HOOKER FURNITURE CORP
Form 10-Q
June 09, 2010

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

FORM 10-Q

Quarterly report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the quarterly period ended May 2, 2010

Commission file number 000-25349

HOOKER FURNITURE CORPORATION
(Exact name of registrant as specified in its charter)

Virginia (State or other jurisdiction of incorporation or organization)	54-0251350 (IRS employer identification no.)

440 East Commonwealth Boulevard, Martinsville, VA 24112
(Address of principal executive offices, zip code)

(276) 632-0459
(Registrant's telephone number, including area code)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (Section 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ¨ No ¨

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated Filer ¨	Accelerated filer x
Non-accelerated Filer ¨ (Do not check if a smaller reporting company)	Smaller reporting company ¨

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ¨ No x

Indicate the number of shares outstanding of each of the issuer's classes of common stock as of June 7, 2010

Common stock, no par value	10,774,743
(Class of common stock)	(Number of shares)

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

HOOKER FURNITURE CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
(In thousands, including share data)
(Unaudited)

		May 2, 2010		January 31, 2010
Assets				
Current Assets				
Cash and cash equivalents	$	38,747	$	37,995
Accounts receivable, less allowance for doubtful accounts				
of $1,559 and $1,938 on each date		24,388		25,894
Inventories		38,541		36,176
Prepaid expenses and other current assets		4,426		3,468
Total current assets		106,102		103,533
Property, plant, and equipment, net		22,198		22,747
Intangible assets		3,468		3,468
Cash surrender value of life insurance policies		15,315		14,810
Other assets		4,593		4,541
Total assets	$	151,676	$	149,099
Liabilities and Shareholders' Equity				
Current Liabilities				
Trade acccounts payable	$	11,781	$	10,425
Accrued salaries, wages and benefits		2,565		2,184
Other accrued expenses		2,588		1,953
Accrued dividends		1,077		1,077
Total current liabilities		18,011		15,639
Deferred compensation		6,099		5,868
Total liabilities		24,110		21,507
Shareholders' equity				
Common stock, no par value, 20,000 shares authorized,				
10,775 shares issued and oustanding on each date		17,091		17,076
Retained earnings		110,069		110,073
Accumulated other comprehensive income		406		443
Total shareholders' equity		127,566		127,592
Total liabilities and shareholders' equity	$	151,676	$	149,099

The accompanying notes are an integral part of the unaudited condensed consolidated financial statements.

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HOOKER FURNITURE CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(In thousands, except per share data)
(Unaudited)

	Thirteen Weeks Ended May 2, 2010	Thirteen Weeks Ended May 3, 2009
Net Sales	$51,353	$52,063
Cost of Sales	39,084	40,836
Casualty loss	2,025	-
Insurance recovery	(1,525)	-
Total Cost of Sales	39,584	40,836
Gross Profit	11,769	11,227
Selling and administrative expenses	10,063	11,181
Asset impairment charge	-	673
Operating income (loss)	1,706	(627)
Other (expense) income, net	12	(3)
Income (loss) before income taxes	1,718	(630)
Income tax expense (benefit)	644	(174)
Net income (loss)	$1,074	$(456)
Earnings (loss) per share		
Basic	$0.10	$(0.04)
Diluted	$0.10	$(0.04)
Weighted average shares outstanding:		
Basic	10,757	10,752
Diluted	10,767	10,757
Cash dividends declared per share	$0.10	$0.10

The accompanying notes are an integral part of the unaudited condensed consolidated financial statements.

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HOOKER FURNITURE CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)
(Unaudited)

	Thirteen Weeks Ended	
	May 2, 2010	May 3, 2009
Cash flows from operating activities		
Cash received from customers	$52,427	$56,838
Cash paid to suppliers and employees	(50,378)	(39,872)
Insurance procceds received on casualty loss	500	-
Income taxes paid, net	(227)	(156)
Interest (paid), net	(45)	(128)
Net cash provided by operating activities	$2,277	$16,682
Cash flows from investing activities		
Purchase of property, plant, and equipment	(198)	(602)
Proceeds from the sale of property and equipment	5	9
Premiums paid on officers' life insurance	(255)	(280)
Proceeds received on officers' life insurance	-	374
Net cash used in investing activities	(448)	(499)
Cash flows from financing activities		
Cash dividends paid	(1,077)	(1,077)
Payments on long-term debt	-	(705)
Net cash used in financing activities	(1,077)	(1,782)
Net increase in cash and cash equivalents	$752	$14,401
Cash and cash equivalents at the beginning of the period	37,995	11,804
Cash and cash equivalents at the end of the period	$38,747	$26,205
Reconciliation of net income to net cash provided by operating activities:		
Net income (loss)	$1,074	$(456)
Depreciation and amortization	748	730
Non-cash restricted stock awards and performance grants	15	20
Asset impairment charges	-	673
Provision for doubtful accounts	(329)	183
Deferred income taxes	(159)	(141)
Changes in assets and liabilities:		
Trade accounts receivable	1,835	4,521
Inventories	(2,365)	13,109
Prepaid expenses and other current assets	(30)	(83)
Trade accounts payable	279	(1,780)
Accrued salaries, wages, and benefits	381	64
Accrued income taxes	576	-
Other accrued expenses	59	(382)
Deferred compensation	193	192
Other long-term liabilities	-	32

Net cash provided by operating activties	$2,277	$16,682

The accompanying notes are an integral part of the unaudited condensed consolidated financial statements.

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HOOKER FURNITURE CORPORATION AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Dollar and share amounts in tables, except per share amounts, in thousands unless otherwise indicated)
(Unaudited)
For the Thirteen Weeks Ended May 2, 2010

1. Preparation of Interim Financial Statements

The condensed consolidated financial statements of Hooker Furniture Corporation and subsidiaries (referred to as "we," "us," "our," "Hooker" or the "Company") have been prepared in accordance with the rules and regulations of the Securities and Exchange Commission ("SEC"). In the opinion of management, these statements include all adjustments necessary for a fair statement of the results of all interim periods reported herein. All such adjustments are of a normal recurring nature. Certain information and footnote disclosures prepared in accordance with U.S. generally accepted accounting principles ("GAAP") are condensed or omitted pursuant to SEC rules and regulations. However, we believe that the disclosures made are adequate for a fair presentation of our results of operations and financial position. Operating results for the interim periods reported herein may not be indicative of the results expected for the year. These financial statements should be read in conjunction with the audited consolidated financial statements and accompanying notes included in our annual report on Form 10-K for the fiscal year ended January 31, 2010.

The preparation of financial statements in conformity with GAAP requires us to make estimates and assumptions that affect both the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from our estimates.

The financial statements contained herein are being filed as part of a quarterly report on Form 10-Q covering the thirteen-week period (also referred to as "three months," "three-month period," "quarter" or "quarterly period") that began February 1, 2010 and ended on May 2, 2010. These financial statements also include the thirteen-week period that began February 2, 2009 and ended on May 3, 2009.

References in these notes to the condensed consolidated financial statements of the Company to:

§ the 2011 fiscal year and comparable terminology mean the fiscal year that began February 1, 2010 and will end January 30, 2011; and

§ the 2010 fiscal year and comparable terminology mean the fiscal year that began February 2, 2009 and ended January 31, 2010.

2. Inventories

	May 2, 2010	January 31, 2010
Finished furniture	$ 42,060	$ 40,205
Furniture in process	864	798
Materials and supplies	7,866	7,258
Inventories at FIFO	50,790	48,261
Reduction to LIFO basis	12,249	12,085
Inventories	$ 38,541	$ 36,176

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3. Property, Plant and Equipment

	May 2, 2010	January 31, 2010
Buildings and land improvements	$ 23,814	$ 23,708
Machinery and equipment	3,553	3,507
Furniture and fixtures	27,608	27,494
Other	4,104	4,043
Total depreciable property at cost	59,079	58,752
Less accumulated depreciation	38,346	37,603
Total depreciable property, net	20,733	21,149
Land	1,357	1,357
Construction in progress	108	241
Property, plant and equipment, net	$ 22,198	$ 22,747

4. Intangible Assets

	May 2, 2010	January 31, 2010
Non-amortizable Intangible Assets		
Trademarks and trade names - Bradington-Young	$ 2,676	$ 2,676
Trademarks and trade names - Sam Moore	396	396
Trademarks and trade names - Opus Designs	396	396
Total trademarks and tradenames	3,468	3,468

5. Accounts Receivable

	May 2, 2010	January 31, 2010
Trade accounts receivable	$ 16,917	$ 19,400
Receivable from factor	9,030	8,432

Allowance for doubtful accounts	(1,559)	(1,938)
Accounts receivable	$ 24,388	$ 25,894

“Receivable from factor” represents amounts due with respect to factored accounts receivable. We factor substantially all of our upholstery division accounts receivable without recourse to us.

Under our factoring agreement entered into on July 15, 2009, invoices for upholstery products are generated and transmitted to our customers, with copies to the factor on a daily basis, as products are shipped to our upholstery customers. The factor collects the amounts due and remits collected funds to us semi-weekly. We retain ownership of the accounts receivable until the invoices are 90 days past due. At that time, the factor pays us the net invoice amount, less factoring fees and takes ownership of the accounts receivable. The factor is then entitled to collect the invoices on its own behalf and retain any subsequent remittances. The invoiced amounts are reported as accounts receivable on our condensed consolidated balance sheets when the merchandise is delivered to our customer until payment is received from the factor.

A limited number of accounts receivable are factored with recourse to us. The amounts of these receivables at May 2, 2010 and January 31, 2010 were $117,000 and $205,000, respectively. If the factor is unable to collect the amounts due, invoices are returned to us for collection. We include an estimate for these potentially uncollectible receivables in our calculation of our allowance for doubtful accounts.

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6. Other Comprehensive Income

	Thirteen Weeks Ended May 2, 2010	Thirteen Weeks Ended May 3, 2009
Net income	$ 1,074	$ (456)
Loss on interest rate swap	-	(19)
Portion of swap agreement's fair value reclassified to interest expense	-	62
Unrealized gain on interest rate swap	-	43
Portion of accumulated acturial gain on Supplemental Retirement Income Plan reclassified to deferred compensation expense	(59)	(55)
Other comprehensive loss before tax	(59)	(12)
Income tax benefit	22	4
Other comprehensive loss, net of tax	(37)	(8)
Comprehensive net income (loss)	$ 1,037	$ (464)

7. Supplier Receivable

From May 2007 through September 2009, we advanced payments to, and provided financing guarantees for one of our finished goods suppliers to facilitate the supplier’s purchase of raw materials and supplies to ensure timely delivery of finished goods to us. The balance of the advances and other miscellaneous amounts due from this supplier at May 2, 2010 and January 31, 2010 were $132,000 and $124,000, respectively, and are fully reserved. In order for the supplier to obtain additional bank financing, we issued a standby letter of credit on July 14, 2008 as security in the amount of $600,000. In conjunction with the issuance of the letter of credit, we entered into a security agreement with the supplier and the supplier’s shareholders, which provided us with a security interest in certain assets of the supplier and its shareholders. During September 2009, prior to the expiration of the letter of credit, the supplier ceased operations, and defaulted on its bank notes, and its lender drew on our $600,000 letter of credit. Subsequently, we reimbursed our letter of credit provider for the $600,000. During fiscal year 2010 we wrote down the pledged collateral to our estimate of its net realizable value of $300,000. The estimated net realizable amount for the pledged collateral of $300,000 at May 2, 2010 and January 31, 2010 is recorded in the long-term section of our condensed consolidated balance sheets in “Other assets.” Based on a recent appraisal, we believe that the net realizable value of $300,000 is reasonable and approximates the pledged collateral’s fair value. We are currently working with the supplier and its shareholders to have the pledged collateral conveyed to us and plan to offer the property for sale.

8. Earnings Per Share

Since 2006, we have issued restricted stock awards to non-employee members of the board of directors under the Stock Plan each January, and expect to continue to grant these awards to non-employee board members in the future. As of May 2, 2010 and January 31, 2010 there were 17,640 shares of restricted stock outstanding, net of forfeitures and vested shares on each date. Restricted shares awarded that have not yet vested are considered when computing diluted earnings per share.

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The following table sets forth the computation of basic and diluted earnings per share:

	Thirteen Weeks Ended May 2, 2010	Thirteen Weeks Ended May 3, 2009
Net income	$ 1,074	$ (456)
Less: Unvested participating restricted stock dividends	2	-
Net earnings allocated to unvested participating restricted stock	1	-
Earnings available for common shareholders	1,071	(456)
Weighted average shares outstanding for basic earnings per share	10,757	10,752
Dilutive effect of non-vested restricted stock awards	10	5
Weighted average shares outstanding for diluted earnings per share	10,767	10,757
Basic earnings (loss) per share	$ 0.10	$ (0.04)
Diluted earnings (loss) per share	$ 0.10	$ (0.04)

9. Long Term Debt and Interest Rate Swaps

As of May 2, 2010, we had an aggregate $13.1 million available under our revolving credit facility to fund working capital needs. Standby letters of credit in the aggregate amount of $1.9 million, used to collateralize certain insurance arrangements and for imported product purchases, were outstanding under our revolving credit facility as of May 2, 2010. There were no additional borrowings outstanding under the revolving credit line on May 2, 2010. Any principal outstanding under the credit line is due March 1, 2011.

From time to time we have entered into swap agreements to hedge against the potential impact of increases in interest rates on our floating-rate debt instruments. Swap agreements that hedge exposures to changes in interest rates expose us to credit risk and market risk. Credit risk is the potential failure of the counterparty to perform under the terms of the swap agreement. We attempt to minimize this risk by entering into transactions with high-quality counterparties. Market risk is the potential adverse effect on the value of the swap agreement that results from a decline in interest rates. The market risk associated with interest-rate contracts is managed by establishing and monitoring parameters that limit the types and degree of market risk that may be undertaken.

We are party to an interest rate swap agreement that provided, in effect, for a fixed interest rate of 4.1% through 2010 on our term loans. Prior to our fiscal 2010 third quarter, we accounted for our interest rate swap agreement as a cash flow hedge and recognized the fair value of the agreement on the balance sheet in shareholders' equity under the caption "accumulated other comprehensive income." The related gains or losses on this instrument were recorded through comprehensive income and, accordingly, were included in accumulated other comprehensive income on the balance sheet until recognized in net income. The gains or losses on this transaction were recognized in net income in the periods in which interest expense on our term notes (the related hedged item) were recognized in net income. In August 2009, we repaid our term loans in full. As a result, our interest rate swap no longer qualifies as an effective hedge. Through the remainder of the term of this interest rate swap, which terminates on September 1, 2010, all changes in the swap's fair value will be charged against net income except for scheduled payments under the agreement.

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As of May 2, 2010 we were party to one derivative financial instrument, as described in the following table:

Agreement	Notional Amount	Fixed Interest Rate	Expiration Date	Fair Value
Interest rate swap	$ 1,560	3.09 %	September 1, 2010	$ (17)

Fair Value Disclosure of Derivative Instruments

The following table provides quantitative fair value disclosures regarding our interest rate swap at May 2, 2010 and January 31, 2010:

		Fair Value at Dates Indicated		
	Carrying Value and Balance Sheet Location (Other Accrued Expenses)	Quoted Prices in Active Markets for Identical Instruments (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Interest rate swap at May 2, 2010	$(17)		$(17)	
Interest rate swap at January 31, 2010	(33)		(33)	

	Thirteen Weeks Ended	
	May 2, 2010	May 3, 2009
Interest rate swap:		
Loss recognized in other comprehensive income	$ -	$ (19)
Loss reclassified from accumulated other comprehensive income into interest expense, net	-	62

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10. Employee Benefit Plans

Components of net periodic benefit cost:

	Thirteen Weeks Ended	
	May 2, 2010	May 3, 2009
Net periodic benefit cost		
Service cost	$ 146	$ 158
Interest cost	85	89
Gain	(59)	(54)
Net periodic benefit cost	$ 172	$ 193

11. Casualty Loss

On March 10, 2010, we experienced a fire at one of our warehouse facilities in Martinsville, Va. The fire was contained to an area of approximately 2,000 square feet within a 580,000 square foot facility. The costs associated with the fire exceeded our insurance deductible of $500,000, but we expect that amounts in excess of our deductible will be fully covered by insurance. During the fiscal 2011 first quarter, we recorded a casualty loss of $2.0 million and an insurance recovery of $1.5 million, both in cost of sales. The net charge to cost of sales of $500,000 represents our insurance deductible. Additionally, we recorded a receivable of $1.0 million for amounts due to us from our insurance carrier. The receivable is recorded in the "Prepaid expenses and other current assets" line of the current assets portion of our condensed consolidated balance sheet. We also recorded a payable of $1.1 million for amounts due to vendors for our fire recovery and remediation efforts. The payable is recorded in the "trade accounts payable" line of the current liabilities portion of our condensed consolidated balance sheet.

12. Subsequent Events

We have evaluated events that occurred subsequent to May 2, 2010, through the financial statement issuance date and determined that there were no recordable or reportable subsequent events.

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

This quarterly report on Form 10-Q includes our unaudited condensed consolidated financial statements for the thirteen-week period (also referred to as "three months," "three-month period," "quarter" or "quarterly period") that began February 1, 2010 and ended on May 2, 2010. This report discusses our results of operations for this period compared to the fiscal year 2010 thirteen-week first quarter that began on February 2, 2009 and ended on May 3, 2009; and our financial condition as of January 31, 2010.

References in this report to:

§ the 2011 fiscal year and comparable terminology mean the fiscal year that began February 1, 2010 and will end January 30, 2011; and

§ the 2010 fiscal year and comparable terminology mean the fiscal year that began February 2, 2009 and ended January 31, 2010.

Nature of Operations

Incorporated in Virginia in 1924, Hooker Furniture Corporation ("Company", "we", "us", and "our") is ranked among the nation's top 10 largest publicly traded furniture sources, based on 2009 shipments to U.S. retailers, according to Furniture/Today, a leading trade publication. We are a key resource for residential wood, metal and upholstered furniture. Our major wood furniture product categories include home entertainment, home office, accent, dining, bedroom and bath furniture under the Hooker Furniture brand, and youth furniture sold under the Opus Designs by Hooker brand. Our residential upholstered seating companies include Cherryville, N.C.-based Bradington-Young, LLC, a specialist in upscale motion and stationary leather furniture, and Bedford, Va.-based Sam Moore Furniture LLC, a specialist in upscale occasional chairs with an emphasis on cover-to-frame customization. An extensive selection of designs and formats along with finish and cover options in each of these product categories makes us a comprehensive residential furniture resource, primarily for retailers targeting the medium and upper-medium price range. Our principal customers are retailers of residential home furnishings who are broadly dispersed throughout North America. Customers include independent furniture stores, specialty retailers, department stores, catalog merchants, interior designers and national and regional chains.

Overview

We have seen a growing consumer preference for lower-priced, high-quality imported furniture products since 2001. Led by the change in consumer demand, from 2003 to 2008 we systematically increased our focus on high-quality imported home furnishings with a coordinated exit from domestic wood furniture manufacturing. We closed our last domestic wood manufacturing plant during the fiscal year 2008 first quarter and completed the sale of all wood furniture manufacturing assets no longer needed in the business in December 2007. As a result, we have replaced a domestic operating model for wood furniture, which had high overhead and high fixed costs, with a low overhead, variable cost import model. We are now focused on imported wood and metal furniture, as well as both domestically produced and imported upholstered home furnishings. Maintaining domestic upholstered furniture manufacturing allows us to offer quick turnaround on orders for custom leather and fabric upholstered seating and remains an important part of our strategy.

Since the fall of 2006, our business has been impacted by low levels of consumer confidence and a weakening housing market. By late 2008, this malaise, exacerbated by weak credit markets, had spread to the broader U.S. economy. As a result, the residential home furnishings industry has seen an unprecedented decline in demand for its products. Discretionary purchases of furniture, particularly at the middle and upper-middle price points where we compete, have been highly affected by low consumer confidence. Current economic factors, such as high unemployment and difficult housing and mortgage markets, have resulted in a weak retail environment. We believe, however, that our business model continues to provide us with flexibility to respond to changing market conditions by adjusting inventory purchases from suppliers.

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Due to the prolonged downturn and weak demand for residential furniture products as a result of the recession, our Asian sourcing partners realigned production in their plants by closing production lines, laying off employees and making other changes in order to balance production with decreased demand. The shipping lines that we utilize to transport these sourced goods to us have likewise adjusted their capacity by temporarily taking portions of their fleets out of service, which has lengthened the time it takes to get our products to our distribution facilities in the U.S. As our incoming order rates have increased, our order backlog has increased substantially due to these issues. At May 2, 2010 our order backlog stood at 8.2 weeks of sales as compared to 4.6 weeks at May 3, 2009. We are working with our sourcing and transportation partners to alleviate these backlog issues, as well as working to secure new sources in these areas. As Asian manufacturing and transportation capacity increases due to increased demand, we believe that these backlog issues will begin to improve. However, we are likely to experience continued backlog issues in the short to medium term, which will in-turn negatively affect our revenues and margins.

Year-over-year declines in net sales continued through the fiscal year 2011 first quarter. However, fiscal year 2011 first quarter sales decreased by only 1.4% compared to the fiscal year 2010 first quarter, which is the lowest year-over year sales decrease in eleven fiscal quarters and continues a trend that began with the fiscal 2010 fourth quarter’s 6.7% year-over-year decrease, which, at that time, was the lowest decrease in ten fiscal quarters. While overall wood and metal furniture sales decreased, we realized significant increases in upholstery sales over the prior year quarter and over the fiscal 2010 fourth quarter. This increase in upholstery sales mirrors current furniture industry trends. Generally, past furniture industry recoveries were first marked by increased upholstery sales. While the uniqueness of the present economic situation and unpredictable nature of consumer behavior may complicate our industry’s recovery, we are very encouraged by these sales increases both at Hooker and for the industry at large.

The following are the principal factors that impacted our results of operations during the three month period ended May 2, 2010:

§ Net sales declined by $710,000, or 1.4%, to $51.4 million during the fiscal year 2011 first quarter compared to net sales of $52.1 million during the fiscal year 2010 first quarter. This decline reflects the continued year-over-year declines in case goods incoming order rates experienced since the fiscal 2006 third quarter, resulting from the industry-wide slowdown in business at retail and, more recently, delays in obtaining some of our sourced product (as discussed above.) However, the case goods order rate decrease was partially offset by significantly increased upholstery order rates in the current quarter. Additionally, case goods order rates appear to be stabilizing as decreases in the fiscal 2011 first quarter are significantly lower than the comparable prior year fiscal quarter and are lower than the fiscal year 2010 fourth quarter decrease.

§ Gross margins for the fiscal 2011 first quarter improved primarily due to

o lower freight costs as a percentage of sales for wood and metal furniture and
o slightly increased margins at our upholstery division primarily due to increased upholstery sales.

These improvements were partially offset by a $500,000 net charge ($312,000 or $0.03 per share, after tax) to cost of sales to recognize our insurance deductible for a fire that occurred at one of our distribution facilities during the fiscal 2011 first quarter.

§ Selling and administrative expenses decreased in both absolute terms and as a percentage of sales compared to the corresponding fiscal year 2010 period, primarily as a result of cost cutting measures implemented during fiscal 2010 and lower selling expenses due to lower commissions.

§ Operating income for the fiscal year 2011 first quarter was $1.7 million, or 3.3% of net sales, compared to an operating loss of $627,000, or -1.2% of net sales, in the fiscal year 2010 first quarter. This improvement was principally due to lower fixed operating and domestic upholstery overhead costs as a percent of net sales and the lack of asset impairment activity during the fiscal year 2011 first quarter as compared to the corresponding prior year quarter, partially offset by expenses related to the fire at our distribution center.

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Results of Operations

The following table sets forth the percentage relationship to net sales of certain items included in the condensed consolidated statements of operations included in this report.

	Thirteen Weeks Ended	
	May 2, 2010	May 3, 2009
Net sales	100.0 %	100.0 %
Cost of sales	76.1	78.4
Casualty loss	3.9	-
Insurance recovery	(2.9)	-
Total cost of sales	77.1	78.4
Gross profit	22.9	21.6
Selling and administrative expenses	19.6	21.5
Restructuring and asset impairment (credit) charge	-	1.3
Operating income (loss)	3.3	(1.2)
Income before income taxes	3.3	(1.2)
Income tax expense	1.2	(0.3)
Net income (loss)	2.1	(0.9)

Fiscal 2011 First Quarter Compared to Fiscal 2010 First Quarter

Net sales for the fiscal year 2011 first quarter declined $710,000, or 1.4% to $51.4 million compared to $52.1 million for the fiscal 2010 first quarter. This decline was principally due to lower overall selling prices, due to the mix of products sold, partially offset by slightly higher overall unit volume.

Unit volume decreased for our wood and metal furniture compared to the fiscal 2010 first quarter. Unit volume increased for Bradington-Young domestic and imported leather upholstery and Sam Moore domestic and imported upholstered furniture. Total sales of imported upholstery increased approximately 50.0% from the prior year quarter, while overall domestic upholstery sales increased approximately 23.0% in the same period.

Overall, average selling prices decreased in the low single digits during the fiscal year 2011 first quarter compared to the fiscal year 2010 first quarter, primarily due to increased sales of lower-priced products. Wood and metal furniture average selling prices decreased slightly as a result of a higher proportion of lower-priced Envision furniture sold. Selling prices of imported leather upholstery declined slightly due to the mix of products shipped. The average selling prices for domestic leather upholstered furniture decreased modestly, also due to the mix of products shipped. The average selling prices for imported upholstered furniture decreased significantly due to the mix of products shipped, while the average selling price for our domestically produced upholstered furniture decreased only slightly.

Overall, gross profit margin increased to 22.9% of net sales in the fiscal year 2011 first quarter compared to 21.6% in the fiscal year 2010 first quarter, mainly as a result of lower freight costs for wood and metal furniture. Gross margins for wood and metal furniture improved significantly in the fiscal year 2011 first quarter compared to the fiscal 2010 first quarter, primarily due to decreased levels of product discounting and returns and allowances and the exit from our California warehouse during fiscal 2010. Offsetting these improvements was a net charge to cost of sales for

$500,000, which represents our insurance deductible for the casualty loss related to the distribution center fire. Margins for upholstered furniture improved moderately due to lower fixed costs as a percentage of sales resulting from higher sales and cost reduction efforts partially offset by higher raw material and manufacturing costs due to product mix and inefficiencies from increased production rates.

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Selling and administrative expenses decreased to $10.1 million or 19.6% of net sales for the fiscal year 2011 first quarter, compared to $11.2 million or 21.5% of net sales for the fiscal year 2010 first quarter. The decrease in spending was principally due to the impact of cost reductions implemented in fiscal year 2010, undertaken in response to lower sales volume, as well as lower bad debt expense during the fiscal 2011 quarter.

Operating profitability for the fiscal 2011 first quarter increased year over year compared to the fiscal 2010 first quarter, primarily as a result of higher gross profit margins, the absence of any impairment charges in fiscal 2011 and lower fixed costs as a percentage of sales due to higher sales volumes at our upholstery companies. During the fiscal 2010 first quarter, we determined that our Bradington-Young trade name was impaired and recorded an intangible asset impairment charge of $673,000 ($419,000 or $0.04 per share, after tax.) The following table reconciles operating income as a percentage of net sales ("operating margin") to operating margin excluding this intangible asset impairment charge as a percentage of net sales for each period:

	Thirteen Weeks Ended			
	May 2, 2010		May 3, 2009	
Operating margin, including asset impairment charge	3.3	%	-1.2	%
Intangible asset impairment charge	0.0	%	1.3	%
Operating margin, excluding asset impairment charge	3.3	%	0.1	%

The operating margin excluding the impact of the asset impairment charge is a “non-GAAP” financial measure. We have provided this information because we believe it is useful to investors in evaluating our ongoing operations. Non-GAAP financial measures are intended to provide insight into selected financial information and should be evaluated in the context in which they are presented. These measures are of limited usefulness in evaluating our overall financial results presented in accordance with GAAP and should be considered in conjunction with the condensed consolidated financial statements, including the related notes, included elsewhere in this report.

As a result, we realized operating income for the fiscal year 2011 first quarter of $1.7 million, or 3.3% of net sales, compared to operating loss of $627,000, or 1.2% of net sales, in the fiscal year 2010 first quarter.

We recorded income tax expense of $644,000 for the fiscal 2011 first quarter and an income tax benefit of $174,000 for the fiscal year 2010 first quarter. Our effective tax rate increased to 37.5% for the fiscal year 2011 first quarter from 27.7% for the fiscal year 2010 first quarter, primarily due to the expectation that annual pre-tax income for FY 2011 will exceed annual pre-tax income experienced in FY 2010. This increase in pre-tax income reduces the relative benefit received from favorable net permanent differences which have been comparatively stable amounts from year to year. The current rate of 37.5% approximates our expected long-term effective tax rate.

Fiscal year 2011 first quarter net income was $1.1 million, or $0.10 per share, compared to a net loss of $456,000, or ($0.04) per share, in the fiscal year 2010 first quarter.

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Although we report operating results in one operating segment on a consolidated basis, we are providing the following information because we believe it helps supplement the detail provided:

	Thirteen Weeks Ended			
	May 2, 2010		May 3, 2009	
		% Segment Net Sales		% Segment Net Sales
Net Sales				
Case Goods	$ 32.6		$ 37.2	
Upholstery	18.8		14.9	
Total	51.4		52.1	
Gross Margin				
Case Goods	9.4	28.8 %	9.6	25.9 %
Upholstery	2.4	12.6 %	1.6	10.8 %
Total	11.8	22.9 %	11.2	21.6 %
Operating Margin				
Case Goods	2.7	8.4 %	1.6	4.4 %
Upholstery	(1.0)	-5.5 %	(2.3)	-15.3 %
Total	1.7	3.3 %	(0.6)	-1.2 %

Outlook

The year-over-year declines in quarterly incoming orders, which began in the Fall of 2006, continued during the fiscal year 2011 first quarter. While business has improved somewhat since the end of fiscal 2010, we believe that additional growth may be slow, irregular, and easily derailed. Our outlook for the remainder of fiscal year 2011 is one of continued cautious optimism. While we expect general retail conditions to remain weak, we have seen signs of improving consumer demand. However, continuing economic uncertainty, difficulty obtaining or shipping imported products and aggressive competition for consumer discretionary dollars could derail our recovery. We believe that our product and business model uniquely position us to take advantage of any upturn in the economy. That optimism, however, is tempered by the uniqueness of the present economic situation and our foreign supply chain challenges. Continued attention to cost control and an intense focus on improving sourced product availability continue to be priorities.

Our new Envision product line, which was designed to address the needs of Gen X and Gen Y consumers, was introduced in October 2008 and debuted on retail sales floors during the fiscal 2010 first quarter. While response to this new line has been encouraging, we have not yet seen an overall rebound in big-ticket consumer products such as furniture, so we remain cautious in our planning and continue to take actions to address challenges to our profitability. Some of those actions include:

- deferring, reducing or eliminating certain spending plans;
- continuing to refine the management of our supply chain, warehousing and distribution operations; and
- adjusting our inventory levels to reflect current business conditions.

Our domestic upholstery manufacturing operations have been particularly impacted by the prolonged sales downturn due to higher fixed overhead costs as a percentage of reduced net sales. To mitigate the impact of these sales declines we are: