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RAYOVAC CORP  
Form 10-Q  
August 09, 2001

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

FORM 10Q

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

For the quarterly period ended July 1, 2001

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  
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Rayovac Corporation  
-----

(Exact name of registrant as specified in its charter)

Wisconsin  
-----

(State or other jurisdiction of  
incorporation or organization)

22-2423556  
-----

(I.R.S. Employer  
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

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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 August 1, 2001, was 32,038,821.

RAYOVAC CORPORATION  
 CONDENSED CONSOLIDATED BALANCE SHEETS  
 July 1, 2001 and September 30, 2000  
 (Unaudited)  
 (In thousands)

	JULY 1, 2001
	-----
-ASSETS-	
Current assets:	
Cash and cash equivalents	\$ 10,260
Receivables	153,720
Inventories	92,313
Prepaid expenses and other	37,868
	-----
Total current assets	294,161
Property, plant and equipment, net	108,013
Deferred charges and other, net	39,994
Intangible assets, net	119,418
	-----
Total assets	\$ 561,586
	=====
-LIABILITIES AND SHAREHOLDERS' EQUITY -	
Current liabilities:	
Current maturities of long-term debt	\$ 25,075
Accounts payable	98,441
Accrued liabilities:	
Wages and benefits and other	30,515
Recapitalization and other special charges	4,931
	-----
Total current liabilities	158,962
Long-term debt, net of current maturities	217,816
Employee benefit obligations, net of current portion	16,345
Other	12,480
	-----
Total liabilities	405,603

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Shareholders' equity:	
Commonstock, \$.01 par value, authorized 150,000 shares; issued 61,574 and 57,101 shares, respectively; outstanding 32,038 and 27,570 shares, respectively	616
Additional paid-in capital	181,019
Retained earnings	113,531
Accumulated other comprehensive (loss) income	(1,889)
Notes receivable from officers/shareholders	(3,665)
	-----
	289,612
Less Treasury stock, at cost, 29,536 and 29,531 shares, respectively	(130,070)
Less: Unearned restricted stock compensation	(3,559)
	-----
Total shareholders' equity	155,983
	-----
Total liabilities and shareholders' equity	\$ 561,586
	=====

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RAYOVAC CORPORATION  
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS  
For the three and nine month periods ended July 1, 2001 and July 2, 2000  
(Unaudited)  
(In thousands)

	THREE MONTHS	
	2001	2000
	-----	-----
Net sales	\$ 159,132	\$ 150,351
Cost of goods sold	81,951	77,302
Special charges	2,279	-
	-----	-----
Gross profit	74,902	73,049
Selling	42,757	37,592
General and administrative	9,893	13,109
Research and development	2,990	2,580
Other special charges	300	-
	-----	-----
Total operating expenses	55,940	53,281
Income from operations	18,962	19,768
Interest expense	7,017	7,727
Other (income) expense, net	(180)	(387)

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Income before income taxes and extraordinary item	12,125	12,428
Income tax expense	4,053	4,350
Income before extraordinary item	8,072	8,078
Extraordinary item, loss on early extinguishment of debt, net of income tax benefit of \$3,279	(5,350)	-
Net Income	\$ 2,722	\$ 8,078
BASIC EARNINGS PER SHARE		
Weighted average shares and equivalents outstanding	28,080	27,511
Income before extraordinary item	\$ 0.29	\$ 0.29
Extraordinary item	(0.19)	-
Net income	\$ 0.10	\$ 0.29
DILUTED EARNINGS PER SHARE		
Weighted average shares and equivalents outstanding	29,128	29,044
Income before extraordinary item	\$ 0.28	\$ 0.28
Extraordinary item	(0.19)	-
Net income	\$ 0.09	\$ 0.28

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 nine month periods ended July 1, 2001 and July 2, 2000  
(Unaudited)  
(In thousands)

	2001
Cash flows from operating activities:	
Net income	\$ 5,081
Non-cash adjustments to net income:	
Extraordinary item, loss on early retirement of debt	8,628
Amortization	4,329
Depreciation	12,849
Other non-cash adjustments	4,685
Net changes in assets and liabilities	(7,956)
Net cash provided by operating activities	27,616

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Cash flows from investing activities:	
Purchases of property, plant and equipment	(15,215)
Purchases of investments	(799)
Proceeds from sale of investments	1,361
Proceeds from sale of property, plant and equipment	509
	-----
Net cash used by investing activities	(14,144)
Cash flows from financing activities:	
Reduction of debt	(320,619)
Early retirement of debt	(69,693)
Proceeds from debt financing	310,601
Issuance of common stock	67,781
Other	(1,246)
	-----
Net cash used by financing activities	(13,176)
Effect of exchange rate changes on cash and cash equivalents	207
	-----
Net increase in cash and cash equivalents	503
Cash and cash equivalents, beginning of period	9,757
	-----
Cash and cash equivalents, end of period	\$ 10,260
	=====

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 July 1, 2001, results of operations for the three and nine month periods ended July 1, 2001, and July 2, 2000, and cash flows for the nine month periods ended July 1, 2001 and July 2, 2000. 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, 2000. Certain prior year amounts have been reclassified to conform with the current year presentation.

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**ADOPTION OF NEW ACCOUNTING PRONOUNCEMENTS:** In January 2001, the Financial Accounting Standards Board's Emerging Issues Task Force (EITF) reached a consensus on Issue 3 of EITF 00-22, "Accounting for "Points" and Certain Other Time-Based or Volume-Based Sales Incentive Offers, and Offers for Free Products or Services to Be Delivered in the Future". Issue 3 addresses the recognition, measurement, and income statement classification for offers to a customer to rebate or refund a specified amount of cash that may be redeemed if the customer completes a specified volume of transactions. The consensus was effective for quarters ending after February 15, 2001. The Company adopted the consensus reached on Issue 3, in the second fiscal quarter of 2001. The adoption and subsequent restatement of the Fiscal 2000 three and nine month periods resulted in the reclassification of certain selling expenses as a reduction in revenue of \$1,649 and \$7,547, respectively. The reclassifications had no impact on pre-tax income, net income, or earnings per share.

### 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 nine month periods ended July 1, 2001, \$326 and \$368, respectively, of pretax derivative losses from such hedges were recorded as an adjustment to interest expense. At July 1, 2001, the Company had a series of interest rate swap agreements outstanding which effectively fix the interest rate on floating rate debt at a rate of 6.404% for a notional principal amount of \$75,000 through October 2002 and a series of interest rate swap agreements outstanding which effectively fix the interest rate on floating rate debt at a rate of 4.99% for a notional principal amount of \$25,000 through December 2001. The derivative net losses on these contracts recorded in OCI at July 1, 2001 was an after-tax loss of \$1,310.

The Company enters into forward and swap foreign exchange contracts, to hedge the risk from forecasted settlement in local currencies of intercompany 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 nine month periods ended July 1, 2001, \$56 and \$3, respectively, of pretax derivative gains were recorded as an adjustment to earnings for cash flow hedges related to an asset or liability. During the three and nine month periods ended July 1, 2001, \$327 and \$908, respectively, of pretax derivative losses were recorded as an adjustment to earnings for forward and swap contracts settled at maturity. At July 1, 2001, the Company had a series of forward and swap contracts outstanding with a

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contract value of \$4,485. The derivative net gain on these contracts recorded in OCI at July 1, 2001 was an after-tax gain of \$56.

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 has entered into a series of forward contracts for the period July 2001 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 nine month periods ended July 1, 2001, \$433 of pretax derivative gains and \$289 of pretax derivative losses, respectively, were recorded as an adjustment to earnings for fair value hedges of this firm purchase commitment and \$433 of pretax losses and \$289 of pretax gains, respectively, were recorded as an adjustment to earnings for changes in fair value of this firm purchase commitment. During the three and nine month periods ended July 1, 2001, \$314 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 \$314 of pretax gains were recorded as an adjustment to earnings for payments made against this firm purchase commitment. At July 1, 2001, the series of outstanding forward contracts for this firm purchase commitment had a contract value of \$3,170.

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 earnings. The swaps effectively fix the floating price on a specified quantity of a commodity through a specified date. During the three and nine month periods ended July 1, 2001, \$373 and \$653, respectively, of pretax derivative losses were recorded as an adjustment to cost of sales for swap contracts settled at maturity. At July 1, 2001, the Company had a series of swap contracts outstanding through September 2002 with a contract value of \$12,057. The derivative net losses on these contracts recorded in OCI at July 1, 2001 was an after-tax loss of \$1,077.

### 2 INVENTORIES

Inventories consist of the following:

	JULY 1, 2001	SEPTEMBER 30, 2001
	-----	-----
Raw material.....	\$28,864	\$28,864
Work-in-process.....	18,129	18,129
Finished goods.....	45,320	45,320
	-----	-----
	\$92,313	\$92,313
	=====	=====

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3 OTHER COMPREHENSIVE INCOME

Comprehensive income and the components of other comprehensive income for the three and nine months ended July 1, 2001 and July 2, 2000 are as follows:

	THREE MONTHS -----	
	2001 ----	2000 ----
Net income.....	\$2,722	\$8,078
Other comprehensive income (loss):		
Foreign currency translation.....	44	(657)
Net unrealized gain on available for sale securities.....	105	--
Cumulative effect of change in accounting principle	--	--
Net loss on derivative instruments.....	(490)	--
	-----	-----
Comprehensive income.....	\$2,381	\$7,421
	=====	=====

4 NET INCOME PER COMMON SHARE

Net income per common share for the three and nine months ended July 1, 2001 and July 2, 2000 is calculated based upon the following shares:

	THREE MONTHS -----	
	2001 ----	2000 ----
Basic.....	28,080	27,511
Effect of assumed conversion of options.....	1,048	1,533
	-----	-----
Diluted.....	29,128	29,044
	=====	=====

5 SHAREHOLDERS' EQUITY

On June 22, 2001, the Company completed a primary offering of 3,500 shares of Common Stock. The net proceeds of approximately \$64,500, after deducting the underwriting discounts and offering expenses, were used to repurchase approximately \$64,800 principal amount of 10-1/4% Series B Senior Subordinated Notes.



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Concurrently, the Thomas H. Lee Group and its affiliates sold approximately 4,200 shares and certain Rayovac officers and employees sold approximately 900 shares in a secondary offering of common stock. The Company did not receive any proceeds from the sale of the secondary offering shares but incurred expenses for the offering of approximately \$300 which are included in Other Special Charges.

### 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 1998, 1999 and \$2,250 for 2000. At July 1, 2001, the Company had commitments of approximately \$3,170 for the acquisition of manufacturing equipment, all of which is expected to be incurred in calendar 2001.

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 parties, has been designated a potentially responsible party of various third-party sites on the United States EPA National Priorities

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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 \$2,776, 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, such contingent liabilities are not likely to 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 our 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 our June 2001 secondary offering. The amount recorded includes \$7,100 of employee termination benefits for approximately 500 employees, \$10,600 of equipment, inventory, and other asset write-offs, and \$1,100 of other expenses. A summary of the 2001 restructuring activities follows:

#### 2001 RESTRUCTURING SUMMARY

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	TERMINATION BENEFITS -----	OTHER COSTS -----
Expense accrued.....	\$5,000	\$11,000
Balance December 31, 2000.....	\$5,000	\$11,000
Expense as incurred.....	100	200
Cash expenditures.....	(800)	(200)
Non cash charges.....	--	(3,000)
Balance April 1, 2001.....	\$4,300	\$8,000
Change in estimate.....	2,000	(100)
Expense as incurred.....	--	200
Cash expenditures.....	(3,100)	--
Non cash charges.....	--	(3,000)
Balance July 1, 2001.....	\$3,200	\$5,100
	=====	=====

During 1999, the Company recorded special charges as follows: (i) \$2,528 of employee termination benefits for 43 employees related to organizational restructuring in the U.S. and Europe, (ii) \$1,300 of charges related to the discontinuation of the manufacturing of silver-oxide cells at the Company's Portage, Wisconsin, facility, and (iii) \$2,100 of charges related to the termination of non-performing foreign distributors. The Company also recognized special charges of \$803 related to the investigation of financing options and developing organizational strategies for the Latin American acquisition. A summary of the 1999 restructuring activities follows:

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1999 RESTRUCTURING SUMMARY

	TERMINATION BENEFITS -----	OTHER COSTS -----
Expense accrued.....	\$2,500	\$3,400
Cash expenditures.....	(200)	--
Balance September 30, 1999.....	\$2,300	\$3,400
Change in estimate.....	--	100
Cash expenditures.....	(2,200)	--
Non cash charges.....	--	(3,300)
Balance September 30, 2000.....	\$100	\$200

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Cash expenditures.....	(100)	--
Non cash charges.....	--	(200)
	-----	-----
Balance July 1, 2001.....	\$--	\$--
	=====	=====

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 MONTH PERIODS ENDED	
	JULY 1, 2001	JULY 2, 2000
	-----	-----
North America.....	\$119,005	\$111,530
Latin America.....	29,062	27,369
Europe/ROW.....	11,065	11,452
	-----	-----
Total segments.....	\$159,132	\$150,351
	=====	=====

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	THREE MONTH PERIODS ENDED	
	JULY 1, 2001	JULY 2, 2000
INTER SEGMENT REVENUES		
North America.....	\$6,724	\$4,665
Latin America.....	2,711	208
Europe/ROW.....	574	327
	---	---
Total segments.....	\$10,009	\$5,200
	=====	=====

	THREE MONTH PERIODS ENDED	
	JULY 1, 2001	JULY 2, 2000
SEGMENT PROFIT		
North America.....	\$22,347	\$21,338
Latin America.....	3,529	5,036
Europe/ROW.....	1,583	628
	-----	-----
Total segments.....	27,459	27,002
Corporate.....	5,918	7,234
Special charges.....	2,579	--
Interest expense.....	7,017	7,727
Other (income) expense, net.....	(180)	(387)
	-----	-----
Income before income taxes and extraordinary item.....	\$12,125	\$12,428
	=====	=====

SEGMENT ASSETS
North America.....
Latin America.....
Europe/ROW.....
Total segments.....
Corporate.....
Total assets at period end.....

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

The following condensed consolidating financial data illustrate the composition

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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 July 1, 2001  
(Unaudited)  
(In thousands)

	PARENT	GUARANTOR SUBSIDIARIES	NONGUARANTOR SUBSIDIARIES
	-----	-----	-----
-ASSETS-			
Current assets:			
Cash and cash equivalents	\$ 1,814	\$ 48	\$ 8,398
Receivables	69,230	45,414	59,072
Inventories	65,359	-	27,053
Prepaid expenses and other	25,255	342	12,271
	-----	-----	-----
Total current assets	161,658	45,804	106,794
Property, plant and equipment, net	77,113	37	30,863
Deferred charges and other, net	57,490	274	2,412
Intangible assets, net	90,096	-	29,510
Investments in subsidiaries	143,063	99,049	-
	-----	-----	-----
Total assets	\$ 529,420	\$ 145,164	\$ 169,579
	=====	=====	=====
-LIABILITIES AND SHAREHOLDERS' EQUITY-			
Current liabilities:			
Current maturities of long-term debt	\$ 23,282	\$ -	\$ 8,979
Accounts payable	87,461	16	23,392
Accrued liabilities:			
Wages benefits and other	17,256	2,085	11,174
Recapitalization and other special charges	4,931	-	-
	-----	-----	-----
Total current liabilities	132,930	2,101	43,545
Long term debt, net of current maturities	218,511	-	18,490
Employee benefit obligations, net of current portion	15,744	-	601
Other	4,586	-	7,894
	-----	-----	-----

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Total liabilities	371,771	2,101	70,530
Shareholders' equity:			
Common stock	615	1	12,072
Additional paid-in capital	180,901	62,788	54,904
Retained earnings	114,959	80,440	33,593
Accumulated other comprehensive loss	(1,532)	(166)	(1,520)
Notes receivable from officers/shareholders	(3,665)	-	-
	-----	-----	-----
	291,278	143,063	99,049
Less treasury stock, at cost	(130,070)	-	-
Less unearned restricted stock compensation	(3,559)	-	-
	-----	-----	-----
Total shareholders' equity	157,649	143,063	99,049
	-----	-----	-----
Total liabilities & shareholders' equity	\$ 529,420	\$ 145,164	\$ 169,579
	=====	=====	=====

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RAYOVAC CORPORATION AND SUBSIDIARIES  
CONDENSED CONSOLIDATING STATEMENT OF OPERATIONS  
For the three month period ended July 1, 2001  
(Unaudited)  
(In thousands)

	PARENT	GUARANTOR SUBSIDIARIES	NONGUARANTOR SUBSIDIARIES
	-----	-----	-----
Net sales	\$ 113,453	\$ 10,917	\$ 47,216
Cost of goods sold	54,536	10,589	28,837
Special charges	287	-	1,992
	-----	-----	-----
Gross profit	58,630	328	16,387
Selling expense	32,781	167	9,852
General and administrative	10,356	(2,714)	2,251
Research and development	2,990	-	-
Other special charges	300	-	-
	-----	-----	-----
Total operating expenses	46,427	(2,547)	12,103
Income from operations	12,203	2,875	4,284
Interest expense	6,656	-	1,152
Equity income	(4,948)	(1,878)	-
Other (income) expense, net	(639)	(429)	97
	-----	-----	-----
Income before income taxes and extraordinary item	11,134	5,182	3,035
Income tax expense	2,662	234	1,157
	-----	-----	-----

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Income before extraordinary item	8,472	4,948	1,878
Extraordinary item, loss on early extinguishment of debt, net of income tax benefit of \$3,279	(5,350)	-	-
Net Income	\$ 3,122	\$ 4,948	\$ 1,878

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RAYOVAC CORPORATION AND SUBSIDIARIES  
CONDENSED CONSOLIDATING STATEMENT OF OPERATIONS  
For the nine month period ended July 1, 2001  
(Unaudited)  
(In thousands)

	PARENT	GUARANTOR SUBSIDIARIES	NONGUARANTOR SUBSIDIARIES
Net sales	\$ 349,922	\$ 32,730	\$ 146,836
Cost of goods sold	171,131	31,748	87,286
Special charges	16,346	-	2,193
Gross profit	162,445	982	57,357
Selling expense	105,932	521	31,210
General and administrative	32,321	(8,377)	9,968
Research and development	9,010	-	-
Other special charges	300	-	-
Total operating expenses	147,563	(7,856)	41,178
Income from operations	14,882	8,838	16,179
Interest expense	21,280	-	2,522
Equity income	(16,963)	(8,155)	-
Other (income) expense, net	(1,368)	(427)	1,337
Income before income taxes and extraordinary item	11,933	17,420	12,320
Income tax expense	1,002	457	4,165
Income before extraordinary item	10,931	16,963	8,155
Extraordinary item, loss on early extinguishment of debt, net of income tax benefit of \$3,279	(5,350)	-	-
Net Income	\$ 5,581	\$ 16,963	\$ 8,155

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RAYOVAC CORPORATION AND SUBSIDIARIES  
 CONDENSED CONSOLIDATING STATEMENTS OF CASH FLOWS  
 For the nine month period ended July 1, 2001  
 (Unaudited)  
 (In thousands)

	PARENT	GUARANTOR SUBSIDIARIES	NONGUARANTOR SUBSIDIARIES
Net cash provided by operating activities	\$ 21,623	\$ 10	\$ 5,983
Cash flows from investing activities:			
Purchases of property, plant and equipment	(14,007)	-	(1,208)
Purchases of investments	(500)	-	(299)
Proceeds from sale of investments	-	-	1,361
Proceeds from sale of property, plant, and equipment	487	-	22
Net cash used by investing activities	(14,020)		
Cash flows from financing activities:			
Reduction of debt	(316,094)	-	(4,525)
Extinguishment of debt	(69,693)	-	-
Proceeds from debt financing	310,601	-	-
Issuance of stock	67,781	-	-
Other	(1,075)	(6)	(165)
Net cash used by financing activities	(8,480)	(6)	(4,690)
Effect of exchange rate changes on cash and cash equivalents	-	-	207
Net (decrease) increase in cash and cash equivalents	(877)	4	1,376
Cash and cash equivalents, beginning of period	2,691	44	7,022
Cash and cash equivalents, end of period	\$ 1,814	\$ 48	\$ 8,398

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

FISCAL QUARTER AND NINE MONTHS ENDED JULY 1, 2001 COMPARED TO  
 FISCAL QUARTER AND NINE MONTHS ENDED JULY 2, 2000

NET SALES. Net sales for the three months ended July 1, 2001 (the



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"Fiscal 2001 Quarter") increased \$8.7 million, or 5.8%, to \$159.1 million from \$150.4 million in the three months ended July 2, 2000 (the "Fiscal 2000 Quarter"). The increase was driven by growth in alkaline battery sales attributable to new distribution, product line expansion, promotional timing, and growth in the OEM trade channel. Partially offsetting the alkaline battery increases were decreases in lighting products primarily reflecting reduced sales in North America attributable to hurricane shipments in the Fiscal 2000 Quarter and general market softness compounded by lower sales of specialty batteries to OEM customers in the PC, telecommunications and electronics industries and softness in rechargeable sales.

Net sales for the nine months ended July 1, 2001 (the "Fiscal 2001 Nine Months") decreased \$13.9 million, or 2.8%, to \$487.9 million from \$501.8 million in the nine months ended July 2, 2000 (the "Fiscal 2000 Nine Months"). Increases in hearing aid batteries and alkaline sales were offset by decreased lighting products sales, softness in sales of specialty batteries to OEM customers in the PC, telecommunications and electronics industries, and the transition to the camcorder license arrangement.

NET INCOME. Net income for the Fiscal 2001 Quarter decreased \$5.4 million to \$2.7 million from \$8.1 million in the Fiscal 2000 Quarter. The decrease reflects an extraordinary loss of \$5.4 million, net of tax, resulting from the premium on the repurchase of \$64.8 million of Senior Subordinated Notes following the Company's secondary offering in June 2001 and related write-off of unamortized debt issuance costs. Restructuring charges and expenses associated with our June 2001 secondary offering were offset by income from sales growth in North America.

Net income for the Fiscal 2001 Nine Months decreased \$20.5 million to \$5.1 million from \$25.6 million in the Fiscal 2000 Nine Months. The decrease reflects the impact of a \$18.5 million pretax restructuring charge, a \$5.4 million extraordinary loss, net of tax, and sales softness in North America and Europe/ROW partially offset by sales growth in Latin America.

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 which includes corporate purchasing expense, general and administrative expense and research and development expense.

	FISCAL QUARTER		NINE MONTHS	
	2001	2000	2001	2000
NORTH AMERICA				
Revenue from external customers.....	\$119.0	\$111.5	\$361.9	\$377.5
Profitability.....	22.4	21.4	61.1	63.9
Profitability as a % of net sales.....	18.8%	19.2%	16.9%	16.9%
Assets.....	\$283.8	\$266.1	\$283.8	\$266.1

Our sales to external customers increased \$7.5 million, or 6.7%, to \$119.0 million in the Fiscal 2001 Quarter from \$111.5 million the previous year due primarily to strong sales of alkaline, heavy duty, and hearing aid batteries partially offset by weakness in specialty batteries, lighting products, and rechargeable batteries. Alkaline sales increases of \$15.0 million, or 24.9%, were primarily attributable to strong sales at retail, distribution gains, and product line expansion compounded by strong sales in the OEM trade channel partially offset by weakness in the food and drug trade channels. Heavy duty sales increases of \$1.5 million, or 17.9%, were primarily driven by product line expansion at retail. Hearing aid battery sales increases of \$0.6 million, or

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6.1%, primarily reflect strong growth in the

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professional hearing aid trade channel and expanded retail distribution. Specialty batteries sales decreases versus last year primarily reflect softness in camcorder battery and lithium battery sales of \$2.6 million and \$1.9 million, respectively. These decreases reflect the transition to the camcorder licensing agreement with our Hong Kong licensee and general softness in demand from OEM customers in the PC, telecommunications and electronics industries. Lighting product sales decreases of \$3.1 million, or 17.7%, were driven by general weakness in the lights category. Rechargeable battery sales decreases of \$2.1 million, or 25.0%, were driven by promotional timing and our inability to anniversary an initial sell-in last year to a major mass retailer.

In the Fiscal 2001 Nine Months, our sales to external customers decreased \$15.6 million, or 4.1%, to \$361.9 million from \$377.5 million the previous year. Increased sales of hearing aid, alkaline, and heavy duty batteries were offset by decreased sales of lighting products and specialty batteries. Lighting product sales decreases of \$13.4 million, or 23.8%, were driven by weakness in the lights and lantern battery category reflecting the impact of the Y2K phenomenon. Specialty batteries sales versus last year primarily reflect softness in camcorder battery and lithium battery sales of \$5.8 and \$8.0 million, respectively, reflecting the transition to a licensing agreement and general softness in lithium battery demand from OEM customers in the PC, telecommunications and electronics industries. Hearing aid battery sales increases of \$4.8 million, or 16.5%, primarily reflect strength in the professional channel and expanded retail distribution in Fiscal 2001. Alkaline sales increases of \$3.6 million, or 1.7%, were driven by distribution gains, product line expansion, and strong sales in the mass merchandiser and OEM trade channels partially offset by the impacts of Y2K on sales volumes and lower promotional activity at certain food retailers this year. Heavy duty sales increases of \$3.0 million, or 10.3%, primarily reflect product line expansion at retail.

Our profitability increased \$1.0 million, or 4.7%, to \$22.4 million in the Fiscal 2001 Quarter from \$21.4 million in the Fiscal 2000 Quarter. The increase in profitability in the Fiscal 2001 Quarter was primarily attributable to the sales expansion partially offset by higher selling and distribution expenses. Our profitability margins decreased 40 basis points to 18.8% from 19.2% in the previous year. The decrease primarily reflects higher operating expenses as a percentage of sales partially offset by improved gross profit margins.

In the Fiscal 2001 Nine Months, our profitability decreased \$2.8 million, or 4.4%, to \$61.1 million from \$63.9 million. The decrease in profitability in the Fiscal 2001 Nine Months was primarily attributable to the sales shortfall partially offset by improved gross profit margins, reflecting a favorable product mix, price increases and operating expense decreases. Our profitability margins were unchanged from the previous year.

Our assets increased \$17.7 million, or 6.7%, to \$283.8 million in the Fiscal 2001 Quarter from \$266.1 million the previous year. The increase was primarily attributable to an increase in accounts receivable partially offset by lower inventories.

FISCAL QUARTER

NINE MONTHS

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LATIN AMERICA	2001	2000	2001	2000
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Revenue from external customers.....	\$29.0	\$27.4	\$89.4	\$83.6
Profitability.....	3.5	5.0	14.9	15.3
Profitability as a % of net sales.....	12.1%	18.2%	16.7%	18.3%
Assets.....	\$207.8	\$192.6	\$207.8	\$192.6

Our sales to external customers increased \$1.6 million, or 5.8% to \$29.0 million in the Fiscal 2001 Quarter from \$27.4 million and increased \$5.8 million, or 6.9% to \$89.4 million in the Fiscal 2001 Nine Months from \$83.6 million the previous year due primarily to increased sales of alkaline batteries partially offset by lower sales of zinc carbon batteries affected by a slowing economic environment and the unfavorable impacts of currency devaluation of \$0.2 million and \$1.6 million, respectively. Alkaline sales increases of \$1.3 million and \$6.1 million in the Fiscal 2001 Quarter and Nine Months, respectively, were driven by new distribution in mass merchandiser chains compounded by expansion into the Southern region of South America in Fiscal 2000. Heavy duty battery sales were relatively unchanged for the Fiscal 2001 Quarter and Nine Months versus last year.

Our profitability declined \$1.5 million, or 30.0%, in the Fiscal 2001 Quarter and decreased \$0.4 million, or 2.6% in the Fiscal 2001 Nine Months versus the Fiscal 2000 Nine Months. The decrease in profitability versus the Fiscal 2000 Quarter primarily reflects higher operating expenses reflecting expansion into the

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Southern region of South America and higher costs associated with our Mexican operations. The operating expense increases reflect our ongoing expansion in the Southern region and an increase in Mexico reflecting increased marketing and promotional expenses associated with new distribution at larger retail accounts. The decrease in profitability in the Fiscal 2001 Nine Months is primarily attributable to the higher operating expenses reflecting the expansion into the Southern region of South America in Fiscal 2000 partially offset by of increased sales and gross profit.

Our profitability margins in the Fiscal 2001 Quarter decreased 610 basis points primarily reflecting an increase in operating expenses compounded by weakness in gross profit margins. The operating expense increase primarily reflects increases in the Southern region of South America and in Mexico. Our profitability margins in the Fiscal 2001 Nine Months decreased 160 basis points primarily reflecting an increase in operating expense attributable to a full year impact of expansion into the Southern region of South America compounded by an increase in expenses associated with new distribution at larger retail accounts, partially offset by improved gross profit margins.

Our assets increased \$15.2 million, or 7.9%, to \$207.8 million in the Fiscal 2001 Quarter from \$192.6 million the previous year. The increase was primarily attributable to an increase in accounts receivable of \$19.5 million reflecting longer terms associated with distribution at larger retail accounts and general economic weakness partially offset by a decrease in inventory of \$3.9 million reflecting improved inventory management in Mexico.

	FISCAL QUARTER		NINE MONTHS	
	-----	-----	-----	-----
EUROPE/ROW	2001	2000	2001	2000
	----	----	----	----
Revenue from external customers.....	\$11.1	\$11.5	\$36.6	\$40.7

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Profitability.....	1.6	0.6	2.9	4.7
Profitability as a % of net sales.....	14.4%	5.2%	7.9%	11.6%
Assets.....	\$27.4	\$27.8	\$27.4	\$27.8

Our sales to external customers decreased \$0.4 million, or 3.5%, to \$11.1 million in the Fiscal 2001 Quarter from \$11.5 million and decreased \$4.1 million, or 10.1%, to \$36.6 million in the Fiscal 2001 Nine Months from \$40.7 million the previous year primarily reflecting the impacts of currency devaluation of \$0.8 million and \$3.8 million, respectively. Excluding the effects of foreign exchange, Europe/ROW for the Fiscal 2001 Quarter experienced volume gains in alkaline and hearing aid battery sales.

Our profitability increased \$1.0 million to \$1.6 million in the Fiscal 2001 Quarter and decreased \$1.8 million to \$2.9 million in the Fiscal 2001 Nine Months. The increase in profitability in the Fiscal 2001 Quarter primarily reflects lower selling expenses reflecting changes in estimated costs of promotional programs. The profitability decrease in the Fiscal 2001 Nine Months reflects the impact of currency devaluation on gross profit compounded by higher selling and distribution expenses.

Our profitability margin increase, as a percentage of sales, in the Fiscal 2001 Quarter is primarily driven by our favorable selling expenses and the profitability margin decrease, as a percentage of sales, in the Fiscal 2001 Nine Months, is attributable to the fixed nature of our expenses over lower sales volumes.

Our assets decreased \$0.4 million, or 1.4%, to \$27.4 million from \$27.8 million the previous year due primarily to a decrease in inventory reflecting improvements in inventory management and a decrease in accounts receivable.

CORPORATE EXPENSE. Our corporate expense decreased \$1.3 million, or 18.1%, to \$5.9 million in the Fiscal 2001 Quarter from \$7.2 million in the Fiscal 2000 Quarter and \$0.7 million, or 3.3%, to \$20.7 million in the Fiscal 2001 Nine Months from \$21.4 million in the Fiscal 2000 Nine months. These decreases were primarily attributable to lower management incentives, legal expenses, a gain on the sale of an investment partially offset by higher research and development expenses reflecting an increase in technology spending. As a percentage of total sales, our corporate expense was 3.7% and 4.8% in the Fiscal 2001 and Fiscal 2000 Quarters and was 4.2% and 4.3% in the Fiscal 2001 and Fiscal 2000 Nine Months, respectively.

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SPECIAL CHARGES. The Company recorded special charges of \$2.6 million in the Fiscal 2001 Quarter primarily reflecting expenses associated with the shutdown of the Company's Wonewoc, Wisconsin, manufacturing facility and restructuring initiatives in Latin America and the U.S.

In the Fiscal 2001 Nine Months, 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 our 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, (v) and costs associated with our secondary offering in June 2001. The amount recorded includes \$7.1 million of employee termination benefits for approximately 500 employees, \$10.6 million of equipment, inventory, and other asset write-offs, and \$1.1 million of other expenses.

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INCOME FROM OPERATIONS. Our income from operations decreased \$0.8 million, or 4.0%, to \$19.0 million in the Fiscal 2001 Quarter from \$19.8 million the previous year. The decrease was attributable to special charges of \$2.6 million partially offset by improved profitability in North America and Europe/ROW. Excluding the impact of the special charges, income from operations increased \$1.8 million, or 9.1%.

In the Fiscal 2001 Nine Months, our income from operations decreased \$23.1 million, or 37.0%, to \$39.4 million from \$62.5 million the previous year. These decreases were primarily due to special charges of \$18.8 million, decreased profitability in North America, Latin America, and Europe/ROW. Excluding the impact of the special charges, income from operations decreased \$4.3 million, or 6.9%.

INTEREST EXPENSE. Interest expense decreased \$0.7 million to \$7.0 million in the Fiscal 2001 Quarter and decreased \$0.6 million to \$22.4 million Fiscal 2001 Nine Months versus the comparable periods in the prior year due primarily to lower effective interest rates.

OTHER (INCOME) EXPENSE. Other (income) expense decreased \$0.2 million to a \$0.2 million net income in the Fiscal 2001 Quarter. The decrease in the net income in the Fiscal 2001 Quarter primarily reflects foreign exchange losses partially offset by higher interest income. In the Fiscal 2001 Nine Months other (income) expense increased to a \$0.9 million net expense primarily reflecting foreign exchange losses, primarily in Latin America, partially offset by higher interest income.

INCOME TAX EXPENSE. Our effective tax rate was 33.4% for the Fiscal 2001 Quarter which brought the Fiscal 2001 Nine Months rate to 35.0%, equal to last year's rate for the Fiscal 2000 Nine Months.

EXTRAORDINARY ITEM. In the Fiscal 2001 Quarter, the Company recorded an extraordinary loss of \$5.4 million, net of tax, resulting from the premium on the repurchase of \$64.8 million Senior B Subordinated Notes and the related write-off of unamortized debt issuance costs.

### ADOPTION OF NEW ACCOUNTING PRONOUNCEMENTS

Effective October 1, 2000, the Company adopted SFAS 133, which establishes accounting and reporting standards for derivative instruments, including certain derivative instruments embedded in other contracts and for hedging activities. All derivatives, whether designated in hedging relationships or not, are required to be recorded on the balance sheet at fair value. If the derivative is designated as a fair value hedge, the change in the fair value of the derivative and of the hedged item attributable to the hedged risk are recognized in earnings. If the derivative is designated as a cash flow hedge, the effective portions of changes in the fair value of the derivative are recorded in other comprehensive income (OCI) and are recognized in the income statement when the hedged item affects earnings. Ineffective portions of changes in the fair value of cash flow hedges are recognized in earnings.

The adoption of SFAS 133 resulted in a pre-tax reduction to OCI of \$0.3 million (\$0.2 million after tax). The reduction to OCI is primarily attributable to losses of approximately \$0.5 million for foreign exchange forward cash flow hedges partially offset by gains of approximately \$0.2 million on interest rate swap cash flow hedges. The net derivative losses included in OCI as of October 1, 2000 will be reclassified into earnings during the twelve months ending September 30, 2001.

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In January 2001, the Financial Accounting Standards Board's Emerging Issues Task Force (EITF) reached a consensus on Issue 3 of EITF Issue 00-22, "Accounting for "Points" and Certain Other Time-Based or Volume-Based Sales Incentive Offers, and Offers for Free Products or Services to Be Delivered in the Future". Issue 3 addresses the recognition, measurement, and income statement classification for offers to a customer to rebate or refund a specified amount of cash that may be redeemed if the customer completes a specified volume of transactions. The consensus was effective for quarters ending after February 15, 2001. The Company adopted the consensus reached on Issue 3, in the second fiscal quarter of 2001. The adoption and subsequent restatement of the Fiscal 2001 and Fiscal 2000 Quarter and Nine Months resulted in the reclassification of certain selling expenses as a reduction in revenue and had no impact on pre-tax income, net income, or earnings per share.

### LIQUIDITY AND CAPITAL RESOURCES

For the Fiscal 2001 Nine Months, operating activities provided \$27.6 million in net cash compared with \$31.1 million the previous year. Operating cash flow decreases versus the previous year primarily reflect lower operating earnings attributable to our decrease in sales partially offset by working capital which was \$3.7 million lower than the previous year. The lower investment in working capital versus the comparable period a year ago primarily reflects lower inventory investments and higher special charge restructuring liabilities partially offset by increased accounts receivable and prepaid expenses and a decrease in accounts payable.

Net cash used by investing activities increased \$2.1 million versus the same period a year ago primarily reflecting an increase in capital expenditures partially offset by proceeds from the sale of investments and property, plant, and equipment. Expenditures in the current year were primarily for improvements to alkaline battery manufacturing and information systems hardware and software. The Company currently expects capital spending for Fiscal 2001 to be approximately \$20.0 million primarily due to alkaline battery manufacturing.

During the Fiscal 2001 Nine Months we granted approximately 0.8 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. We also granted approximately 277,000 shares of restricted stock on October 1, 2000, from the 1997 incentive plan, to certain members of management. Approximately 210,000 of these shares will vest on September 30, 2003 provided the recipient is still employed by the Company. The remainder vests one third each year for the next three years. The total market value of the restricted shares on date of grant totaled approximately \$4.7 million and has been recorded as restricted stock as a separate component of shareholders' equity. Unearned compensation is being amortized to expense over the three-year vesting period.

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 July 1, 2001, \$37.8 million of the term loan remained outstanding and \$195.2 million was outstanding under the revolving facility with approximately \$13.3 million of the remaining availability utilized for outstanding letters of credit.

### IMPACT OF RECENTLY ISSUED ACCOUNTING STANDARDS

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In December 1999, the Securities and Exchange Commission issued Staff Accounting Bulletin No. 101, "Revenue Recognition" (SAB 101). The SAB summarizes certain of the SEC's views in applying U.S. generally accepted accounting principles to revenue recognition in financial statements. In June 2000, the SEC issued SAB 101B, which delays the implementation date of SAB 101 until no later than the fourth fiscal quarter of fiscal years beginning after December 15, 1999. In October 2000, the SEC issued frequently asked questions and answers about how guidance in accounting standards and SAB 101 would apply to particular transactions. The amendment in June 2000 delayed the effective date for the Company until the fourth fiscal quarter of 2001, which is when the Company will adopt the bulletin. The adoption will not have a material impact on the consolidated financial statements.

In May 2000, the 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

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including discounts, coupons, rebates and free products. In July 2001, the EITF delayed the implementation of EITF 00-14 until no later than quarters beginning after December 15, 2001. The Company is required to adopt this consensus in the second fiscal quarter of 2002. The impact of this consensus on the Company's consolidated financial statements is still being evaluated. The Company does not currently believe its adoption will have a material impact on the consolidated financial statements other than the reclassification of certain selling expenses to cost of sales or a reduction of revenue.

In July and September 2000, the EITF reached a consensus on Issue No. 00-10, "Accounting for Shipping and Handling Fees and Costs." This Issue addresses the income statement classification for shipping and handling fees and costs. The Company will adopt this consensus in the fourth fiscal quarter of 2001. The impact of this consensus on the Company's consolidated financial statements is still being evaluated. The adoption will not have a material impact on the consolidated financial statements.

In April 2001, the EITF reached a consensus on Issue 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 is required to adopt this consensus in the second fiscal quarter of 2002. The Company does not currently believe its adoption will have a material impact on the consolidated financial statements, other than the reclassification of certain selling expenses to cost of sales or a reduction in revenue.

On July 20, 2001, the FASB issued Statement No. 141, BUSINESS COMBINATIONS, and Statement No. 142, GOODWILL AND OTHER INTANGIBLE ASSETS. Statement 141 requires that all business combinations be accounted for under a single method -- the purchase method. Use of the pooling-of-interests method no longer is permitted. Statement 141 requires that the purchase method be used for business combinations initiated after June 30, 2001. Statement 142 requires that goodwill and intangible assets with an indefinite life no longer be amortized to earnings, but instead be reviewed for impairment. The amortization of goodwill and intangible assets with an indefinite life acquired in a transaction completed prior to June 30, 2001, ceases upon adoption of the Statement, which the Company is required to adopt no later than our fiscal year beginning October

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1, 2002. Management is currently evaluating the impact of adoption on the consolidated financial statements.

### 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 Condensed 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 swaps are designated as cash flow hedges with the fair value recorded in 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.

#### FOREIGN EXCHANGE RISK

We are subject to risk from sales to, purchases from 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,

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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 forecasted sales, accounts receivable, forecasted purchases, accounts payable, intercompany loans, firm purchase commitments and credit obligations through the use of naturally occurring offsetting positions (borrowing in local currency) and forward foreign exchange contracts. Forward foreign exchange contracts to hedge forecasted transactions 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 sale or purchase and a related asset or liability recorded in the balance sheet, the gain or loss on the related derivative hedge contract is re-classified from OCI into earnings as an offset to the change in value of the asset or liability. Forward foreign exchange contracts to hedge firm purchase commitments are designated as fair value hedges with the fair value recorded in earnings and as a hedge asset or liability as applicable.

#### COMMODITY PRICE RISK



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We are exposed to fluctuation in market prices for purchases of zinc metal-based items used in the manufacturing process. We hedge 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 forecasted purchase of zinc metal-based items also affects earnings.

### SENSITIVITY ANALYSIS

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

As of July 1, 2001, 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 \$0.9 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 gain of \$1.5 million.

As of July 1, 2001, 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 \$0.5 million. The net impact on future cash flows, after also including the gain in value on the related accounts receivable payment obligations outstanding at July 1, 2001 due to the same change in exchange rates, would be a net gain of \$2.2 million.

As of July 1, 2001, 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 \$1.2 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.

### 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" 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

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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 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.

### 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, 2000 ("2000 Form 10-K") except as follows:

On February 9, 2001, the Wisconsin Department of Natural Resources approved our request to proceed under Wisconsin's Voluntary Party Liability Exemption program to investigate and, if necessary, remediate environmental matters at our Wonewoc, Wisconsin, manufacturing facility. Investigative work to date suggests there may be battery materials containing various heavy metals in fill on the property. However, we do not expect this matter to result in material expenditures.

On April 11, 2001, Eveready Battery Company, Inc. filed a complaint against us in U.S. District Court for the Northern District of Ohio, Eastern Division, alleging that we have infringed on a patent held by Eveready relating to mercury-free alkaline batteries. Eveready is seeking injunctive relief as well as treble damages and other costs and expenses. We have not been served with the complaint in this matter. We believe we have meritorious defenses to the claims presented in the complaint and, should we ultimately be served, we

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intend to dispute the allegations and otherwise defend our position. We cannot estimate at this time the effect, if any, that this claim may have on our business or financial condition.

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### ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

#### (a) Exhibits

EXHIBIT NUMBER	DESCRIPTION
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 10 1/4% 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

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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, N.A. 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 Security Agreement, dated as of September 12, 1996, by and among the Company, ROV Holding, Inc. and BofA.
- 4.12\*\* The Company Pledge Agreement, dated as of September 12, 1996, by and between the Company and BofA.
- 4.13\*\*\* Shareholders Agreement, dated as of September 12, 1996, by and among the Company and the shareholders of the Company referred to therein.
- 4.14\*\*\* 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.
- 4.15\*\*\*\*\* 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.
- 4.16+++++++ 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.
- 4.17\* Specimen certificate representing the Common Stock.
- 10.1+++++ Amended and Restated Employment Agreement, dated as of October 1, 2000, by and between the Company and David A. Jones.
- 10.2+++++ Amended and Restated Employment Agreement, dated as of October 1, 2000, by and between the Company and Kent J. Hussey.
- 10.3+++++ Employment Agreement, dated as of October 1, 2000, by and between the Company and Randall J. Steward.
- 10.4+++++ Employment Agreement, dated as of October 1, 2000, by and between the Company and Kenneth V. Biller.
- 10.5+++++ Employment Agreement, dated as of October 1, 2000, by and between the Company and Stephen P. Shanesy.
- 10.6+++++ Employment Agreement, dated as of October 1, 2000, by and

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between the Company and Merrell M. Tomlin.

10.7+++++

Employment Agreement, dated as of October 1, 2000, by and between the Company and Luis A. Cancio.

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

\*\* 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.

\*\*\*\*\* 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 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.

(b) Reports on Form 8-K: The Company has filed the following reports on Form 8-K during the three-month period ending July 1, 2001:

1. On June 14, 2001, the Company filed with the Commission a Report on Form 8-K to report issuance of a press release regarding the expiration of its consent solicitation and receipt of consents sufficient to amend the indenture relating to the Company's 10 1/4% Series B Senior

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Subordinated Notes due 2006.

2. On June 19, 2001, the Company filed with the Commission a Report on Form 8-K to report that a supplemental indenture incorporating the amendments to the indenture referenced in the Company's June 14, 2001, Form 8-K was executed on June 17, 2001, and will become operative when the tendered notes are accepted for payment.
3. On June 20, 2001, the Company filed with the Commission a Report on Form 8-K for the purpose of filing the Purchase Agreement dated June 20, 2001, by and among the Company, certain shareholders

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identified in the Purchase Agreement ("Selling Shareholders") and Salomon Smith Barney Inc., and certain other underwriters identified in the Purchase Agreement ("Underwriters") as an exhibit to the Company's shelf registration statement on Form S-3 (Registration No. 333-59086).

4. On June 25, 2001, the Company filed with the Commission a Report on Form 8-K to report issuance of a press release announcing the pricing terms for the tender offer for all of its outstanding \$65 million principal amount of 10 1/4% Series B Senior Subordinated Notes due 2006.
5. On June 28, 2001, the Company filed with the Commission a Report on Form 8-K to report issuance of a press release announcing the closing of the offer to purchase for cash and consent solicitation with respect to its outstanding \$65 million principal amount of 10 1/4% Series B Senior Subordinated Notes due 2006.

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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: August 9, 2001

RAYOVAC CORPORATION

By: /s/ Randall J. Steward

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Randall J. Steward  
Executive Vice President of Administration  
and Chief Financial Officer

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