

ETHAN ALLEN INTERIORS INC
Form 10-K
August 19, 2010
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

(Mark One)

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

For the fiscal year ended June 30, 2010

OR

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

For the transition period from _____ to _____

Commission file number 1-11692

Ethan Allen Interiors Inc.

(Exact name of registrant as specified in its charter)

Delaware

(State or other jurisdiction of incorporation or organization)

06-1275288

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

Ethan Allen Drive, Danbury, CT

(Address of principal executive offices)

06811

(Zip Code)

Registrant's telephone number, including area code **(203) 743-8000**

Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class	Name of Each Exchange On Which Registered
Common Stock, \$.01 par value	New York Stock Exchange, Inc.

Securities registered pursuant to Section 12(g) of the Act:

None

(Title of Class)

Indicate by check mark if the Registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes No

Indicate by check mark if the Registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes No

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes 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 (§232.405 of this chapter) during the preceding 12 months (or such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of Registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this

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Form 10-K or any amendment to this Form 10-K.

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

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 Act). Yes No

The aggregate market value of the Registrant's common stock, par value \$.01 per share, held by non-affiliates (based upon the closing sale price on the New York Stock Exchange) on December 31, 2009, (the last day of the Registrant's most recently completed second fiscal quarter) was approximately \$388,065,187. As of July 31, 2010, there were 28,740,575 shares of the Registrant's common stock, par value \$.01 per share, outstanding.

DOCUMENTS INCORPORATED BY REFERENCE: The Registrant's definitive Proxy Statement for the 2010 Annual Meeting of stockholders, which will be filed with the Securities and Exchange Commission pursuant to Regulation 14A of the Securities Exchange Act of 1934, is incorporated by reference into Part III hereof.

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PART I

Item 1. Business

Background

Incorporated in Delaware in 1989, Ethan Allen Interiors Inc., through its wholly-owned subsidiary, Ethan Allen Global, Inc., and Ethan Allen Global, Inc.'s subsidiaries (collectively, We, Us, Our, Ethan Allen or the Company), is a leading manufacturer and retailer of quality home furnishings and accessories, offering a full complement of home decorating and design solutions through one of the country's largest home furnishing retail networks. We refer to our Ethan Allen retail outlets as design centers instead of stores to better reflect these expanded capabilities. We have made, and continue to make, considerable investment in our business in order to expand and improve our interior design capabilities and to leverage our domestic manufacturing and logistics operations. The Company was founded in 1932 and has sold products under the Ethan Allen brand name since 1937.

Mission Statement

Our primary business objective is to provide our customers with a convenient, full-service, one-stop shopping solution for their home decorating needs by offering stylish, high-quality products at good value. In order to meet our stated objective, we have developed and adhere to a focused and comprehensive business strategy. The elements of this strategy, each of which is integral to our solutions-based philosophy, include (i) our vertically integrated operating structure, (ii) our stylish products and related marketing initiatives, (iii) our retail design center network, (iv) our people, and (v) our focus on providing design solutions.

Operating Segments

Our products are sold through a dedicated network of 281 retail design centers. As of June 30, 2010, the Company operated 145 design centers (our retail segment) and our independent retailers operated 136 design centers (as compared to 159 and 134, respectively, at the end of the prior fiscal year). Our wholesale segment net sales include sales to our retail segment and sales to our independent retailers. Our retail segment net sales accounted for 74% of our consolidated net sales in fiscal 2010 while wholesale segment net sales to independent retailers accounted for 26%. Our net sales to the ten largest independent retailers, who operate 68 design centers, accounted for approximately 15% of our consolidated net sales in fiscal 2010.

Our wholesale and retail operating segments represent strategic business areas of our vertically integrated business that operate separately and provide their own distinctive services (further outlined below). This enables us to more effectively offer our complete line of home furnishings and accessories and more efficiently control quality and cost. For certain financial information regarding our operating segments, see Note 16 to the Consolidated Financial Statements included under Item 8 of this Annual Report and incorporated herein by reference.

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While the manner in which our home furnishings and accessories are marketed and sold is consistent between our wholesale and retail segments, the nature of the underlying recorded sales (i.e. wholesale versus retail) and the specific services that each operating segment provides (i.e. wholesale manufacturing, sourcing, and distribution versus retail selling) are different. Within the wholesale segment, we maintain revenue information according to each respective product line (i.e. case goods, upholstery, or home accessories and other). Sales of case good items include, but are not limited to, beds, dressers, armoires, tables, chairs, buffets, entertainment units, home office furniture, and wooden accents. Sales of upholstery home furnishing items include sleepers, recliners, chairs, sofas, loveseats, cut fabrics and leather. Skilled craftsmen cut, sew and upholster custom-designed upholstery items which are available in a variety of frame and fabric options. Home accessory and

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other items include window treatments, wall decor, lighting, clocks, bedding and bedspreads, decorative accessories, area rugs, and home and garden furnishings.

Revenue information by product line is not as easily determined within the retail segment. However, because wholesale sales are matched, for the most part, to incoming orders, we believe that the allocation of retail sales by product line would be similar to that of the wholesale segment.

We evaluate performance of the respective segments based upon revenues and operating income. Inter-segment eliminations result, primarily, from the wholesale sale of inventory to the retail segment, including the related profit margin.

Wholesale Segment Overview:

Wholesale net sales for each of the last three fiscal years are summarized below (in millions):

	Fiscal Year Ended June 30,		
	2010	2009	2008
Wholesale net sales	\$ 362.5	\$ 403.4	\$ 616.2

Wholesale net sales for each of the last three fiscal years, allocated by product line, were as follows:

	Fiscal Year Ended June 30,		
	2010	2009	2008
Case Goods	40%	41%	43%
Upholstered Products	46	41	40
Home Accessories and Other	14	18	17
	100%	100%	100%

The wholesale segment, principally involved in the development of the Ethan Allen brand, encompasses all aspects of design, manufacture, sourcing, sale, and distribution of our broad range of home furnishings and accessories. Wholesale revenue is generated upon the wholesale sale and shipment of our products to our network of independently operated design centers and Ethan Allen operated design centers (see Company operated retail comments below) through its national distribution center and one other smaller fulfillment center.

During the past year, independent retailers opened 12 new design centers (of which two were relocations), and closed seven design centers. We continue to promote the growth and expansion of our independent retailers through ongoing support in the areas of market analysis, site selection, and business development. As in the past, our independent retailers are required to enter into license agreements with us, which (i) authorize the use of certain Ethan Allen service marks and (ii) require adherence to certain standards of operation, including a requirement to fulfill related warranty service agreements. We are not subject to any territorial or exclusive retailer agreements in North America. The wholesale segment also develops and implements related marketing and brand awareness programs.

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Wholesale profitability includes (i) the wholesale gross margin, which represents the difference between the wholesale net sales price and the cost associated with manufacturing and/or sourcing the related product, and (ii) other operating costs associated with wholesale segment activities.

The Company's domestic manufacturing is included in the results of the wholesale segment. During fiscal years 2009 and 2010, we consolidated two upholstery plants and one case goods sawmill plant and dramatically reduced operations of another case goods plant. All redundant operations were moved into other existing plants, thereby improving overall utilization of our domestic manufacturing. During fiscal 2010, we also converted our domestic case goods manufacturing to custom operations. Case goods products are no longer produced to a

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forecast and held in inventory; but rather, are produced to specific customer orders with the options specified by our clients. We now operate three case goods plants (including one sawmill), three upholstery plants (two upholstery plants on our Maiden, North Carolina campus and one cut and sew plant in Mexico) and one home accessory plant. We also source selected case good, upholstery, and home accessory items from third-party suppliers located both domestically and outside the United States.

As of June 30, 2010, we maintained a wholesale backlog of \$57.0 million (as compared to \$20.6 million as of June 30, 2009) which is anticipated to be serviced in the first quarter of fiscal 2011. Backlog at a point in time is a result, primarily, of net orders booked in prior periods, manufacturing schedules, timing associated with the receipt of sourced product, and the timing and volume of wholesale shipments. Because orders may be rescheduled and/or canceled, the measure of backlog at a point in time may not necessarily be indicative of future sales performance.

For the twelve months ended June 30, 2010, net orders booked at the wholesale level, which includes orders generated by independently operated and Company operated design centers, totaled \$403.7 million as compared to \$398.5 million for the twelve months ended June 30, 2009. In any given period, net orders booked may be impacted by the timing of floor sample orders received in connection with new product introductions. New product offerings may be made available to the retail network at any time during the year, including in connection with our periodic retailer conferences.

Retail Segment Overview:

Retail net sales for each of the last three fiscal years are summarized below (in millions):

	Fiscal Year Ended June 30,		
	2010	2009	2008
Retail net sales	\$ 438.5	\$ 508.6	\$ 724.6

The retail segment sells home furnishings and accessories to consumers through a network of Company-operated design centers. During fiscal 2010 we acquired one design center from an independent retailer, opened four new design centers (of which three were relocations), and closed sixteen design centers. In addition, we recently initiated a program that provides the opportunity for Ethan Allen designers to work with independent interior design affiliates that apply and meet Ethan Allen standards. This program provides the opportunity for the Company to reach additional clients with over 1,300 interior designers (serving both Company operated and independent retail operations) not otherwise affiliated with Ethan Allen and compensates them for the incremental business. Retail revenue is generated upon the retail sale and delivery of our products to our retail customers through its network of 18 service centers (as of June 30, 2010). Retail profitability includes (i) the retail gross margin, which represents the difference between the retail net sales price and the cost of goods purchased from the wholesale segment, and (ii) other operating costs associated with retail segment activities.

We pursue further expansion of the Company-operated retail business by opening new design centers, relocating existing design centers and, when appropriate, acquiring design centers from independent retailers. The geographic distribution of retail design center locations is included under Item 2 of Part I of this Annual Report.

Products

Our strategy has been to position Ethan Allen as a preferred brand with superior style, quality and value while, at the same time, providing consumers with a comprehensive, one-stop shopping solution for their home furnishing and design needs. In carrying out our strategy, we continue to expand our reach to a broader consumer base through a diverse selection of attractively priced products, designed to complement one another, reflecting the popular trend toward eclectic home decorating. Regular product introductions, a broad range of styles and selections within our custom upholstery and case good lines, new finishes for, and redesigns of, previous product introductions, and expanded product offerings to accommodate today's home decorating trends, continue to

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redefine Ethan Allen, positioning us as a leader in style. During fiscal 2010, we further enhanced the opportunities to create individualized design solutions for our clients with the conversion of our entire domestic case goods products to custom, made-to-order manufacturing.

In an effort to more effectively position ourselves as a provider of interior design solutions, we offer a merchandising strategy which involves the grouping of our product offerings, previously categorized by collection, into seven distinct product lifestyles, each reflecting the diversity and eclecticism that we believe represents the best in American design. In accordance with this merchandising strategy, new products are designed and developed to reflect unique elements applicable to one or more of the following lifestyles: Country House; Estate; Glamour; Global; Loft; Metro; and Villa.

All of our case goods, upholstered products, and home accessories are styled with distinct design characteristics. Home accessories play an important role in our marketing strategy as they enable us to offer the consumer the convenience of one-stop shopping by creating a comprehensive home furnishing solution. The interior of our design centers is organized to facilitate display of our product offerings, both in room settings that project the category lifestyle and by product grouping to facilitate comparisons of the styles and tastes of our clients. To further enhance the experience, technology is used to expand the range of products viewed by including content from our award-winning website and advanced large touch-screen flat panel displays.

We continuously monitor changes in home design trends through attendance at international industry events and fashion shows, internal market research, and regular communication with our retailers and design center design consultants who provide valuable input on consumer tendencies. We believe that the observations and input gathered enables us to incorporate appropriate style details into our products to react quickly to changing consumer tastes. For example, since 2006, 58% of our current product lines are new. Much of the balance has been refined and enhanced through product redesign, additions, deletions, and/or finish changes. Such undertakings are indicative of our ability to adapt to the current consumer trend toward more casual and eclectic lifestyles while, at the same time, maintaining a classic appeal.

In response to the demands of our clients for even greater values during the recession of 2009 and 2010, the Company began offering special savings on many products during specified marketing initiatives. This was a necessary move away from our discipline of an everyday best price on all of our product offerings. While we believe that a stable uniform everyday best price approach best allows us to differentiate ourselves through strategies focused on customer credibility and excellence in service, we recognize that in today's economy, consumers demand the even greater values obtained through our periodic savings events. We will continue to monitor consumer sentiments and adjust our promotional activity accordingly.

Product Sourcing Activities

We are one of the largest manufacturers of home furnishings in the United States, manufacturing and/or assembling approximately 70% of our products in our six domestic manufacturing facilities. Our facilities are located in the Northeast and Southeast regions of the United States where they are close to sources of raw materials and skilled craftsmen. Our domestic upholstery manufacturing is supported by our high quality upholstery cut and sew plant in Mexico that doubled in size during fiscal 2010. The balance of our production is outsourced according to our own internally-developed design specifications, through third-party suppliers, most of which are located outside the United States. These suppliers, primarily in Asia, have been carefully selected and generally have supplied us for many years. We believe that strategic investment in our manufacturing facilities, combined with an appropriate level of outsourcing through both foreign and domestic suppliers, will accommodate future sales growth and allow us to maintain an appropriate degree of control over cost, quality and service to our customers.

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We also take pride in our green initiatives that include, in select product offerings, the use of responsibly harvested Appalachian woods, water based finishes, organic textiles and recycled materials.

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Raw Materials and Other Suppliers

The most important raw materials we use in furniture manufacturing are lumber, veneers, plywood, hardware, glue, finishing materials, glass, mirrored glass, laminates, fabrics, foam, and filling material. The various types of wood used in our products include cherry, ash, oak, maple, prima vera, mahogany, birch and pine, substantially all of which are purchased domestically.

Fabrics and other raw materials are purchased both domestically and outside the United States. We have no significant long-term supply contracts, and have sufficient alternate sources of supply to prevent disruption in supplying our operations. We maintain a number of sources for our raw materials which, we believe, contributes to our ability to obtain competitive pricing. Lumber prices fluctuate over time based on factors such as weather and demand, which, in turn, impact availability. Higher material prices could have an adverse effect on margins.

Appropriate amounts of lumber and fabric inventory are typically stocked so as to maintain adequate production levels. We believe that our sources of supply for these materials are sufficient and that we are not dependent on any one supplier.

We enter into standard purchase agreements with certain foreign and domestic suppliers to source selected case good, upholstery, and home accessory items. The terms of these arrangements are customary for the industry and do not contain any long-term contractual obligations on our behalf. We believe we maintain good relationships with our suppliers.

Distribution and Logistics

We continued to streamline our logistics operations during fiscal 2010 in both our wholesale and retail segments.

In the wholesale segment, the conversion of our domestic case goods to custom manufacturing enabled us to consolidate the warehousing and distribution of our products through one primary distribution center, owned by the Company, strategically located in the Southeast United States. This national distribution center is supported by a smaller Company-owned order fulfillment center located in the South Central United States. Our primary distribution center provides efficient cross-dock operations to receive and ship product from our manufacturing facilities and third-party suppliers to our network of retail design centers and retail service centers. While we manufacture to custom order the majority of our products, we also stock selected case goods, upholstery and accessories to provide for quick delivery of in-stock items and to allow for more efficient production runs. We have established two large supermarkets of parts within our existing manufacturing sites for the components used in our custom case goods manufacturing.

Wholesale shipments utilize our own fleet of trucks and trailers or are subcontracted with independent carriers. Approximately 45% of our fleet (trucks and trailers) is leased under operating lease agreements with remaining terms ranging from one to 27 months.

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Our policy is to sell our products at the same delivered cost to all Company-operated and independently operated design centers nationwide, regardless of their shipping point. The adoption of this policy has created pricing credibility with our wholesale customers and provided our retail network the opportunity to achieve more consistent margins as fluctuations attributable to the cost of shipping have been eliminated. Further, this policy has eliminated the need for our independent retailers to carry significant amounts of inventory in their own warehouses. As a result, we obtain more accurate end-consumer product demand information.

Retail service centers are operated by the Company and the independent retailers to prepare products for delivery into clients' homes. We continued to streamline Company-operated service centers and reduced the total number

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from 26 at the end of fiscal 2009 to 18 at the end of fiscal 2010. We continue to evaluate the entire logistics and distribution model to further improve these operations.

Marketing Programs

Our marketing and advertising strategies are developed to drive traffic into our network of design centers or to shop online at ethanallen.com. We believe these strategies give Ethan Allen a strong competitive advantage in the home furnishings industry. We create and coordinate print and television campaigns nationally, as well as assist in local marketing and promotional efforts. The Company's network of approximately 280 retail design centers and more than 1,300 independent members of the Interior Design Affiliate program benefit from these marketing efforts, and we believe these efforts position us to consistently fulfill our brand promise.

Our in-house team of advertising specialists in collaboration with outside professionals sends consistent, clear messages that Ethan Allen is a leader in style and service, with everything for the well-designed home. We use several forms of media to accomplish this, including television (national and local), direct mail, newspapers, shelter magazines, email, and online, at ethanallen.com. A strong national email marketing campaign delivers emails and design and product brochures to a growing database of clients.

Our national television and print advertising campaigns are designed to leverage our strong brand equity, finding creative and compelling ways to remind consumers of our tremendous range of products, services, special programs, and custom options. We believe that we consistently deliver the most cohesive national advertising campaign in the home furnishings industry. Coordinated local television and print, to the extent these media are utilized, serve to support our national programs.

The Ethan Allen direct mail magazine, which brands our product lifestyles and communicates the breadth of our products and services, is one of our most important marketing tools. We publish these magazines and sell them to Company and independently operated design centers who use demographic information collected through independent market research to target potential clients. Given the importance of this advertising medium, direct mail marketing lists are continually refined to target those consumers who are most likely to purchase, and improve the return on direct mail expenditures. Approximately 11 million copies of our direct mail magazine were distributed to consumers during fiscal 2010.

Our television advertising and direct mail efforts are supported by strong print campaigns. We also update our Style Book approximately every six months. In addition to its use as a catalog of our case goods and upholstery products, the Style Book is full of quality, design, and service stories, and looks and ideas to spark inspiration. This publication is a comprehensive and effective resource for clients.

The Company's award winning website, ethanallen.com, provides our customers and design associates a great way to shop and design with videos, feature stories, design and style solutions, and fresh, new looks. Visitors will find all our latest news and promotional information here too. The site's myprojects tool lets visitors create idea boards and room plans. If they like, a design professional from their local Ethan Allen design center can give them feedback.

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The website's Inspire section includes editorial features, new product stories, design trend information, decorating solutions, and a collection of creative films and TV clips showcasing the many looks of Ethan Allen. The As Seen In area shows visitors how Ethan Allen products have influenced style around the globe. Ethan Allen's direct mail magazines are viewable online with full browsing and shopping capabilities. In the Design section, visitors can find their own style with our style quiz and shop the full assortment of furnishings. Nearly all of Ethan Allen's products are now available for purchase online.

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We also have a robust and informative extranet available to our retailers and design professionals. It is the primary source of communication in and among members of our retail network. It provides information about every aspect of the business of Ethan Allen at retail, including advertising materials, prototype floor plan displays, and extensive product details.

Retail Design Center Network

Ethan Allen design centers are typically located in