

BASSETT FURNITURE INDUSTRIES INC

Form 10-Q

June 30, 2016

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 May 28, 2016

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. 0-209

BASSETT FURNITURE INDUSTRIES, INCORPORATED

(Exact name of Registrant as specified in its charter)

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Virginia

(State or other jurisdiction of incorporation or organization)

54-0135270

(I.R.S. Employer Identification No.)

3525 Fairystone Park Highway

Bassett, Virginia 24055

(Address of principal executive offices)

(Zip Code)

(276) 629-6000

(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, and (2) has been subject to such filing requirements for the past 90 days. Yes 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 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.

Large Accelerated Filer Accelerated Filer Non-accelerated Filer 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

At June 17, 2016, 10,904,934 shares of common stock of the Registrant were outstanding.

BASSETT FURNITURE INDUSTRIES, INCORPORATED AND SUBSIDIARIES

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(In thousands except per share data)

	Quarter Ended		Six Months Ended	
	May 28, 2016	May 30, 2015	May 28, 2016	May 30, 2015
Sales revenue:				
Furniture and accessories	\$92,990	\$99,467	\$185,392	\$189,015
Logistics	13,677	12,086	28,148	15,345
Total sales revenue	106,667	111,553	213,540	204,360
Cost of furniture and accessories sold	42,419	46,921	84,405	88,851
Selling, general and administrative expenses excluding new store pre-opening costs	58,088	57,425	117,045	104,900
New store pre-opening costs	307	44	446	44
Lease exit costs	-	-	-	419
Asset impairment charges	-	-	-	106
Management restructuring costs	-	449	-	449
Income from operations	5,853	6,714	11,644	9,591
Remeasurement gain on acquisition of affiliate	-	-	-	7,212
Income from Continued Dumping & Subsidy Offset Act	-	1,066	-	1,066
Other loss, net	(600)	(597)	(1,257)	(1,220)
Income before income taxes	5,253	7,183	10,387	16,649
Income tax expense	1,868	2,654	3,768	6,164
Net income	\$3,385	\$4,529	\$6,619	\$10,485
Retained earnings-beginning of period	123,176	111,474	120,904	106,339
Cash dividends	(998)	(854)	(1,960)	(1,675)
Retained earnings-end of period	\$125,563	\$115,149	\$125,563	\$115,149

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Basic earnings per share	\$0.31	\$0.42	\$0.61	\$0.99
Diluted earnings per share	\$0.31	\$0.42	\$0.61	\$0.98
Dividends per share	\$0.09	\$0.08	\$0.18	\$0.16

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

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PART I – FINANCIAL INFORMATION – CONTINUED

ITEM 1. FINANCIAL STATEMENTS

BASSETT FURNITURE INDUSTRIES, INCORPORATED AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

FOR THE PERIODS ENDED MAY 28, 2016 AND MAY 30, 2015 – UNAUDITED

(In thousands)

	Quarter Ended		Six Months Ended	
	May 28, 2016	May 30, 2015	May 28, 2016	May 30, 2015
Net income	\$3,385	\$4,529	\$6,619	\$10,485
Other comprehensive income (loss):				
Amortization associated with supplemental executive retirement defined benefit plan (SERP)	92	58	183	117
Income taxes related to SERP	(36)	(22)	(70)	(44)
Other comprehensive income, net of tax	56	36	113	73
Total comprehensive income	\$3,441	\$4,565	\$6,732	\$10,558

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

PART I – FINANCIAL INFORMATION – CONTINUEDITEM 1. FINANCIAL STATEMENTSBASSETT FURNITURE INDUSTRIES, INCORPORATED AND SUBSIDIARIESCONDENSED CONSOLIDATED BALANCE SHEETSMAY 28, 2016 AND NOVEMBER 28, 2015

(In thousands)

	(Unaudited)	
Assets	May 28, 2016	November 28, 2015
Current assets		
Cash and cash equivalents	\$ 29,726	\$ 36,268
Short-term investments	23,125	23,125
Accounts receivable, net	18,987	21,197
Inventories	54,834	59,896
Other current assets	8,249	6,798
Total current assets	134,921	147,284
Property and equipment, net	104,075	96,104
Deferred income taxes	12,205	13,471
Goodwill and other intangible assets	17,521	17,682
Other	7,525	8,002
Total long-term assets	37,251	39,155
Total assets	\$ 276,247	\$ 282,543
<u>Liabilities and Stockholders' Equity</u>		
Current liabilities		
Accounts payable	\$ 20,198	\$ 20,916
Accrued compensation and benefits	11,614	14,345
Customer deposits	20,132	23,999
Dividends payable	-	2,184
Current portion of long-term debt	6,438	5,273
Other accrued liabilities	10,907	13,133
Total current liabilities	69,289	79,850
Long-term liabilities		
Post employment benefit obligations	12,654	12,694
Notes payable	9,220	8,500
Other long-term liabilities	4,151	4,133
Total long-term liabilities	26,025	25,327

Stockholders' equity

Common stock	54,525		54,580	
Retained earnings	125,563		120,904	
Additional paid-in capital	3,409		4,560	
Accumulated other comprehensive loss	(2,564	)	(2,678)
Total stockholders' equity	180,933		177,366	
Total liabilities and stockholders' equity	\$ 276,247		\$ 282,543	

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

PART I – FINANCIAL INFORMATION – CONTINUEDITEM 1. FINANCIAL STATEMENTSBASSETT FURNITURE INDUSTRIES, INCORPORATED AND SUBSIDIARIESCONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWSFOR THE PERIODS ENDED MAY 28, 2016 AND MAY 30, 2015 – UNAUDITED

(In thousands)

	Six Months Ended	
	May 28,	May 30,
	2016	2015
Operating activities:		
Net income	\$6,619	\$10,485
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Depreciation and amortization	5,611	4,729
Equity in undistributed income of investments and unconsolidated affiliated companies	-	(220)
Provision for restructuring and asset impairment charges	-	106
Non-cash portion of lease exit costs	-	419
Remeasurement gain on acquisition of affiliate	-	(7,212)
Tenant improvement allowance received from lessors	590	330
Deferred income taxes	1,198	4,212
Excess tax benefits from stock-based compensation	41	1,032
Other, net	697	1,018
Changes in operating assets and liabilities:		
Accounts receivable	2,436	(1,490)
Inventories	5,062	(5,706)
Other current assets	(1,451)	(2,121)
Customer deposits	(3,867)	763
Accounts payable and accrued liabilities	(5,926)	3,882
Net cash provided by operating activities	11,010	10,227
Investing activities:		
Purchases of property and equipment	(14,116)	(7,942)
Proceeds from sales of property and equipment	577	2,952
Cash paid for business acquisition, net of cash acquired	-	(7,323)
Capital contribution to affiliate	-	(1,345)
Net cash used in investing activities	(13,539)	(13,658)
Financing activities:		
Cash dividends	(4,145)	(3,777)
Proceeds from the exercise of stock options	114	2,993
Other issuance of common stock	176	171

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Repurchases of common stock	(1,930)	(255)
Repayments of notes payable	(4,920)	(1,214)
Proceeds from equipment loans	6,692	1,307
Net cash used in financing activities	(4,013)	(775)
Change in cash and cash equivalents	(6,542)	(4,206)
Cash and cash equivalents - beginning of period	36,268	26,673
Cash and cash equivalents - end of period	\$29,726	\$22,467

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

PART I-FINANCIAL INFORMATION-CONTINUED

BASSETT FURNITURE INDUSTRIES, INCORPORATED AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS-UNAUDITED

MAY 28 2016

(Dollars in thousands except share and per share data)

1. Basis of Presentation

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with the instructions to Form 10-Q and do not include all of the information and footnotes required by accounting principles generally accepted in the United States (“GAAP”) for complete financial statements. In our opinion, all adjustments (consisting of normal recurring adjustments) considered necessary for a fair presentation have been included.

References to “ASC” included hereinafter refer to the Accounting Standards Codification established by the Financial Accounting Standards Board (“FASB”) as the source of authoritative GAAP.

The condensed consolidated financial statements include the accounts of Bassett Furniture Industries, Incorporated (“Bassett”, “we”, “our”, or the “Company”) and our wholly-owned subsidiaries of which we have a controlling interest. The equity method of accounting was used for our investment in an affiliated company in which we exercised significant influence but did not maintain a controlling interest prior to the Zenith acquisition mentioned below. In accordance with ASC Topic 810, we have evaluated our licensees and certain other entities to determine whether they are variable interest entities (“VIEs”) of which we are the primary beneficiary and thus would require consolidation in our financial statements. To date we have concluded that none of our licensees nor any other of our counterparties represent VIEs.

Revenue from the sale of furniture and accessories is reported in the accompanying condensed consolidated statements of income net of estimates for returns and allowances.

Zenith Acquisition

Prior to February 2, 2015 we held a 49% interest in Zenith Freight Lines, LLC (“Zenith”) for which we used the equity method of accounting. On February 2, 2015 we acquired the remaining 51% ownership interest (see Note 3, Business Combinations). Accordingly, the results of Zenith have been consolidated with our results since the date of the acquisition. Sales of logistical services from Zenith to our wholesale and retail segments have been eliminated, and Zenith’s operating costs and expenses since the date of acquisition are included in selling, general and administrative expenses in our condensed consolidated statements of income. Our equity in the earnings of Zenith prior to the date of the acquisition is included in other loss, net, in the accompanying condensed consolidated statements of income.

Adoption of Accounting Standards Update 2016-09

In March 2016, the FASB issued Accounting Standards Update No. 2016-09, *Compensation – Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting* (ASU 2016-09). While the effective date of ASU 2016-09 is for fiscal years beginning after December 15, 2016, earlier adoption is permitted and we have chosen to adopt the amendments in ASU 2016-09 during the second quarter of fiscal 2016. This standard simplifies or clarifies several aspects of the accounting for equity-based payment awards, including the income tax consequences, classification of awards as either equity or liabilities, and classification on the statement of cash flows. Certain of these changes are required to be applied retrospectively, while other changes are required to be applied prospectively.

The impact of early adoption resulted in the following:

We recorded an immaterial tax benefit within income tax expense for the three months ended May 28, 2016 related to the excess tax benefit on stock based compensation. Prior to adoption this amount would have been recorded as additional paid-in capital. This change could create future volatility in our effective tax rate depending upon the amount of exercise or vesting activity from our stock based awards.

We have elected to recognize forfeitures as they occur. There was no cumulative effect adjustment as a result of the adoption of this amendment on a modified retrospective basis.

We have elected to apply the change in classification of cash flows resulting from excess tax benefits or deficiencies on a retrospective basis. Accordingly, \$1,032 of excess tax benefits previously reported as a cash flow provided by financing activities during the six months ended May 30, 2015 has been reclassified to be included in cash flows provided by operating activities.

PART I-FINANCIAL INFORMATION-CONTINUED

BASSETT FURNITURE INDUSTRIES, INCORPORATED AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS-UNAUDITED

MAY 28 2016

(Dollars in thousands except share and per share data)

We have excluded the excess tax benefits from the assumed proceeds available to repurchase shares in the computation of our diluted earnings per share for the three and six months ended May 28, 2016. The effect of this change on our diluted earnings per share was not significant.

ASU 2016-09 also requires the presentation of employee taxes paid by the Company through the withholding of shares as a financing activity on the statement of cash flows, which is where we had previously reclassified these items.

The impact of the adoption of this standard retroactively as of November 29, 2015 (the first day of our fiscal year 2016), was not significant as there was no significant award vesting or settlement activity during the first quarter of fiscal 2016.

There were no other material impacts to our consolidated financial statements as a result of adopting this updated standard.

2. Interim Financial Presentation

All intercompany accounts and transactions have been eliminated in the condensed consolidated financial statements. The results of operations for the three and six months ended May 28, 2016 are not necessarily indicative of results for the full fiscal year. These interim condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and accompanying notes included in our Annual Report on Form 10-K for the year ended November 28, 2015.

We calculate an anticipated effective tax rate for the year based on our annual estimates of pretax income and use that effective tax rate to record our year-to-date income tax provision. Any change in annual projections of pretax income could have a significant impact on our effective tax rate for the respective quarter. Our effective tax rates for the three

and six month periods ended May 28, 2016 and May 30, 2015 differ from the federal statutory rate primarily due to the effects of state income taxes and various permanent differences including the favorable impact of the Section 199 manufacturing deduction.

3. Business Combination – Acquisition of Zenith

Prior to February 2, 2015 we held a 49% interest in Zenith for which we used the equity method of accounting. Zenith provides domestic transportation and warehousing services primarily to furniture manufacturers and distributors and also provides home delivery services to furniture retailers. We historically have contracted with Zenith to provide substantially all of our domestic freight, transportation and warehousing needs for the wholesale business. In addition, Zenith provides home delivery services for many of our Company-owned retail stores. On February 2, 2015, we acquired the remaining 51% of Zenith in exchange for cash, Bassett common stock and a note payable with a total fair value of \$19,111. The value of the Bassett common stock was based on the closing market price of our shares on the acquisition date, discounted for lack of marketability due to restrictions on the seller's ability to transfer the shares. The restrictions on one half of the shares expired on the first anniversary of the acquisition, with the remainder expiring on the second anniversary. The note is payable in three annual installments of \$3,000 each beginning February 2, 2016, and has been discounted to its fair value as of the date of the acquisition based on our estimated borrowing rate.

The carrying value of our 49% interest in Zenith prior to the acquisition was \$9,480 (see Note 8, unconsolidated affiliated company). In connection with the acquisition, this investment was remeasured to a fair value of \$16,692 resulting in the recognition of a gain of \$7,212 during the six months ended May 30, 2015. The impact of this gain upon our basic and diluted earnings per share was approximately \$0.42, net of the related tax expense. The remeasured fair value of our prior interest in Zenith was estimated based on the fair value of the consideration transferred to acquire the remaining 51% of Zenith less an estimated control premium.

Under the acquisition method of accounting, the fair value of the consideration transferred along with the fair value of our previous 49% interest in Zenith was allocated to the tangible and intangible assets acquired and the liabilities assumed based on their estimated fair values as of the acquisition date with the remaining unallocated amount recorded as goodwill.

PART I-FINANCIAL INFORMATION-CONTINUED

BASSETT FURNITURE INDUSTRIES, INCORPORATED AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS-UNAUDITED

MAY 28 2016

(Dollars in thousands except share and per share data)

The total fair value of the acquired business was determined as follows:

Fair value of consideration transferred in exchange for 51% of Zenith:	
Cash	\$9,000
Bassett common stock, 89,485 shares, par value \$5.00 per share, fair value at closing \$18.72 per share	1,675
Note payable	8,436
Total fair value of consideration transferred to seller	19,111
Less effective settlement of previous amounts payable to Zenith at acquisition	(3,622)
Total fair value of consideration net of effective settlement	15,489
Fair value of Bassett's previous 49% interest in Zenith	16,692
 Total fair value of acquired business	 \$32,181

The allocation of the fair value of the acquired business is as follows:

Allocation of the fair value of consideration transferred:	
Identifiable assets acquired:	
Acquired cash and cash equivalents	\$1,677
Accounts receivable, net	3,399
Prepaid expenses and other current assets	496
Property and equipment	18,110
Other long-term assets	646
Intangible assets	6,362
Total identifiable assets acquired	30,690
Liabilities assumed:	
Accounts payable and accrued liabilities	(4,038)
Notes payable	(4,329)
Total liabilities assumed	(8,367)
Net identifiable assets acquired	22,323
Goodwill	9,858
Total net assets acquired	\$32,181

Goodwill was determined based on the residual difference between the fair value of the consideration transferred and the value assigned to tangible and intangible assets and liabilities. Approximately \$6,982 of the acquired goodwill is deductible for tax purposes. Among the factors that contributed to a purchase price resulting in the recognition of goodwill were Zenith's reputation for best-in-class, fully integrated logistical services which are uniquely tailored to the needs of the furniture industry, as well as their ability to provide expedited delivery service which is increasingly in demand in the furniture industry.

A portion of the fair value of consideration transferred was assigned to identifiable intangible assets as follows:

Description:	Useful Life In Years	Fair Value
Customer relationships	15	\$3,038
Trade names	Indefinite	2,490
Technology - customized applications	7	834
Total acquired intangible assets		\$6,362

PART I-FINANCIAL INFORMATION-CONTINUED

BASSETT FURNITURE INDUSTRIES, INCORPORATED AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS-UNAUDITED

MAY 28 2016

(Dollars in thousands except share and per share data)

The finite-lived intangible assets are being amortized on a straight-line basis over their useful lives. The indefinite-lived intangible asset and goodwill are not amortized but will be tested for impairment annually or between annual tests if an indicator of impairment exists.

The fair values of consideration transferred and net assets acquired were determined using a combination of Level 2 and Level 3 inputs as specified in the fair value hierarchy in ASC 820, *Fair Value Measurements and Disclosures*. See Note 4.

Acquisition costs related to the Zenith acquisition totaled \$88 and \$209 during the three and six months ended May 28, 2015, respectively, and are included in selling, general and administrative expenses in the condensed consolidated statements of income. The acquisition costs are primarily related to legal, accounting and valuation services.

The revenue and pre-tax profit of Zenith that is included in our condensed consolidated statements of income is as follows:

	Quarter Ended		Six Months Ended	
	May 28, 2016	May 30, 2015	May 28, 2016	May 30, 2015 (1)
Zenith revenue (2)	\$13,677	\$12,086	\$28,148	\$15,345
Zenith pre-tax income	\$614	\$982	\$1,309	\$962

(1)From date of acquisition, February 2, 2015.

(2)Net of eliminated inter-company transactions. See Note 14.

The pro forma results of operations for the acquisition of Zenith have not been presented because they are not material to our consolidated results of operations.

4. Financial Instruments and Fair Value Measurements

Financial Instruments

Our financial instruments include cash and cash equivalents, short-term investments in certificates of deposit, accounts receivable, cost method investments, accounts payable and notes payable/long-term debt. Because of their short maturities, the carrying amounts of cash and cash equivalents, short-term investments in certificates of deposit, accounts receivable, and accounts payable approximate fair value. Our cost method investments generally involve entities for which it is not practical to determine fair values.

Investments

Our short-term investments of \$23,125 at both May 28, 2016 and November 28, 2015 consisted of certificates of deposit (CDs) with original terms of twelve months, bearing interest at rates ranging from 0.28% to 1.00%. At May 28, 2016, the weighted average remaining time to maturity of the CDs was approximately two months and the weighted average yield of the CDs was approximately 0.42%. Each CD is placed with a Federally insured financial institution and all deposits are within Federal deposit insurance limits. Due to the nature of these investments and their relatively short maturities, the carrying amount of the short-term investments at May 28, 2016 and November 28, 2015 approximates their fair value.

Fair Value Measurement

The Company accounts for items measured at fair value in accordance with ASC Topic 820, *Fair Value Measurements and Disclosures*. ASC 820's valuation techniques are based on observable and unobservable inputs. Observable inputs reflect readily obtainable data from independent sources, while unobservable inputs reflect our market assumptions. ASC 820 classifies these inputs into the following hierarchy:

Level 1 Inputs— Quoted prices for identical instruments in active markets.

PART I-FINANCIAL INFORMATION-CONTINUED

BASSETT FURNITURE INDUSTRIES, INCORPORATED AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS-UNAUDITED

MAY 28 2016

(Dollars in thousands except share and per share data)

Level 2 Inputs– Quoted prices for similar instruments in active markets; quoted prices for identical or similar instruments in markets that are not active; and model-derived valuations whose inputs are observable or whose significant value drivers are observable.

Level 3 Inputs– Instruments with primarily unobservable value drivers.

We believe that the carrying amounts of our current assets and current liabilities approximate fair value due to the short-term nature of these items. The recurring estimate of the fair value of our notes payable for disclosure purposes (see Note 9) involves Level 3 inputs. Our primary non-recurring fair value estimates typically involve business acquisitions (Note 3) which involve a combination of Level 2 and Level 3 inputs, and asset impairments (Note 11) which utilize Level 3 inputs.

5. Accounts Receivable

Accounts receivable consists of the following:

	May 28, 2016	November 28, 2015
Gross accounts receivable	\$ 19,993	\$ 22,372
Allowance for doubtful accounts	(1,006)	(1,175)
Accounts receivable, net	\$ 18,987	\$ 21,197

Activity in the allowance for doubtful accounts for the six months ended May 28, 2016 was as follows:

2016

Balance at November 28, 2015	\$1,175
Reductions to allowance	(169)
Balance at May 28, 2016	\$1,006

We believe that the carrying value of our net accounts receivable approximates fair value. The inputs into these fair value estimates reflect our market assumptions and are not observable. Consequently, the inputs are considered to be Level 3 as specified in the fair value hierarchy in ASC Topic 820, *Fair Value Measurements and Disclosures*. See Note 4.

6. Inventories

Inventories are valued at the lower of cost or market. Cost is determined for domestic furniture inventories using the last-in, first-out (LIFO) method. The costs for imported inventories are determined using the first-in, first-out (FIFO) method.

Inventories were comprised of the following:

	May 28, 2016	November 28, 2015
Wholesale finished goods	\$25,066	\$ 31,253
Work in process	348	318
Raw materials and supplies	11,321	9,793
Retail merchandise	27,470	27,680
Total inventories on first-in, first-out method	64,205	69,044
LIFO adjustment	(7,985)	(7,751)
Reserve for excess and obsolete inventory	(1,386)	(1,397)
	\$54,834	\$ 59,896

PART I-FINANCIAL INFORMATION-CONTINUEDBASSETT FURNITURE INDUSTRIES, INCORPORATED AND SUBSIDIARIESNOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS-UNAUDITEDMAY 28 2016(Dollars in thousands except share and per share data)

We estimate an inventory reserve for excess quantities and obsolete items based on specific identification and historical write-offs, taking into account future demand, market conditions and the respective valuations at LIFO. The need for these reserves is primarily driven by the normal product life cycle. As products mature and sales volumes decline, we rationalize our product offerings to respond to consumer tastes and keep our product lines fresh. If actual demand or market conditions in the future are less favorable than those estimated, additional inventory write-downs may be required. In determining reserves, we calculate separate reserves on our wholesale and retail inventories. Our wholesale inventories tend to carry the majority of the reserves for excess quantities and obsolete inventory due to the nature of our distribution model. These wholesale reserves primarily represent design and/or style obsolescence. Typically, product is not shipped to our retail warehouses until a consumer has ordered and paid a deposit for the product. We do not typically hold retail inventory for stock purposes. Consequently, floor sample inventory and inventory for delivery to customers account for the majority of our inventory at retail. Retail reserves are based on accessory and clearance floor sample inventory in our stores and any inventory that is not associated with a specific customer order in our retail warehouses.

Activity in the reserves for excess quantities and obsolete inventory by segment are as follows:

	Wholesale Segment	Retail Segment	Total
Balance at November 28, 2015	\$ 1,087	\$ 310	\$ 1,397
Additions charged to expense	1,048	261	1,309
Write-offs	(1,053)	(267)	(1,320)
Balance at May 28, 2016	\$ 1,082	\$ 304	\$ 1,386

Our estimates and assumptions have been reasonably accurate in the past. We have not made any significant changes to our methodology for determining inventory reserves in 2016 and do not anticipate that our methodology is likely to change in the future.

PART I-FINANCIAL INFORMATION-CONTINUEDBASSETT FURNITURE INDUSTRIES, INCORPORATED AND SUBSIDIARIESNOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS-UNAUDITEDMAY 28 2016(Dollars in thousands except share and per share data)**7. Goodwill and Other Intangible Assets**

Goodwill and other intangible assets consisted of the following:

	May 28, 2016		
	Gross Carrying Amount	Accumulated Amortization	Intangible Assets, Net
Intangibles subject to amortization			
Customer relationships	\$3,038	\$ (270	) \$ 2,768
Technology - customized applications	834	(159	) 675
Total intangible assets subject to amortization	3,872	(429	) 3,443
Intangibles not subject to amortization:			
Trade names	2,490	-	2,490
Goodwill	11,588	-	11,588
Total goodwill and other intangible assets	\$17,950	\$ (429	) \$ 17,521

	November 28, 2015		
	Gross Carrying Amount	Accumulated Amortization	Intangible Assets, Net
Intangibles subject to amortization			
Customer relationships	\$3,038	\$ (169	) \$ 2,869
Technology - customized applications	834	(99	) 735
Total intangible assets subject to amortization	3,872	(268) 3,604

Intangibles not subject to amortization:

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Trade names	2,490	-	2,490
Goodwill	11,588	-	11,588
Total goodwill and other intangible assets	\$ 17,950	\$ (268) \$ 17,682

The carrying amounts of goodwill by reportable segment at both May 28, 2016 and November 28, 2015 were as follows:

Wholesale	\$4,839
Retail	1,820
Logistical services	4,929
Total goodwill	\$ 11,588

There were no accumulated impairment losses on goodwill as of May 28, 2016 or November 28, 2015.

Amortization expense associated with intangible assets during the three and six months ended May 28, 2016 and May 30, 2015 was as follows:

	Quarter Ended		Six Months Ended	
	May 28, 2016	May 30, 2015	May 28, 2016	May 30, 2015
Intangible asset amortization expense	\$80	\$ 66	\$161	\$ 108

PART I-FINANCIAL INFORMATION-CONTINUEDBASSETT FURNITURE INDUSTRIES, INCORPORATED AND SUBSIDIARIESNOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS-UNAUDITEDMAY 28 2016(Dollars in thousands except share and per share data)**8. Unconsolidated Affiliate**

Prior to February 2, 2015 we owned 49% of Zenith and accounted for our investment under the equity method. The balance of our investment in Zenith was adjusted for our equity in the earnings of Zenith through February 2, 2015 of \$220 (included in other loss, net in our condensed consolidated statement of income for the six months ended May 30, 2015), and increased by \$1,345 representing our 49% share of a \$2,745 capital contribution made to Zenith, a portion of which was used for retirement of certain of Zenith's debt prior to the acquisition. This activity resulted in a carrying value for our investment in Zenith of \$9,480 on the date of acquisition. See Note 3 regarding the remeasurement of this carrying value to fair value in connection with the acquisition and the resulting remeasurement gain of \$7,212.

9. Notes Payable and Bank Credit Facility

Our notes payable consist of the following:

	May 28, 2016		
	Principal Balance	Unamortized Discount	Net Carrying Amount
Zenith acquisition note payable	\$6,000	\$ (200	) \$ 5,800
Transportation equipment notes payable	7,207	-	7,207
Real estate notes payable	2,651	-	2,651
Total Debt	15,858	(200	) 15,658
Less current portion	(6,586)	148	(6,438)
Total long-term debt	\$9,272	\$ (52	) \$ 9,220

	November 28, 2015		
	Principal Balance	Unamortized Discount	Net Carrying Amount
Zenith acquisition note payable	\$9,000	\$ (312)	\$ 8,688
Transportation equipment notes payable	2,152	-	2,152
Real estate notes payable	2,933	-	2,933
Total Debt	14,085	(312)	13,773
Less current portion	(5,477)	204	(5,273)
Total long-term debt	\$8,608	\$ (108)	\$ 8,500

The future maturities of our notes payable are as follows:

Remainder of fiscal 2016	\$2,290
Fiscal 2017	5,415
Fiscal 2018	5,137
Fiscal 2019	2,148
Fiscal 2020	868
Fiscal 2021	-
Thereafter	-
	\$15,858

PART I-FINANCIAL INFORMATION-CONTINUED

BASSETT FURNITURE INDUSTRIES, INCORPORATED AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS-UNAUDITED

MAY 28 2016

(Dollars in thousands except share and per share data)

Zenith Acquisition Note Payable

As part of the consideration given for our acquisition of Zenith on February 2, 2015, we issued an unsecured note payable to the former owner in the amount of \$9,000, payable in three annual installments of \$3,000 due on each anniversary of the note, the first installment having been paid on February 2, 2016. Interest is payable annually at the one year LIBOR rate, which was established at 0.62% on February 2, 2015 and resets on each anniversary of the note, having reset to the current rate of 1.14% on February 2, 2016. The note was recorded at its fair value in connection with the acquisition resulting in a debt discount that is amortized to the principal amount through the recognition of non-cash interest expense over the term of the note. Interest expense resulting from the amortization of the discount was \$46 and \$112 for the three and six months ended May 28, 2016, respectively, and \$78 and \$101 for the three and six months ended May 30, 2015, respectively. The current portion of the note due within one year, including unamortized discount, was \$2,852 and \$2,796 at May 28, 2016 and November 28, 2015, respectively.

Transportation Equipment Notes Payable

Certain of the transportation equipment operated in our logistical services segment is financed by notes payable in the amount of \$7,207 and \$2,152 at May 28, 2016 and November 28, 2015, respectively. These notes are payable in fixed monthly payments of principal and interest at fixed and variable rates ranging from 2.63% to 3.75% at May 28, 2016, with remaining terms of twelve to fifty months. The current portion of these notes due within one year was \$2,108 and \$901 at May 28, 2016 and November 28, 2015, respectively. The notes are secured by tractors, trailers and local delivery trucks with a total net book value of \$9,260 and \$3,796 at May 28, 2016 and November 28, 2015, respectively.

Real Estate Notes Payable

Certain of our retail real estate properties have been financed through commercial mortgages with outstanding principal totaling \$1,536 and \$1,709 at May 28, 2016 and November 28, 2015, respectively. The mortgages bear interest at fixed rates of 6.73%. They are collateralized by the respective properties with net book values totaling approximately \$5,925 and \$5,993 at May 28, 2016 and November 28, 2015, respectively. The current portion of these mortgages due within one year was \$363 and \$351 as of May 28, 2016 and November 28, 2015, respectively.

Certain of the real estate located in Conover, North Carolina and operated in our logistical services segment is subject to a note payable in the amount of \$1,115 and \$1,224 at May 28, 2016 and November 28, 2015, respectively. The note is payable in monthly installments of principal and interest at the fixed rate of 3.75% through October 2016, at which time the remaining balance on the note of approximately \$1,005 will be due. Therefore, the entire balance of this note is included in the current portion of our long-term debt at May 28, 2016 and November 28, 2015. The note is secured by land and buildings with a total net book value of \$6,157 and \$6,226 at May 28, 2016 and November 28, 2015, respectively.

Fair Value

We believe that the carrying amount of our notes payable approximates fair value at both May 28, 2016 and November 28, 2015. In estimating the fair value, we utilize current market interest rates for similar instruments. The inputs into these fair value calculations reflect our market assumptions and are not observable. Consequently, the inputs are considered to be Level 3 as specified in the fair value hierarchy in ASC Topic 820, *Fair Value Measurements and Disclosures*. See Note 3.

Bank Credit Facility

Effective December 5, 2015, we entered into a new credit facility with our bank which provides for a line of credit of up to \$15,000. This credit facility, which matures in December of 2018, is unsecured and contains covenants requiring us to maintain certain key financial ratios. We are in compliance with all covenants under the agreement and expect to remain in compliance for the foreseeable future.

At May 28, 2016, we had \$1,970 outstanding under standby letters of credit against our line, leaving availability under our credit line of \$13,030. In addition, we have outstanding standby letters of credit with another bank totaling \$356.

PART I-FINANCIAL INFORMATION-CONTINUEDBASSETT FURNITURE INDUSTRIES, INCORPORATED AND SUBSIDIARIESNOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS-UNAUDITEDMAY 28 2016(Dollars in thousands except share and per share data)**10. Post Employment Benefit Obligations**

We have an unfunded Supplemental Retirement Income Plan (the "Supplemental Plan") that covers one current and certain former executives. The liability for this plan was \$11,688 and \$11,678 as of May 28, 2016 and November 28, 2015, respectively, and is recorded as follows in the condensed consolidated balance sheets:

	May 28, 2016	November 28, 2015
Accrued compensation and benefits	\$749	\$ 749
Post employment benefit obligations	10,939	10,929
Total pension liability	\$11,688	\$ 11,678

Components of net periodic pension costs are as follows:

	Quarter Ended		Six Months Ended	
	May 28, 2016	May 30, 2015	May 28, 2016	May 30, 2015
Service cost	\$36	\$26	\$73	\$52
Interest cost	106	94	211	187
Amortization of transition obligation	11	11	21	21
Amortization of loss	81	49	162	97
Net periodic pension cost	\$234	\$ 180	\$467	\$ 357

We have an unfunded Deferred Compensation Plan that covers one current executive and certain former executives and provides for voluntary deferral of compensation. This plan has been frozen with no additional participants or deferrals permitted. Our liability under this plan was \$2,035 and \$2,085 as of May 28, 2016 and November 28, 2015, respectively, and is recorded as follows in the condensed consolidated balance sheets:

	May 28, 2016	November 28, 2015
Accrued compensation and benefits	\$ 320	\$ 320
Post employment benefit obligations	1,715	1,765
Total deferred compensation liability	\$ 2,035	\$ 2,085

We recognized expense under this plan during the three and six months ended May 28, 2016 and May 30, 2015 as follows:

	Quarter Ended		Six Months Ended	
	May 28, 2016	May 30, 2015	May 28, 2016	May 30, 2015
Deferred compensation expense	\$ 57	\$ 54	\$ 114	\$ 108

PART I-FINANCIAL INFORMATION-CONTINUEDBASSETT FURNITURE INDUSTRIES, INCORPORATED AND SUBSIDIARIESNOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS-UNAUDITEDMAY 28 2016(Dollars in thousands except share and per share data)**11. Impairment Charges and Accrued Lease Exit Costs**

During the first quarter of fiscal 2015 we announced the closing of our Company-owned retail store location in Memphis, Tennessee. In connection with this closing, we recognized non-cash charges during the six months ended May 30, 2015 of \$419 for the accrual of lease exit costs and \$106 for the write off of abandoned leasehold improvements and other store assets.

The following table summarized the activity related to our accrued lease exit costs:

Balance at November 28, 2015	\$566
Provisions made to adjust previous estimates	54
Payments and other	(260)
Accretion of interest on obligations	5
Balance at May 28, 2016	\$365
Current portion included in other accrued liabilities	\$203
Long-term portion included in other long-term liabilities	162
Total accrued lease exit costs at May 28, 2016	\$365

Management Restructuring Costs

During the three and six months ended May 30, 2015, we recognized \$449 of expense related to severance payable to a former executive, who left the Company in April, 2015. As of November 28, 2015, all required payments of severance had been disbursed. These management restructuring costs were incurred within our wholesale segment.

Income from Continue Dumping & Subsidy Offset Act

During the three and six months ended May 30, 2015, we recognized income of \$1,066 arising from distributions received from U.S. Customs and Border Protection (“Customs”) under the Continued Dumping and Subsidy Offset Act of 2000 (“CDSOA”). These distributions primarily represent amounts previously withheld by Customs pending the resolution of claims filed by certain manufacturers who did not support the antidumping petition (“Non-Supporting Producers”) challenging certain provisions of the CDSOA and seeking to share in the distributions. The Non-Supporting Producers’ claims were dismissed by the courts and all appeals were exhausted in 2014. While it is possible that we may receive additional distributions from Customs, we cannot estimate the likelihood or amount of any future distributions.

PART I-FINANCIAL INFORMATION-CONTINUEDBASSETT FURNITURE INDUSTRIES, INCORPORATED AND SUBSIDIARIESNOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS-UNAUDITEDMAY 28 2016(Dollars in thousands except share and per share data)**12. Commitments and Contingencies**

We are involved in various legal and environmental matters, which arise in the normal course of business. Although the final outcome of these matters cannot be determined, based on the facts presently known, we believe that the final resolution of these matters will not have a material adverse effect on our financial position or future results of operations.

We lease land and buildings that are used in the operation of our Company-owned retail stores as well as in the operation of certain of our licensee-owned stores, and we lease land and buildings at various locations throughout the continental United States for warehousing and distribution hubs used in our logistical services segment. We also lease tractors, trailers and local delivery trucks used in our logistical services segment. Our real estate lease terms range from one to 15 years and generally have renewal options of between five and 15 years. Some store leases contain contingent rental provisions based upon sales volume. Our transportation equipment leases have terms ranging from two to seven years with fixed monthly rental payments plus variable charges based upon mileage. The following schedule shows future minimum lease payments under non-cancellable operating leases with terms in excess of one year as of May 28, 2016:

	Retail Stores	Distribution Centers	Transportation Equipment	Total
Remainder of fiscal 2016	\$9,473	\$ 2,085	\$ 1,835	\$13,393
Fiscal 2017	20,519	4,041	3,060	27,620
Fiscal 2018	18,350	2,736	1,835	22,921
Fiscal 2019	16,501	1,745	1,808	20,054
Fiscal 2020	15,206	1,230	1,743	18,179
Fiscal 2021	12,927	1,254	1,169	15,350
Thereafter	37,460	3,023	1,217	41,700
Total future minimum lease payments	\$130,436	\$ 16,114	\$ 12,667	\$159,217

We also have guaranteed certain lease obligations of licensee operators. Lease guarantees range from one to ten years. We were contingently liable under licensee lease obligation guarantees in the amount of \$2,254 and \$2,494 at May 28, 2016 and November 28, 2015, respectively.

In the event of default by an independent dealer under the guaranteed lease, we believe that the risk of loss is mitigated through a combination of options that include, but are not limited to, arranging for a replacement dealer, liquidating the collateral (primarily inventory), and pursuing payment under the personal guarantees of the independent dealer. The proceeds of the above options are expected to cover the estimated amount of our future payments under the guarantee obligations, net of recorded reserves. The fair value of lease guarantees (an estimate of the cost to the Company to perform on these guarantees) at May 28, 2016 and November 28, 2015 was not material.

PART I-FINANCIAL INFORMATION-CONTINUEDBASSETT FURNITURE INDUSTRIES, INCORPORATED AND SUBSIDIARIESNOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS-UNAUDITEDMAY 28 2016(Dollars in thousands except share and per share data)**13. Earnings Per Share**

The following reconciles basic and diluted earnings per share:

	Net Income	Weighted Average Shares	Net Income Per Share
<u>For the quarter ended May 28, 2016:</u>			
Basic earnings per share	\$3,385	10,767,082	\$ 0.31
Add effect of dilutive securities:			
Options and restricted shares	-	145,609	-
Diluted earnings per share	\$3,385	10,912,691	\$ 0.31
<u>For the quarter ended May 30, 2015:</u>			
Basic earnings per share	\$4,529	10,678,298	\$ 0.42
Add effect of dilutive securities:			
Options and restricted shares	-	165,918	-
Diluted earnings per share	\$4,529	10,844,216	\$ 0.42
<u>For the six months ended May 28, 2016:</u>			
Basic earnings per share	\$6,619	10,773,656	\$ 0.61
Add effect of dilutive securities:			
Options and restricted shares		142,584	-
Diluted earnings per share	\$6,619	10,916,240	\$ 0.61
<u>For the nine months ended May 30, 2015:</u>			
Basic earnings per share	\$10,485	10,579,477	\$ 0.99

Add effect of dilutive securities:

Options and restricted shares	-	171,720	(0.01)
Diluted earnings per share	\$10,485	10,751,197	\$ 0.98

For the three and six months ended May 28, 2016 and May 30, 2015, the following potentially dilutive shares were excluded from the computations as their effect was anti-dilutive:

Quarter		Six Months	
Ended		Ended	
May	May	May	May
28,	30,	28,	30,
2016	2015	2016	2015

Unvested shares	5,814	6,354	7,814	46,354
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PART I-FINANCIAL INFORMATION-CONTINUED

BASSETT FURNITURE INDUSTRIES, INCORPORATED AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS-UNAUDITED

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(Dollars in thousands except share and per share data)

14. Segment Information

We have strategically aligned our business into three reportable segments as defined in ASC 280, *Segment Reporting*, and as described below:

Wholesale. The wholesale home furnishings segment is involved principally in the design, manufacture, sourcing, sale and distribution of furniture products to a network of Bassett stores (Company-owned and licensee-owned retail stores) and independent furniture retailers. Our wholesale segment includes our wood and upholstery operations as well as all corporate selling, general and administrative expenses, including those corporate expenses related to both Company- and licensee-owned stores. Also included in our wholesale segment are our short-term investments and our holdings of retail real estate previously leased as licensee stores. The earnings and costs associated with these assets are included in other income (loss), net, in our condensed consolidated statements of income.

Retail – Company-owned stores. Our retail segment consists of Company-owned stores and includes the revenues, expenses, assets and liabilities and capital expenditures directly related to these stores.

Logistical services. With our acquisition of Zenith on February 2, 2015, we created the logistical services operating segment which reflects the operations of Zenith. In addition to providing shipping, delivery and warehousing services for the Company, Zenith also provides similar services to other customers, primarily in the furniture industry. Revenue from the performance of these services to other customers is included in logistical services revenue in our condensed consolidated statement of income. Zenith's operating costs are included in selling, general and administrative expenses and were \$23,149 and \$47,084 for the three and six months ended May 28, 2016, respectively; \$20,931 for the three months ended May 30, 2015 and \$26,938 from the date of acquisition through May 30, 2015. Amounts charged by Zenith to the Company for logistical services prior to the date of acquisition are included in selling, general and administrative expenses, and our equity in the earnings of Zenith prior to the date of acquisition is included in other income (loss), net, in the accompanying statements of income.

Inter-company net sales elimination represents the elimination of wholesale sales to our Company-owned stores and the elimination of Zenith logistics revenue from our wholesale and retail segments. Inter-company income elimination

includes the embedded wholesale profit in the Company-owned store inventory that has not been realized. These profits will be recorded when merchandise is delivered to the retail consumer. The inter-company income elimination also includes rent paid by our retail stores occupying Company-owned real estate, and the elimination of shipping and handling charges from Zenith for services provided to our wholesale and retail operations.

PART I-FINANCIAL INFORMATION-CONTINUEDBASSETT FURNITURE INDUSTRIES, INCORPORATED AND SUBSIDIARIESNOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS-UNAUDITEDMAY 28 2016(Dollars in thousands except share and per share data)

The following table presents our segment information:

	Quarter Ended		Six Months Ended	
	May 28, 2016	May 30, 2015	May 28, 2016	May 30, 2015
Sales Revenue				
Wholesale	\$59,906	\$66,705	\$119,482	\$125,510
Retail - Company-owned stores	61,943	63,921	123,538	121,104
Logistical services	23,810	21,958	48,489	27,957
Inter-company eliminations:				
Furniture and accessories	(28,859)	(31,159)	(57,628)	(57,599)
Logistical services	(10,133)	(9,872)	(20,341)	(12,612)
Consolidated	\$106,667	\$111,553	\$213,540	\$204,360
Income from Operations				
Wholesale	\$4,334	\$4,796	\$8,732	\$7,723
Retail - Company-owned stores	381	1,971	697	1,929
Logistical services	661	1,027	1,405	1,019
Inter-company elimination	477	(631)	810	(106)
Management restructuring costs	-	(449)	-	(449)
Lease exit costs	-	-	-	(419)
Asset impairment charges	-	-	-	(106)
Consolidated	\$5,853	\$6,714	\$11,644	\$9,591
Depreciation and Amortization				
Wholesale	\$459	\$504	\$915	\$1,038
Retail - Company-owned stores	1,529	1,343	3,060	2,698
Logistical services	806	736	1,636	993
Consolidated	\$2,794	\$2,583	\$5,611	\$4,729
Capital Expenditures				
Wholesale	\$1,454	\$1,384	\$2,991	\$2,345
Retail - Company-owned stores	959	1,767	2,980	3,878
Logistical services	3,135	873	8,145	1,719

Consolidated	\$5,548	\$4,024	\$14,116	\$7,942
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	As of May 28, 2016	As of November 28, 2015
Identifiable Assets		
Wholesale	\$133,608	\$146,878
Retail - Company-owned stores	90,254	88,878
Logistical services	52,385	46,787
Consolidated	\$276,247	\$282,543

PART I-FINANCIAL INFORMATION-CONTINUED

BASSETT FURNITURE INDUSTRIES, INCORPORATED AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS-UNAUDITED

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(Dollars in thousands except share and per share data)

15. Recent Accounting Pronouncements

In May 2014, the FASB issued Accounting Standards Update No. 2014-09 (ASU 2014-09), which creates ASC Topic 606, Revenue from Contracts with Customers, and supersedes the revenue recognition requirements in Topic 605, Revenue Recognition, including most industry-specific revenue recognition guidance throughout the Industry Topics of the Codification. In addition, ASU 2014-09 supersedes the cost guidance in Subtopic 605-35, Revenue Recognition—Construction-Type and Production-Type Contracts, and creates new Subtopic 340-40, Other Assets and Deferred Costs—Contracts with Customers. In summary, the core principle of Topic 606 is to recognize revenue when promised goods or services are transferred to customers in an amount that reflects the consideration that is expected to be received for those goods or services. Companies are allowed to select between two transition methods: (1) a full retrospective transition method with the application of the new guidance to each prior reporting period presented, or (2) a retrospective transition method that recognizes the cumulative effect on prior periods at the date of adoption together with additional footnote disclosures. In addition, during 2016 the FASB has issued ASU 2016-08, ASU 2016-10 and ASU 2016-12, all of which clarify certain implementation guidance within ASU 2014-09. The amendments in ASU 2014-09 are effective for annual reporting periods beginning after December 15, 2017, including interim periods within that reporting period, and early application is not permitted. Therefore the amendments in ASU 2014-09 will become effective for us as of the beginning of our 2019 fiscal year. We are currently evaluating the impact that the adoption of ASU 2014-09 will have on our consolidated financial statements and have not made any decision on the method of adoption.

In July 2015, the FASB issued Accounting Standards Update No. 2015-11, Inventory (Topic 330): Simplifying the Measurement of Inventory. ASU 2015-11 requires that inventory within the scope of this Update be measured at the lower of cost and net realizable value. Net realizable value is the estimated selling prices in the ordinary course of business, less reasonably predictable costs of completion, disposal, and transportation. The amendments in this Update do not apply to inventory that is measured using last-in, first-out (LIFO) or the retail inventory method. The amendments apply to all other inventory, which includes inventory that is measured using first-in, first-out (FIFO) or average cost. For all entities, the guidance is effective for annual periods, and interim periods within those annual periods, beginning after December 15, 2016. Early adoption is permitted. Therefore the amendments in ASU 2015-11 will become effective for us as of the beginning of our 2018 fiscal year. The adoption of this guidance is not expected to have a material impact upon our financial condition or results of operations.

In July 2015, the FASB issued Accounting Standards Update No. 2015-16, Business Combinations (Topic 805): Simplifying the Accounting for Measurement Period Adjustments. ASU 2015-16 requires that an acquirer recognize adjustments to provisional amounts that are identified during the measurement period in the reporting period in which the adjustment amounts are determined. The amendments in this Update require that the acquirer record, in the same period's financial statements, the effect on earnings of changes in depreciation, amortization, or other income effects, if any, as a result of the change to the provisional amounts, calculated as if the accounting had been completed at the acquisition date. Any current period adjustments to provisional amounts that would have impacted a prior period's earnings had they been recognized at the acquisition date are required to be presented separately on the face of the income statement or disclosed in the notes. The amendments in this Update are effective for fiscal years beginning after December 15, 2015, including interim periods within those fiscal years. The amendments in this Update should be applied prospectively to adjustments to provisional amounts that occur after the effective date of this Update with earlier application permitted for financial statements that have not been issued. Therefore the amendments in ASU 2015-16 will become effective for us as of the beginning of our 2017 fiscal year. The adoption of this guidance is not expected to have a material impact upon our financial condition or results of operations.

In January 2016, the FASB issued Accounting Standards Update No. 2016-01, Financial Instruments - Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities. ASU 2016-01 requires that equity investments (except those accounted for under the equity method of accounting or those that result in consolidation of the investee) are to be measured at fair value with changes in fair value recognized in net income. However, an entity may choose to measure equity investments that do not have readily determinable fair values at cost minus impairment, if any, plus or minus changes resulting from observable price changes in orderly transactions for the identical or a similar investment of the same issuer. Furthermore, equity investments without readily determinable fair values are to be assessed for impairment using a quantitative approach. The amendments in ASU 2016-01 should be applied by means of a cumulative-effect adjustment to the balance sheet as of the beginning of the fiscal year of adoption, with other amendments related specifically to equity securities without readily determinable fair values applied prospectively. The amendments in ASU 2016-01 will become effective for us as of the beginning of our 2019 fiscal year. The adoption of this guidance is not expected to have a material impact upon our financial condition or results of operations.

PART I-FINANCIAL INFORMATION-CONTINUED

BASSETT FURNITURE INDUSTRIES, INCORPORATED AND SUBSIDIARIES

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In February 2016, the FASB issued Accounting Standards Update No. 2016-02, Leases (Topic 842). The guidance in ASU 2016-02 requires that a lessee recognize in the statement of financial position a liability to make lease payments (the lease liability) and a right-of-use asset representing its right to use the underlying asset for the lease term. For leases with a term of 12 months or less, a lessee is permitted to make an accounting policy election by class of underlying asset not to recognize lease assets and lease liabilities. As with previous guidance, there continues to be a differentiation between finance leases and operating leases, however this distinction now primarily relates to differences in the manner of expense recognition over time and in the classification of lease payments in the statement of cash flows. Lease assets and liabilities arising from both finance and operating leases will be recognized in the statement of financial position. ASU 2016-02 leaves the accounting for leases by lessors largely unchanged from previous GAAP. The transitional guidance for adopting the requirements of ASU 2016-02 calls for a modified retrospective approach that includes a number of optional practical expedients that entities may elect to apply. The guidance in ASU 2016-02 will become effective for us as of the beginning of our 2020 fiscal year. We are currently evaluating the impact that the adoption of ASU 2016-02 will have on our consolidated financial statements, which we expect will have a material effect on our statement of financial position, and have not made any decision on the method of adoption with respect to the optional practical expedients.

See Note 1 regarding our adoption of ASU 2016-09, issued by the FASB in March 2016.

PART I-FINANCIAL INFORMATION-CONTINUED

BASSETT FURNITURE INDUSTRIES, INCORPORATED AND SUBSIDIARIES

May 28, 2016

(Dollars in thousands except share and per share data)

Item 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Overview

Bassett is a leading retailer, manufacturer and marketer of branded home furnishings. Our products are sold primarily through a network of Company-owned and licensee-owned branded stores under the Bassett Home Furnishings (“BHF”) name, with additional distribution through other wholesale channels including multi-line furniture stores, many of which feature Bassett galleries or design centers, specialty stores and mass merchants. We were founded in 1902 and incorporated under the laws of Virginia in 1930. Our rich 114-year history has instilled the principles of quality, value, and integrity in everything we do, while simultaneously providing us with the expertise to respond to ever-changing consumer tastes and meet the demands of a global economy.

With 90 BHF stores at May 28, 2016, we have leveraged our strong brand name in furniture into a network of Company-owned and licensed stores that focus on providing consumers with a friendly environment for buying furniture and accessories. We created our store program in 1997 to provide a single source home furnishings retail store that provides a unique combination of stylish, quality furniture and accessories with a high level of customer service. In order to reach markets that cannot be effectively served by our retail store network, we also distribute our products through other wholesale channels including multi-line furniture stores, many of which feature Bassett galleries or design centers, specialty stores and mass merchants. We use a network of over 25 independent sales representatives who have stated geographical territories. These sales representatives are compensated based on a standard commission rate. We believe this blended strategy provides us the greatest ability to effectively distribute our products throughout the United States and ultimately gain market share.

The BHF stores feature custom order furniture ready for delivery in less than 30 days, free in-home design visits (“home makeovers”), and coordinated decorating accessories. Our philosophy is based on building strong long-term relationships with each customer. Sales people are referred to as “Design Consultants” and are each trained to evaluate customer needs and provide comprehensive solutions for their home decor. Until a rigorous training and design certification program is completed, Design Consultants are not authorized to perform in-home design services for our customers.

We have factories in Newton, North Carolina and Grand Prairie, Texas that manufacture upholstered furniture, a factory in Martinsville, Virginia that primarily assembles and finishes our custom casual dining offerings and a factory in Bassett, Virginia that assembles and finishes our recently introduced “Bench Made” line of furniture, more fully described below. Our manufacturing team takes great pride in the breadth of its options, the precision of its craftsmanship, and the speed of its process, with custom pieces often manufactured within two weeks of taking the order in our stores. Our logistics team then promptly ships the product to one of our home delivery hubs or to a location specified by our licensees in a timeframe to meet the 30 day promise. In addition to the furniture that we manufacture domestically, we source most of our formal bedroom and dining room furniture and certain upholstery offerings from several foreign plants, primarily in Vietnam, Indonesia and China. Over 60% of the products we currently sell are manufactured in the United States.

“Bench Made” is a selection of American dining furniture that first appeared in retail showrooms during the second quarter of 2015. Partnering with nearby hardwood component manufacturers, we are preparing, distressing, finishing, and assembling an assortment of solid maple tables and chairs in our newly renovated facility in Bassett, Virginia. Due to its strong reception, we have expanded “Bench Made” offerings to include bedroom and occasional furniture starting in May of 2016. Also in 2016 we began moving to a great room centric floor plan for our retail locations that will focus more on our domestic upholstery products that have lead our sales increases in recent years complemented by both imported and domestically produced entertainment and occasional furnishings. All of these new products have been carefully designed in coordination with our merchants, designers, engineers and finishing technicians to achieve the upscale casual decor that we believe speaks to today’s consumer.

For many years we owned 49% of Zenith Freight Lines, LLC (“Zenith”). During that time the strategic significance of our partnership with Zenith had risen to include the over-the-road transportation of furniture, the operation of regional freight terminals, warehouse and distribution facilities in eleven states, and the management of various home delivery facilities that service BHF stores and other clients in local markets around the United States. On February 2, 2015, we acquired the remaining 51% of Zenith, which now operates as a wholly-owned subsidiary of Bassett. Our acquisition of Zenith brings to our Company the ability to deliver best-of-class shipping and logistical support services that are uniquely tailored to the needs of the furniture industry, as well as the ability to provide the expedited delivery service which is increasingly demanded by our industry. We believe that our ownership of Zenith will not only enhance our own wholesale and retail distribution capabilities, but will provide additional growth opportunities as Zenith continues to expand its service to other customers.

PART I-FINANCIAL INFORMATION-CONTINUED

BASSETT FURNITURE INDUSTRIES, INCORPORATED AND SUBSIDIARIES

May 28, 2016

(Dollars in thousands except share and per share data)

In September of 2011, we announced the formation of a strategic partnership with HGTV (Home and Garden Television), a division of Scripps Networks, LLC, which combines our heritage in the furniture industry with the penetration of 96 million households in the United States that HGTV enjoys today. As part of this alliance, the in-store design centers have been co-branded with HGTV to more forcefully market the concept of a “home makeover”, an important point of differentiation for our stores that also mirrors much of the programming content on the HGTV network. We believe the new co-branded design centers coupled with the targeted national advertising on HGTV have played a key role in our improved comparable store sales since their introduction. In October of 2015, we announced the extension of our partnership with HGTV through 2019. While continuing to feature HGTV branded custom upholstery products in our HGTV Home Design Studios in Bassett Home Furnishings stores, we will now expand the concept to select independent dealers. We believe this will provide additional growth outside our BHF store network.

At May 28, 2016, our BHF store network included 58 Company-owned stores and 32 licensee-owned stores. During the first half of 2016, we closed three underperforming stores in Tucson, Arizona; Egg Harbor, New Jersey and Fountain Valley, California. We opened a new store in Sterling, Virginia during the second quarter of 2016 and expect to open another new store in Hunt Valley, Maryland late in 2016.

Due to the improved operating performance of our retail network over the last few years along with continued improvement in underlying economic factors such as the housing market and consumer confidence, we have been expanding our retail presence in various parts of the country. As part of this expansion, we opened one new store and relocated two stores during fiscal 2015 and opened six new stores and relocated two stores in fiscal 2014. Our plan is to average opening three to five new stores per year, net of closings, over the next five years, primarily in underpenetrated markets where we currently have stores.

As with any retail operation, prior to opening a new store we incur such expenses as rent, training costs and other payroll related costs. These costs generally range between \$100 to \$300 per store depending on the overall rent costs for the location and the period between the time when we take physical possession of the store space and the time of the store opening. Generally, rent payments during a buildout period between delivery of possession and opening of a new store are deferred and therefore straight line rent expense recognized during that time does not require cash. Inherent in our retail business model, we also incur losses in the two to three months of operation following a new store opening. Like other furniture retailers, we do not recognize a sale until the furniture is delivered to our customer. Because our retail business model does not involve maintaining a stock of retail inventory that would result in quick delivery and because of the custom nature of many of our furniture offerings, delivery to our customers usually occurs

about 30 days after an order is placed. We generally require a deposit at the time of order and collect the remaining balance when the furniture is delivered, at which time the sale is recognized. Coupled with the previously discussed store pre-opening costs, total start-up losses can range from \$300 to \$500 per store. While our retail expansion is initially costly, we believe our site selection and new store presentation will generally result in locations that operate at or above a retail break-even level within a reasonable period of time following store opening. Factors affecting the length of time required to achieve this goal on a store-by-store basis may include the level of brand recognition, the degree of local competition and the depth of penetration in a particular market. Even as new stores ramp up to break-even, we do realize additional wholesale sales volume that leverages the fixed costs in our wholesale business.

PART I-FINANCIAL INFORMATION-CONTINUEDBASSETT FURNITURE INDUSTRIES, INCORPORATED AND SUBSIDIARIESMay 28, 2016(Dollars in thousands except share and per share data)**Results of Operations – Periods ended May 28, 2016 compared with periods ended May 30, 2015:**

Net sales of furniture and accessories, logistics revenue, cost of furniture and accessories sold, selling, general and administrative (SG&A) expense, other charges and income from operations were as follows for the periods ended May 28, 2016 and May 30, 2015:

	Quarter Ended May 28, 2016		May 30, 2015		Six Months Ended May 28, 2016		May 30, 2015	
Sales revenue:								
Furniture and accessories	\$92,990	87.2 %	\$99,467	89.2 %	\$185,392	86.8 %	\$189,015	92.5 %
Logistics revenue	13,677	12.8 %	12,086	10.8 %	28,148	13.2 %	15,345	7.5 %
Total sales revenue	106,667	100.0%	111,553	100.0%	213,540	100.0%	204,360	100.0%
Cost of furniture and accessories sold	42,419	39.8 %	46,921	42.1 %	84,405	39.5 %	88,851	43.5 %
SG&A expenses	58,088	54.5 %	57,425	51.5 %	117,045	54.8 %	104,900	51.3 %
New store pre-opening costs	307	0.2 %	44	0.0 %	446	0.2 %	44	0.0 %
Other charges	-	0.0 %	449	0.4 %	-	0.0 %	974	0.5 %
Income from operations	\$5,853	5.5 %	\$6,714	6.0 %	\$11,644	5.5 %	\$9,591	4.7 %

Quarterly Analysis of Results

On a consolidated basis, we reported total sales revenue for the second quarter of 2016 of \$106,667 as compared to \$111,553 for the second quarter of 2015. Total revenues for the second quarter of 2016 include \$13,677 of logistics revenue for the quarter as compared to \$12,086 for the second quarter of 2015. Revenue from sales of furniture and accessories, net of estimates for returns and allowances, for the second quarter of 2016 were \$92,990, a decrease of \$6,477, or 6.5%, from the second quarter of 2015. Gross profit on the sale of furniture and accessories for the second quarter of 2016 was \$50,571, or 54.4% of the respective revenue, as compared with \$52,546, or 52.8%, for the comparable prior year period. Improved margins at wholesale were partially offset by lower margins at retail resulting from store closure activity and increased discounting of clearance items in preparation for a significant product rollout

for the Memorial Day holiday promotion. SG&A expenses as a percentage of sales increased due to reduced leverage of fixed charges due to lower sales. Operating income was \$5,853 for the second quarter of 2016 as compared to \$6,714 for the second quarter of 2015, a decrease of \$861.

Year-to-date Analysis of Results

On a consolidated basis, we reported total sales revenue for the first half of 2016 of \$213,540 as compared to \$204,360 for the first half of 2015. Total revenues for the first half of 2016 include \$28,148 of logistics revenue for the full six months as compared to \$15,345 for the first half of 2015 from the date of our acquisition of Zenith, February 2, 2015, through May 30, 2015. Revenue from sales of furniture and accessories, net of estimates for returns and allowances, for the first half of 2016 were \$185,392, a decrease of \$3,623, or 1.9%, from the first half of 2015. Gross profit on the sale of furniture and accessories for the first half of 2016 was \$100,987, or 54.5% of the respective revenue, as compared with \$100,164, or 53.0%, for the comparable prior year period. Improved margins at wholesale were partially offset by lower margins at retail resulting from store closure activity and increased discounting of clearance items in preparation for a significant product rollout for the Memorial Day holiday promotion. SG&A expenses as a percentage of sales increased primarily due to the inclusion of Zenith for the full six months of 2016 as compared to four months for 2015. Zenith is a service business with all operating costs being included in SG&A expenses. Operating income was \$11,644 for the first half of 2016 as compared to \$9,591 for the first half of 2015, an increase of \$2,053. In addition, the first half of 2015 included \$525 of charges related to the closing of our Company-owned retail store in Memphis, Tennessee, and a management restructuring charge of \$449 for severance costs related to the departure of a former executive. Also, Zenith contributed \$1,405 to our operating income for the full first half of 2016 compared to \$1,109 for four months of operations following its acquisition in the first half of 2015.

PART I-FINANCIAL INFORMATION-CONTINUED

BASSETT FURNITURE INDUSTRIES, INCORPORATED AND SUBSIDIARIES

May 28, 2016

(Dollars in thousands except share and per share data)

Segment Information

We have strategically aligned our business into three reportable segments as described below:

Wholesale. The wholesale home furnishings segment is involved principally in the design, manufacture, sourcing, sale and distribution of furniture products to a network of Bassett stores (Company-owned and licensee-owned retail stores) and independent furniture retailers. Our wholesale segment includes our wood and upholstery operations as well as all corporate selling, general and administrative expenses, including those corporate expenses related to both Company- and licensee-owned stores. We eliminate the sales between our wholesale and retail segments as well as the imbedded profit in the retail inventory for the consolidated presentation in our financial statements. Also included in our wholesale segment are our short-term investments and our holdings of retail real estate previously leased as licensee stores. The earnings and costs associated with these assets are included in other income (loss), net, in our condensed consolidated statements of income.

Retail – Company-owned stores. Our retail segment consists of Company-owned stores and includes the revenues, expenses, assets and liabilities (including real estate) and capital expenditures directly related to these stores.

Logistical services. With our acquisition of Zenith on February 2, 2015, we created the logistical services operating segment which reflects the operations of Zenith. In addition to providing shipping, delivery and warehousing services for the Company, Zenith also provides similar services to other customers, primarily in the furniture industry. Revenue from the performance of these services to other customers is included in logistical services revenue in our condensed consolidated statement of income. Zenith's operating costs are included in selling, general and administrative expenses. Amounts charged by Zenith to the Company for transportation and logistical services prior to February 2, 2015 are included in selling, general and administrative expenses, and our equity in the earnings of Zenith prior to the date of acquisition is included in other income (loss), net, in the accompanying statements of income.

The following tables illustrate the effects of various intercompany eliminations on income (loss) from operations in the consolidation of our segment results:

	Quarter Ended May 28, 2016				
	Wholesale	Retail	Logistics	Eliminations	Consolidated
Sales revenue:					
Furniture & accessories	\$59,906	\$61,943	\$-	\$ (28,859)	(1) \$ 92,990
Logistics	-	-	23,810	(10,133)	(2) 13,677
Total sales revenue	59,906	61,943	23,810	(38,992)	106,667
Cost of furniture and accessories sold	39,636	31,641	-	(28,858)	(3) 42,419
SG&A expense	15,936	29,614	23,149	(10,611)	(4) 58,088
New store pre-opening costs	-	307	-	-	307
Income from operations	\$4,334	\$381	\$661	\$ 477	\$ 5,853

	Quarter Ended May 30, 2015				
	Wholesale	Retail	Logistics	Eliminations	Consolidated
Sales revenue:					
Furniture & accessories	\$66,705	\$63,921	\$-	\$ (31,159)	(1) \$ 99,467
Logistics	-	-	21,958	(9,872)	(2) 12,086
Total sales revenue	66,705	63,921	21,958	(41,031)	111,553
Cost of furniture and accessories sold	44,816	32,164	-	(30,059)	(3) 46,921
SG&A expense	17,093	29,742	20,931	(10,341)	(4) 57,425
New store pre-opening costs	-	44	-	-	44
Income from operations (5)	\$4,796	\$1,971	\$1,027	\$ (631)	\$ 7,163

PART I-FINANCIAL INFORMATION-CONTINUEDBASSETT FURNITURE INDUSTRIES, INCORPORATED AND SUBSIDIARIESMay 28, 2016(Dollars in thousands except share and per share data)

	Six Months Ended May 28, 2016					Consolidated
	Wholesale	Retail		Eliminations		
Sales revenue:						
Furniture & accessories	\$ 119,482	\$ 123,538	\$-	\$ (57,628)	) (1)	\$ 185,392
Logistics	-	-	48,489	(20,341)	) (2)	28,148
Total sales revenue	119,482	123,538	48,489	(77,969)	)	213,540
Cost of furniture and accessories sold	78,934	62,956	-	(57,485)	) (3)	84,405
SG&A expense	31,816	59,439	47,084	(21,294)	) (4)	117,045
New store pre-opening costs	-	446	-	-		446
Income from operations (5)	\$8,732	\$697	\$1,405	\$ 810		\$ 11,644

	Six Months Ended May 30, 2015					Consolidated
	Wholesale	Retail		Eliminations		
Sales revenue:						
Furniture & accessories	\$ 125,510	\$ 121,104	\$-	\$ (57,599)	) (1)	\$ 189,015
Logistics	-	-	27,957	(12,612)	) (2)	15,345
Total sales revenue	125,510	121,104	27,957	(70,211)	)	204,360
Cost of furniture and accessories sold	84,798	60,564	-	(56,511)	) (3)	88,851
SG&A expense	32,989	58,567	26,938	(13,594)	) (4)	104,900
New store pre-opening costs	-	44	-	-		44
Income from operations (5)	\$7,723	\$1,929	\$1,019	\$ (106)	)	\$ 10,565

(1) Represents the elimination of sales from our wholesale segment to our Company-owned BHF stores.

(2) Represents the elimination of logistical services billed to our wholesale and retail segments.

(3) Represents the elimination of purchases by our Company-owned BHF stores from our wholesale segment, as well as the change for the period in the elimination of intercompany profit in ending retail inventory.

(4) Represents the elimination of rent paid by our retail stores occupying Company-owned real estate, and the elimination of logistical services charged by Zenith to Bassett's retail and wholesale segments as follows:

Quarter Ended		Six Months Ended	
May 28, 2016	May 30, 2015	May 28, 2016	May 30, 2015

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Intercompany logistical services	\$(10,133)	\$(9,872)	\$(20,341)	\$(12,612)
Intercompany rents	(478)	(469)	(953)	(982)
Total SG&A expense elimination	\$(10,611)	\$(10,341)	\$(21,294)	\$(13,594)

(5) Excludes the effects of asset impairment charges and lease exit costs, which are not allocated to our segments.

PART I-FINANCIAL INFORMATION-CONTINUEDBASSETT FURNITURE INDUSTRIES, INCORPORATED AND SUBSIDIARIESMay 28, 2016(Dollars in thousands except share and per share data)

The following is a discussion of operating results for our wholesale, retail and logistical services segments:

Wholesale segment

Results for the wholesale segment for the three months ended May 28, 2016 and May 30, 2015 are as follows:

	Quarter Ended		May 30, 2015		Six Months Ended		May 30, 2015	
	May 28, 2016				May 28, 2016			
Net sales	\$59,906	100.0 %	\$66,705	100.0 %	\$119,482	100.0 %	\$125,510	100.0 %
Gross profit	20,270	33.8 %	21,889	32.8 %	40,548	33.9 %	40,712	32.4 %
SG&A expenses	15,936	26.5 %	17,093	25.6 %	31,816	26.6 %	32,989	26.3 %
Income from operations	\$4,334	7.3 %	\$4,796	7.2 %	\$8,732	7.3 %	\$7,723	6.2 %

Quarterly Analysis of Results - Wholesale

Net sales for the wholesale segment were \$59,906 for the second quarter of 2016 as compared to \$66,705 for the second quarter of 2015, a decrease of \$6,799 or 10%. This sales decrease was driven by a 9.8% decrease in shipments to the BHF store network along with a 13% decrease in open market shipments (outside the BHF store network). The decrease in the sales to the BHF network and the open market was primarily due to general softness at retail. In addition, sales to the open market were impacted by lower sales of the HGTV Home Collection brand that was discontinued in late 2015. Gross margins for the wholesale segment increased to 33.8% for the second quarter of 2016 as compared to 32.8% for the second quarter of 2015 driven largely by higher margins in the imported wood operation from favorable ocean freight and lower impact from discounting in 2016, as we were exiting the open market HGTV Home Collection brand in 2015. In addition, gross margins in the upholstery operation improved due to improved pricing strategies coupled with favorable raw material costs. SG&A as a percentage of sales increased to 26.5% as compared to 25.6% for the second quarter of 2015 primarily due to reduced leverage of fixed costs from lower sales levels partially offset by lower incentive compensation expenses of \$489 and bad debt costs of \$319. Operating

income was \$4,334 or 7.3% of sales as compared to \$4,796 or 7.2% of sales in the prior year quarter.

Year-to-date Analysis of Results - Wholesale

Net sales for the wholesale segment were \$119,482 for the first half of 2016 as compared to \$125,510 for the first half of 2015, a decrease of \$6,028 or 4.8%. This sales decrease was driven by a 2.9% decrease in shipments to the BHF store network along with a 9.3% decrease in open market shipments (outside the BHF store network). The decrease in sales to the BHF network and the open market was primarily due to general softness at retail. In addition, sales to the open market were impacted by lower sales of the HGTV Home Collection brand that was discontinued in late 2015. Gross margins for the wholesale segment increased to 33.9% for the first half of 2016 as compared to 32.4% for the first half of 2015 driven largely by higher margins in the imported wood operation from favorable ocean freight and lower impact from discounting, as we were exiting the open market HGTV Home Collection brand in 2015. In addition, gross margins in the upholstery operation improved due to improved pricing strategies coupled with favorable raw material costs. SG&A as a percentage of sales increased to 26.6% as compared to 26.3% for the first half of 2015 primarily due to reduced leverage of fixed costs from lower sales levels. The prior year period also included \$209 of costs associated with the acquisition of Zenith Freight Lines, LLC. Operating income for the first half of 2016 was \$8,732 or 7.3% of sales as compared to \$7,723 or 6.2% of sales in the comparable prior year period.

PART I-FINANCIAL INFORMATION-CONTINUEDBASSETT FURNITURE INDUSTRIES, INCORPORATED AND SUBSIDIARIESMay 28, 2016(Dollars in thousands except share and per share data)

Wholesale shipments by type:	Quarter Ended			Six Months Ended				
	May 28, 2016		May 30, 2015		May 28, 2016		May 30, 2015	
Wood	\$22,210	37.1 %	\$24,878	37.3 %	\$44,442	37.2 %	\$45,191	36.0 %
Upholstery	36,806	61.4 %	41,042	61.5 %	73,568	61.6 %	78,914	62.9 %
Other	890	1.5 %	785	1.2 %	1,472	1.2 %	1,405	1.1 %
Total	\$59,906	100.0 %	\$66,705	100.0 %	\$119,482	100.0 %	\$125,510	100.0 %

Wholesale Backlog

The dollar value of wholesale backlog, representing orders received but not yet shipped to dealers and Company stores, was \$10,094 at May 28, 2016 as compared with \$16,005 at May 30, 2015.

Retail – Company-owned stores segment

Results for the retail segment for the periods ended May 28, 2016 and May 30, 2015 are as follows:

	Quarter Ended		May 30, 2015		Six Months Ended		May 30, 2015	
	May 28, 2016				May 28, 2016			
Net sales	\$61,943	100.0 %	\$63,921	100.0 %	\$123,538	100.0 %	\$121,104	100.0 %
Gross profit	30,302	48.9 %	31,757	49.7 %	60,582	49.0 %	60,540	50.0 %
SG&A expenses	29,614	47.9 %	29,742	46.5 %	59,439	48.1 %	58,567	48.4 %
New store pre-opening costs	307	0.4 %	44	0.1 %	446	0.3 %	44	0.0 %
Income (loss) from operations	\$381	0.6 %	\$1,971	3.1 %	\$697	0.6 %	\$1,929	1.6 %

Results for comparable stores[†](56 stores for both the quarter and six months) are as follows:

	Quarter Ended		May 30, 2015		Six Months Ended		May 30, 2015	
	May 28, 2016				May 28, 2016			
Net sales	\$59,003	100.0%	\$61,192	100.0%	\$117,054	100.0%	\$115,965	100.0%
Gross profit	29,169	49.4 %	30,559	49.9 %	58,077	49.6 %	58,192	50.2 %
SG&A expenses	27,963	47.4 %	28,269	46.2 %	55,736	47.6 %	55,616	48.0 %
Income from operations	\$1,206	2.0 %	\$2,290	3.7 %	\$2,341	2.0 %	\$2,576	2.2 %

†“Comparable” stores include those locations that have been open and operated by the Company for all of each respective comparable period.

PART I-FINANCIAL INFORMATION-CONTINUEDBASSETT FURNITURE INDUSTRIES, INCORPORATED AND SUBSIDIARIESMay 28, 2016(Dollars in thousands except share and per share data)

Results for all other stores are as follows:

	Quarter Ended				Six Months Ended			
	May 28, 2016		May 30, 2015		May 28, 2016		May 30, 2015	
Net sales	\$2,940	100.0%	\$2,729	100.0%	\$6,484	100.0%	\$5,139	100.0%
Gross profit	1,133	38.5 %	1,198	43.9 %	2,505	38.6 %	2,348	45.7 %
SG&A expenses	1,651	56.2 %	1,473	54.0 %	3,703	57.1 %	2,951	57.4 %
New store pre-opening costs	307	10.4 %	44	1.6 %	446	6.9 %	44	0.9 %
Loss from operations	\$(825)	-28.1 %	\$(319)	-11.7 %	\$(1,644)	-25.4 %	\$(647)	-12.6 %

Quarterly Analysis of Results - Retail

Net sales for the 58 Company-owned BHF stores were \$61,943 for the second quarter of 2016 as compared to \$63,921 for the second quarter of 2015, a decrease of \$1,978 or 3.1%. The decrease was primarily due to a \$2,189 or 3.6% decrease in comparable store sales partially offset by a \$211 increase in non-comparable store sales.

While we do not recognize sales until goods are delivered to the consumer, management tracks written sales (the retail dollar value of sales orders taken, rather than delivered) as a key store performance indicator. Written sales for comparable stores decreased by 3.9% for the second quarter of 2016 as compared to the second quarter of 2015. However, comparable store written sales for the 12-day Memorial Day promotional period increased 24% as compared to the 2015 promotional period.

The consolidated retail operating income for the second quarter of 2016 was \$381 as compared to \$1,971 for the second quarter of 2015. The 56 comparable stores generated operating income of \$1,206 for the quarter, or 2.0% of sales, as compared to \$2,290, or 3.7% of sales, for the prior year quarter. Gross margins for comparable stores were 49.4% for the second quarter of 2016 compared to 49.9% for the second quarter of 2015. Lower gross margins were due primarily to increased discounting of clearance items in preparation for a significant product rollout for the Memorial Day holiday promotion. SG&A expenses for comparable stores decreased \$306 to \$27,936 or 47.4% of

sales as compared to 46.2% of sales for the second quarter of 2015. This increase in SG&A as a percentage of sales was primarily driven by reduced leverage of fixed costs from lower sales levels.

Losses from the non-comparable stores in the second quarter of fiscal 2016 were \$825 compared with \$319 for the second quarter of fiscal 2015, an increase of \$506. The loss during the second quarter of 2016 included \$307 of pre-opening costs recognized in the quarter primarily associated with the Sterling, Virginia store which opened at the end of the second quarter of 2016. These costs include rent, training costs and other payroll-related costs specific to a new store location incurred during the period leading up to its opening and generally range between \$100 to \$300 per store based on the overall rent costs for the location and the period between the time when the Company takes possession of the physical store space and the time of the store opening. Also included in the non-comparable store loss for the second quarter of 2016 are losses arising from the closure of our stores in Egg Harbor, New Jersey and Fountain Valley, California.

We incur losses in the first two to three months of operation following a store opening as sales are not recognized in the income statement until the furniture is delivered to its customers resulting in operating expenses without the normal sales volume. Because we do not maintain a stock of retail inventory that would result in quick delivery, and because of the custom nature of the furniture offerings, such deliveries are generally not made until after 30 days from when the furniture is ordered by the customer. Coupled with the pre-opening costs, total start-up losses typically amount to \$300 to \$500 per store. We had no post-opening losses in the second quarter of 2016.

Each addition to our Company-owned store network results in incremental fixed overhead costs, primarily associated with local store personnel, occupancy costs and warehousing expenses. The incremental SG&A expenses associated with each new store will be ongoing.

PART I-FINANCIAL INFORMATION-CONTINUED

BASSETT FURNITURE INDUSTRIES, INCORPORATED AND SUBSIDIARIES

May 28, 2016

(Dollars in thousands except share and per share data)

Year-to-date Analysis of Results - Retail

Net sales for the 58 Company-owned BHF stores were \$123,538 for the first half of 2016 as compared to \$121,104 for the first half of 2015, an increase of \$2,434 or 2.0%. The increase was due to a \$1,089 or 0.9% increase in comparable store sales coupled with a \$1,345 increase in non-comparable store sales.

While we do not recognize sales until goods are delivered to the consumer, management tracks written sales (the retail dollar value of sales orders taken, rather than delivered) as a key store performance indicator. Written sales for comparable stores decreased by 2.8% for the first half of 2016 as compared to the first half of 2015.

The consolidated retail operating income for the first half of 2016 was \$697 as compared to \$1,929 for the first half of 2015. The 56 comparable stores generated operating income of \$2,341 for the six months ended May 28, 2016, or 2.0% of sales, as compared to \$2,576, or 2.3% of sales, for the comparable prior year period. Gross margins for comparable stores were 49.6% for the first half of 2016 compared to 50.2% for the first half of 2015. Lower gross margins were due primarily to increased discounting of clearance items in preparation for a significant product rollout for the Memorial Day holiday promotion. Also, Company-owned stores experienced increased clearance activity in reducing imported wood furniture placements to make room for more upholstery on its retail floors. SG&A expenses for comparable stores increased \$120 to \$55,736 or 47.6% of sales as compared to 48.0% of sales for the first half of 2015. This decrease as a percentage of sales is primarily due to greater leverage of fixed costs due to higher sales volumes.

Losses from the non-comparable stores in the first half of fiscal 2016 were \$1,644 compared with \$647 for the first half of fiscal 2015, an increase of \$997. The loss for the six months ended May 28, 2016 included \$446 of pre-opening costs recognized in the first half of 2016 primarily associated with the Sterling, Virginia store which opened at the end of the second quarter of 2016. These costs include rent, training costs and other payroll-related costs specific to a new store location incurred during the period leading up to its opening and generally range between \$100 to \$300 per store based on the overall rent costs for the location and the period between the time when the Company takes possession of the physical store space and the time of the store opening. Also included in the non-comparable store loss for the first half of 2016 are losses arising from the closure of our stores in Tucson, Arizona; Egg Harbor, New Jersey and Fountain Valley, California.

We incur losses in the first two to three months of operation following a store opening as sales are not recognized in the income statement until the furniture is delivered to its customers resulting in operating expenses without the normal sales volume. Because we do not maintain a stock of retail inventory that would result in quick delivery, and because of the custom nature of the furniture offerings, such deliveries are generally not made until 30 days after the furniture is ordered by the customer. Coupled with the pre-opening costs, total start-up losses typically amount to \$300 to \$500 per store. We had no post-opening losses for the six months ended May 28, 2016.

Each addition to our Company-owned store network results in incremental fixed overhead costs, primarily associated with local store personnel, occupancy costs and warehousing expenses. The incremental SG&A expenses associated with each new store will be ongoing.

Retail Backlog

The dollar value of our retail backlog, representing orders received but not yet delivered to customers, was \$26,471, or an average of \$456 per open store at May 30, 2016 as compared with was \$30,225, or an average of \$512 per open store at May 30, 2015.

PART I-FINANCIAL INFORMATION-CONTINUED

BASSETT FURNITURE INDUSTRIES, INCORPORATED AND SUBSIDIARIES

May 28, 2016

(Dollars in thousands except share and per share data)

Logistical services segment

Results for our logistical services segment for the periods ended May 28, 2016 and May 30, 2015 are as follows:

	Quarter Ended		Six Months Ended					
	May 28, 2016	May 30, 2015	May 28, 2016	May 30, 2015 (1)				
Logistical services revenue	\$23,810	100.0%	\$21,958	100.0%	\$48,489	100.0%	\$27,957	100.0%
Operating expenses	23,149	97.2 %						