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

FORM 10-Q

(Mark One)

[X] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended March 31, 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 No. 0-24333

RAINBOW RENTALS, INC.
(Exact name of Registrant as specified in its charter)

Ohio	34-1512520
(State of Incorporation)	(IRS Employer Identification No.)

3711 Starr Centre Drive
Canfield, Ohio 44406
(Address of principal executive offices)

330-533-5363
(Registrant’s telephone number)

(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 _____

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

CLASS	SHARES OUTSTANDING AT APRIL 30, 2001
Common stock, no par value	5,925,735

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RAINBOW RENTALS, INC.
CONDENSED BALANCE SHEETS
(Dollars in thousands)

	(unaudited) March 31, 2001	December 31, 2000
Assets		
Current assets		
Cash	$ 1,206	$ 1,426
Rental-purchase merchandise, net	36,804	36,545
Income tax receivable	824	777
Prepaid expenses and other current assets	1,929	1,709
Total current assets	40,763	40,457
Property and equipment, net	5,348	5,259
Deferred income taxes	1,460	1,460
Goodwill, net	9,846	9,887
Other assets, net	1,283	1,365
Total assets	$58,700	$58,428
Liabilities and Shareholders' Equity		
Current liabilities		
Short-term debt	$10,905	$ —
Accounts payable	3,201	2,409
Accrued compensation and related costs	832	1,525
Other liabilities and accrued expenses	2,178	1,704
Deferred revenue	1,084	781
Deferred income taxes	3,978	3,678
Total current liabilities	22,178	10,097
Long-term debt	—	12,340
Total liabilities	22,178	22,437
Shareholders' equity		
Serial preferred stock, no par value; 2,000,000 shares authorized, none issued	—	—
Common stock, no par value; 10,000,000 shares authorized, 6,392,610 issued and 5,925,735 outstanding	11,039	11,039
Retained earnings	27,390	26,859
Treasury stock, 466,875 common shares at cost	(1,907)	(1,907)
Total shareholders' equity	36,522	35,991
Total liabilities and shareholders' equity	$58,700	$58,428

See accompanying notes to condensed financial statements.

RAINBOW RENTALS, INC.
CONDENSED STATEMENTS OF INCOME
(Dollars in thousands, except per share amounts)

	(unaudited) For the three months ended March 31, 2001	2000
Revenues		
Rental revenue	$ 22,466	$ 20,761
Fees	686	671
Merchandise sales	1,138	1,030
Total revenues	24,290	22,462
Operating expenses		
Merchandise costs	8,388	7,507
Store expenses		
Salaries and related	5,710	5,135
Occupancy	2,092	1,618
Advertising	1,524	1,046
Other expenses	3,344	2,861
Total store expenses	12,670	10,660
Total merchandise costs and store expenses	21,058	18,167
General and administrative expenses	1,855	1,618
Amortization of goodwill and noncompete agreements	175	132
Total operating expenses	23,088	19,917
Operating income	1,202	2,545
Interest expense	226	198
Other expense, net	85	73
Income before income taxes	891	2,274
Income taxes	360	932
Net income	$ 531	$ 1,342
Earnings per common share:		
Basic and diluted earnings per share	$ 0.09	$ 0.23
Weighted average common shares outstanding:		
Basic	5,925,735	5,925,735
Diluted	5,935,968	5,925,735

See accompanying notes to condensed financial statements.

RAINBOW RENTALS, INC.
CONDENSED STATEMENTS OF SHAREHOLDERS' EQUITY
(Dollars in thousands)

	Common Stock		Retained Earnings	Treasury Stock	Total Shareholders' Equity
	Shares	Cost			
Balance at December 31, 1999	5,925,735	$11,039	$22,754	$(1,907)	$31,886
Net income	—	—	4,105	—	4,105
Balance at December 31, 2000	5,925,735	11,039	26,859	(1,907)	35,991
Net income (unaudited)	—	—	531	—	531
Balance at March 31, 2001 (unaudited)	5,925,735	$11,039	$27,390	$(1,907)	$36,522

See accompanying notes to condensed financial statements.

RAINBOW RENTALS, INC.
CONDENSED STATEMENTS OF CASH FLOWS
(Dollars in thousands)

	(unaudited) For three months ended March 31, 2001	2000
Cash flows from operating activities		
Net income	$ 531	$ 1,342
Reconciliation of net income to net cash provided by operating activities		
Depreciation of property and equipment and amortization of intangibles	722	622
Depreciation of rental-purchase merchandise	6,615	5,876
Deferred income taxes	300	150
(Gain) loss on disposal of property and equipment	—	(81)
Purchases of rental-purchase merchandise	(8,490)	(6,945)
Rental-purchase merchandise disposed, net	1,743	1,627
Increase (decrease) in		
Income tax receivable	(47)	(161)
Prepaid expenses and other current assets	(220)	(130)
Accounts payable	792	336
Accrued compensation and related costs	(693)	(793)
Other liabilities and accrued expenses	474	(43)
Deferred revenue	303	—
Net cash provided by operating activities	2,030	1,800
Cash flows from investing activities		
Purchase of property and equipment, net	(578)	(751)
Proceeds on the sale of property and equipment	10	93
Acquisitions	(247)	—
Net cash used in investing activities	(815)	(658)
Cash flows from financing activities		
Proceeds from long-term debt	5,865	7,330
Repayments of long-term debt	(7,300)	(8,833)
Principal payments under capital lease obligations	—	(38)
Net cash used in financing activities	(1,435)	(1,541)
Net decrease in cash	(220)	(399)
Cash at beginning of period	1,426	440
Cash at end of period	$ 1,206	$ 41
Supplemental cash flow information:		
Net cash paid during the period for		
Interest	$ 195	$ 204
Income taxes	169	973

See accompanying notes to condensed financial statements.

RAINBOW RENTALS, INC.
NOTES TO CONDENSED FINANCIAL STATEMENTS
(Dollars in thousands, except per share amounts)

1. Basis of Presentation

Rainbow Rentals, Inc. (“Company”) is engaged in the rental and sale of home electronics, furniture, appliances and computers to the general public. The Company operates 112 stores in eleven states: Connecticut, Massachusetts, Michigan, New York, North Carolina, Ohio, Pennsylvania, Rhode Island, South Carolina, Tennessee and Virginia. The Company’s corporate headquarters is located in Canfield, Ohio.

The financial statements have been prepared in accordance with the instructions to Form 10-Q. Therefore, certain information and disclosures, normally required with financial statements prepared in accordance with accounting principles generally accepted in the United States of America, have been condensed or omitted. In the opinion of management, the financial statements contain all adjustments (consisting only of normal, recurring adjustments) necessary to present fairly the financial position, results of operations and cash flows of the Company. The results of operations for the periods presented are not necessarily indicative of the results for the entire year. It is suggested these financial statements be read in conjunction with the financial statements and notes included in the Company’s Annual Report for fiscal year ended December 31, 2000.

2. Earnings Per Share

Basic earnings per common share are computed using net income available to common shareholders divided by the weighted average number of common shares outstanding. For computation of diluted earnings per share, the weighted average number of common shares outstanding is increased to give effect to stock options considered to be common stock equivalents.

The following table shows the amounts used in computing earnings per share.

	For the three months ended March 31,	
	2001	**2000**
Numerator:		
Net income available to common shareholders	$ 531	$ 1,342
Denominator:		
Basic weighted average shares	5,925,735	5,925,735
Effect of dilutive stock options	10,233	—
Diluted weighted average shares	5,935,968	5,925,735
Basic earnings per share	$ 0.09	$ 0.23
Diluted earnings per share	$ 0.09	$ 0.23

3. Acquisitions

The Company has recently made acquisitions of stores, rental purchase merchandise and rental purchase agreements. All acquisitions made were accounted for using the purchase method of accounting. Accordingly, all identifiable assets were recorded at their estimated fair market value at the date of acquisition. The excess of the acquisition cost over the estimated fair value of the net assets acquired (“goodwill”) is being amortized on a straight-line basis over periods ranging from 18 to 20 years. Assets acquired, other than goodwill, consisted primarily of rental-purchase merchandise, property and equipment and noncompete agreements. The aggregate purchase price of acquisitions for the three months ended March 31, 2001 and the year ended December 31, 2000 were $247 and $3,385, respectively.

4. Short-Term Debt

The Company has a revolving loan agreement with a lending institution, which matures March 1, 2002 and is classified as short-term based on the maturity date. The maximum revolving loan amount under this agreement at March 31, 2001 was $16.0 million, of which $10.9 million was outstanding. Interest is charged on the outstanding loan balance at prime, however, the Company can request to have interest charged on a portion of the outstanding loan balance at the Interbank Offering Rate (IBOR) plus 200 basis points. At March 31, 2001, $10.0 million of the outstanding loan balance was subject to a rate of 7.06% (IBOR plus 200 basis points) and the remaining loan balance was subject to the prime rate of 8.0%. Additionally, the loan agreement calls for a nonuse fee equal to 0.25% per annum on the daily average amount by which the maximum revolving amount exceeds the outstanding loan balance.

The loan agreement is secured by substantially all assets, contract rights, documents and all rental agreements of the Company. There are four debt covenants that require the Company to maintain certain financial ratios as well as a minimum net worth. At March 31, 2001, the Company was in compliance with the covenants in the amended loan agreement.

Item 2: Management’s Discussion and Analysis of Financial Condition and Results of Operations

General

Generally, rental-purchase merchandise is rented to individuals under flexible agreements that allow customers to own the merchandise after making a specified number of rental payments (ranging from 12 to 24 months). Customers have the option to return the merchandise at any time without further obligation, and also have the option to purchase the merchandise at any time during the rental term.

During the current first quarter, the Company opened two new stores in existing markets and completed one acquisition. On March 1, 2001, the Company purchased the assets of two stores located in Tennessee and consolidated them into existing Company locations.

New Store Openings

The Company’s primary method of growth is through the opening of new store locations. New store openings are dilutive to earnings for the first nine to twelve months as they build a customer base and develop a recurring revenue stream. Generally, new stores have a maturation period of approximately three years. The timing of new store openings and the number of stores in various stages of the three-year maturation process will have an effect on quarterly comparisons.

Results of Operations

The following table sets forth, for the periods indicated, certain Statements of Income data as a percentage of total revenues.

	For the three months ended	
	2001	2000
Statement of Income Data:		
Revenues		
Rental revenue	92.5%	92.4%
Fees	2.8	3.0
Merchandise sales	4.7	4.6
Total revenues	100.0	100.0
Operating expenses		
Merchandise costs	34.5	33.4
Store expenses		
Salaries and related	23.5	22.9
Occupancy	8.6	7.2
Advertising	6.3	4.7
Other expenses	13.8	12.7
Total store expenses	52.2	47.5
Total merchandise costs and store expenses	86.7	80.9
General and administrative expenses	7.6	7.2
Amortization of goodwill and noncompete agreements	0.7	0.6
Total operating expenses	95.0	88.7
Operating income	5.0	11.3
Interest expense	0.9	0.9
Other expense, net	0.4	0.3
Income before income taxes	3.7	10.1
Income taxes	1.5	4.1
Net income	2.2%	6.0%

Comparison of Three Months Ended March 31, 2001 and 2000

For the three months ended March 31, 2001, total revenues increased $1.8 million to $24.3 million from $22.5 million, an increase of 8.1% over the comparable 2000 period. Revenue from the 18 stores opened and acquired in 2000 increased $2.3 million, offsetting a decrease of $0.5 million in revenue from comparable stores (stores in operation on January 1, 2000). Comparable store revenue decreased to $21.9 million from $22.4 million, a decrease of 2.5%. The decrease in comparable store revenue was due to a decline in the number of customers per store during the last half of 2000. Management believes the decline in customers was due to staffing shortages, increased competition and other market factors.

For the three months ended March 31, 2001, merchandise costs increased to $8.4 million from $7.5 million, an increase of 11.7% over the comparable 2000 period due to merchandise costs associated with stores opened and acquired in 2000. As a percentage of revenues, merchandise costs increased to 34.5% from 33.4% due primarily to increased rentals of older, pre-rented merchandise at reduced rental rates in order to decrease the amount of pre-rented merchandise accumulated during 2000. Promotional merchandise and special offers also contributed to the percentage increase of merchandise costs.

For the three months ended March 31, 2001, total store expenses increased $2.0 million to $12.7 million from $10.7 million, an increase of 18.8% over the comparable 2000 period. The increase in total store expenses was primarily due to the expenses associated with the 18 stores opened and acquired in 2000, which accounted for 78.1% of the total increase in store expenses, or $1.6 million. Store expenses of comparable stores increased $0.4 million (3.4%) due primarily to an increase in advertising and, to a lesser extent, expenses associated with the growth of stores opened during 1999. The increase in advertising expense of comparable stores was due to increased levels of spending in an effort to rebuild the Company's customer base. As a percentage of total revenues, total store expenses increased to 52.2% from 47.5% primarily due to store expenses of comparable stores, which increased to 49.0% in 2001 from 46.8% in the comparable 2000 period. The percentage increase was primarily due to a 2.5% decrease in comparable store revenue and an increase in advertising expense. Also contributing to the percentage increase in total store expenses was the increased number of new store openings in 2000 compared to 1999, which totaled 11 and 9, respectively, and expenses of the stores acquired in 2000 which totaled $0.6 million and 67% of revenue.

For the three months ended March 31, 2001, general and administrative expenses increased to $1.9 million from $1.6 million, an increase of 14.6% over the comparable 2000 period and, as a percentage of total revenues, increased to 7.6% from 7.2%. The increase was primarily due to the expansion of the Company's regional management team, the addition of several key support personnel and increased consulting fees, all of which were necessitated by the Company's anticipated growth.

For the three months ended March 31, 2001, operating income decreased to $1.2 million from $2.5 million, a decrease of 52.8% over the comparable 2000 period and, as a percentage of total revenues, decreased to 5.0% from 11.3% due to the factors discussed above.

For the three months ended March 31, 2001, the Company's effective tax rate decreased to 40.5% from 41.0% due to lower effective state tax rates.

For the three months ended March 31, 2001, net income decreased to $0.5 million from $1.3 million, a decrease of 60.4% over the comparable 2000 period and, as a percentage of total revenues, decreased to 2.2% from 6.0% due to the factors discussed above.

Liquidity and Capital Resources

The Company's primary requirements for capital consist of purchasing additional and replacement rental-purchase merchandise, expenditures related to new store openings, acquisitions and working capital requirements for new and existing stores. For the three months ended March 31, 2001 and 2000, purchases of rental merchandise (excluding acquisitions) amounted to $8.5 million and $6.9 million, respectively. The increase reflects merchandise inventory purchased for new store openings and acquisitions (excludes acquired inventory).

For the three months ended March 31, 2001, cash provided by operating activities increased to $2.0 million from $1.8 million for the comparable 2000 period. Cash used in investing activities increased to $0.8 million from $0.7 million. Cash used in financing activities decreased to $1.4 million from $1.5 million.

The Company currently has a $14.0 million revolving loan agreement with a lending institution (the "Credit Facility") with a maturity date of March 1, 2002. The Credit Facility includes certain cash flow, net worth and idle inventory requirements, as well as covenants which limit the ability of the Company to incur additional indebtedness, grant liens, transfer assets outside the ordinary course of business, pay dividends, engage in acquisition transactions and make capital expenditures (excluding the purchase of rental merchandise) in excess of a specified amount. Availability under the Company's Credit Facility as of May 15, 2001 was approximately $3.0 million. The Company is seeking new long-term debt financing with other institutional lenders to replace its current Credit Facility.

The Company plans to open approximately four stores during the remainder of the year. The Company believes it will continue to have the opportunity to increase the number of its stores and rental-purchase agreements through selective acquisitions. Potential acquisitions may vary in size and the Company may consider larger acquisitions that could be material to the Company. To provide any additional funds necessary for the continued pursuit of its growth strategies, the Company may use cash flow from operations, seek to obtain additional debt or equity financing, or use its own equity securities, the availability of which will depend upon market and other conditions. There can be no assurance that such additional financing will be available on terms acceptable to the Company.

Forward- Looking Statements

When used in this Form 10-Q, or, in future filings by Rainbow Rentals, Inc. with the Securities and Exchange Commission, in the Company's press releases or other public or shareholder communications, or in oral statements made with the approval of an authorized executive officer, the words or phrases "will likely result", "are expected to", "will continue", "is anticipated", "estimate", "project" or similar expressions are intended to identify "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995. Such statements are subject to certain risks and uncertainties including, but not limited to, (i) the ability of the Company to execute effectively its expansion program, (ii) the ability to attract and retain quality store personnel and (iii) changes in the government's regulation of the industry, that could cause actual results to differ materially from historical earnings and those presently anticipated or projected. The Company wishes to caution readers not to place undue reliance on any such forward-looking statements, which speak only as of the date made. The Company wishes to advise readers that the factors listed above and other factors could affect the Company's financial performance and could cause the Company's actual results for future periods to differ materially from any opinions or statements expressed with respect to future periods in any current statements. For further information, please refer to the Company's filings with the Securities and Exchange Commission, including specifically the Risk Factors contained in the Company's prospectus dated June 4, 1998.

The Company does not undertake, and specifically disclaims any obligation, to publicly release the result of any revisions, which may be made to any forward-looking statements to reflect events or circumstances after the date of such statements or to reflect the occurrence of anticipated or unanticipated events.

Item 3: Quantitative and Qualitative Disclosures About Market Risk

There were no material changes in information about market risk from that provided in the 2000 Annual Report to Shareholders.

PART II — OTHER INFORMATION
RAINBOW RENTALS, INC.
MARCH 31, 2001

Item 6. Exhibits and Reports on Form 8-K

A. Exhibit No.

4.6 Consent and Amendment No. 14 and Fifth Amended and Restated Supplement A to Loan and Security Agreement between the Company and Bank of America National Trust and Savings Association, dated May 15, 2001.

B. Reports on Form 8-K: None

SIGNATURES

In accordance with the Exchange Act, the registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

RAINBOW RENTALS, INC
(Registrant)

/s/ WAYLAND J. RUSSELL

Wayland J. Russell, Chairman and
Chief Executive Officer
(Principal Executive Officer)
Date: May 15, 2001

/s/ MICHAEL A. PECCHIA

Michael A. Pecchia,
Chief Financial Officer
(Principal Financial and Accounting Officer)
Date: May 15, 2001