FLEXSTEEL INDUSTRIES INC
Form 10-Q
April 21, 2011

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D. C. 20549

# FORM 10-Q

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

For the quarterly period ended March 31, 2011

or

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

For the transition period from to

Commission file number **0-5151**

# FLEXSTEEL INDUSTRIES, INC.

(Exact Name of Registrant as Specified in Its Charter)

| | |
|---|---|
| Incorporated in State of Minnesota | 42-0442319 |
| (State or other Jurisdiction of Incorporation or Organization) | (I.R.S. Identification No.) |

3400 JACKSON STREET
DUBUQUE, IOWA 52004-0877
(Address of Principal Executive Offices) (Zip Code)

(563) 556-7730
(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 o.

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 (§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 o. No o.

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 definition of large accelerated filer , accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act (check one).

Large accelerated filer o Accelerated filer o Non-accelerated filer o Smaller reporting company x

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

| | |
|---|---|
| Common Stock - $1.00 Par Value<br>Shares Outstanding as of March 31, 2011 | 6,710,112 |

PART I FINANCIAL INFORMATION

Item 1. Financial Statements

FLEXSTEEL INDUSTRIES, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
(Amounts in thousands, except share data)

| | March 31, 2011 (UNAUDITED) | June 30, 2010 |
|---|---|---|
| ASSETS | | |
| CURRENT ASSETS: | | |
| Cash | $ 12,201 | $ 8,278 |
| Trade receivables less allowance for doubtful accounts: | | |
| March 31, 2011, $2,200; June 30, 2010, $2,020 | 35,612 | 35,748 |
| Inventories | 74,737 | 72,637 |
| Deferred income taxes | 3,850 | 4,050 |
| Other | 1,470 | 1,076 |
| Total current assets | 127,870 | 121,789 |
| NON-CURRENT ASSETS: | | |
| Property, plant and equipment, net | 20,453 | 21,614 |
| Deferred income taxes | 3,800 | 3,010 |
| Other | 12,067 | 11,257 |
| TOTAL | $ 164,190 | $ 157,670 |
| LIABILITIES AND SHAREHOLDERS EQUITY | | |
| CURRENT LIABILITIES: | | |
| Accounts payable trade | $ 10,778 | $ 10,815 |
| Accrued liabilities: | | |
| Payroll and related items | 7,116 | 7,023 |
| Insurance | 6,752 | 6,192 |
| Other | 5,507 | 6,959 |
| Total current liabilities | 30,153 | 30,989 |
| LONG-TERM LIABILITIES: | | |
| Deferred compensation | 5,167 | 5,096 |
| Other | 4,318 | 3,973 |
| Total liabilities | 39,638 | 40,058 |
| SHAREHOLDERS EQUITY: | | |
| Cumulative preferred stock $50 par value; authorized 60,000 shares; outstanding none | | |
| Undesignated (subordinated) stock $1 par value; authorized 700,000 shares; outstanding none | | |
| Common stock $1 par value; authorized 15,000,000 shares; outstanding March 31, 2011, 6,710,112 shares; outstanding June 30, 2010, 6,645,532 shares | 6,710 | 6,646 |
| Additional paid-in capital | 6,522 | 5,425 |
| Retained earnings | 112,715 | 107,293 |
| Accumulated other comprehensive loss | (1,395) | (1,752) |
| Total shareholders equity | 124,552 | 117,612 |
| TOTAL | $ 164,190 | $ 157,670 |

See accompanying Notes to Consolidated Financial Statements (Unaudited).

FLEXSTEEL INDUSTRIES, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME (UNAUDITED)
(Amounts in thousands, except per share data)

| | Three Months Ended March 31, | | Nine Months Ended March 31, | |
|---|---|---|---|---|
| | 2011 | 2010 | 2011 | 2010 |
| NET SALES | $ 85,175 | $ 81,451 | $ 255,226 | $ 240,916 |
| COST OF GOODS SOLD | (66,968) | (63,418) | (198,589) | (186,286) |
| GROSS MARGIN | 18,207 | 18,033 | 56,637 | 54,630 |
| SELLING, GENERAL AND ADMINISTRATIVE | (14,561) | (14,122) | (44,966) | (43,526) |
| FACILITY CLOSING COSTS | | | (1,016) | |
| OPERATING INCOME | 3,646 | 3,911 | 10,655 | 11,104 |
| OTHER INCOME (EXPENSE): | | | | |
| Interest and other income | 129 | 115 | 244 | 238 |
| Interest expense | | (206) | | (439) |
| Total | 129 | (91) | 244 | (201) |
| INCOME BEFORE INCOME TAXES | 3,775 | 3,820 | 10,899 | 10,903 |
| PROVISION FOR INCOME TAXES | (1,320) | (1,500) | (3,970) | (4,240) |
| NET INCOME | $ 2,455 | $ 2,320 | $ 6,929 | $ 6,663 |
| | | | | |
| WEIGHTED AVERAGE NUMBER OF COMMON SHARES OUTSTANDING: | | | | |
| Basic | 6,710 | 6,622 | 6,687 | 6,596 |
| Diluted | 6,968 | 6,739 | 6,910 | 6,666 |
| | | | | |
| EARNINGS PER SHARE OF COMMON STOCK: | | | | |
| Basic | $ 0.37 | $ 0.35 | $ 1.04 | $ 1.01 |
| Diluted | $ 0.35 | $ 0.34 | $ 1.00 | $ 1.00 |
| | | | | |
| DIVIDENDS DECLARED PER COMMON SHARE | $ 0.075 | $ 0.05 | $ 0.225 | $ 0.15 |

See accompanying Notes to Consolidated Financial Statements (Unaudited).

FLEXSTEEL INDUSTRIES, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)
(Amounts in thousands)

| | Nine Months Ended March 31, 2011 | Nine Months Ended March 31, 2010 |
|---|---|---|
| OPERATING ACTIVITIES: | | |
| Net income | $ 6,929 | $ 6,663 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Depreciation | 2,028 | 2,261 |
| Provision for losses on accounts receivable | 890 | 789 |
| Deferred income taxes | (809) | (1,009) |
| Stock-based compensation expense | 844 | 681 |
| Gain on disposition of capital assets | (108) | (15) |
| Changes in operating assets and liabilities: | | |
| Trade receivables | (754) | (2,677) |
| Inventories | (2,100) | 6,196 |
| Other current assets | (394) | 1,880 |
| Other assets | (5) | 226 |
| Accounts payable trade | 52 | (310) |
| Accrued liabilities | (970) | 3,609 |
| Other long-term liabilities | 345 | 951 |
| Deferred compensation | 71 | (10) |
| Net cash provided by operating activities | 6,019 | 19,235 |
| INVESTING ACTIVITIES: | | |
| Proceeds from sales of investments | 307 | 301 |
| Purchases of investments | (537) | (584) |
| Proceeds from sale of capital assets | 143 | 20 |
| Capital expenditures | (991) | (1,175) |
| Net cash used in investing activities | (1,078) | (1,438) |
| FINANCING ACTIVITIES: | | |
| Repayment of short-term borrowings, net | | (10,000) |
| Dividends paid | (1,336) | (988) |
| Proceeds from the exercise of stock options | 318 | 292 |
| Net cash used in financing activities | (1,018) | (10,696) |
| Increase in cash | 3,923 | 7,101 |
| Cash at beginning of period | 8,278 | 1,714 |
| Cash at end of period | $ 12,201 | $ 8,815 |

SUPPLEMENTAL CASH FLOW INFORMATION Cash paid during the period for:
(Amounts in thousands)

| | Nine Months Ended March 31, 2011 | Nine Months Ended March 31, 2010 |
|---|---|---|
| Interest | $ | $ 439 |
| Income taxes paid, net | $ 6,039 | $ 1,890 |

See accompanying Notes to Consolidated Financial Statements (Unaudited).

FLEXSTEEL INDUSTRIES, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)
FOR THE PERIOD ENDED MARCH 31, 2011

1. The consolidated financial statements included herein have been prepared by Flexsteel Industries, Inc. and Subsidiaries (the Company or Flexsteel ), without audit, pursuant to the rules and regulations of the Securities and Exchange Commission ( SEC ). The information furnished in the consolidated financial statements includes normal recurring adjustments and reflects all adjustments, which are, in the opinion of management, necessary for a fair presentation of such consolidated financial statements. Operating results for the three and nine-month periods ended March 31, 2011 are not necessarily indicative of the results that may be expected for the fiscal year ending June 30, 2011. Certain information and footnote disclosures normally included in the consolidated financial statements prepared in accordance with accounting principles generally accepted in the United States of America ( GAAP ) have been condensed or omitted pursuant to such rules and regulations, although the Company believes that the disclosures are adequate to make the information presented not misleading. Except to the extent updated or described below, the significant accounting policies set forth in Note 1 to the consolidated financial statements in the Company s Annual Report on Form 10-K for the year ended June 30, 2010, appropriately represent, in all material respects, the current status of accounting policies and are incorporated by reference.

DESCRIPTION OF BUSINESS Flexsteel was incorporated in 1929 and is one of the oldest and largest manufacturers, importers and marketers of residential and commercial upholstered and wooden furniture products in the country. Product offerings include a wide variety of upholstered and wood furniture such as sofas, loveseats, chairs, reclining and rocker-reclining chairs, swivel rockers, sofa beds, convertible bedding units, occasional tables, desks, dining tables and chairs and bedroom furniture. The Company s products are intended for use in home, office, hotel and other commercial applications. Featured as a basic component in most of the upholstered furniture is a unique steel drop-in seat spring from which our name Flexsteel is derived. The Company distributes its products throughout the United States through the Company s sales force and various independent representatives. The Company s products are also sold to several national and regional chains, some of which sell on a private label basis.

The Company has one active wholly-owned subsidiary, DMI Furniture, Inc. ( DMI ), which is a Louisville, Kentucky-based, manufacturer, importer and marketer of residential and commercial office furniture. DMI s divisions are WYNWOOD, Homestyles and DMI Commercial Office Furniture.

2. INVENTORIES

The Company values inventory at the lower of cost or market. Raw steel is valued on the last-in, first-out ( LIFO ) method. Other inventories are valued on the first-in, first-out ( FIFO ) method. Inventories valued on the LIFO method would have been approximately $1.9 million higher at March 31, 2011 and $1.7 million higher at June 30, 2010, if they had been valued on the FIFO method. At March 31, 2011 and June 30, 2010 the total value of LIFO inventory was $2.0 million and $2.3 million, respectively. A comparison of inventories is as follows (in thousands):

| | March 31, 2011 | June 30, 2010 |
|---|---|---|
| Raw materials | $ 8,141 | $ 9,696 |
| Work in process and finished parts | 4,638 | 4,943 |
| Finished goods | 61,958 | 57,998 |
| Total | $ 74,737 | $ 72,637 |

3. BORROWINGS AND CREDIT ARRANGEMENTS

The Company maintains a credit agreement which provides short-term working capital financing up to $15.0 million with interest of LIBOR plus 1% including $10.0 million of letters of credit availability. No amounts were outstanding at March 31, 2011 and June 30, 2010 under the working capital facility. The Company is contingently liable to insurance carriers under its comprehensive general, product, and vehicle liability policies, as well as some workers compensation, and has provided letters of credit in the amount of $3.0 million. The credit agreement contains financial covenants. The primary covenant is an interest coverage ratio of 3.0 to 1.0. The ratio is computed as net income plus interest expense and stock-based compensation expense less dividends divided by interest expense. In addition, the Company must maintain working capital of $60 million. At March 31, 2011, the Company was in compliance with all of the financial covenants contained in the credit agreement.

An officer of the Company is a director at a bank where the Company maintains an unsecured $5.0 million line of credit at prime minus 1%, but not less than 2.5%, and where its routine daily banking transactions are processed. No amount was outstanding on the line of credit at March 31, 2011 and June 30, 2010. In addition, the Rabbi Trust assets of $5.5 million are administered by this bank s trust department. The Company receives no special services or pricing on the services performed by the bank due to the directorship of this officer.

4. STOCK-BASED COMPENSATION

The Company has two stock-based compensation methods available when determining employee compensation.

(1) Long-Term Management Incentive Compensation Plan The plan provides for shares of common stock and cash to be awarded to officers and key employees based on performance targets set by the Nominating and Compensation Committee of the Board of Directors (the Committee ). The Company s shareholders approved 500,000 shares to be issued under the plan. No shares have been issued as of March 31, 2011. The Committee selected consolidated operating results for organic net sales growth and fully-diluted earnings per share for the three-year performance periods beginning July 1, 2008 and ending on June 30, 2011, beginning July 1, 2009 and ending on June 30, 2012, and beginning July 1, 2010 and ending on June 30, 2013. The Committee has also specified that payouts, if any, for awards earned in these performance periods will be 60% stock and 40% cash. Awards will be paid to participants as soon as practicable following the end of the performance periods and verification of results. The compensation cost related to the number of shares to be granted under each performance period is fixed on the grant date, which is the date the performance period begins. The compensation cost related to the cash portion of the award is re-measured based on the award s estimated fair value at the end of each reporting period. The accrual is based on the probable outcomes of the performance conditions. The portion of the accrued award payable in stock is classified within equity and the portion of the accrued award payable in cash is classified within payroll and related accruals and other long-term liabilities. At March 31, 2011 and June 30, 2010, the Company accrued $0.3 million and $0, respectively, in payroll and related accruals for the short-term portion of estimated awards of stock and cash under the long-term incentive plan. At March 31, 2011 and March 31, 2010, the Company has recorded expense of $1.0 million and $0.6 million, respectively, for estimated awards of stock and cash under the long-term incentive plan.

If the target performance goals would be achieved, the total amount of compensation cost recognized over the requisite service periods would be $0.9 million (2009-2011), $1.1 million (2010-2012) and $1.0 million (2011-2013) based on the estimated fair values at March 31, 2011.

(2) Stock Option Plans The stock option plans for key employees and directors provide for the granting of incentive and nonqualified stock options. Under the plans, options are granted at an exercise price equal to the fair market value of the underlying common stock at the date of grant, and may be exercisable for up to 10 years. All options are exercisable when granted.

At March 31, 2011, 0.4 million shares were available for future grants. It is the Company s policy to issue new shares upon exercise of stock options. The Company accepts shares of the Company s common stock as payment for the exercise price of options. These shares received as payment are retired upon receipt.

A summary of the status of the Company s stock option plans as of March 31, 2011, June 30, 2010 and 2009 and the changes during the periods then ended is presented below:

| | Shares (in thousands) | Weighted Average Exercise Price | Aggregate Intrinsic Value (in thousands) |
|---|---|---|---|
| Outstanding and exercisable at June 30, 2009 | 1,020 | $ 12.94 | $ 407 |
| Granted | 165 | 8.43 | |
| Exercised | (99) | 7.52 | |
| Canceled | (34) | 13.40 | |
| Outstanding and exercisable at June 30, 2010 | 1,052 | 12.70 | 1,168 |
| Granted | 88 | 17.23 | |
| Exercised | (91) | 7.40 | |
| Canceled | (3) | 10.89 | |
| Outstanding and exercisable at March 31, 2011 | 1,046 | $ 13.55 | $ 2,546 |

The following table summarizes information for options outstanding and exercisable at March 31, 2011:

| Range of Prices | | Options Outstanding (in thousands) | Weighted Average Remaining Life (Years) | Weighted Average Exercise Price |
|---|---|---|---|---|
| $ 6.81 | 10.75 | 254 | 8.2 | $ 7.71 |
| 12.35 | 12.74 | 230 | 6.2 | 12.51 |
| 14.40 | 16.52 | 353 | 3.6 | 15.54 |
| 17.23 | 20.27 | 209 | 5.6 | 18.46 |
| $ 6.81 | 20.27 | 1,046 | 5.7 | $ 13.55 |

5. INCOME TAXES

In determining the quarterly provision for income taxes, the Company uses an estimated annual effective tax rate, which is based on the expected annual income, statutory tax rates and tax planning opportunities available to the Company in the various jurisdictions in which it operates. This includes recognition of deferred tax assets and liabilities for the expected future tax consequences of events that have been included in the financial statements or tax returns to the extent pervasive evidence exists that they will be realized in future periods. The deferred tax balances are adjusted to reflect tax rates by tax jurisdiction, based on currently enacted tax laws, which are expected to be in effect in the years in which the temporary differences are expected to reverse. In accordance with the Company s income tax policy, significant or unusual items are separately recognized in the quarter in which they occur.

The components of the gross liabilities related to unrecognized tax benefits and the related deferred tax assets are as follows (in thousands):

| | March 31, 2011 | June 30, 2010 |
|---|---|---|
| Gross unrecognized tax benefits | $ 1,060 | $ 995 |
| Accrued interest and penalties | 260 | 215 |
| Gross liabilities related to unrecognized tax benefits | $ 1,320 | $ 1,210 |
| Deferred tax assets | $ 260 | $ 230 |

The recognition of the above amounts would impact the Company s effective tax rate. The Company does not expect that there will be any positions for which it is reasonably possible that the total amounts of unrecognized tax benefits will significantly increase or decrease within twelve months. The Company records interest and penalties related to income taxes as income tax expense in the Consolidated Statements of Income.

6. EARNINGS PER SHARE Basic earnings per share ( EPS ) is computed based upon the weighted-average number of common shares outstanding for each period. Diluted EPS is computed based on the weighted-average number of common shares and common equivalent shares. Common equivalent shares represent the effect of stock options during each period presented, which if exercised, would dilute EPS and the dilutive effect of long-term incentive compensation shares granted. In computing EPS for the three and nine months ended March 31, 2011 and 2010, net income as reported for each respective period is divided by (in thousands):

| | Three Months Ended March 31, 2011 | Three Months Ended March 31, 2010 | Nine Months Ended March 31, 2011 | Nine Months Ended March 31, 2010 |
|---|---|---|---|---|
| Basic shares outstanding | 6,710 | 6,622 | 6,687 | 6,596 |
| Dilutive effect of stock options | 162 | 117 | 142 | 70 |
| Dilutive effect of long-term incentive compensation shares granted | 96 | | 81 | |
| Diluted shares outstanding | 6,968 | 6,739 | 6,910 | 6,666 |
| | 424 | 724 | 424 | 724 |

| | |
|---|---|
| Stock options excluded from the calculation of diluted EPS because the option exercise price was greater than the average market price of the common shares or the net loss would cause the effect of the options to be anti-dilutive | |

7. COMPREHENSIVE INCOME

The components of comprehensive income, net of income taxes, for the three and nine months ended, were as follows (in thousands):

| | Three Months Ended March 31, | | Nine Months Ended March 31, | |
|---|---|---|---|---|
| | 2011 | 2010 | 2011 | 2010 |
| Net income | $ 2,455 | $ 2,320 | $ 6,929 | $ 6,663 |
| Other comprehensive income (OCI): | | | | |
| Change in fair value of derivatives, net of income taxes of $0, $(69), $0 and $(108), respectively | | 113 | | 177 |
| Change in fair value of available-for-sale securities, net of income taxes of $(31), $(58), $(218) and $(151), respectively | 51 | 95 | 357 | 247 |
| Total other comprehensive income | 51 | 208 | 357 | 424 |
| Total comprehensive income | $ 2,506 | $ 2,528 | $ 7,286 | $ 7,087 |

The components of accumulated other comprehensive loss, net of income tax, are as follows (in thousands):

| | March 31, 2011 | June 30, 2010 |
|---|---|---|
| Available-for-sale securities | $ 346 | $ (11) |
| Pension and other post-retirement benefit adjustments | (1,741) | (1,741) |
| Accumulated other comprehensive loss | $ (1,395) | $ (1,752) |

8. LITIGATION

From time to time, the Company is subject to various legal proceedings, including lawsuits, which arise out of, and are incidental to, the conduct of the Company s business. The Company does not consider any of such proceedings that are currently pending, individually or in the aggregate, to be material to its business or likely to result in a material adverse effect on its consolidated operating results, financial condition, or cash flows.

9. ACCOUNTING DEVELOPMENTS

No accounting pronouncements have been adopted or have become effective during the third quarter of fiscal 2011 that impact the Company.

10. FACILITY CLOSING COSTS

During the quarter ended September 30, 2010, the Company announced the planned closure of a manufacturing facility and recorded pre-tax charges for facility closing costs of $1.0 million. The charges represent employee separation costs of $0.6 million and other closing costs of $0.4 million with no future benefit to the Company and are classified as Facility Closing Costs in the Consolidated Statements of Income at March 31, 2011. At March 31, 2011, the closure is completed and $0.1 million remains to be paid and is included in other current liabilities.

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

GENERAL:

The following analysis of the results of operations and financial condition of the Company should be read in conjunction with the consolidated financial statements and related notes included elsewhere in this quarterly report on Form 10-Q.

CRITICAL ACCOUNTING POLICIES:

There have been no material changes to our critical accounting policies and estimates from the information provided in Item 7, Management s Discussion and Analysis of Financial Condition and Results of Operations , included in our 2010 annual report on Form 10-K.

Overview

The following table has been prepared as an aid in understanding the Company s results of operations on a comparative basis for the three and nine months ended March 31, 2011 and 2010. Amounts presented are percentages of the Company s net sales.

| | Three Months Ended March 31, | | Nine Months Ended March 31, | |
|---|---|---|---|---|
| | 2011 | 2010 | 2011 | 2010 |
| Net sales | 100.0% | 100.0% | 100% | 100.0% |
| Cost of goods sold | (78.6) | (77.9) | (77.8) | (77.3) |
| Gross margin | 21.4 | 22.1 | 22.2 | 22.7 |
| Selling, general and administrative | (17.1) | (17.3) | (17.6) | (18.1) |
| Facility consolidation and other costs | | | (0.4) | |
| Operating income | 4.3 | 4.8 | 4.2 | 4.6 |
| Other income (expense), net | 0.1 | (0.2) | 0.1 | (0.1) |
| Income before income taxes | 4.4 | 4.6 | 4.3 | 4.5 |
| Income tax expense | (1.5) | (1.8) | (1.6) | (1.8) |
| Net income | 2.9% | 2.8% | 2.7% | 2.7% |

Results of Operations for the Quarter Ended March 31, 2011 vs. 2010

The following table compares net sales in total and by area of application for the quarter ended March 31, 2011 to the prior year quarter.

| | Net Sales (in thousands) Quarter Ended March 31, | | $ Change | |
|---|---|---|---|---|
| Area of Application | 2011 | 2010 | (in thousands) | % Change |
| Residential | $ 64,938 | $ 61,516 | $ 3,422 | 5.6% |
| Commercial | 20,237 | 19,935 | 302 | 1.5 |
| Total | $ 85,175 | $ 81,451 | $ 3,724 | 4.6% |

Gross margin for the quarter ended March 31, 2011 was 21.4% compared to 22.1% in the prior year quarter reflecting the impact of increases in material costs.

Selling, general and administrative expenses were $14.6 million or 17.1% of net sales and $14.1 million or 17.3% of net sales for the quarters ended March 31, 2011 and 2010, respectively.

Operating income for the current quarter was $3.6 million compared to $3.9 million in the prior year quarter reflecting the aforementioned factors.

The effective income tax expense rate for the current fiscal quarter was 35.0% compared to a rate of 39.3% in the prior year fiscal quarter. This rate fluctuates due to projected income levels and the impact of various state taxing jurisdictions.

The above factors resulted in net income of $2.5 million or $0.35 per share, compared to the prior year quarter of $2.3 million or $0.34 per share.

All earnings per share amounts are on a diluted basis.

Results of Operations for the Nine Months Ended March 31, 2011 vs. 2010

The following table compares net sales in total and by area of application for the nine months ended March 31, 2011 to the prior year period.

| | Net Sales (in thousands) Nine Months Ended March 31, | | $ Change | |
|---|---|---|---|---|
| Area of Application | 2011 | 2010 | (in thousands) | % Change |
| Residential | $ 193,691 | $ 180,313 | $ 13,378 | 7.4% |
| Commercial | 61,535 | 60,603 | 932 | 1.5 |
| Total | $ 255,226 | $ 240,916 | $ 14,310 | 5.9% |

Gross margin for the nine months ended March 31, 2011 was 22.2% compared to 22.7% in the prior year period. Gross margin for the nine-month period was adversely impacted by inventory write-down of $0.6 million associated with the facility closing and increases in material costs.

Selling, general and administrative expenses were $45.0 million or 17.6% of net sales and $43.5 million or 18.1% of net sales for the nine months ended March 31, 2011 and 2010, respectively, reflecting better absorption of fixed costs.

The current nine-month period includes a pre-tax charge of approximately $1.0 million for employee separation and other costs related to finalizing the closing of a facility.

Operating income for the nine months ended March 31, 2011 was $10.7 million compared to $11.1 million in the prior year period reflecting the aforementioned factors**.**

The effective income tax expense rate for the current nine-month period ended was 36.4% compared to a rate of 38.9% in the prior year period. This rate fluctuates due to projected income levels and the impact of various state taxing jurisdictions.

The above factors resulted in nine months ended net income of $6.9 million or $1.00 per share, compared to the prior year of $6.7 million or $1.00 per share.

All earnings per share amounts are on a diluted basis.

Liquidity and Capital Resources

Operating Activities:

Working Capital (current assets less current liabilities) at March 31, 2011 was $97.7 million. Net cash provided by operating activities was $6.0 million during the nine months ended March 31, 2011. Net income of $6.9 million and depreciation of $2.0 million were offset by a $2.1 million increase in inventory and a $0.8 million increase in accounts receivable.

The Company expects that due to the nature of our operations that there will be continuing fluctuations in accounts receivable, inventory, accounts payable, and cash flows from operations due to the following: (i) we purchase inventory from overseas suppliers with long lead times and depending on the timing of the delivery of those orders, inventory levels can be greatly impacted, and (ii) we have various customers that purchase large quantities of inventory periodically and the timing of those purchases can significantly impact inventory levels, accounts receivable, accounts payable and short-term borrowings. As discussed below, the Company believes it has adequate financing arrangements and access to capital to absorb these fluctuations in operating cash flow.

Investing Activities:

Net cash used in investing activities was $1.1 million during the nine month period ended March 31, 2011 primarily related to $1.0 million for the purchase of capital assets. The Company expects that capital expenditures will be less than $2.0 million for the remainder of the fiscal year. On April 1, 2011, the Company announced plans to construct a $12 million, four-story, 40,000 square foot, corporate office building in Dubuque, Iowa, the majority of which will occur in fiscal year 2012.

Financing Activities:

Net cash used in financing activities was $1.0 million during the nine month period ended March 31, 2011. Dividends of $1.3 million were paid during the nine month period ended March 31, 2011 offset by $0.3 million of cash received from the exercise of stock options.

Management believes that the Company has adequate cash and credit arrangements to meet its operating and capital requirements for fiscal year 2011. In the opinion of management, the Company s liquidity and credit resources provide it with the ability to react to opportunities as they arise, to pay quarterly dividends to its shareholders, and to purchase capital assets that enhance safety and improve operations. The Company has begun the process of obtaining a renewal of its working capital line of credit that expires June 30, 2011. The Company believes that it will be able to successfully renew the terms of the current agreement prior to its expiration date.

Outlook

Our balance sheet remains strong reflecting working capital in excess of $97 million and no bank borrowings. We were able to realize gains in residential sales for the current year over the prior year. There are indications that improving job prospects and improving consumer sentiment are having a positive impact on residential sales even though the housing market remains weak. We expect to continue top-line growth of our residential products through fiscal year 2012. Our commercial product sales are up slightly for the current year over the prior year. The commercial office industry continues to report increases in sales over last year. While we have benefited minimally from those increases to date, we believe we will see increased sales volume during fiscal year 2012. Based on low demand for an extended period, we anticipate increased orders for hospitality products during fiscal year 2012 as the economy improves.

The Company continues to experience increases in the cost of certain raw materials, such as steel, polyester fiber, fabric and leather, and finished products. We are implementing price increases to help mitigate the impact of the increased material and finished product costs, however, we will continue to experience downward pressure on gross margin until we realize the full benefits of these sell price increases and see an end to the cost increases.

We remain committed to our core strategies, which include a wide range of quality product offerings and price points to the residential and commercial markets, combined with a conservative approach to business. We will maintain our focus on a strong balance sheet through emphasis on cash flow and improving profitability. We believe these core strategies are in the best interest of our shareholders.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

*General* Market risk represents the risk of changes in value of a financial instrument, derivative or non-derivative, caused by fluctuations in interest rates, foreign exchange rates and equity prices. As discussed below, management of the Company does not believe that changes in these factors could cause material fluctuations in the Company s results of operations or cash flows. The ability to import furniture products can be adversely affected by political issues in the countries where suppliers are located, disruptions associated with shipping distances and negotiations with port employees. Other risks related to furniture product importation include government imposition of regulations and/or quotas; duties and taxes on imports; and significant fluctuation in the value of the U. S. dollar against foreign currencies. Any of these factors could interrupt supply, increase costs and decrease earnings.

*Foreign Currency Risk* During the three and nine months ended March 31, 2011 and 2010, the Company did not have sales, purchases, or other expenses denominated in foreign currencies. As such, the Company is not exposed to material market risk associated with currency exchange rates and prices.

*Interest Rate Risk* The Company s primary market risk exposure with regard to financial instruments is changes in interest rates. At March 31, 2011, the Company had no debt outstanding.

*Tariffs* The Company has exposure to actions by governments, including tariffs. Tariffs are a possibility on any imported or exported products.

*Inflation* Increased operating costs are reflected in product or services pricing with any limitations on price increases determined by the marketplace. Inflation or other pricing pressures could impact raw material costs, labor costs and interest rates which are important components of costs for the Company and could have an adverse effect on our profitability, especially where increases in these costs exceed price increases on finished products.

Item 4. Controls and Procedures

(a) *Evaluation of disclosure controls and procedures.* Based on their evaluation as of the end of the period covered by this Quarterly Report on Form 10-Q, our chief executive officer and chief financial officer have concluded that our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended) were effective as of March 31, 2011.

(b) *Changes in internal control over financial reporting.* During the quarter ended March 31, 2011, there were no significant changes in our internal control over financial reporting (as defined in Rule 13a-15(f) under the Securities Exchange Act of 1934, as amended) that has materially affected, or is reasonably likely to materially affect the Company s internal control over financial reporting.

**Cautionary Statement Relevant to Forward-Looking Information for the Purpose of Safe Harbor Provisions of the Private Securities Litigation Reform Act of 1995**

The Company and its representatives may from time to time make written or oral forward-looking statements with respect to long-term goals or anticipated results of the Company, including statements contained in the Company s filings with the Securities and Exchange Commission and in its reports to stockholders.

Statements, including those in this Quarterly Report on Form 10-Q, which are not historical or current facts, are forward-looking statements made pursuant to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. There are certain important factors that could cause our results to differ materially from those anticipated by some of the statements made herein. Investors are cautioned that all forward-looking statements involve risk and uncertainty. Some of the factors that could affect results are the cyclical nature of the furniture industry, the effectiveness of new product introductions and distribution channels, the product mix of sales, pricing pressures, the cost of raw materials and fuel, foreign currency valuations, actions by governments including taxes and tariffs, inflation, the amount of sales generated and the profit margins thereon, competition (both foreign and domestic), changes in interest rates, credit exposure with customers and general economic conditions. For further information regarding these risks and uncertainties, see the Risk Factors section in Item 1A of the Company s Annual Report on Form 10-K for the fiscal year ended June 30, 2010.

The Company specifically declines to undertake any obligation to publicly revise any forward-looking statements that have been made to reflect events or circumstances after the date of such statements or to reflect the occurrence of anticipated or unanticipated events.

PART II OTHER INFORMATION

Item 1A. Risk Factors

There has been no material change in the risk factors set forth under Part 1, Item 1A Risk Factors in the Company s Annual Report on Form 10-K for the fiscal year ended June 30, 2010.

Item 6. Exhibits

31.1 Certification.

31.2 Certification.

32 Certification by Chief Executive Officer and Chief Financial Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

**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.

FLEXSTEEL INDUSTRIES, INC.

Date: April 21, 2011

By: */S/ Timothy E. Hall*
Timothy E. Hall
Chief Financial Officer
(Principal Financial & Accounting Officer)