordance with Statement 121, ACCOUNTING FOR THE IMPAIRMENT OF LONG-LIVED ASSETS AND FOR LONG-LIVED ASSETS TO BE DISPOSED OF. Upon the transition to Statement 142, no goodwill was deemed to be impaired.

An identification of the impacts to date of adopting Statement 142 follows:

THREE MONTHS ENDING

SIX

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| | MARCH 31, ----- 2002 ---- | APRIL 1, ----- 2001 ---- | MARCH ----- 200 ---- |
|---|------------------------------------|-----------------------------------|-------------------------------|
| Reported net income..... | \$5,380 | \$4,125 | \$5, |
| Add back: Goodwill amortization, net of tax of \$0..... | -- | 258 | |
| Add back: Trade name amortization, net of tax of \$213 and \$427, respectively..... | -- | 349 | |
| | ----- | ----- | ---- |
| Adjusted net income..... | \$5,380 | \$4,732 | \$5, |
| | ===== | ===== | ===== |
| BASIC EARNINGS PER SHARE: | | | |
| ----- | | | |
| Reported net income..... | \$0.17 | \$0.15 | \$0 |
| Goodwill amortization..... | -- | 0.01 | |
| Trade name amortization..... | -- | 0.01 | |
| | ----- | ----- | ---- |
| Adjusted net income..... | \$0.17 | \$0.17 | \$0 |
| | ===== | ===== | ===== |
| DILUTED EARNINGS PER SHARE: | | | |
| ----- | | | |
| Reported net income..... | \$0.17 | \$0.14 | \$0 |
| Goodwill amortization..... | -- | 0.01 | |
| Trade name amortization..... | -- | 0.01 | |
| | ----- | ----- | ---- |
| Adjusted net income..... | \$0.17 | \$0.16 | \$0 |
| | ===== | ===== | ===== |

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DERIVATIVE FINANCIAL INSTRUMENTS:

Derivative financial instruments are used by the Company principally in the management of its interest rate, foreign currency and raw material price exposures. The Company does not hold or issue derivative financial instruments for trading purposes.

The Company uses interest rate swaps to manage its interest rate risk. The swaps are designated as cash flow hedges with the fair value recorded in Other Comprehensive Income ("OCI") and as a hedge asset or liability, as applicable. The swaps settle periodically in arrears with the related amounts for the current settlement period payable to, or receivable from, the counter-parties included in accrued liabilities or accounts receivable and recognized in earnings as an adjustment to interest expense from the underlying debt to which the swap is designated. During the three and six month periods ended March 31, 2002, \$1,273 and \$2,348, respectively, of pretax derivative losses from such hedges were recorded as an adjustment to interest expense. At March 31, 2002, the Company had a portfolio of interest rate swaps outstanding which effectively fixes the interest rates on floating rate debt at rates as follows: 6.404% for a notional principal amount of \$75,000 through October 2002, 4.458% for a notional principal amount of \$70,000 from October 2002 through July 2004 and 3.769% for a notional principal amount of \$100,000 through August 2004. The derivative net gains on these contracts recorded in OCI at March 31, 2002 was an after-tax gain of \$57.

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The Company enters into forward and swap foreign exchange contracts, to hedge the risk from forecasted settlement in local currencies of inter-company purchases and sales, trade sales, and trade purchases. These contracts generally require the Company to exchange foreign currencies for U.S. dollars or Pounds Sterling. These contracts are designated as cash flow hedges with the fair value recorded in OCI and as a hedge asset or liability, as applicable. Once the forecasted transaction has been recognized as a purchase or sale and a related liability or asset recorded in the balance sheet, the gain or loss on the related derivative hedge contract is reclassified from OCI into earnings as an offset to the change in value of the liability or asset. During the three and six month periods ended March 31, 2002, \$0 and \$17, respectively, of pretax derivative losses were recorded as an adjustment to earnings for cash flow hedges related to an asset or liability. During the three and six month periods ended March 31, 2002, \$9 and \$66, respectively, of pretax derivative gains were recorded as an adjustment to earnings for forward and swap contracts settled at maturity. At March 31, 2002, the Company had a series of swap contracts outstanding with a contract value of \$740. The derivative net gain on these contracts recorded in OCI at March 31, 2002 was an after-tax gain of \$22.

The Company periodically enters into forward foreign exchange contracts, to hedge the risk from changes in fair value from unrecognized firm purchase commitments. These firm purchase commitments generally require the Company to exchange U.S. dollars for foreign currencies. These hedge contracts are designated as fair value hedges with the fair value recorded in earnings on a pretax basis and as a hedge asset or liability, as applicable. To the extent effective, changes in the value of the forward contracts recorded in earnings will be offset by changes in the value of the hedged item, also recorded in earnings on a pretax basis and as an asset or liability, as applicable. Once the firm purchase commitment has been consummated, the firm commitment asset or liability balance will be reclassified as an addition to or subtraction from, the carrying value of the purchased asset. The Company previously entered into a series of forward contracts through October 2001 to hedge the exposure from a firm commitment to purchase certain battery manufacturing equipment denominated in Japanese Yen. During the three and six month periods ended March 31, 2002, \$0 and \$63, respectively, of pretax derivative gains were recorded as an adjustment to earnings for fair value hedges of this firm purchase commitment and \$0 and \$63, respectively, of pretax losses were recorded as an adjustment to earnings for changes in fair value of this firm purchase commitment. During the three and six month periods ended March 31, 2002, \$0 and \$78, respectively, of pretax derivative losses were recorded as an adjustment to earnings for fair value hedges of this firm purchase commitment that were settled at maturity and \$0 and \$78, respectively, of pretax gains were recorded as an adjustment to earnings for payments made against this firm purchase commitment.

The Company is exposed to risk from fluctuating prices for zinc used in the manufacturing process. The Company hedges a portion of this risk through the use of commodity swaps. The swaps are designated as cash flow hedges with the fair value recorded in OCI and as a hedge asset or liability, as applicable. The fair value of the swaps is reclassified from OCI into earnings when the hedged purchase of zinc metal-based items also affects

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earnings. The swaps effectively fix the floating price on a specified quantity of zinc through a specified date. During the three and six month periods ended March 31, 2002, \$699 and \$1,576, respectively, of pretax derivative losses were recorded as an adjustment to cost of sales for swap contracts settled at maturity. At March 31, 2002, the Company had a series of swap contracts outstanding through August 2003 with a contract value of \$9,470. The derivative net losses on these contracts recorded in OCI at March 31, 2002 was an after-tax loss of \$301.

2 INVENTORIES

Inventories consist of the following:

| | MARCH 31, 2002 |
|----------------------|----------------|
| Raw material..... | \$21,480 |
| Work-in-process..... | 20,153 |
| Finished goods..... | 39,383 |
| | \$81,016 |
| | ===== |

3 ACQUIRED INTANGIBLE ASSETS AND GOODWILL

| | MARCH 31, 2002 | | | |
|---|-----------------------------|-----------------------------|-------------------|-----------------------------|
| | GROSS CARRYING AMOUNT | ACCUMULATED AMORTIZATION | NET INTANGIBLE | GROSS CARRYING AMOUNT |
| AMORTIZED INTANGIBLE ASSETS | | | | |
| Non-compete agreement | \$ 700 | \$ 560 | \$ 140 | \$ 700 |
| Proprietary technology | 525 | 291 | 234 | 525 |
| | \$ 1,225 | \$ 851 | \$ 374 | \$ 1,225 |
| | ===== | ===== | ===== | ===== |
| PENSION INTANGIBLES | | | | |
| Under-funded pension | \$ 3,081 | \$-- | \$ 3,081 | \$ 3,081 |
| | ===== | ===== | ===== | ===== |
| UNAMORTIZED INTANGIBLE ASSETS | | | | |
| Trade name | \$90,000 | \$ 4,875 | \$85,125 | \$90,000 |
| | ===== | ===== | ===== | ===== |
| GOODWILL | | | | |
| | | NORTH AMERICA | LATIN AMERICA | EUROPE/ ASIA |
| Balance as of October 1, 2001, net..... | | \$1,035 | \$26,884 | \$2,919 |
| Effect of translation..... | | -- | -- | (1) |
| | | \$1,035 | \$26,884 | \$2,918 |
| Balance as of March 31, 2002, net..... | | \$1,035 | \$26,884 | \$2,917 |

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The non-compete agreement is being amortized on a straight-line basis over 5 years. The proprietary technology assets are being amortized on a straight-line basis over 15 to 17 years.

The trade name and Latin America segment goodwill are associated with the 1999 acquisition of ROV Limited and were being amortized on a straight-line basis over 40 years. The North America segment goodwill is associated with the 1998 acquisition of Best Labs and was being amortized on a straight-line basis over 15 years. The Europe/ROW segment goodwill is associated with the 1998 acquisition of Brisco GmbH in Germany and was being amortized on a straight-line basis over 15 years.

Pursuant to Statement 142, the Company ceased amortizing goodwill assets on October 1, 2001. Upon initial application of Statement 142, the Company reassessed the useful lives of its intangible assets and deemed only the trade name asset to have an indefinite useful life because it is expected to generate cash flows indefinitely. Based on this, the Company ceased amortizing the trade name on October 1, 2001 also.

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The amortization expense for the three and six months ended March 31, 2002 and April 1, 2001 are as follows:

| | THREE MONTHS ENDING | |
|---|---------------------|---------------|
| | MARCH 31, 2002 | APRIL 1, 2001 |
| | ----- | ----- |
| AMORTIZATION EXPENSE | | |
| Goodwill amortization..... | \$-- | \$258 |
| Trade name amortization..... | -- | \$562 |
| Non-compete and proprietary technology..... | 43 | 43 |
| | --- | --- |
| | \$43 | \$863 |
| | === | === |

4 OTHER COMPREHENSIVE INCOME

Comprehensive income and the components of other comprehensive income for the three and six months ended March 31, 2002 and April 1, 2001 are as follows:

| | THREE MONTHS ENDING | | |
|------------------------------------|---------------------|---------------|-------|
| | MARCH 31, 2002 | APRIL 1, 2001 | MAR |
| | ----- | ----- | ----- |
| Net income | \$ 5,380 | \$ 4,125 | |
| Other comprehensive income (loss): | | | |
| Foreign currency translation | (4,589) | (663) | |

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| | | |
|--|----------|----------|
| Net unrealized loss on available for sale securities | (6) | -- |
| Cumulative effect of change in accounting principle | -- | -- |
| Net unrealized gain (loss) on derivative instruments | 1,574 | (981) |
| | ----- | ----- |
| Comprehensive income | \$ 2,359 | \$ 2,481 |
| | ===== | ===== |

Net exchange gains or losses resulting from the translation of assets and liabilities of foreign subsidiaries are accumulated in a separate section of stockholder's equity. Also included are the effects of exchange rate changes of intercompany balances of a long-term nature and transactions designated as hedges of net foreign investments. The changes in accumulated foreign currency translation for the three and six months ended March 31, 2002 were primarily attributable to currency devaluation in Argentina, \$2,381 and \$2,383, respectively, and in Venezuela, \$1,672 and \$1,718, respectively.

5 NET INCOME PER COMMON SHARE

Net income per common share for the three and six months ended March 31, 2002 and April 1, 2001 is calculated based upon the following shares:

| | THREE MONTHS ENDING | |
|---|---------------------|---------------|
| | MARCH 31, 2002 | APRIL 1, 2001 |
| | ----- | ----- |
| Basic..... | 31,767 | 27,578 |
| Effect of restricted stock and assumed conversion of options..... | 577 | 1,141 |
| | ----- | ----- |
| Diluted..... | 32,344 | 28,719 |
| | ===== | ===== |

6 COMMITMENTS AND CONTINGENCIES

In March 1998, the Company entered into an agreement to purchase certain equipment and to pay annual royalties. In connection with this 1998 agreement, which supersedes previous agreements dated December 1991, and March 1994, the Company committed to pay royalties of \$2,000 in 1998 and 1999, \$3,000 in 2000 through 2002, and \$500 in each year thereafter, as long as the related equipment patents are enforceable (2022). The Company incurred royalty expenses of \$2,000 for 1999, \$2,250 for 2000 and \$3,000 for 2001. At March 31, 2002, the Company had commitments of approximately \$1,004 for the acquisition of inventory and manufacturing equipment, all of which are expected to be incurred in calendar 2002.

The Company has provided for the estimated costs associated with environmental remediation activities at some of its current and former manufacturing sites. In addition, the Company, together with other

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parties, has been designated a potentially responsible party of various third-party sites on the United States EPA National Priorities List (Superfund). The Company provides for the estimated costs of investigation and remediation of these sites when such losses are probable and the amounts can be reasonably estimated. The actual cost incurred may vary from these estimates due to the inherent uncertainties involved. The Company believes that any additional liability in excess of the amounts provided of \$1,598, which may result from resolution of these matters, will not have a material adverse effect on the financial condition, liquidity, or cash flow of the Company.

The Company has certain other contingent liabilities with respect to litigation, claims and contractual agreements arising in the ordinary course of business. In the opinion of management, it is either not likely or premature to determine whether such contingent liabilities will have a material adverse effect on the financial condition, liquidity or cash flow of the Company.

7 OTHER

During Fiscal 2001, the Company recorded special charges related to: (i) an organizational restructuring in the U.S, (ii) manufacturing and distribution cost rationalization initiatives in the Company's Tegucigalpa, Honduras and Mexico City, Mexico manufacturing facilities and in the Company's European operations, (iii) the closure of the Company's Wonewoc, Wisconsin, manufacturing facility, (iv) the rationalization of uneconomic manufacturing processes at the Company's Fennimore, Wisconsin, manufacturing facility, and rationalization of packaging operations and product lines, and (v) costs associated with the Company's June 2001 secondary offering. The amount recorded includes \$10,100 of employee termination benefits for approximately 570 employees, \$10,200 of equipment, inventory, and other asset write-offs, and \$2,000 of other expenses. A summary of the 2001 restructuring activities follows:

2001 RESTRUCTURING SUMMARY

| | TERMINATION BENEFITS ----- | OTH COS ---- |
|----------------------------|----------------------------------|--------------------|
| Expense accrued | \$ 5,000 | \$ 11 |
| Change in estimate | 4,400 | |
| Expense as incurred | 700 | 1 |
| Cash expenditures | (5,800) | (1 |
| Non-cash charges | -- | (9 |
| | ----- | ---- |
| Balance September 30, 2001 | \$ 4,300 | \$ 1 |
| Cash expenditures | (1,300) | |
| Non-cash charges | -- | |
| | ----- | ---- |
| Balance December 30, 2001 | \$ 3,000 | \$ 1 |
| Cash expenditures | (1,500) | |
| Non-cash charges | -- | |
| | ----- | ---- |
| Balance March 31, 2002 | \$ 1,500 ===== | \$ 1 ===== |

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8 SEGMENT INFORMATION

The Company manages operations in three reportable segments based upon geographic area. North America includes the United States and Canada; Latin America includes Mexico, Central America, and South America; Europe/Rest of World ("Europe/ROW") includes the United Kingdom, Europe and all other countries in which the Company does business.

The Company manufactures and markets dry cell batteries including alkaline, zinc carbon, alkaline rechargeable, hearing aid, and other specialty batteries and lighting products throughout the world.

Net sales and cost of sales to other segments have been eliminated. The gross contribution of inter segment sales is included in the segment selling the product to the external customer. Segment revenues are based upon the geographic area in which the product is sold.

The reportable segment profits do not include interest expense, interest income, and income tax expense. Also, not included in the reportable segments, are corporate expenses including corporate purchasing expense, general and administrative expense and research and development expense. All depreciation and amortization included in income from operations is related to corporate or reportable segments. Costs are identified to reportable segments or corporate, according to the function of each cost center.

The reportable segment assets do not include cash, deferred tax benefits, investments, long-term intercompany receivables, most deferred charges, and miscellaneous assets. Capital expenditures are related to reportable segments or corporate. Variable allocations of assets are not made for segment reporting.

REVENUES FROM EXTERNAL CUSTOMERS

| | THREE MONTHS ENDING | | MAR |
|---------------------|---------------------|---------------|-----|
| | MARCH 31, 2002 | APRIL 1, 2001 | |
| North America..... | \$89,752 | \$96,527 | |
| Latin America..... | 18,378 | 26,498 | |
| Europe/ROW..... | 13,023 | 11,654 | |
| Total segments..... | \$121,153 | \$134,679 | |

INTER SEGMENT REVENUES

| | THREE MONTHS ENDING | | MAR |
|---------------------|---------------------|---------------|-----|
| | MARCH 31, 2002 | APRIL 1, 2001 | |
| North America..... | \$7,695 | \$8,728 | |
| Latin America..... | 1,972 | 2,965 | |
| Europe/ROW..... | 730 | 582 | |
| Total segments..... | \$10,397 | \$12,275 | |

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| SEGMENT PROFIT | THREE MONTHS ENDING | | |
|----------------------------------|---------------------|---------------|----------------|
| | MARCH 31, 2002 | APRIL 1, 2001 | MARCH 31, 2001 |
| | ----- | ----- | ----- |
| North America..... | \$17,752 | \$15,192 | |
| Latin America..... | 504 | 4,510 | |
| Europe/ROW..... | 1,108 | 1,118 | |
| Total segments..... | 19,364 | 20,820 | |
| Corporate..... | 6,505 | 6,781 | |
| Special charges..... | 16 | 230 | |
| Interest expense..... | 4,057 | 7,182 | |
| Other expense (income), net..... | 397 | 181 | |
| Income before income taxes..... | \$8,389 | \$6,446 | |

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| SEGMENT ASSETS | SIX MONTHS |
|---------------------------------|----------------------------------|
| | ----- MARCH 31, 2002 ----- |
| North America..... | \$232,287 |
| Latin America..... | 202,054 |
| Europe/ROW..... | 29,305 |
| Total segments..... | \$463,646 |
| Corporate..... | 43,991 |
| Total assets at period end..... | \$507,637 |

9 GUARANTOR SUBSIDIARIES (ROV HOLDING, INC. AND ROVCAL, INC.)

The following condensed consolidating financial data illustrate the composition of the consolidated financial statements. Investments in subsidiaries are accounted for by the Company and the Guarantor Subsidiaries using the equity method for purposes of the consolidating presentation. Earnings of subsidiaries are therefore reflected in the Company's and Guarantor Subsidiary's' investment accounts and earnings. The principal elimination entries eliminate investments in subsidiaries and inter-company balances and transactions. Separate financial statements of the Guarantor Subsidiaries are not presented because management has determined that such financial statements would not be material to investors.

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RAYOVAC CORPORATION AND SUBSIDIARIES
 CONDENSED CONSOLIDATING BALANCE SHEET
 As of March 31, 2002
 (Unaudited)
 (In thousands)

| | PARENT | GUARANTOR SUBSIDIARIES | NONGU SUBSI |
|--|------------|---------------------------|--------------------|
| | ----- | ----- | ----- |
| | | | -AS |
| Current assets: | | | |
| Cash and cash equivalents | \$ 3,256 | \$ 47 | \$ |
| Receivables | 20,151 | 54,875 | |
| Inventories | 54,770 | -- | |
| Prepaid expenses and other | 23,188 | 497 | |
| | ----- | ----- | --- |
| Total current assets | 101,365 | 55,419 | 1 |
| Property, plant and equipment, net | 77,781 | 27 | |
| Deferred charges and other, net | 64,999 | 631 | |
| Intangible assets, net | 89,802 | -- | |
| Investments in subsidiaries | 146,689 | 91,263 | |
| | ----- | ----- | --- |
| Total assets | \$ 480,636 | \$ 147,340 | \$ 1 |
| | ===== | ===== | === |
| | | | -LIABILITIES AND S |
| Current liabilities: | | | |
| Current maturities of long-term debt | \$ 22,935 | \$ -- | \$ |
| Accounts payable | 34,503 | 5 | |
| Accrued liabilities: | | | |
| Wages and benefits and other | 22,153 | 406 | |
| Other special charges | 2,526 | -- | |
| | ----- | ----- | --- |
| Total current liabilities | 82,117 | 411 | |
| Long term debt, net of current maturities | 208,004 | -- | |
| Employee benefit obligations, net of current portion | 20,271 | -- | |
| Other | 4,796 | 240 | |
| | ----- | ----- | --- |
| Total liabilities | 315,188 | 651 | |
| Shareholders' equity: | | | |
| Common stock | 615 | 1 | |
| Additional paid-in capital | 180,303 | 62,788 | |
| Retained earnings | 128,978 | 90,855 | |
| Accumulated other comprehensive loss | (8,346) | (6,955) | |
| Notes receivable from officers/shareholders | (3,865) | -- | |
| | ----- | ----- | --- |
| Total equity | 297,685 | 146,689 | |
| Less: Treasury stock, at cost | (130,070) | -- | |
| Less: Unearned restricted stock compensation | (2,167) | -- | |

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| | | | |
|--|------------------------------|------------------------------|------------------------|
| Total shareholders' equity | ----- 165,448 | ----- 146,689 | ----- |
| Total liabilities & shareholders' equity | ----- \$ 480,636 ===== | ----- \$ 147,340 ===== | ----- \$ 1 ===== |

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RAYOVAC CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATING STATEMENT OF OPERATIONS
For the three month period ended March 31, 2002
(Unaudited)
(In thousands)

| | PARENT | GUARANTOR SUBSIDIARIES | NONGUARANTOR SUBSIDIARIES |
|-----------------------------------|----------------------------|---------------------------|------------------------------|
| | ----- | ----- | ----- |
| Net sales | \$ 87,759 | \$ 8,159 | \$ 37,43 |
| Cost of goods sold | 49,438 | 7,914 | 25,96 |
| Special charges | (149) | -- | 16 |
| Gross profit | ----- 38,470 | ----- 245 | ----- 11,30 |
| Selling expense | 16,195 | 194 | 8,30 |
| General and administrative | 8,305 | (2,723) | 3,48 |
| Research and development | 3,412 | -- | - |
| Total operating expenses | ----- 27,912 | ----- (2,529) | ----- 11,78 |
| Income (loss) from operations | 10,558 | 2,774 | (48 |
| Interest expense | 3,836 | -- | 60 |
| Equity (income) loss | (739) | 2,008 | - |
| Other (income) expense, net | (466) | (111) | 59 |
| Income (loss) before income taxes | ----- 7,927 | ----- 877 | ----- (1,67 |
| Income tax expense | 2,540 | 138 | 33 |
| Net income (loss) | ----- \$ 5,387 ===== | ----- \$ 739 ===== | ----- \$ (2,00 ===== |

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RAYOVAC CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATING STATEMENT OF OPERATIONS
For the six month period ended March 31, 2002
(Unaudited)
(In thousands)

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| | PARENT | GUARANTOR SUBSIDIARIES | NONGUARANTOR SUBSIDIARIES |
|-----------------------------|------------|---------------------------|------------------------------|
| | ----- | ----- | ----- |
| Net sales | \$ 208,727 | \$ 19,540 | \$ 83,245 |
| Cost of goods sold | 122,490 | 18,954 | 56,260 |
| Special charges | (68) | -- | 84 |
| | ----- | ----- | ----- |
| Gross profit | 86,305 | 586 | 26,901 |
| Selling expense | 35,586 | 357 | 16,279 |
| General and administrative | 35,963 | (5,655) | 7,326 |
| Research and development | 6,630 | -- | -- |
| | ----- | ----- | ----- |
| Total operating expenses | 78,179 | (5,298) | 23,605 |
| Income from operations | 8,126 | 5,884 | 3,296 |
| Interest expense | 7,840 | -- | 1,309 |
| Equity income | (6,702) | (601) | -- |
| Other (income) expense, net | (1,303) | (468) | 213 |
| | ----- | ----- | ----- |
| Income before income taxes | 8,291 | 6,953 | 1,774 |
| Income tax expense | 1,336 | 251 | 1,173 |
| | ----- | ----- | ----- |
| Net income | \$ 6,955 | \$ 6,702 | \$ 601 |
| | ===== | ===== | ===== |

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RAYOVAC CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATING STATEMENTS OF CASH FLOWS
For the six month period ended March 31, 2002
(Unaudited)
(In thousands)

| | PARENT | GUARANTOR SUBSIDIARIES | NONGUARANTOR SUBSIDIARIES |
|--|-----------|---------------------------|------------------------------|
| | ----- | ----- | ----- |
| Net cash provided (used) by operating activities | \$ 32,922 | \$ 1 | \$ (1,306) |
| Cash flows from investing activities: | | | |
| Purchases of property, plant and equipment | (6,962) | -- | (723) |
| | ----- | ----- | ----- |
| Net cash used by investing activities | (6,962) | -- | (723) |
| Cash flows from financing activities: | | | |
| Reduction of debt | (119,171) | -- | 303 |
| Proceeds from debt financing | 94,200 | -- | -- |
| Issuance of stock | 82 | -- | -- |
| Other | (664) | -- | (356) |
| | ----- | ----- | ----- |
| Net cash used by financing activities | (25,553) | -- | (53) |

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| | | | |
|--|----------|-------|----------|
| Effect of exchange rate changes on cash and cash equivalents | -- | -- | (202 |
| | 407 | 1 | (2,284 |
| Net increase (decrease) in cash and cash equivalents | | | |
| Cash and cash equivalents, beginning of period | 2,849 | 46 | 8,463 |
| | \$ 3,256 | \$ 47 | \$ 6,179 |
| Cash and cash equivalents, end of period | | | |

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

FISCAL QUARTER AND SIX MONTHS ENDED MARCH 31, 2002 COMPARED TO FISCAL QUARTER AND SIX MONTHS ENDED APRIL 1, 2001

NET SALES. Net sales for the three months ended March 31, 2002 (the "Fiscal 2002 Quarter") decreased \$13.5 million, or 10.0%, to \$121.2 million from \$134.7 million in the three months ended April 1, 2001 (the "Fiscal 2001 Quarter"). The sales decline reflects continued economic weakness in Latin America and continued high levels of industry promotional activity in North America partially offset by increased volume in Europe/ROW.

Net sales for the six months ended March 31, 2002 (the "Fiscal 2002 Six Months") decreased \$16.0 million, or 5.4%, to \$283.0 million from \$299.0 million in the six months ended April 1, 2001 (the "Fiscal 2001 Six Months"). The sales decline reflects continued economic weakness in the Latin America region partially offset by product line extension gains in North America and volume increases in Europe/ROW.

NET INCOME. Net income for the Fiscal 2002 Quarter increased \$1.3 million to \$5.4 million from \$4.1 million in the Fiscal 2001 Quarter. The increase reflects a reduction in interest expense primarily attributable to the retirement of \$65.0 million in Senior Subordinated Notes following the June 2001 stock offering.

Net income for the Fiscal 2002 Six Months increased \$3.4 million to \$5.8 million from \$2.4 million in the Fiscal 2001 Six Months. The increase reflects a reduction in interest expense primarily attributable to the retirement of \$65.0 million in Senior Subordinated Notes following the June 2001 stock offering. In addition, a bad debt reserve of \$10.0 million, net of tax, related to the bankruptcy filing of a major customer was recognized in the Fiscal 2002 Six Months, while the Fiscal 2001 Six Month's results reflected a special charge reserve of \$10.7 million, net of tax.

SEGMENT RESULTS. The Company manages operations in three reportable segments based upon geographic area. North America includes the United States and Canada; Latin America includes Mexico, Central America, and South America; Europe/ROW includes the United Kingdom, Europe and all other countries in which the company does business. We evaluate segment profitability based on income from operations before corporate expense. Corporate expense includes corporate purchasing expense, general and administrative expense and research and

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development expense.

| NORTH AMERICA | FISCAL QUARTER | |
|--|----------------|---------|
| | 2002 | 2001 |
| Revenue from external customers..... | \$ 89.8 | \$ 96.5 |
| Profitability..... | 17.8 | 15.2 |
| Profitability as a % of net sales..... | 19.8% | 15.8% |
| Assets..... | \$232.3 | \$233.7 |

Our sales to external customers decreased \$6.7 million, or 6.9%, to \$89.8 million in the Fiscal 2002 Quarter from \$96.5 million the previous year due primarily to weakness in alkaline, hearing aid, and heavy duty batteries. Alkaline sales decreases were primarily attributable to new distribution which was offset by the sluggish economy, increased promotional activity, and our inability to anniversary an order from an OEM customer in the prior year. Heavy duty sales decreases reflect a discontinuation of certain products at certain stores of a major retailer and general industry trends. The hearing aid softness is primarily attributable to timing of promotional shipments to key customers.

In the Fiscal 2002 Six Months, our sales to external customers decreased \$3.7 million, or 1.7%, to \$212.1 million in the Fiscal 2002 Six Months from \$215.8 million the previous year as a result of strong sales of alkaline batteries and lighting products offset by weakness in heavy duty and specialty batteries. Alkaline sales increases were primarily attributable to new distribution, while lighting products increases were primarily attributable to product line extension and the introduction of new products. Heavy duty sales decreases reflect the trend in the industry

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toward alkaline in place of heavy duty and the discontinuation of certain products at certain stores of a major retailer. Specialty batteries sales decreases versus last year primarily reflect a decline in camcorder battery sales, as well as a reduction of lithium battery sales due to softness in demand from OEM customers in the PC, telecommunications and electronics industries.

Our profitability increased \$2.6 million, or 17.1%, to \$17.8 million in the Fiscal 2002 Quarter from \$15.2 million in the Fiscal 2001 Quarter. The increase in profitability in the Fiscal 2002 Quarter was attributable to lower selling expenses primarily reflecting lower advertising and other selling expenses in addition to favorable distribution expenses reflecting favorable freight rates. Our profitability margins increased 400 basis points to 19.8% from 15.8% in the same quarter last year. The increase primarily reflects lower operating expenses as a percentage of sales in addition to favorable gross profit margins.

In the Fiscal 2002 Six Months, our profitability decreased \$12.5 million, or 33.2%, to \$25.1 million in the Fiscal 2002 Six Months from \$37.6 million in the Fiscal 2001 Six Months. The decrease in profitability in the

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Fiscal 2002 Six Months was primarily attributable to a \$16.1 million bad debt reserve attributable to the bankruptcy filing of a major customer. Excluding the impact of this reserve, profitability increased \$3.6 million, or 9.6%, versus the same period last year due to lower advertising, promotional, and distribution expenses. Our profitability margins, excluding the bad debt reserve, increased 200 basis points to 19.4% from 17.4% in the previous year. The increase primarily reflects lower operating expenses as a percentage of sales partially offset by a reduction in gross profit margins reflecting a shift in customer mix and increased promotional activity.

Our assets decreased \$1.4 million, or 0.6%, to \$232.3 million in the Fiscal 2002 Quarter from \$233.7 million the previous year. The decrease was primarily attributable to a decrease in receivables and inventory partially offset by increased capital investment.

| | FISCAL QUARTER | |
|--|----------------|---------|
| LATIN AMERICA | 2002 | 2001 |
| | ---- | ---- |
| Revenue from external customers..... | \$ 18.4 | \$ 26.5 |
| Profitability..... | 0.5 | 4.5 |
| Profitability as a % of net sales..... | 2.7% | 17.0% |
| Assets..... | \$202.1 | \$206.2 |

Our sales to external customers decreased \$8.1 million, or 30.6% to \$18.4 million in the Fiscal 2002 Quarter from \$26.5 million in the same period last year, and decreased \$15.6 million, or 26.0%, to \$44.4 million in the Fiscal 2002 Six Months from \$60.0 million the same period last year due primarily to decreased sales of zinc carbon and alkaline batteries. Net sales were impacted by unfavorable economic conditions, planned curtailment of shipments to certain distributors and wholesalers who were delinquent in payments, political uncertainties in Argentina and Venezuela, and the unfavorable impacts of currency devaluation which contributed approximately 6.3% and 4.3%, respectively, to the sales decline versus the prior year periods.

Our profitability declined \$4.0 million in the Fiscal 2002 Quarter and \$7.3 million in the Fiscal 2002 Six Months. The decrease in profitability versus the same period last year was primarily attributable to the sales and gross profit margin decline, partially offset by a reduction in operating expenses primarily reflecting the adoption of SFAS 142 which resulted in a reduction of amortization expense. The Venezuelan Bolivars devaluation did not have a significant impact on the operating results for the Fiscal 2002 Quarter.

Our profitability margins in the Fiscal 2002 Quarter and Fiscal 2002 Six Months decreased primarily due to an unfavorable product line mix compounded by our relatively fixed operating expenses spread over lower sales.

Our assets decreased \$4.1 million, or 2.0%, to \$202.1 million in the Fiscal 2002 Quarter from \$206.2 million the previous year. Increases in accounts receivable, reflecting longer terms associated with distribution at larger retail accounts and general economic weakness, were offset by decreases in inventory throughout the region and lower advertising and other prepaid assets.

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| EUROPE/ROW | FISCAL QUARTER | |
|--|----------------|--------|
| | 2002 | 2001 |
| | ---- | ---- |
| Revenue from external customers..... | \$13.0 | \$11.7 |
| Profitability..... | 1.1 | 1.1 |
| Profitability as a % of net sales..... | 8.5% | 9.4% |
| Assets..... | \$29.3 | \$26.7 |

Our sales to external customers increased \$1.3 million, or 11.1%, to \$13.0 million in the Fiscal 2002 Quarter from \$11.7 million the same period last year and increased \$3.3 million, or 14.2%, to \$26.5 million in the Fiscal 2002 Six Months from \$23.2 million the same period last year primarily reflecting strong sales of alkaline and hearing aid batteries attributable to distribution gains partially offset by the unfavorable impacts of currency devaluation.

Our profitability was flat in the Fiscal 2002 Quarter and increased \$0.9 million, or 69.2%, to \$2.2 million in the Fiscal 2002 Six Months. Profitability in the Fiscal 2002 Quarter was impacted by unfavorable gross profit margins which offset the favorable impacts of volume gains. The increase in profitability in the Fiscal 2002 Six Months primarily reflects the benefits of volume gains compounded by a reduction in operating expenses reflecting the adoption of SFAS 142, which resulted in lower amortization expense. Our profitability margin increase, as a percentage of sales, in the Fiscal 2002 Six Months is primarily driven by lower general and administrative expenses.

Our assets increased \$2.6 million, or 9.7%, to \$29.3 million from \$26.7 million the previous year due primarily to an increase in inventory and receivables reflecting the sales growth.

CORPORATE EXPENSE. Our corporate expense decreased \$0.3 million, or 4.4%, to \$6.5 million in the Fiscal 2002 Quarter from \$6.8 million in the Fiscal 2001 Quarter and increased \$1.5 million, or 11.0%, to \$15.1 million in the Fiscal 2002 Six Months from \$13.6 million the same period last year. The increase in the Fiscal 2002 Six Months was attributable to increased technology spending and the accrual of management incentives, which were unearned in the previous year. As a percentage of total sales, our corporate expense was 5.4% and 5.1% in the Fiscal 2002 and Fiscal 2001 Quarters, respectively, and 5.3% and 4.6% in the Fiscal 2002 and Fiscal 2001 Six Months, respectively.

SPECIAL CHARGES. The Company incurred minimal special charges in the Fiscal 2002 Quarter and Six Months. The Fiscal 2001 Six Months reflects \$16.3 million in special charges primarily associated with expenses for the shutdown of our Wonewoc, Wisconsin, manufacturing facility and restructuring initiatives in Latin America and North America.

INCOME FROM OPERATIONS. Our income from operations decreased \$1.0 million, or 7.3%, to \$12.8 million in the Fiscal 2002 Quarter from \$13.8 million the same period last year. The decrease was primarily attributable to the profitability decline in Latin America partially offset by increased profitability in North America.

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In the Fiscal 2002 Six Months, our income from operations decreased \$4.0 million, or 19.6%, to \$16.4 million from \$20.4 million the previous year. The decrease was primarily attributable to the profitability decline in Latin America. A bad debt reserve associated with the bankruptcy filing of a major customer was recognized in the Fiscal 2002 Six Months, while the Fiscal 2001 Six Month's reflects the special charge reserve.

INTEREST EXPENSE. Interest expense decreased \$3.1 million to \$4.1 million in the Fiscal 2002 Quarter and decreased \$7.2 million to \$8.2 million in the Fiscal 2002 Six Months due to the retirement of \$65.0 million in Senior Subordinated Notes following the June 2001 stock offering combined with lower effective interest rates.

OTHER EXPENSE (INCOME). Other expense increased \$0.2 million to \$0.4 million in the Fiscal 2002 Quarter. The increase in the Fiscal 2002 Quarter was attributable to foreign exchange losses reflecting the unfavorable impacts of currency devaluations in Argentina and Venezuela.

Other income increased \$1.5 million to income of \$0.4 million in the Fiscal 2002 Six Months. The increase in the Fiscal 2002 Six Months was attributable to foreign exchange gains versus foreign exchange losses in the same period last year, primarily Mexico, partially offset by the unfavorable impacts of currency devaluations in Venezuela and Argentina.

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INCOME TAX EXPENSE. Our effective tax rate was 35.8% and 36.0% for the Fiscal 2002 Quarter and the Fiscal 2001 Quarter, respectively. Our effective tax rate was 32.3% for the Fiscal 2002 Six Months compared to 40.0% for the Fiscal 2001 Six Months. The effective tax rate for the prior year reflects a larger percentage of our income being derived from foreign jurisdictions.

ADOPTION OF NEW ACCOUNTING PRONOUNCEMENTS

Effective October 1, 2001, the Company adopted Statement of Financial Accounting Standards (SFAS) 141, BUSINESS COMBINATIONS, and SFAS 142, GOODWILL AND OTHER INTANGIBLE ASSETS. Statement 141 requires that the purchase method of accounting be used for all business combinations initiated or completed after June 30, 2001. Statement 141 also specifies criteria that intangible assets acquired in a purchase method business combination must meet to be recognized and reported apart from goodwill. Statement 142 requires that goodwill and intangible assets with indefinite useful lives no longer be amortized, but instead be tested for impairment at least annually in accordance with the provisions of Statement 142. Statement 142 also requires that intangible assets with estimable useful lives be amortized over their respective estimated useful lives to their estimated residual values, and reviewed for impairment in accordance with Statement 121, ACCOUNTING FOR THE IMPAIRMENT OF LONG-LIVED ASSETS AND FOR LONG-LIVED ASSETS TO BE DISPOSED OF.

The adoption of Statement 142 resulted in an increase to pre-tax income of \$0.8 million (\$0.6 million after-tax) versus the previous year's quarter and \$1.6 million (\$1.2 million after-tax) versus the Fiscal 2001 Six Months. The increase is attributable to the discontinuation of amortization of the trade name and Latin America, North America, and Europe/ROW segment goodwill. These assets were being amortized on a straight line basis over 15 to 40 years. Upon initial application of Statement 142, the Company reassessed the useful lives of its intangible assets and deemed only the trade name to have an indefinite

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useful life because it is expected to generate cash flows indefinitely. The unamortized book value of these assets is \$115.4 million. Upon the transition to Statement 142, no goodwill was deemed to be impaired.

Effective January 1, 2002, the Company adopted Emerging Issues Task Force (EITF) Issue No. 00-14, "Accounting for Certain Sales Incentives" and Issue No. 00-25, "Vendor Income Statement Characterization of Consideration to a Purchaser of the Vendor's Products or Services". These Issues address the recognition, measurement, and income statement classification for various types of sales incentives including discounts, coupons, rebates and free products and when consideration from a vendor to a retailer or distributor in connection with the purchase of the vendor's products to promote sales of the vendor's products should be classified in the vendor's income statement as a reduction of revenue or expense.

The adoption of these EITF's resulted in the following reclassifications in the Company's results of operations. For the three months ended March 31, 2002 and April 1, 2001, net sales were reduced by \$8.8 and \$10.5 million, respectively; cost of sales were increased by \$2.7 and \$2.4 million, respectively; and selling expenses were reduced by \$11.5 and \$12.9 million, respectively. For the six months ended March 31, 2002 and April 1, 2001, net sales were reduced by \$29.3 and \$29.8 million, respectively; cost of sales were increased by \$7.9 and \$7.0 million, respectively; and selling expenses were reduced by \$37.2 and \$36.8 million, respectively.

Concurrent with the adoption of EITF 00-25, the Company reclassified certain accrued trade incentives as a contra receivable versus the Company's previous presentation as a component of accounts payable. Historically, customers offset earned trade incentives when making payments on account. Therefore, the Company believes the reclassification of these accrued trade incentives as a contra receivable better reflects the underlying economics of the Company's net receivable due from out trade customers.

The reclassification results in a reduction in accounts receivable and accounts payable in our Consolidated Balance Sheets of \$22.2 million and \$21.4 million at March 31, 2002 and September 30, 2001, respectively.

LIQUIDITY AND CAPITAL RESOURCES

For the Fiscal 2002 Six Months, operating activities provided \$30.9 million in net cash compared with \$11.1 million the previous year. Operating cash flow increases versus the previous year primarily reflect the reduction of

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interest payments due to the retirement of \$65.0 million in Senior Subordinated Notes following the June 2001 stock offering as well as a lower investment in working capital.

Net cash used by investing activities increased \$3.5 million versus the same period a year ago reflecting an increase in capital expenditures. Expenditures in the Fiscal 2002 Six Months were primarily for improvements to alkaline battery manufacturing. Capital expenditures for fiscal 2002 are expected to be approximately \$20.0 million which will include continued performance upgrades to our alkaline and zinc air manufacturing and packaging operations and continued investment in technology.

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During the Fiscal 2002 Six Months we granted approximately 0.9 million options to purchase shares of common stock to various employees of the company. All grants have been at an exercise price equal to the market price of the common stock on the date of the grant.

As a result of the bad debt reserve for Kmart receivables in the quarter ended December 30, 2001, the Company was out of compliance with the leverage ratio covenant of its senior bank credit agreement ("Second Amended Restated Credit Agreement"). On February 12, 2002, the Company amended the Second Amended Restated Credit Agreement ("Fourth Amendment") which placed it in compliance with an amended leverage ratio based on an amended definition of EBITDA (see Exhibit 4.11). The Company recorded \$0.3 million of fees paid as a result of the amendment as a debt issuance cost which will be amortized over the remaining life of the agreement.

The Company believes that cash flow from operating activities and periodic borrowings under its amended credit facilities will be adequate to meet the Company's short-term and long-term liquidity requirements prior to the maturity of those credit facilities, although no guarantee can be given in this regard. The Company's current credit facilities include a revolving credit facility of \$250.0 million and term loan of \$75.0 million. As of March 31, 2002, \$28.3 million of the term loan remained outstanding and \$194.5 million was outstanding under the revolving facility with approximately \$10.7 million of the remaining availability utilized for outstanding letters of credit.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

MARKET RISK FACTORS

We have market risk exposure from changes in interest rates, foreign currency exchange rates and commodity prices. We use derivative financial instruments for purposes other than trading to mitigate the risk from such exposures.

A discussion of our accounting policies for derivative financial instruments is included in Note 1 "Significant Accounting Policies" in Notes to our consolidated financial statements.

INTEREST RATE RISK

We have bank lines of credit at variable interest rates. The general level of U.S. interest rates, LIBOR, IBOR, and to a lesser extent European Base rates, primarily affects interest expense. We use interest rate swaps to manage such risk. The net amounts to be paid or received under interest rate swap agreements are accrued as interest rates change, and are recognized over the life of the swap agreements, as an adjustment to interest expense from the underlying debt to which the swap is designated. The related amounts payable to, or receivable from, the contract counter-parties are included in accrued liabilities or accounts receivable.

FOREIGN EXCHANGE RISK

We are subject to risk from sales and loans to our subsidiaries as well as sales to, purchases from and bank lines of credit with, third-party customers, suppliers and creditors, respectively, denominated in foreign currencies. Foreign currency sales are made primarily in Pounds Sterling, Canadian Dollars, Euro, German Marks, French Francs, Italian Lira, Spanish Pesetas, Dutch Guilders, Mexican Pesos, Guatemalan Quetzals, Dominican Pesos, Venezuelan Bolivars, Argentine Pesos, Chilean Pesos and Honduran Lempira. Foreign currency purchases are made primarily in Pounds Sterling, German Marks, French Francs, Mexican Pesos, Dominican Pesos, Guatemalan Quetzals and Honduran Lempira. We manage our foreign exchange exposure from anticipated sales,

accounts receivable,

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intercompany loans, firm purchase commitments and credit obligations through the use of naturally occurring offsetting positions (borrowing in local currency), forward foreign exchange contracts, foreign exchange rate swaps and foreign exchange options. The related amounts payable to, or receivable from, the contract counter parties are included in accounts payable or accounts receivable.

COMMODITY PRICE RISK

We are exposed to fluctuation in market prices for purchases of zinc used in the manufacturing process. We use commodity swaps, calls and puts to manage such risk. The maturity of, and the quantities covered by, the contracts are closely correlated to our anticipated purchases of the commodities. The cost of calls, and the premiums received from the puts, are amortized over the life of the contracts and are recorded in cost of goods sold, along with the effects of the swap, put and call contracts. The related amounts payable to, or receivable from, the counterparties are included in accounts payable or accounts receivable.

SENSITIVITY ANALYSIS

The analysis below is hypothetical and should not be considered a projection of future risks. Earnings projections are before tax.

As of March 31, 2002, the potential change in fair value of outstanding interest rate derivative instruments, assuming a 1% unfavorable shift in the underlying interest rates would be a loss of \$4.2 million. The net impact on reported earnings, after also including the reduction in one year's interest expense on the related debt due to the same shift in interest rates, would be a net loss of \$1.9 million.

As of March 31, 2002, the potential change in fair value of outstanding foreign exchange rate derivative instruments, assuming a 10% unfavorable change in the underlying foreign exchange rates would be a loss of \$0.1 million. The net impact on future cash flows, after also including the gain in value on the related accounts receivable and contractual payment obligations outstanding at March 31, 2002 due to the same change in exchange rates, would be a net gain of \$0.5 million.

As of March 31, 2002, the potential change in fair value of outstanding commodity price derivative instruments, assuming a 10% unfavorable change in the underlying commodity prices would be a loss of \$0.9 million. The net impact on reported earnings, after also including the reduction in cost of one year's purchases of the related commodities due to the same change in commodity prices, would be immaterial.

IMPACT OF RECENTLY ISSUED ACCOUNTING STANDARDS

In August 2001, FASB issued Statement No. 143, ACCOUNTING FOR ASSET RETIREMENT OBLIGATIONS. Statement No. 143 addresses financial accounting and reporting for obligations associated with the retirement of tangible long-lived assets and the associated asset retirement costs. The Company is required to adopt no later than its fiscal year beginning October 1, 2002. Management is

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currently evaluating the impact of adoption on the consolidated financial statements.

In October 2001, the FASB Issued Statement No. 144, ACCOUNTING FOR THE IMPAIRMENT OR DISPOSAL OF LONG-LIVED ASSETS. This statement supersedes FASB Statement No. 121, ACCOUNTING FOR THE IMPAIRMENT OF LONG-LIVED ASSETS AND FOR LONG-LIVED ASSETS TO BE DISPOSED OF, and the accounting and reporting provisions of APB Opinion No. 30, REPORTING THE RESULTS OF OPERATIONS - REPORTING THE EFFECTS OF DISPOSAL OF A SEGMENT OF A BUSINESS, AND EXTRAORDINARY, UNUSUAL AND INFREQUENTLY OCCURRING EVENTS AND TRANSACTIONS, for the disposal of a segment of a business. The Company is required to adopt no later than its fiscal year beginning October 1, 2002. Management is currently evaluating the impact of adoption on the consolidated financial statements

FORWARD LOOKING STATEMENTS

Certain of the information contained in this Form 10-Q, including without limitation statements made under Part I, Item 1, "Financial Statements" and Part I, Item 2, "Management's Discussion and Analysis of Financial Condition and Results of Operations" and Part I, Item 3, "Quantitative and Qualitative Disclosures about Market Risk"

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which are not historical facts, may include "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act, as amended. In reviewing such information, you should note that our actual results may differ materially from those set forth in such forward-looking statements.

Important factors that could cause our actual results to differ materially from those included in the forward-looking statements made herein include, without limitation, (1) significant changes in consumer demand and buying practices for household batteries, hearing aid batteries or other products we manufacture or sell in North America, Latin America or Europe/ROW; (2) the loss of, or a significant reduction in, sales through a significant retail customer; (3) the successful introduction or expansion of competitive brands into the marketplace, including private label offerings; (4) the introduction of new product features or new battery technologies by a competitor; (5) promotional campaigns and spending by a competitor; (6) difficulties or delays in the integration of operations of acquired companies; (7) our ability to successfully implement manufacturing and distribution cost efficiencies and improvements; (8) delays in manufacturing or distribution due to work stoppages, problems with suppliers, natural causes or other factors; (9) the enactment or imposition of unexpected environmental regulations negatively impacting consumer demand for certain of our battery products or increasing our cost of manufacture or distribution; (10) the costs and effects of unanticipated legal, tax or regulatory proceedings; (11) the effects of competitors' patents or other intellectual property rights; (12) interest rate, exchange rate and raw material price fluctuations; (13) impact of unusual items resulting from evaluation of business strategies, acquisitions and divestitures and organizational structure; (14) changes in accounting standards applicable to our business; and (15) the effects of changes in trade, monetary or fiscal policies and regulations by governments in countries where we do business.

Additional factors and assumptions that could generally cause our actual results to differ materially from those included in the forward-looking statements made herein include, without limitation, (1) our ability to develop and introduce new products; (2) the effects of general economic conditions in

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North America, Europe, Latin America or other countries where we do business, including inflation, labor costs and stock market volatility; (3) the effects of political or economic conditions, unrest or volatility in Latin America and other international markets; (4) the sufficiency of our production and distribution capacity to meet future demand for our products; (5) our ability to keep pace with the product and manufacturing technological standards in our industry; (6) our ability to continue to penetrate and develop new distribution channels for our products; and (7) various other factors, including those discussed herein and those set forth in our most recent Annual Report on Form 10-K and the prospectus supplement for our most recent public offering of common stock. Other factors and assumptions not identified above were also involved in the derivation of the forward-looking statements contained in this Form 10-Q and the failure of such other assumptions to be realized, as well as other factors, may also cause actual results to differ materially from those projected. We assume no obligations to update these forward-looking statements to reflect actual results or changes in factors or assumptions affecting such forward-looking statements.

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Part II. Other Information

Item 1: Legal Proceedings

There have been no significant changes in the status of Rayovac's legal proceedings since the filing of Rayovac's Annual Report on Form 10-K for its fiscal year ended September 30, 2001.

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ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

(a) Exhibits

| EXHIBIT NUMBER | DESCRIPTION |
|----------------|--|
| ----- | ----- |
| 2.1++++ | Share Purchase Agreement made as of June 11, 1999, by and among the Company, Vidor Battery Company, Rayovac Latin America, Ltd., the shareholders of ROV Limited, ROV Limited, ESB ROV Ltd., Duranmas, S.A., certain second-tier subsidiaries of ROV Limited, Ray-O-Vac Overseas Corporation, and Alfredo J. Diez and Richard T. Doyle, Jr., as selling group representatives. |
| 2.2++++ | Form of Stock Purchase Agreement entered into on or around June 11, 1999, by and among the Company, Rayovac Latin America, Ltd. and certain persons who hold minority |

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interests in certain of the operating subsidiaries of Ray-O-Vac Overseas Corporation.

- 3.1+ Amended and Restated Articles of Incorporation of the Company.
- 3.2***** Amended and Restated By-laws of the Company, as amended through May 17, 1999.
- 4.1** Indenture, dated as of October 22, 1996, by and among the Company, ROV Holding, Inc. and Marine Midland Bank, as trustee, relating to the Company's 10 1/4% Senior Subordinated Notes due 2006.
- 4.2***** First Supplemental Indenture, dated as of February 26, 1999, by and among the Company, ROV Holding, Inc. and HSBC Bank USA (formerly known as Marine Midland Bank) as trustee, relating to the Company's 10 1/4% Senior Subordinated Notes due 2006.
- 4.3++++ Second Supplemental Indenture, dated as of August 6, 1999, by and among the Company, ROV Holding, Inc. and HSBC Bank USA (formerly known as Marine Midland Bank) as trustee, relating to the Company's 10 1/4% Senior Subordinated Notes due 2006.
- 4.4***** Third Supplemental Indenture, dated as of June 13, 2001, by and among the Company, ROV Holding, Inc., ROVCAL, Inc. and HSBC Bank USA (formerly known as Marine Midland Bank) as trustee, relating to the Company's 101/4% Senior Subordinated Notes due 2006.
- 4.5** Specimen of the Notes (included as an exhibit to Exhibit 4.1)
- 4.6**** Amended and Restated Credit Agreement, dated as of December 30, 1997, by and among the Company, the lenders party thereto and Bank of America National Trust and Savings Association ("BofA"), as Administrative Agent.
- 4.7++++ Second Amended and Restated Credit Agreement, dated as of August 9, 1999, by and among the Company, the lenders party thereto and Bank of America, NA as Administrative Agent.
- 4.8+++++ The First Amendment dated as of July 28, 2000 to the Second Amended and Restated Credit Agreement, dated as of August 9, 1999, by and among the Company, the lenders party thereto and Bank of America, NA as Administrative Agent.
- 4.9+++++++ The Second Amendment dated as of December 31, 2000 to the Second Amended and Restated Credit Agreement, dated as of August 9, 1999, by and among the Company, various financial institutions, and Bank of America, NA as Administrative Agent.
- 4.10+++++++ The Third Amendment dated as of June 11, 2001, to the Second Amended and Restated Credit Agreement, dated as of August 9, 1999, by and among the Company, various financial institutions, and Bank of America, NA as Administrative Agent.
- 4.11+++++++ The Fourth Amendment dated as of February 12, 2002, to the

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Second Amended and Restated Credit Agreement, dated as of August 9, 1999, by and among the Company, various financial institutions, and Bank of America, NA as Administrative Agent.

- 4.12** The Security Agreement, dated as of September 12, 1996, by and among the Company, ROV Holding, Inc. and Bank of America, NA.
- 4.13** The Company Pledge Agreement, dated as of September 12, 1996, by and between the Company and Bank of America, NA.
- 4.14*** Shareholders Agreement, dated as of September 12, 1996, by and among the Company and the shareholders of the Company referred to therein.
- 4.15*** Amendment No. 1 to Rayovac Shareholders Agreement dated August 1, 1997, by and among the Company and the shareholders of the Company referred to therein.
- 4.16***** Amendment No. 2 to Rayovac Shareholders Agreement, dated as of January 8, 1999, by and among the Company and the Shareholders of the Company referred to therein.
- 4.17+++++ Amendment No. 3 to Rayovac Shareholders Agreement dated January 1, 2001, by and among the Company and the shareholders of the Company referred to therein.
- 4.18+++++++ Amendment No. 4 to Rayovac Shareholders Agreement dated February 8, 2002, by and among the Company and the Shareholders of the Company referred to therein.
- 4.19* Specimen certificate representing the Common Stock.
- 10.1** Management Agreement, dated as of September 12, 1996, by and between the Company and Thomas H. Lee Company.
- 10.2** Confidentiality, Non-Competition and No-Hire Agreement, dated as of September 12, 1996, by and between the Company and Thomas F. Pyle.
- 10.3+++++ Amended and Restated Employment Agreement, dated as of October 1, 2000, by and between the Company and David A. Jones.
- 10.4+++++ Amended and Restated Employment Agreement, dated as of October 1, 2000, by and between the Company and Kent J. Hussey.
- 10.5+++++ Employment Agreement, dated as of October 1, 2000, by and between the Company and Kenneth V. Biller.

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- 10.6+++++ Employment Agreement, dated as of October 1, 2000, by and between the Company and Stephen P. Shanesy.
- 10.7+++++ Employment Agreement, dated as of October 1, 2000, by and between the Company and Merrell M. Tomlin.
- 10.8+++++ Employment Agreement, dated as of October 1, 2000, by and between the Company and Luis A. Cancio.
- 10.9** Technology, License and Service Agreement between Battery Technologies (International) Limited and the Company, dated June 1, 1991, as amended April 19, 1993, and December 31, 1995.
- 10.10** Building Lease between the Company and SPG Partners dated May 14, 1985, as amended June 24, 1986, and June 10, 1987.
- 10.11***** Amendment, dated December 31, 1998, between the Company and SPG Partners, to the Building Lease, between the Company and SPG Partners, dated May 14, 1985.
- 10.12*** Rayovac Corporation 1996 Stock Option Plan.
- 10.13* 1997 Rayovac Incentive Plan.
- 10.14* Rayovac Profit Sharing and Savings Plan.
- 10.15+++ Technical Collaboration, Sale and Supply Agreement, dated as of March 5, 1998, by and among the Company, Matsushita Battery Industrial Co., Ltd. and Matsushita Electric Industrial Co., Ltd.

* Incorporated by reference to the Company's Registration Statement on Form S-1 (Registration No. 333-35181) filed with the Commission.

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** Incorporated by reference to the Company's Registration Statement on Form S-1 (Registration No. 333-17895) filed with the Commission.

*** Incorporated by reference to the Company's Quarterly Report on Form 10-Q for the quarterly period ended June 29, 1997, filed with the Commission on August 13, 1997.

**** Incorporated by reference to the Company's Registration Statement on Form S-3 (Registration No. 333-49281) filed with the Commission.

***** Incorporated by reference to the Company's Quarterly Report on Form 10-Q for the quarterly period ended January 3, 1999, filed with the Commission on February 17, 1999.

***** Incorporated by reference to the Company's Quarterly Report on Form 10-Q for the quarterly period ended April 4, 1999, filed with the Commission on May 17, 1999.

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- ***** Incorporated by reference to the Company's Report on Form 8-K filed with the Commission on June 19, 2001.
- + Incorporated by reference to the Company's Annual Report on Form 10-K for the fiscal year ended September 30, 1997, filed with the Commission on December 23, 1997.
- ++ Incorporated by reference to the Company's Quarterly Report on Form 10-Q for the Quarterly period ended June 27, 1998, filed with the Commission on August 4, 1998.
- +++ Incorporated by reference to the Company's Quarterly Report on Form 10-Q for the quarterly period ended March 28, 1998, filed with the Commission on May 5, 1998.
- ++++ Incorporated by reference to the Company's Current Report on Form 8-K filed with the Commission on August 24, 1999, as subsequently amended on October 26, 1999.
- +++++ Incorporated by reference to the Company's Annual Report on Form 10-K for the fiscal year ended September 30, 2000, filed with the Commission on December 19, 2000.
- ++++++ Incorporated by reference to the Company's Quarterly Report on Form 10-Q for the quarterly period ended December 31, 2000, filed with the Commission on February 14, 2001.
- +++++++ Incorporated by reference to the Company's Quarterly Report on Form 10-Q for the quarterly period ended March 31, 2001, filed with the Commission on May 14, 2001.
- +++++++ Incorporated by reference to the Company's Quarterly Report on Form 10-Q for the quarterly period ended July 1, 2001, filed with the Commission on August 9, 2001.
- +++++++ Incorporated by reference to the Company's Quarterly Report on Form 10-Q for the quarterly period ended December 30, 2001, filed with the Commission on February 13, 2002.
- (b) Reports on Form 8-K. The Company has not filed any reports on Form 8-K during the three month period ended March 31, 2002.

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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.

DATE: May 14, 2002

RAYOVAC CORPORATION

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By: /s/ Kent J. Hussey

Kent J. Hussey
President and Chief Financial Officer

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