

BASSETT FURNITURE INDUSTRIES INC

Form 10-Q

June 28, 2018

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF

THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended May 26, 2018

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. 000-00209

BASSETT FURNITURE INDUSTRIES, INCORPORATED

(Exact name of Registrant as specified in its charter)

Virginia

54-0135270

(State or other jurisdiction

(I.R.S. Employer

of incorporation or organization)

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, smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

| | | |
|-------------------------|---|-------------------------------------|
| Large Accelerated Filer | Accelerated Filer | <input checked="" type="checkbox"/> |
| Non-accelerated Filer | (Do not check if a smaller reporting company) | |
| | Smaller Reporting Company | |
| | Emerging Growth Company | |

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the

Exchange Act. _____

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 21, 2018, 10,735,929 shares of common stock of the Registrant were outstanding.

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BASSETT FURNITURE INDUSTRIES, INCORPORATED AND SUBSIDIARIES

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PART I - FINANCIAL INFORMATIONITEM 1. FINANCIAL STATEMENTSBASSETT FURNITURE INDUSTRIES, INCORPORATED AND SUBSIDIARIESCONDENSED CONSOLIDATED STATEMENTS OF INCOME AND RETAINED EARNINGSFOR THE PERIODS ENDED MAY 26, 2018 AND MAY 27, 2017 – UNAUDITED

(In thousands except per share data)

| | Quarter Ended | | Six Months Ended | |
|--|-------------------------|-------------------------|-------------------------|-------------------------|
| | May 26, 2018 | May 27, 2017 | May 26, 2018 | May 27, 2017 |
| Sales revenue: | | | | |
| Furniture and accessories | \$ 102,675 | \$ 100,294 | \$ 198,798 | \$ 193,992 |
| Logistics | 14,305 | 13,831 | 28,454 | 26,025 |
| Total sales revenue | 116,980 | 114,125 | 227,252 | 220,017 |
| Cost of furniture and accessories sold | 45,660 | 44,981 | 88,929 | 86,879 |
| Selling, general and administrative expenses excluding new store pre-opening costs | 65,456 | 61,075 | 129,707 | 119,599 |
| New store pre-opening costs | 201 | 469 | 903 | 1,275 |
| Income from operations | 5,663 | 7,600 | 7,713 | 12,264 |
| Gain on sale of investment | - | 3,267 | - | 3,267 |
| Impairment of investment in real estate | - | (1,084) | - | (1,084) |
| Other loss, net | (233) | (678) | (860) | (1,411) |
| Income before income taxes | 5,430 | 9,105 | 6,853 | 13,036 |
| Income tax expense | 1,141 | 3,263 | 3,477 | 4,333 |
| Net income | \$ 4,289 | \$ 5,842 | \$ 3,376 | \$ 8,703 |
| Retained earnings-beginning of period | 137,827 | 131,178 | 139,378 | 129,388 |
| Reclassification of certain tax effects from accumulated other comprehensive loss | - | - | 545 | - |
| Cash dividends | (1,182) | (1,073) | (2,365) | (2,144) |
| Retained earnings-end of period | \$ 140,934 | \$ 135,947 | \$ 140,934 | \$ 135,947 |

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| | | | | |
|----------------------------|--------|--------|--------|--------|
| Basic earnings per share | \$0.40 | \$0.55 | \$0.32 | \$0.82 |
| Diluted earnings per share | \$0.40 | \$0.54 | \$0.31 | \$0.81 |
| Dividends per share | \$0.11 | \$0.10 | \$0.22 | \$0.20 |

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 – CONTINUEDITEM 1. FINANCIAL STATEMENTSBASSETT FURNITURE INDUSTRIES, INCORPORATED AND SUBSIDIARIESCONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOMEFOR THE PERIODS ENDED MAY 26, 2018 AND MAY 27, 2017 – UNAUDITED(In thousands)

| | Quarter Ended | | Six Months Ended | |
|--|-----------------------------|-----------------------------|-----------------------------|-----------------------------|
| | May 26, 2018 | May 27, 2017 | May 26, 2018 | May 27, 2017 |
| Net income | \$4,289 | \$5,842 | \$3,376 | \$8,703 |
| Other comprehensive income: | | | | |
| Recognize prior service cost associated with Long Term Cash Awards (LTCA) | - | (932) | - | (932) |
| Amortization associated with Long Term Cash Awards (LTCA) | 31 | 24 | 62 | 24 |
| Income taxes related to LTCA | (8) | 350 | (16) | 350 |
| Amortization associated with supplemental executive retirement defined benefit plan (SERP) | 76 | 94 | 152 | 187 |
| Income taxes related to SERP | (19) | (36) | (38) | (71) |
| Other comprehensive income, net of tax | 80 | (500) | 160 | (442) |
| Total comprehensive income | \$4,369 | \$5,342 | \$3,536 | \$8,261 |

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 26, 2018 AND NOVEMBER 25, 2017

(In thousands)

| | (Unaudited) | |
|--------------------------------------|--------------------|-------------------|
| | May 26, | November |
| | 2018 | 25, |
| | | 2017 |
| <u>Assets</u> | | |
| Current assets | | |
| Cash and cash equivalents | \$ 22,549 | \$ 53,949 |
| Short-term investments | 23,125 | 23,125 |
| Accounts receivable, net | 20,619 | 19,640 |
| Inventories | 62,086 | 54,476 |
| Other current assets | 10,539 | 8,192 |
| Total current assets | 138,918 | 159,382 |
| | | |
| Property and equipment, net | 101,658 | 103,244 |
| | | |
| Deferred income taxes | 6,210 | 8,393 |
| Goodwill and other intangible assets | 28,616 | 17,351 |
| Other | 5,946 | 5,378 |
| Total long-term assets | 40,772 | 31,122 |
| Total assets | \$ 281,348 | \$ 293,748 |

Liabilities and Stockholders' Equity**Current liabilities**

| | | |
|-----------------------------------|---------------|---------------|
| Accounts payable | \$ 21,787 | \$ 21,760 |
| Accrued compensation and benefits | 13,195 | 14,670 |
| Customer deposits | 22,093 | 27,107 |
| Dividends payable | - | 3,759 |
| Current portion of long-term debt | 432 | 3,405 |
| Other accrued liabilities | 12,323 | 12,655 |
| Total current liabilities | 69,830 | 83,356 |

Long-term liabilities

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| | | |
|---|-------------------|-------------------|
| Post employment benefit obligations | 13,672 | 13,326 |
| Notes payable | 109 | 329 |
| Other long-term liabilities | 5,641 | 5,277 |
| Total long-term liabilities | 19,422 | 18,932 |
| Stockholders' equity | | |
| Common stock | 53,736 | 53,690 |
| Retained earnings | 140,934 | 139,378 |
| Additional paid-in capital | 382 | 962 |
| Accumulated other comprehensive loss | (2,956) | (2,570) |
| Total stockholders' equity | 192,096 | 191,460 |
| Total liabilities and stockholders' equity | \$ 281,348 | \$ 293,748 |

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 26, 2018 AND MAY 27, 2017 – UNAUDITED

(In thousands)

| | Six Months Ended | |
|---|-------------------------|-----------------------------|
| | May 26, 2018 | May 27, 2017 |
| Operating activities: | | |
| Net income | \$3,376 | \$8,703 |
| Adjustments to reconcile net income to net cash provided by (used in) operating activities: | | |
| Depreciation and amortization | 6,688 | 6,706 |
| Provision for asset impairment charge | - | 1,084 |
| Gain on sale of property and equipment | (136) | - |
| Gain on sale of investment | - | (3,267) |
| Tenant improvement allowance received from lessors | 860 | 715 |
| Deferred income taxes | 2,183 | 318 |
| Other, net | 794 | 960 |
| Changes in operating assets and liabilities: | | |
| Accounts receivable | 124 | (904) |
| Inventories | (3,689) | (4,535) |
| Other current assets | (2,311) | 2,128 |
| Customer deposits | (5,014) | (2,532) |
| Accounts payable and accrued liabilities | (3,045) | 116 |
| Net cash provided by (used in) operating activities | (170) | 9,492 |
| Investing activities: | | |
| Purchases of property and equipment | (7,662) | (9,172) |
| Proceeds from sales of property and equipment | 2,463 | 63 |
| Cash paid for business acquisition | (15,556) | - |
| Proceeds from sale of investment | - | 3,592 |
| Acquisition of retail licensee store | - | (655) |
| Other | - | 223 |
| Net cash used in investing activities | (20,755) | (5,949) |
| Financing activities: | | |
| Cash dividends | (6,124) | (5,363) |

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| | | |
|---|-----------------|-----------------|
| Proceeds from the exercise of stock options | 27 | 221 |
| Other issuance of common stock | 173 | - |
| Repurchases of common stock | (823) | (82) |
| Taxes paid related to net share settlement of equity awards | (522) | (474) |
| Repayments of notes payable | (3,206) | (3,191) |
| Net cash used in financing activities | (10,475) | (8,889) |
| Change in cash and cash equivalents | (31,400) | (5,346) |
| Cash and cash equivalents - beginning of period | 53,949 | 35,144 |
| Cash and cash equivalents - end of period | \$22,549 | \$29,798 |

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 26, 2018

(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. 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.

Revenues from logistical services are generated by our wholly-owned subsidiary, Zenith Freight Lines, LLC (“Zenith”). Sales of logistical services from Zenith to our wholesale and retail segments have been eliminated in consolidation, and Zenith’s operating costs and expenses are included in selling, general and administrative expenses in our condensed consolidated statements of income.

Lane Venture Acquisition

On December 21, 2017, we purchased certain assets and assumed certain liabilities of Lane Venture from Heritage Home Group, LLC. Lane Venture is being operated as a component of our wholesale segment (see Note 3, Business Combinations). Results of operations for the Lane Venture business are included in our condensed consolidated statements of income since the date of acquisition.

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 26, 2018 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 25, 2017.

Income Taxes and Impact of the Tax Cuts and Jobs Act

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.

On December 22, 2017, The Tax Cuts and Jobs Act (the “Act”) was signed into law. The Act reduced the federal statutory corporate income tax rate from 35% to 21% effective January 1, 2018 for all corporate taxpayers, while most other provisions of the Act take effect for fiscal years beginning on or after January 1, 2018. Therefore, we will compute our income tax expense for fiscal 2018 using a blended federal statutory rate of 22.2%. The 21% federal statutory rate, as well as certain other provisions of the Act including the elimination of the domestic manufacturing deduction and new limitations on certain business deductions, will apply to our 2019 fiscal year and thereafter.

The federal rate reduction has had a significant impact on our provision for income taxes for the three and six months ended May 26, 2018. Our effective tax rates for the three and six months ended May 26, 2018 of 21.3% and 51.4%, respectively, differ from the fiscal 2018 blended federal statutory rate of 22.2% primarily due to a discrete charge (benefit) of (\$155) and \$2,032, respectively, arising from the re-measurement of our deferred tax assets. Other items impacting our effective tax rate for the three and six months ended May 26, 2018 include the effects of state income taxes and various permanent differences including the favorable impacts of excess tax benefits on stock-based

compensation of \$16 and \$197, respectively, non-taxable life insurance proceeds of \$266 during the second quarter, and the Section 199: Domestic Production Activities Deduction.

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PART I-FINANCIAL INFORMATION-CONTINUED

BASSETT FURNITURE INDUSTRIES, INCORPORATED AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS-UNAUDITED

MAY 26, 2018

(Dollars in thousands except share and per share data)

Given the significance of the Act, the SEC staff issued Staff Accounting Bulletin No. 118 (“SAB 118”), which allows registrants to record provisional amounts during a one year “measurement period” similar to that used when accounting for business combinations. Per SAB 118, the measurement period is deemed to have an earlier end date when the registrant has obtained, prepared and analyzed the information necessary to finalize its accounting. During the measurement period, impacts of the updated tax law are expected to be recorded at the time a reasonable estimate for all, or a portion, of the effects can be made, and provisional amounts can be recognized and adjusted as information becomes available, prepared or analyzed.

SAB 118 states, that at each reporting period, companies must disclose the effects of the Act for areas where accounting is complete, disclose provisional amounts (or adjustments to provisional amounts) for the effects of the Act for areas where accounting is not complete but a reasonable estimate has been determined, and confirm areas where a reasonable estimate of the effects cannot yet be made, and therefore taxes are reflected in accordance with law prior to the enactment of the Act.

As of May 26, 2018, we were still assessing the overall impact that the Act will have on our financial statements and related disclosures. Therefore, the net charge for the re-measurement of our deferred tax assets was based on reasonable estimates and has been recorded as a provisional amount in accordance with SAB 118. We may alter our estimates during the remainder of fiscal 2018 as we continue to process data to finalize the underlying calculations and also analyze other provisions of the Act to determine if they will impact our effective tax rate in fiscal 2018 or in the future. We will continue to refine our adjustments through the permissible measurement period as described above.

Our effective tax rates for the three and six months ended May 27, 2017 of 35.8% and 33.2%, respectively, differed from the federal statutory rate of 35% primarily due to the effects of state income taxes and various permanent differences including the favorable impacts of excess tax benefits on stock-based compensation of \$327 during the six months ended May 27, 2017 and the Section 199: Domestic Production Activities Deduction.

Adoption of Accounting Standards Update No. 2018-02

The Act has also had a significant impact on the income tax effect of pension costs included in our accumulated other comprehensive loss at November 25, 2017 due to the reduction in Federal statutory rates. Therefore we have adopted Accounting Standards Update 2018-02 (see Note 14, Recent Accounting Pronouncements) effective as of the beginning of fiscal 2018 and have elected to reclassify the income tax effects of the Act from accumulated other comprehensive loss to retained earnings. Accordingly, during the six months ended May 26, 2018 we reclassified \$545 of tax benefits associated with pension costs from accumulated other comprehensive loss to retained earnings.

PART I-FINANCIAL INFORMATION-CONTINUED

BASSETT FURNITURE INDUSTRIES, INCORPORATED AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS-UNAUDITED

MAY 26, 2018

(Dollars in thousands except share and per share data)

3. Business Combinations

Acquisition of Lane Venture

On December 21, 2017, we purchased certain assets and assumed certain liabilities of Lane Venture from Heritage Home Group, LLC for \$15,556 in cash. Lane Venture is a manufacturer and distributor of premium outdoor furniture, and is now being operated as a component of our wholesale segment.

Under the acquisition method of accounting, the fair value of the consideration transferred 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.

The allocation of the fair value of the acquired business was based on a preliminary valuation. Our estimates and assumptions are subject to change as we obtain additional information for our estimates during the measurement period (up to one year from the acquisition date). The primary areas of the preliminary allocation of the fair value of consideration transferred that are not yet finalized relate to the fair values of certain tangible and intangible assets acquired and the residual goodwill. During the three months ended May 26, 2018, we recorded measurement period adjustments to increase the opening value of inventory and accrued liabilities by \$168 and \$38, respectively, resulting in a reduction of recognized goodwill of \$129. The preliminary allocation of the \$15,556 all-cash purchase price to the acquired assets and liabilities of the Lane Venture business, including measurement period adjustments, is as follows:

Allocation of the fair value of consideration transferred:
Identifiable assets acquired:

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| | |
|--|----------|
| Accounts receivable, net of reserve (Note 5) | \$1,357 |
| Inventory, net of reserve (Note 6) | 3,921 |
| Prepaid expenses and other current assets | 37 |
| Intangible assets | 7,360 |
| Total identifiable assets acquired | 12,675 |
| Liabilities assumed: | |
| Accounts payable | (357) |
| Other accrued liabilities | (852) |
| Total liabilities assumed | (1,209) |
| Net identifiable assets acquired | 11,466 |
| Goodwill | 4,090 |
| Total net assets acquired | \$15,556 |

Goodwill was determined based on the residual difference between the fair value of the consideration transferred and the value assigned to the tangible and intangible assets and liabilities recognized in connection with the acquisition and is deductible for tax purposes. Among the factors that contributed to a purchase price resulting in the recognition of goodwill are the expected synergies arising from combining the Company's manufacturing and distribution capabilities with Lane Venture's position in the outdoor furnishings market, a segment of the market not previously served by Bassett.

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

| Description | Useful | Fair |
|----------------------------------|------------|---------|
| | Life | |
| | In Years | Value |
| Trade name | Indefinite | \$6,848 |
| Customer relationships | 9 | 512 |
| Total acquired intangible assets | | \$7,360 |

The finite-lived intangible asset is being amortized on a straight-line basis over its estimated useful life. 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.

PART I-FINANCIAL INFORMATION-CONTINUED

BASSETT FURNITURE INDUSTRIES, INCORPORATED AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS-UNAUDITED

MAY 26, 2018

(Dollars in thousands except share and per share data)

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 Lane Venture acquisition totaled \$26 and \$254 during the three and six months ended May 26, 2018, respectively, and are included in selling, general and administrative expenses in the condensed consolidated statements of income. Additional acquisition costs related to Lane Venture are not expected to be significant during the remainder of fiscal 2018. The acquisition costs are primarily related to legal, accounting and valuation services.

The pro forma impact of the acquisition and the results of operations attributable to Lane Venture since the acquisition have not been presented because they are not material to our consolidated results of operations for the three and six month periods ended May 26, 2018 and May 27, 2017.

Retail Store Acquisition

During the quarter ended February 25, 2017, we acquired the operations of the Bassett Home Furnishings (“BHF”) store located in Columbus, Ohio for a purchase price of \$655. The store had been owned and operated by a licensee that had determined that continued ownership of a BHF store was no longer consistent with its future business objectives. We believe that Columbus, Ohio represents a viable market for a BHF store.

The purchase price was allocated as follows:

| | |
|-----------|-------|
| Inventory | \$343 |
|-----------|-------|

Goodwill 312

Purchase price \$655

The inputs into our valuation of the acquired assets reflect our market assumptions and are not observable. Consequently, the inputs are considered to be Level 3 inputs as specified in the fair value hierarchy in ASC 820, *Fair Value Measurements and Disclosures*. See Note 4.

The pro forma impact of the acquisition and the results of operations for the Columbus store since acquisition were not material to our consolidated results of operations for the three and six months ended May 27, 2017.

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.

Investments

Our short-term investments of \$23,125 at both May 26, 2018 and November 25, 2017 consisted of certificates of deposit (CDs) with original terms averaging ten months, bearing interest at rates ranging from 0.10% to 1.89%. At May 26, 2018, the weighted average remaining time to maturity of the CDs was approximately two months and the weighted average yield of the CDs was approximately 1.40%. 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 26, 2018 and November 25, 2017 approximates their fair value.

PART I-FINANCIAL INFORMATION-CONTINUED

BASSETT FURNITURE INDUSTRIES, INCORPORATED AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS-UNAUDITED

MAY 26, 2018

(Dollars in thousands except share and per share data)

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.

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 8) 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.

5. Accounts Receivable

Accounts receivable consists of the following:

| | May 26, 2018 | November 25, 2017 |
|---------------------------------|-----------------|-------------------------|
| Gross accounts receivable | \$21,645 | \$ 20,257 |
| Allowance for doubtful accounts | (1,026) | (617) |
| Accounts receivable, net | \$20,619 | \$ 19,640 |

Activity in the allowance for doubtful accounts for the six months ended May 26, 2018 was as follows:

| | 2018 |
|--|---------|
| Balance at November 25, 2017 | \$617 |
| Acquired allowance on accounts receivable (Note 3) | 200 |
| Additions charged to expense | 254 |
| Write-offs and other reductions | (45) |
| Balance at May 26, 2018 | \$1,026 |

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.

PART I-FINANCIAL INFORMATION-CONTINUEDBASSETT FURNITURE INDUSTRIES, INCORPORATED AND SUBSIDIARIESNOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS-UNAUDITEDMAY 26, 2018(Dollars in thousands except share and per share data)**6. Inventories**

Inventories are valued at the lower of cost or net realizable value. Cost is determined for domestic furniture inventories using the last-in, first-out (LIFO) method. The costs for imported inventories and those applicable to Lane Venture are determined using the first-in, first-out (FIFO) method.

Inventories were comprised of the following:

| | May 26, 2018 | November 25, 2017 |
|---|-----------------|-------------------------|
| Wholesale finished goods | \$28,437 | \$ 26,145 |
| Work in process | 434 | 388 |
| Raw materials and supplies | 15,995 | 11,808 |
| Retail merchandise | 27,473 | 26,173 |
| Total inventories on first-in, first-out method | 72,339 | 64,514 |
| LIFO adjustment | (8,351) | (8,143) |
| Reserve for excess and obsolete inventory | (1,902) | (1,895) |
| | \$62,086 | \$ 54,476 |

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 25, 2017 | \$ 1,618 | \$ 277 | \$1,895 |
| Acquired reserve on inventory (Note 3) | 400 | - | 400 |
| Additions charged to expense | 702 | 233 | 935 |
| Write-offs | (1,100) | (228) | (1,328) |
| Balance at May 26, 2018 | \$ 1,620 | \$ 282 | \$1,902 |

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 2018 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 26, 2018(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 26, 2018 | | |
|---|---------------------|---------------------|-------------------|
| | Gross | Accumulated | Intangible |
| | Carrying | Amortization | Assets, |
| | Amount | | Net |
| Intangibles subject to amortization | | | |
| Customer relationships | \$3,550 | \$ (699 |) \$ 2,851 |
| Technology - customized applications | 834 | (397 |) 437 |
| Total intangible assets subject to amortization | 4,384 | (1,096 |) 3,288 |
| Intangibles not subject to amortization: | | | |
| Trade names | 9,338 | - | 9,338 |
| Goodwill | 15,990 | - | 15,990 |
| Total goodwill and other intangible assets | \$29,712 | \$ (1,096 |) \$ 28,616 |

| | November 25, 2017 | | |
|--------------------------------------|--------------------------|---------------------|-------------------|
| | Gross | Accumulated | Intangible |
| | Carrying | Amortization | Assets, |
| | Amount | | Net |
| Intangibles subject to amortization | | | |
| Customer relationships | \$3,038 | \$ (574 |) \$ 2,464 |
| Technology - customized applications | 834 | (337 |) 497 |

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| | | | | |
|---|----------|---------|---|-----------|
| Total intangible assets subject to amortization | 3,872 | (911 |) | 2,961 |
| Intangibles not subject to amortization: | | | | |
| Trade names | 2,490 | - | | 2,490 |
| Goodwill | 11,900 | - | | 11,900 |
| Total goodwill and other intangible assets | \$18,262 | \$ (911 |) | \$ 17,351 |

Changes in the carrying amounts of goodwill by reportable segment during the quarters ended May 26, 2018 were as follows:

| | Wholesale | Retail | Logistics | Total |
|--|-----------|----------|-----------|-----------|
| Balance as of November 25, 2017 | \$ 5,045 | \$ 1,926 | \$ 4,929 | \$ 11,900 |
| Goodwill arising from acquisition of Lane Venture (Note 3) | 4,090 | - | - | 4,090 |
| Balance as of May 26, 2018 | \$ 9,135 | \$ 1,926 | \$ 4,929 | \$ 15,990 |

The goodwill recognized in connection with our acquisition of Lane Venture remains subject to future adjustments before the close of the measurement period in the first quarter of fiscal 2019. See Note 3, Business Combinations, for additional information regarding the acquisition of Lane Venture. There were no accumulated impairment losses on goodwill as of May 26, 2018 or November 25, 2017.

PART I-FINANCIAL INFORMATION-CONTINUED

BASSETT FURNITURE INDUSTRIES, INCORPORATED AND SUBSIDIARIES

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Amortization expense associated with intangible assets during the three and six months ended May 26, 2018 and May 27, 2017 was as follows:

| | Quarter | | Six Months | |
|---------------------------------------|----------------|-------------|-------------------|-------------|
| | Ended | | Ended | |
| | May | May | May | May |
| | 26, | 27, | 26, | 27, |
| | 2018 | 2017 | 2018 | 2017 |
| Intangible asset amortization expense | \$95 | \$ 80 | \$185 | \$161 |

Estimated future amortization expense for intangible assets that exist at May 26, 2018 is as follows:

| | |
|--------------------------|----------------|
| Remainder of fiscal 2018 | \$ 189 |
| Fiscal 2019 | 379 |
| Fiscal 2020 | 379 |
| Fiscal 2021 | 379 |
| Fiscal 2022 | 279 |
| Fiscal 2023 | 259 |
| Thereafter | 1,424 |
| Total | \$3,288 |

8. Notes Payable and Bank Credit Facility

Our notes payable consist of the following:

| | May 26, 2018 |
|--------------------------------------|-----------------------------|
| Real estate notes payable | \$541 |
| Less current portion | (432) |
| Total long-term notes payable | \$ 109 |

| | November 25, 2017 | | Net |
|--------------------------------------|--------------------------|--------------------|-----------------|
| | Principal | Unamortized | Carrying |
| | Balance | Discount | Amount |
| Zenith acquisition note payable | \$3,000 | \$ (13) | \$ 2,987 |
| Real estate notes payable | 747 | - | 747 |
| Total notes payable | 3,747 | (13) | 3,734 |
| Less current portion | (3,418) | 13 | (3,405) |
| Total long-term notes payable | \$ 329 | \$ - | \$ 329 |

The future maturities of our notes payable are as follows:

| | |
|--------------------------|--------------|
| Remainder of fiscal 2018 | \$212 |
| Fiscal 2019 | 329 |
| | \$541 |

Zenith Acquisition Note Payable

The final installment of the Zenith acquisition note was paid in full on February 2, 2018. Interest expense resulting from the amortization of the discount was \$13 for the six months ended May 26, 2018 and \$19 and \$57 for the three and six months ended May 27, 2017, respectively.

PART I-FINANCIAL INFORMATION-CONTINUED

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Real Estate Notes Payable

Certain of our retail real estate properties have been financed through commercial mortgages with outstanding principal totaling \$541 and \$747 at May 26, 2018 and November 25, 2017, respectively. The mortgages bear interest at fixed rates of 6.73%. They are collateralized by the respective properties with net book values totaling approximately \$5,663 and \$5,727 at May 26, 2018 and November 25, 2017, respectively. The current portion of these mortgages due within one year was \$432 and \$418 as of May 26, 2018 and November 25, 2017, respectively.

Fair Value

We believe that the carrying amount of our notes payable approximates fair value at both May 26, 2018 and November 25, 2017. 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

Our credit facility with our bank 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 26, 2018, we had \$2,249 outstanding under standby letters of credit against our line, leaving availability under our credit line of \$12,751. In addition, we have outstanding standby letters of credit with another bank totaling \$381.

9. Post Employment Benefit Obligations

Defined Benefit Plans

We have an unfunded Supplemental Retirement Income Plan (the “Supplemental Plan”) that covers one current and certain former executives. The liability for the Supplemental Plan was \$11,329 and \$11,337 as of May 26, 2018 and November 25, 2017, respectively.

We also have the Bassett Furniture Industries, Incorporated Management Savings Plan (the “Management Savings Plan”) which was established in the second quarter of fiscal 2017. The Management Savings Plan is an unfunded, nonqualified deferred compensation plan maintained for the benefit of certain highly compensated or management level employees. As part of the Management Savings Plan, we have made Long Term Cash Awards (“LTC Awards”) totaling \$2,000 to certain management employees in the amount of \$400 each. The liability for the LTC Awards was \$1,032 and \$985 as of May 26, 2018 and November 25, 2017, respectively.

The combined pension liability for the Supplemental Plan and LTC Awards is recorded as follows in the condensed consolidated balance sheets:

| | May 26, 2018 | November 25, 2017 |
|-------------------------------------|-----------------------------|----------------------------------|
| Accrued compensation and benefits | \$ 778 | \$ 778 |
| Post employment benefit obligations | 11,583 | 11,544 |
| Total pension liability | \$ 12,361 | \$ 12,322 |

PART I-FINANCIAL INFORMATION-CONTINUEDBASSETT FURNITURE INDUSTRIES, INCORPORATED AND SUBSIDIARIESNOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS-UNAUDITEDMAY 26, 2018(Dollars in thousands except share and per share data)

Components of net periodic pension costs for our defined benefit plans for the three and six months ended May 26, 2018 and May 27, 2017 are as follows:

| | Quarter Ended | | Six Months Ended | |
|---------------------------------------|--------------------------|--------------------|-----------------------------|--------------------|
| | May 26, | May 27, | May 26, | May 27, |
| | 2018 | 2017 | 2018 | 2017 |
| Service cost | \$49 | \$49 | \$98 | \$87 |
| Interest cost | 105 | 114 | 210 | 222 |
| Amortization of prior service costs | 31 | 24 | 62 | 24 |
| Amortization of transition obligation | 11 | 11 | 22 | 21 |
| Amortization of loss | 65 | 83 | 130 | 166 |
| Net periodic pension cost | \$261 | \$281 | \$522 | \$520 |

The components of net periodic pension cost other than the service cost component are included in other loss, net in our condensed consolidated statements of income.

Deferred Compensation Plans

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 \$1,877 and \$1,916 as of May 26, 2018 and November 25, 2017, respectively.

We also have an unfunded, nonqualified deferred compensation plan maintained for the benefit of certain highly compensated or management level employees which was established under the Management Savings Plan in the second quarter of fiscal 2017. Our liability under this plan, including both accrued Company contributions and participant salary deferrals, was \$485 and \$139 as of May 26, 2018 and November 25, 2017, respectively.

Our combined liability for all deferred compensation arrangements, including Company contributions and participant deferrals under the Management Savings Plan, is recorded as follows in the condensed consolidated balance sheets:

| | May 26, 2018 | November 25, 2017 |
|---------------------------------------|-----------------------------|----------------------------------|
| Accrued compensation and benefits | \$274 | \$ 274 |
| Post employment benefit obligations | 2,088 | 1,782 |
| Total deferred compensation liability | \$2,362 | \$ 2,056 |

We recognized expense under our deferred compensation arrangements during the three and six months ended May 26, 2018 and May 27, 2017 as follows:

| | Quarter Ended May May 26, 27, | | Six Months Ended May May 26, 27, | |
|-------------------------------|--|-------------|---|-------------|
| | 2018 | 2017 | 2018 | 2017 |
| Deferred compensation expense | \$80 | \$ 82 | \$159 | \$136 |

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BASSETT FURNITURE INDUSTRIES, INCORPORATED AND SUBSIDIARIES

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10. Other Gains and Losses

Fiscal 2018

Sale of Retail Location

In May 2018 we sold the land and building occupied by our Spring, Texas retail store in connection with the eventual relocation of the store to another site in the Houston market. We received net cash proceeds of \$2,463 from the sale, resulting in a gain of \$165 recognized during the three and six months ended May 26, 2018 which is included in income from operations in our accompanying condensed consolidated statements of income.

Fiscal 2017

Gain on Sale of Investment

In 1985, we acquired a minority interest in a privately-held, start-up provider of property and casualty insurance for \$325. We have accounted for this investment on the cost method and included it in other long-term assets in our condensed consolidated balance sheet. In April 2017 we sold our interest for \$3,592 in cash, resulting in a gain of \$3,267 recognized for the three and six months ended May 27, 2017.

Impairment of Investment in Real Estate

We own a building in Chesterfield County, Virginia that was formerly leased to a licensee for the operation of a BHF store. The building is subject to a ground lease that expires in 2020, with additional renewal options. Since 2012, we have leased the building to another party who is, as of recently, paying less than the full amount of the lease obligation, resulting in rental income insufficient to cover our ground lease obligation. Efforts to sell our interest in the building have been unsuccessful to date. We have also concluded that, absent a significant cash investment in the building, the likelihood of locating another tenant at a rent that would provide positive cash flow in excess of the ground lease expense is remote. In addition, we obtained an appraisal during the quarter ended May 27, 2017 which indicated that the value of the building had significantly decreased and was now minimal. Given these circumstances, we concluded that we were unlikely to renew the ground lease in 2020 and were therefore likely vacate the property at that time. Consequently, we recorded a non-cash impairment charge of \$1,084 for the three and six months ended May 27, 2017 to write off the value of the building.

PART I-FINANCIAL INFORMATION-CONTINUEDBASSETT FURNITURE INDUSTRIES, INCORPORATED AND SUBSIDIARIESNOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS-UNAUDITEDMAY 26, 2018(Dollars in thousands except share and per share data)**11. 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 26, 2018:

| | Retail Stores | Distribution Centers | Transportation Equipment | Total |
|-------------------------------------|--------------------------|---------------------------------|-------------------------------------|--------------|
| Remainder of fiscal 2018 | \$ 12,156 | \$ 2,635 | \$ 1,521 | \$ 16,312 |
| Fiscal 2019 | 24,486 | 4,237 | 2,750 | 31,473 |
| Fiscal 2020 | 22,887 | 3,495 | 2,486 | 28,868 |
| Fiscal 2021 | 19,855 | 2,771 | 1,552 | 24,178 |
| Fiscal 2022 | 16,993 | 2,583 | 1,346 | 20,922 |
| Fiscal 2023 | 14,136 | 1,517 | 637 | 16,290 |
| Thereafter | 41,344 | 438 | 559 | 42,341 |
| Total future minimum lease payments | \$ 151,857 | \$ 17,676 | \$ 10,851 | \$ 180,384 |

In connection with our long-term real estate leases, our liability for accrued straight-line rent expense was \$5,232 and \$4,821 at May 26, 2018 and November 25, 2017, respectively, and is included in other accrued liabilities in our condensed consolidated balance sheets.

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 \$2,360 and \$2,743 at May 26, 2018 and November 25, 2017, 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 26, 2018 and November 25, 2017 was not material.

PART I-FINANCIAL INFORMATION-CONTINUEDBASSETT FURNITURE INDUSTRIES, INCORPORATED AND SUBSIDIARIESNOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS-UNAUDITEDMAY 26, 2018(Dollars in thousands except share and per share data)**12. 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 26, 2018:</u> | | | |
| Basic earnings per share | \$ 4,289 | 10,701,154 | \$ 0.40 |
| Add effect of dilutive securities: | | | |
| Options and restricted shares | - | 40,182 | - |
| Diluted loss per share | \$ 4,289 | 10,741,336 | \$ 0.40 |

For the quarter ended May 27 2017:

| | | | |
|------------------------------------|----------|------------|---------|
| Basic earnings per share | \$ 5,842 | 10,648,033 | \$ 0.55 |
| Add effect of dilutive securities: | | | |
| Options and restricted shares | - | 74,293 | (0.01) |
| Diluted earnings per share | \$ 5,842 | 10,722,326 | \$ 0.54 |

For the six months ended May 26, 2018:

| | | | |
|------------------------------------|----------|------------|---------|
| Basic earnings per share | \$ 3,376 | 10,693,815 | \$ 0.32 |
| Add effect of dilutive securities: | | | |
| Options and restricted shares | - | 53,936 | (0.01) |
| Diluted earnings per share | \$ 3,376 | 10,747,751 | \$ 0.31 |

For the six months ended May 27, 2017:

| | | | |
|------------------------------------|----------|------------|---------|
| Basic earnings per share | \$ 8,703 | 10,630,836 | \$ 0.82 |
| Add effect of dilutive securities: | | | |
| Options and restricted shares | - | 88,009 | (0.01) |
| Diluted earnings per share | \$ 8,703 | 10,718,845 | \$ 0.81 |

For the three and six months ended May 26, 2018 and May 27, 2017, the following potentially dilutive shares were excluded from the computations as their effect was anti-dilutive:

| | Quarter Ended | | Six Months Ended | |
|-----------------|-----------------------------|-----------------------------|-----------------------------|-----------------------------|
| | May 26, 2018 | May 27, 2017 | May 26, 2018 | May 27, 2017 |
| Unvested shares | 5,292 | - | 5,292 | 6,538 |

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13. 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, which now include Lane Venture (see Note 3, Business Combinations), as well as all corporate selling, general and administrative expenses, including those corporate expenses related to both Company- and licensee-owned stores. Our wholesale segment also includes our holdings of short-term investments and retail real estate previously leased as licensee stores. The earnings and costs associated with these assets are included in other 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. Our logistical services segment 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 statements of income. Zenith's total operating costs, including those associated with providing logistical services to the Company as well as to third-party customers, are included in selling, general and administrative expenses and were \$24,640 and \$49,559 for the three and six months ended May 26, 2018, and \$23,828 and \$46,388 for the three and six months ended May 27, 2017, respectively.

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 26, 2018(Dollars in thousands except share and per share data)

The following table presents our segment information:

| | Quarter Ended | | Six Months Ended | |
|--------------------------------------|----------------------|----------------|-------------------------|----------------|
| | May 26, | May 27, | May 26, | May 27, |
| | 2018 | 2017 | 2018 | 2017 |
| Sales Revenue | | | | |
| Wholesale | \$63,788 | \$62,293 | \$126,888 | \$124,268 |
| Retail - Company-owned stores | 68,682 | 67,144 | 133,343 | 128,737 |
| Logistical services | 24,929 | 24,626 | 50,178 | 46,960 |
| Inter-company eliminations: | | | | |
| Furniture and accessories | (29,795) | (29,143) | (61,433) | (59,013) |
| Logistical services | (10,624) | (10,795) | (21,724) | (20,935) |
| Consolidated | \$116,980 | \$114,125 | \$227,252 | \$220,017 |
| Income from Operations | | | | |
| Wholesale | \$3,039 | \$4,783 | \$6,103 | \$10,676 |
| Retail - Company-owned stores | 1,626 | 1,367 | 113 | 24 |
| Logistical services | 289 | 798 | 619 | 572 |
| Inter-company elimination | 709 | 652 | 878 | 992 |
| Consolidated | \$5,663 | \$7,600 | \$7,713 | \$12,264 |
| Depreciation and Amortization | | | | |
| Wholesale | \$757 | \$664 | \$1,460 | \$1,308 |
| Retail - Company-owned stores | 1,536 | 1,496 | 3,064 | 2,968 |
| Logistical services | 1,091 | 1,195 | 2,164 | 2,430 |
| Consolidated | \$3,384 | \$3,355 | \$6,688 | \$6,706 |
| Capital Expenditures | | | | |
| Wholesale | \$1,113 | \$2,218 | \$2,330 | \$3,845 |
| Retail - Company-owned stores | 1,854 | 1,211 | 4,455 | 4,914 |
| Logistical services | 737 | 133 | 877 | 413 |

| | | | | |
|--------------|---------|---------|---------|---------|
| Consolidated | \$3,704 | \$3,562 | \$7,662 | \$9,172 |
|--------------|---------|---------|---------|---------|

| | As of May 26, 2018 | As of November 25, 2017 |
|-------------------------------|-----------------------------------|--|
| Identifiable Assets | | |
| Wholesale | \$ 139,906 | \$ 152,181 |
| Retail - Company-owned stores | 89,859 | 89,271 |
| Logistical services | 51,583 | 52,296 |
| Consolidated | \$ 281,348 | \$ 293,748 |

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14. 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, and ASU 2016-11, which rescinds certain SEC guidance within the ASC effective upon an entity's adoption of 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. In order to evaluate the impact that the adoption of ASU 2014-09 will have on our consolidated financial statements, we have conducted a comprehensive review of the significant revenue streams across our wholesale, retail and logistical services reportable segments. The focus of this review included, among other things, the identification of the significant contracts and other arrangements we have with our customers to identify significant performance obligations, factors affecting the determination of transaction price, such as variable consideration, and factors affecting the classification of receipts as revenue, such as principal versus agent considerations. We are currently finalizing our assessment of the impact that adoption will have on our consolidated financial statements. While we have not yet made a determination as to the impact on our financial position or results of operations, we do anticipate incorporating additional disclosures, primarily related to disaggregation of revenue. We are also in the process of implementing the necessary changes to our accounting policies, procedures and controls with respect to these contracts and arrangements as required by the adoption of ASU 2014-09. We currently anticipate adopting this standard as of the beginning of our 2019 fiscal year using the full retrospective method of adoption.

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.

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.

PART I-FINANCIAL INFORMATION-CONTINUED

BASSETT FURNITURE INDUSTRIES, INCORPORATED AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS-UNAUDITED

MAY 26, 2018

(Dollars in thousands except share and per share data)

In August 2016, the FASB issued Accounting Standards Update No. 2016-15, *Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments*. ASU 2016-15 addresses how certain cash receipts and cash payments are presented and classified in the statement of cash flows with the objective of reducing existing diversity in practice with respect to these items. Among the types of cash flows addressed are payments for costs related to debt prepayments or extinguishments, payments representing accreted interest on discounted debt, payments of contingent consideration after a business combination, proceeds from insurance claims and company-owned life insurance, and distributions from equity method investees, among others. The amendments in ASU 2016-15 are to be adopted retrospectively and will become effective for us at the beginning of our 2019 fiscal year. Early adoption, including adoption in an interim period, is permitted. The adoption of this guidance is not expected to have a material impact upon our presentation of cash flows.

In January 2017, the FASB issued Accounting Standards Update No. 2017-01, *Business Combinations (Topic 805): Clarifying the Definition of a Business*. ASU 2017-01 provides a screen to determine when an integrated set of assets and activities (collectively referred to as a “set”) does not constitute a business. The screen requires that when substantially all of the fair value of the gross assets acquired (or disposed of) is concentrated in a single identifiable asset or a group of similar identifiable assets, the set is not a business. This screen reduces the number of transactions that need to be further evaluated. If the screen is not met, the amendments in ASU 2017-01 (1) require that to be considered a business, a set must include, at a minimum, an input and a substantive process that together significantly contribute to the ability to create output and (2) remove the evaluation of whether a market participant could replace missing elements. The amendments in ASU 2017-01 shall apply prospectively and will become effective for us at 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.

In January 2017, the FASB issued Accounting Standards Update No. 2017-04, *Intangibles – Goodwill and Other (Topic 350): Simplifying the Test for Goodwill Impairment*. ASU 2017-04 eliminates Step 2 from the goodwill impairment test. Under Step 2, an entity had to perform procedures to determine the fair value at the impairment testing date of its assets and liabilities (including unrecognized assets and liabilities) following the procedure that would be required in determining the fair value of assets acquired and liabilities assumed in a business combination. Instead, under the amendments in ASU 2017-04, an entity should perform its annual, or interim, goodwill impairment test by comparing the fair value of a reporting unit with its carrying amount. An entity should recognize an impairment charge for the amount by which the carrying amount exceeds the reporting unit’s fair value; however, the loss recognized should not exceed the total amount of goodwill allocated to that reporting unit. Additionally, an entity

should consider income tax effects from any tax deductible goodwill on the carrying amount of the reporting unit when measuring the goodwill impairment loss, if applicable. An entity still has the option to perform the qualitative assessment for a reporting unit to determine if the quantitative impairment test is necessary. The amendments in ASU 2017-04 will become effective for us as of the beginning of our 2021 fiscal year. Early adoption is permitted for interim or annual goodwill impairment tests performed on testing dates after January 1, 2017. The adoption of this guidance is not expected to have a material impact upon our financial condition or results of operations.

In May 2017, the FASB issued Accounting Standards Update No. 2017-09, *Compensation – Stock Compensation (Topic 718): Scope of Modification Accounting*. ASU 2017-09 was issued to provide clarity and reduce both (1) diversity in practice and (2) cost and complexity when applying the guidance in Topic 718, *Compensation—Stock Compensation*, to a change to the terms or conditions of a share-based payment award. The amendments in this Update provide guidance about which changes to the terms or conditions of a share-based payment award require an entity to apply modification accounting in Topic 718. Essentially, an entity will not have to account for the effects of a modification if: (1) The fair value of the modified award is the same immediately before and after the modification; (2) the vesting conditions of the modified award are the same immediately before and after the modification; and (3) the classification of the modified award as either an equity instrument or liability instrument is the same immediately before and after the modification. The amendments in ASU 2017-09 will become effective for us as of the beginning of our 2019 fiscal year. Early adoption is permitted, including adoption in any interim period. 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

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS-UNAUDITED

MAY 26, 2018

(Dollars in thousands except share and per share data)

In February 2018, the FASB issued Accounting Standards Update No. 2018-02, *Income Statement—Reporting Comprehensive Income (Topic 220): Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income*. ASU 2018-02 was issued to provide narrow-scope guidance for entities that are required to apply the provisions of Topic 220, *Income Statement—Reporting Comprehensive Income*, and have items of other comprehensive income for which the related tax effects are presented in other comprehensive income as required by GAAP. The amendments in ASU 2018-02 allow a reclassification from accumulated other comprehensive income to retained earnings for stranded tax effects resulting from the Tax Cuts and Jobs Act. Consequently, the amendments eliminate the stranded tax effects resulting from the Act and will improve the usefulness of information reported to financial statement users. However, because the amendments only relate to the reclassification of the income tax effects of the Tax Cuts and Jobs Act, the underlying guidance that requires that the effect of a change in tax laws or rates be included in income from continuing operations is not affected. The amendments in ASU 2018-02 are effective for all entities for fiscal years beginning after December 15, 2018, and interim periods within those fiscal years. Early adoption of the amendments in this Update is permitted, including adoption in any interim period, (1) for public business entities for reporting periods for which financial statements have not yet been issued and (2) for all other entities for reporting periods for which financial statements have not yet been made available for issuance. Because the Act has had a significant impact upon the tax effects of pension costs included in our accumulated other comprehensive loss, we have adopted the guidance in ASU 2018-02 effective as of the beginning of the first quarter of fiscal 2018, resulting in the reclassification of \$545 of tax benefits from accumulated other comprehensive loss to retained earnings (see Note 2).

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PART I-FINANCIAL INFORMATION-CONTINUED

BASSETT FURNITURE INDUSTRIES, INCORPORATED AND SUBSIDIARIES

MAY 26, 2018

(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. We were founded in 1902 and incorporated under the laws of Virginia in 1930. Our rich 116-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 95 BHF stores at May 26, 2018, 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. Our store program is designed 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. We use a network of over 30 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, 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 custom 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 “Bench Made” line of custom, solid hardwood furniture. 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 addition to the furniture that we manufacture domestically, we source most of our formal bedroom and dining room furniture (casegoods) and certain leather upholstery offerings from several foreign plants, primarily in Vietnam and China. Over 70% of the products we currently sell are manufactured in the United States.

We also own Zenith Freight Lines, LLC (“Zenith”) which provides logistical services to both the wholesale and retail operations at Bassett along with other furniture manufacturers and retailers. Zenith delivers best-of-class shipping and logistical support services that are uniquely tailored to the needs of Bassett and the furniture industry, as well as the ability to provide the expedited delivery service which is increasingly demanded by our industry. Zenith operates seven regional freight hubs and 14 home delivery centers in 13 states. Approximately 57% of Zenith’s revenue is generated from services provided to non-Bassett customers.

On December 21, 2017, we purchased certain assets and assumed certain liabilities of Lane Venture from Heritage Home Group, LLC for \$15,556 in cash. Lane Venture is a manufacturer and distributor of premium outdoor furniture, and is now being operated as a component of our wholesale segment. This acquisition marks our entry into the market for outdoor furniture and we believe that Lane Venture will provide a foundation for us to become a significant participant in this category. We plan to distribute this brand outside of our Bassett store network with plans to introduce a Bassett-branded line in the stores in the near future. See Note 3 to our condensed consolidated financial statements for additional details regarding this acquisition.

At May 26, 2018, our BHF store network included 64 Company-owned stores and 31 licensee-owned stores. During the second quarter of fiscal 2018, we opened a new store in El Paso, Texas, and a new licensee store was opened in La Jolla, California.

PART I-FINANCIAL INFORMATION-CONTINUEDBASSETT FURNITURE INDUSTRIES, INCORPORATED AND SUBSIDIARIESMAY 26, 2018(Dollars in thousands except share and per share data)

We continue to execute our strategy of growing the Company through opening new stores, repositioning stores to improved locations within a market and closing underperforming stores. The following table shows planned store openings where leases have been executed:

| Location | Type | Size Sq. Ft. | Planned Opening |
|--|-----------|-----------------|--------------------|
| <i>New Stores:</i> | | | |
| Daly City, CA | Licensed | 9,000 | Q3 2018 |
| Coral Gables, FL | Corporate | 10,000 | Q3 2018 |
| Frisco, TX | Corporate | 15,000 | Q4 2018 |
| Boise, ID | Licensed | 11,000 | Q4 2018 |
| Columbus, OH | Corporate | 11,000 | Q4 2018/Q1 2019 |
| Tucson, AZ | Corporate | 9,000 | Q4 2018/Q1 2019 |
| <i>Repositionings:</i> | | | |
| Spring, TX to The Woodlands, TX | Corporate | 12,000 | Q4 2018/Q1 2019 |
| Friendswood, TX to Baybrook Mall area in Friendswood, TX | Corporate | 16,000 | Q4 2018/Q1 2019 |

We also plan to open a new 16,000 square foot clearance center in Middletown, New York in the third quarter of 2018. Because the nature of this store will differ significantly from the other stores in the BHF network, offering only clearance merchandise at reduced price points and without design consulting services, we will not include this location in our reporting of comparable store results in the future. In addition, lease negotiations are underway for new store locations that could result in additional openings during 2019 and beyond. With a track record of seven consecutive years of positive same store sales growth and our focus on store productivity, we believe that we can take our concept to new markets and consistently grow overall store count in the years to come.

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 \$200 to \$400 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 \$400 to \$600 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. Because of the increased store openings in 2018, we expect to incur approximately \$1,000 more in new store pre-opening costs and post-opening losses in 2018 than we incurred in 2017.

During 2018, we are focusing on our digital effort to improve the customers' journey from the time they begin on our website to the final step of delivering the goods to their homes. Today's customers expect their digital experiences and communications to be personalized and highly-relevant, and catered to match their specific needs and preferences. We are laying the foundation to becoming more connected to our customers and to use the data and insights collected during the customer journey to create a more compelling customized customer experience. This year, we plan to invest in technology, including an order management system, and in digital talent who can direct the strategy, planning and daily business direction and critical decision making required for building a competitive omnichannel retail business.

PART I-FINANCIAL INFORMATION-CONTINUEDBASSETT FURNITURE INDUSTRIES, INCORPORATED AND SUBSIDIARIESMAY 26, 2018(Dollars in thousands except share and per share data)**Results of Operations – Periods ended May 26, 2018 compared with periods ended May 27, 2017:**

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 three and six months ended May 26, 2018 and May 27, 2017:

| | Quarter Ended | | | Change | | | Six Months Ended | | | Change | | | |
|--|---------------|---------|--------------|-----------|---------|--------------|------------------|-----------|---------|--------------|--------------|-----------|---------|
| | May 26, 2018 | | May 27, 2017 | Dollars | Percent | May 26, 2018 | May 27, 2017 | Dollars | Percent | May 26, 2018 | May 27, 2017 | Dollars | Percent |
| Sales revenue: | | | | | | | | | | | | | |
| Furniture and accessories | \$102,675 | 87.8 % | \$100,294 | \$2,381 | 2.4 % | \$198,798 | \$193,992 | \$4,806 | 2.5 % | \$193,992 | \$193,992 | \$4,806 | 2.5 % |
| Logistics revenue | 14,305 | 12.2 % | 13,831 | 474 | 3.4 % | 28,454 | 26,025 | 2,429 | 9.3 % | 26,025 | 26,025 | 2,429 | 9.3 % |
| Total sales revenue | 116,980 | 100.0 % | 114,125 | 2,855 | 2.5 % | 227,252 | 220,017 | 7,235 | 3.3 % | 220,017 | 220,017 | 7,235 | 3.3 % |
| Cost of furniture and accessories sold | 45,660 | 39.0 % | 44,981 | 679 | 1.5 % | 88,929 | 86,879 | 2,050 | 2.3 % | 86,879 | 86,879 | 2,050 | 2.3 % |
| SG&A expenses | 65,456 | 56.0 % | 61,075 | 4,381 | 7.2 % | 129,707 | 119,599 | 10,108 | 8.6 % | 119,599 | 119,599 | 10,108 | 8.6 % |
| New store pre-opening costs | 201 | 0.2 % | 469 | (268) | -57.1 % | 903 | 1,275 | (372) | -29.2 % | 1,275 | 1,275 | (372) | -29.2 % |
| Income from operations | \$5,663 | 4.8 % | \$7,600 | \$(1,937) | -25.5 % | \$7,713 | \$12,264 | \$(4,551) | -37.1 % | \$12,264 | \$12,264 | \$(4,551) | -37.1 % |

Refer to the segment information which follows for a discussion of the significant factors and trends affecting our results of operations for the three and six months ended May 26, 2018 as compared with the prior year periods.

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PART I-FINANCIAL INFORMATION-CONTINUED

BASSETT FURNITURE INDUSTRIES, INCORPORATED AND SUBSIDIARIES

MAY 26, 2018

(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, which now include Lane Venture, 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 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. Our logistical services segment 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 statements of income. Zenith's operating costs are included in selling, general and administrative expenses.

PART I-FINANCIAL INFORMATION-CONTINUEDBASSETT FURNITURE INDUSTRIES, INCORPORATED AND SUBSIDIARIESMAY 26, 2018(Dollars in thousands except share and per share data)

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

| | Quarter Ended May 26, 2018 | | | | Consolidated |
|--|----------------------------|----------|-----------|--------------|----------------|
| | Wholesale | Retail | Logistics | Eliminations | |
| Sales revenue: | | | | | |
| Furniture & accessories | \$63,788 | \$68,682 | \$- | \$ (29,795) | (1) \$ 102,675 |
| Logistics | - | - | 24,929 | (10,624) | (2) 14,305 |
| Total sales revenue | 63,788 | 68,682 | 24,929 | (40,419) | 116,980 |
| Cost of furniture and accessories sold | 42,821 | 32,929 | - | (30,090) | (3) 45,660 |
| SG&A expense | 17,928 | 33,926 | 24,640 | (11,038) | (4) 65,456 |
| New store pre-opening costs | - | 201 | - | - | 201 |
| Income from operations | \$3,039 | \$1,626 | \$ 289 | \$ 709 | \$ 5,663 |

| | Quarter Ended May 27, 2017 | | | | Consolidated |
|--|----------------------------|----------|-----------|--------------|----------------|
| | Wholesale | Retail | Logistics | Eliminations | |
| Sales revenue: | | | | | |
| Furniture & accessories | \$62,293 | \$67,144 | \$- | \$ (29,143) | (1) \$ 100,294 |
| Logistics | - | - | 24,626 | (10,795) | (2) 13,831 |
| Total sales revenue | 62,293 | 67,144 | 24,626 | (39,938) | 114,125 |
| Cost of furniture and accessories sold | 41,222 | 33,072 | - | (29,313) | (3) 44,981 |
| SG&A expense | 16,288 | 32,236 | 23,828 | (11,277) | (4) 61,075 |
| New store pre-opening costs | - | 469 | - | - | 469 |
| Income from operations | \$4,783 | \$1,367 | \$ 798 | \$ 652 | \$ 7,600 |

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PART I-FINANCIAL INFORMATION-CONTINUEDBASSETT FURNITURE INDUSTRIES, INCORPORATED AND SUBSIDIARIESMAY 26, 2018(Dollars in thousands except share and per share data)

| | Six Months Ended May 26, 2018 | | | | | Consolidated |
|--|-------------------------------|------------|-----------|--------------|------|--------------|
| | Wholesale | Retail | Logistics | Eliminations | | |
| Sales revenue: | | | | | | |
| Furniture & accessories | \$ 126,888 | \$ 133,343 | \$ - | \$ (61,433 |)(1) | \$ 198,798 |
| Logistics | - | - | 50,178 | (21,724 |)(2) | 28,454 |
| Total sales revenue | 126,888 | 133,343 | 50,178 | (83,157 |) | 227,252 |
| Cost of furniture and accessories sold | 85,465 | 64,923 | - | (61,459 |)(3) | 88,929 |
| SG&A expense | 35,320 | 67,404 | 49,559 | (22,576 |)(4) | 129,707 |
| New store pre-opening costs | - | 903 | - | - | | 903 |
| Income from operations | \$6,103 | \$ 113 | \$ 619 | \$ 878 | | \$ 7,713 |

| | Six Months Ended May 27, 2017 | | | | | Consolidated |
|--|-------------------------------|------------|-----------|--------------|------|--------------|
| | Wholesale | Retail | Logistics | Eliminations | | |
| Sales revenue: | | | | | | |
| Furniture & accessories | \$ 124,268 | \$ 128,737 | \$ - | \$ (59,013 |)(1) | \$ 193,992 |
| Logistics | - | - | 46,960 | (20,935 |)(2) | 26,025 |
| Total sales revenue | 124,268 | 128,737 | 46,960 | (79,948 |) | 220,017 |
| Cost of furniture and accessories sold | 81,392 | 64,531 | - | (59,044 |)(3) | 86,879 |
| SG&A expense | 32,200 | 62,907 | 46,388 | (21,896 |)(4) | 119,599 |
| New store pre-opening costs | - | 1,275 | - | - | | 1,275 |
| Income from operations | \$ 10,676 | \$ 24 | \$ 572 | \$ 992 | | \$ 12,264 |

(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 26, | May 27, | May 26, | May 27, |
| 2018 | 2017 | 2018 | 2017 |
| | | | |

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| | | | | |
|----------------------------------|------------|------------|------------|------------|
| Intercompany logistical services | \$(10,624) | \$(10,795) | \$(21,724) | \$(20,935) |
| Intercompany rents | (414) | (482) | (852) | (961) |
| Total SG&A expense elimination | \$(11,038) | \$(11,277) | \$(22,576) | \$(21,896) |

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PART I-FINANCIAL INFORMATION-CONTINUEDBASSETT FURNITURE INDUSTRIES, INCORPORATED AND SUBSIDIARIESMAY 26, 2018(Dollars in thousands except share and per share data)Wholesale Segment

Results for the wholesale segment for the three and sixth months ended May 26, 2018 and May 27, 2017 are as follows:

| | Quarter Ended | | | Change | | | Six Months Ended | | | Change | | |
|------------------------|---------------|--------|--------------|---------|-----------|--------|------------------|--------|--------------|---------|-----------|--------|
| | May 26, 2018 | | May 27, 2017 | Dollars | Percent | | May 26, 2018 | | May 27, 2017 | Dollars | Percent | |
| Net sales | \$63,788 | 100.0% | \$62,293 | 100.0% | \$1,495 | 2.4 % | \$126,888 | 100.0% | \$124,268 | 100.0% | \$2,620 | 2.1 % |
| Gross profit | 20,967 | 32.9 % | 21,071 | 33.8 % | (104) | -0.5 % | 41,423 | 32.6 % | 42,876 | 34.5 % | (1,453) | -3.4 % |
| SG&A expenses | 17,928 | 28.1 % | 16,288 | 26.1 % | 1,640 | 10.1 % | 35,320 | 27.8 % | 32,200 | 25.9 % | 3,120 | 9.7 % |
| Income from operations | \$3,039 | 4.8 % | \$4,783 | 7.7 % | \$(1,744) | -36.5% | \$6,103 | 4.8 % | \$10,676 | 8.6 % | \$(4,573) | -42.8% |

Quarterly Analysis of Results - Wholesale

The increase in net sales was driven by the addition of \$3,344 of revenue for Lane Venture, acquired during the first quarter of 2018, partially offset by a 3.8% decrease in furniture shipments to the Bassett Home Furnishings network and a 1.6% decrease in shipments to the open market (outside the Bassett Home Furnishings network and excluding shipments from Lane Venture) as compared to the prior year period. A much smaller component of our wholesale revenues, shipments of wholesale accessories, increased 17% over the prior year period. Gross margins for the wholesale segment were 32.9% for the second quarter of 2018 compared to 33.8% for the prior year quarter. This decrease was primarily driven by lower margins in the Bassett Custom Upholstery operations, excluding Lane Venture, due to continued higher materials costs coupled with lower absorption of fixed costs due to lower volumes, partially offset by improved margins in the Bassett Custom Wood operations due to operational efficiencies. In June

2018, we implemented targeted price increases to our custom upholstery line to mitigate the effects of the cost increases. Wholesale SG&A increased as a percentage of sales over the prior year period primarily driven by planned higher digital marketing and other brand development costs coupled with the shift in timing of certain marketing costs that occurred in the third quarter of the prior year.

Year-to-date Analysis of Results – Wholesale

The increase in net sales was driven by the addition of \$4,004 of revenue for Lane Venture, acquired during the first quarter of 2018, along with a 3.1% increase in furniture shipments to the open market (outside the Bassett Home Furnishings network and excluding shipments from Lane Venture), partially offset by a 3.3% decrease in furniture shipments to the Bassett Home Furnishings network as compared to the prior year period. A much smaller component of our wholesale revenues, shipments of wholesale accessories, increased 34.9% over the prior year period. Gross margins for the wholesale segment were 32.6% for the first half of 2018 compared to 34.5% for the prior year period. This decrease was primarily driven by lower margins in the Bassett Custom Upholstery operations, excluding Lane Venture, due to continued higher materials costs coupled with lower absorption of fixed costs due to lower volumes partially offset by improved margins in the Bassett Custom Wood operations due to operational efficiencies. In June 2018, we implemented targeted price increases to our custom upholstery line to mitigate the effects of the cost increases. Wholesale SG&A increased as a percentage of sales over the prior year period primarily driven by planned higher digital marketing and other brand development costs coupled with the shift in timing of certain marketing costs that occurred in the third quarter of the prior year. In addition, we incurred \$254 of one-time acquisition costs along with other startup costs associated with the Lane Venture operation.

Wholesale shipments by type:

| | Quarter Ended | | | Change | | | Six Months Ended | | | Change | | |
|---------------------------|---------------|---------|--------------|---------|---------|---------|------------------|---------|--------------|---------|---------|---------|
| | May 26, 2018 | | May 27, 2017 | | Dollars | Percent | May 26, 2018 | | May 27, 2017 | | Dollars | Percent |
| Bassett Custom Upholstery | \$36,506 | 57.2 % | \$35,386 | 56.8 % | \$1,120 | 3.2 % | \$70,074 | 55.2 % | \$68,848 | 55.4 % | \$1,226 | 1.8 % |
| Bassett Leather | 5,082 | 8.0 % | 5,474 | 8.8 % | (392) | -7.2 % | 11,606 | 9.1 % | \$11,055 | 8.9 % | 551 | 5.0 % |
| Bassett Custom Wood | 11,184 | 17.5 % | 10,998 | 17.7 % | 186 | 1.7 % | 22,171 | 17.5 % | 20,869 | 16.8 % | 1,302 | 6.2 % |
| Bassett Casegoods | 9,948 | 15.6 % | 9,524 | 15.3 % | 424 | 4.5 % | 20,745 | 16.3 % | 21,797 | 17.5 % | (1,052) | -4.8 % |
| Accessories | 1,068 | 1.7 % | 911 | 1.5 % | 157 | 17.2 % | 2,292 | 1.8 % | 1,699 | 1.4 % | 593 | 34.9 % |
| Total | \$63,788 | 100.0 % | \$62,293 | 100.0 % | \$1,495 | 2.4 % | \$126,888 | 100.0 % | \$124,268 | 100.0 % | \$2,620 | 2.1 % |

PART I-FINANCIAL INFORMATION-CONTINUEDBASSETT FURNITURE INDUSTRIES, INCORPORATED AND SUBSIDIARIESMAY 26, 2018(Dollars in thousands except share and per share data)*Wholesale Backlog*

The dollar value of wholesale backlog, representing orders received but not yet shipped to dealers and Company stores, was \$15,525 at May 26, 2018 as compared with \$16,095 at May 27, 2017.

Retail – Company-owned Stores Segment

Results for the retail segment for the three and six months ended May 26, 2018 and May 27, 2017 are as follows:

| | Quarter Ended | | | Change | | | Six Months Ended | | | Change | | |
|-----------------------------|---------------|--------|--------------|--------|---------|---------|------------------|--------|--------------|--------|---------|---------|
| | May 26, 2018 | | May 27, 2017 | | Dollars | Percent | May 26, 2018 | | May 27, 2017 | | Dollars | Percent |
| Net sales | \$68,682 | 100.0% | \$67,144 | 100.0% | \$1,538 | 2.3 % | \$133,343 | 100.0% | \$128,737 | 100.0% | \$4,606 | 3.6 % |
| Gross profit | 35,753 | 52.1 % | 34,072 | 50.7 % | 1,681 | 4.9 % | 68,420 | 51.3 % | 64,206 | 49.9 % | 4,214 | 6.6 % |
| SG&A expenses | 33,926 | 49.4 % | 32,236 | 48.0 % | 1,690 | 5.2 % | 67,404 | 50.5 % | 62,907 | 48.9 % | 4,497 | 7.1 % |
| New store pre-opening costs | 201 | 0.3 % | 469 | 0.7 % | (268) | -57.1% | 903 | 0.7 % | 1,275 | 1.0 % | (372) | -29.2 % |
| Income from operations | \$1,626 | 2.4 % | \$1,367 | 2.0 % | \$259 | 18.9 % | \$113 | 0.1 % | \$24 | 0.0 % | \$89 | 370.8 % |

Results for comparable stores[†](53 stores for the quarter) are as follows:

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| | Quarter Ended | | | Change | | Six Months Ended | | | | Change | | |
|------------------------|---------------|--------|--------------|--------|-----------|------------------|--------------|--------|--------------|--------|---------|---------|
| | May 26, 2018 | | May 27, 2017 | | Dollars | Percent | May 26, 2018 | | May 27, 2017 | | Dollars | Percent |
| Net sales | \$60,058 | 100.0% | \$61,132 | 100.0% | \$(1,074) | -1.8% | \$118,910 | 100.0% | \$118,106 | 100.0% | \$804 | 0.7% |
| Gross profit | 31,226 | 52.0% | 31,094 | 50.9% | 132 | 0.4% | 61,028 | 51.3% | 59,263 | 50.2% | 1,765 | 3.0% |
| SG&A expenses | 28,563 | 47.6% | 28,325 | 46.3% | 238 | 0.8% | 57,589 | 48.4% | 56,579 | 47.9% | 1,010 | 1.8% |
| Income from operations | \$2,663 | 4.4% | \$2,769 | 4.5% | \$(106) | -3.8% | \$3,439 | 2.9% | \$2,684 | 2.3% | \$755 | 28.1% |

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

Results for all other stores are as follows:

| | Quarter Ended | | | Change | | Six Months Ended | | | | Change | | |
|-----------------------------|---------------|--------|--------------|--------|---------|------------------|--------------|--------|--------------|--------|---------|---------|
| | May 26, 2018 | | May 27, 2017 | | Dollars | Percent | May 26, 2018 | | May 27, 2017 | | Dollars | Percent |
| Net sales | \$8,624 | 100.0% | \$6,012 | 100.0% | \$2,612 | 43.4% | \$14,433 | 100.0% | \$10,631 | 100.0% | \$3,802 | 35.8% |
| Gross profit | 4,527 | 52.5% | 2,978 | 49.5% | 1,549 | 52.0% | 7,392 | 51.2% | 4,943 | 46.5% | 2,449 | 49.5% |
| SG&A expenses | 5,363 | 62.2% | 3,911 | 65.1% | 1,452 | 37.1% | 9,815 | 68.0% | 6,328 | 59.5% | 3,487 | 55.1% |
| New store pre-opening costs | 201 | 2.3% | 469 | 7.8% | (268) | -57.1% | 903 | 6.3% | 1,275 | 12.0% | (372) | -29.2% |
| Loss from operations | \$(1,037) | -12.0% | \$(1,402) | -23.3% | \$365 | -26.0% | \$(3,326) | -23.0% | \$(2,660) | -25.0% | \$(666) | 25.0% |

Quarterly Analysis of Results - Retail

The second quarter 2018 increase in net sales for the 64 Company-owned stores over the prior year was comprised of a \$2,612 increase in non-comparable store sales partially offset by a 1.8% decrease in 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 2.6% for the second quarter of 2018 as compared to the second quarter of 2017.

PART I-FINANCIAL INFORMATION-CONTINUED

BASSETT FURNITURE INDUSTRIES, INCORPORATED AND SUBSIDIARIES

MAY 26, 2018

(Dollars in thousands except share and per share data)

The increase in comparable store gross margins to 52.0% in the second quarter of 2018 from 50.9% in the prior year period is primarily due to improved pricing strategies and product mix. SG&A expenses as a percentage of sales for comparable stores increased over 2017 due primarily to higher personnel and health care costs.

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 \$400 to \$600 per store. During the second quarter of 2018 we incurred \$411 of post-opening losses associated with the four new stores opened during the first and second quarters compared with \$730 of post-opening losses during the second quarter of 2017.

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.

Year-to-date Analysis of Results - Retail

The six month increase in net sales for the 64 Company-owned stores over the prior year was comprised of a 0.7% increase in comparable store sales along with a \$3,802 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 2.6% for the first half of 2018 as compared to prior year period.

The increase in comparable store gross margins to 51.3% for the first half of 2018 from 50.2% in the prior year period is primarily due to improved pricing strategies and product mix. SG&A expenses as a percentage of sales for comparable stores increased over 2017 due primarily to higher personnel and health care costs.

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 \$400 to \$600 per store. During the first half of 2018 we incurred \$1,151 of post-opening losses associated with the six new stores opened during the first half of 2018 and late 2017 compared with \$730 of post-opening losses during the first half of 2017.

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 \$28,697, or an average of \$448 per open store at May 26, 2018 as compared with a retail backlog of \$30,065, or an average of \$485 per open store at May 27, 2017.

PART I-FINANCIAL INFORMATION-CONTINUEDBASSETT FURNITURE INDUSTRIES, INCORPORATED AND SUBSIDIARIESMAY 26, 2018(Dollars in thousands except share and per share data)Logistical Services Segment

Results for our logistical services segment for the three and six months ended May 26, 2018 and May 27, 2017 are as follows:

| | Quarter Ended | | May 27, 2017 | | Change | | Six Months Ended | | May 27, 2017 | | Change | |
|-----------------------------|---------------|--------|--------------|--------|---------|---------|------------------|--------|--------------|--------|---------|---------|
| | May 26, 2018 | | | | Dollars | Percent | May 26, 2018 | | | | Dollars | Percent |
| Logistical services revenue | \$24,929 | 100.0% | \$24,626 | 100.0% | \$303 | 1.2 % | \$50,178 | 100.0% | \$46,960 | 100.0% | \$3,218 | 6.9% |
| Operating expenses | 24,640 | 98.8 % | 23,828 | 96.8 % | 812 | 3.4 % | 49,559 | 98.8 % | 46,388 | 98.8 % | 3,171 | 6.8% |
| Income from operations | \$289 | 1.2 % | \$798 | 3.2 % | \$(509) | -63.8% | \$619 | 1.2 % | \$572 | 1.2 % | \$47 | 8.2% |

Quarterly Analysis of Operations – Logistical Services

Zenith's 2018 increase in revenue over the second quarter of 2017 resulted from a 3.4% increase in revenue from non-Bassett customers partially offset by a 1.6% decline in revenue from Bassett. Zenith's operating profit decreased primarily due to increased fleet insurance costs due to claims experience, higher fuel costs and inefficiencies in the final mile operations. Operating expenses for the three months ended May 26, 2018 and May 27, 2017 include non-cash depreciation and amortization charges of \$1,091 and \$1,195, respectively.

Year-to-date Analysis of Operations – Logistical Services

Zenith's 2018 increase in revenue over the first half of 2017 resulted from a 9.3% increase in revenue from non-Bassett customers along with a 3.8% increase in revenue from Bassett. Zenith's operating profit increased slightly over the first half of 2017 while remaining unchanged as a percentage of revenue. Improved load efficiency in the middle mile operations resulting in higher revenue per mile was offset by increased fleet insurance costs due to claims experience, higher fuel costs and inefficiencies in the final mile operations. Operating expenses for the three months ended May 26, 2018 and May 27, 2017 include non-cash depreciation and amortization charges of \$2,164 and \$2,430, respectively.

PART I-FINANCIAL INFORMATION-CONTINUED

BASSETT FURNITURE INDUSTRIES, INCORPORATED AND SUBSIDIARIES

MAY 26, 2018

(Dollars in thousands except share and per share data)

Other Items Affecting Net Income

Other Loss, Net

Other loss, net, for the three and six months ended May 26, 2018 was \$233 and \$860, respectively, as compared to \$678 and \$1,411 for the three and six months ended May 27, 2017, respectively. The decreases for both the three and six month periods are primarily attributable to the recognition during the second quarter of 2018 of \$266 in death benefits received from life insurance policies covering a former executive, along with lower interest expense due to overall lower levels of debt and increased interest income due to rising yields on our short-term investments compared to the prior year period.

Income Taxes and Impact of Tax Cuts and Jobs Act

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.

On December 22, 2017, The Tax Cuts and Jobs Act (the “Act”) was signed into law. The Act reduced the federal statutory corporate income tax rate from 35% to 21% effective January 1, 2018 for all corporate taxpayers, while most other provisions of the Act take effect for fiscal years beginning on or after January 1, 2018. Therefore, we will compute our income tax expense for fiscal 2018 using a blended federal statutory rate of 22.2%. The 21% federal statutory rate, as well as certain other provisions of the Act including the elimination of the domestic manufacturing deduction and new limitations on certain business deductions, will apply to our 2019 fiscal year and thereafter.

The federal rate reduction has had a significant impact on our provision for income taxes for the three and six months ended May 26, 2018. Our effective tax rates for the three and six months ended May 26, 2018 of 21.3% and 51.4%,

respectively, differ from the fiscal 2018 blended Federal statutory rate of 22.2% primarily due to a discrete charge (benefit) of (\$155) and \$2,032, respectively, arising from the re-measurement of our deferred tax assets. Other items impacting our effective tax rate for the three and six months ended May 26, 2018 include the effects of state income taxes and various permanent differences including the favorable impacts of excess tax benefits on stock-based compensation of \$16 and \$197, respectively, non-taxable life insurance proceeds of \$266 during the second quarter of 2018, and the Section 199: Domestic Production Activities Deduction.

The charge for the re-measurement of our deferred tax assets was based on reasonable estimates and therefore has been recorded as a provisional amount. We may alter our estimates during the remainder of fiscal 2018 as we continue to process data to finalize the underlying calculations and also analyze other provisions of the Act to determine if they will impact our effective tax rate in fiscal 2018 or in the future. We will continue to refine our adjustments through the permissible measurement period, which is not to extend beyond one year from the enactment of the Act.

Our effective tax rates for the three and six months ended May 27, 2017 of 35.8% and 33.2%, respectively, differed from the federal statutory rate of 35% primarily due to the effects of state income taxes and various permanent differences including the favorable impacts of excess tax benefits on stock-based compensation of \$327 during the six months ended May 27, 2017 and the Section 199: Domestic Production Activities Deduction.

PART I-FINANCIAL INFORMATION-CONTINUED

BASSETT FURNITURE INDUSTRIES, INCORPORATED AND SUBSIDIARIES

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(Dollars in thousands except share and per share data)

Liquidity and Capital Resources

We are committed to maintaining a strong balance sheet in order to weather challenging industry conditions, to allow us to take advantage of opportunities as market conditions change, and to execute our long-term retail strategies.

Cash Flows

Cash flow from operations for the first half of 2018 was a net use of \$170 compared to cash provided by operations of \$9,492 for the first half of 2017, representing a decrease of \$9,662 in cash flows from operations. This decrease is primarily due to lower operating margins and changes in working capital as well as a cash flow deficit from the startup of Lane Venture.

Our overall cash position decreased by \$31,400 during the first half of 2018. In addition to cash used in operations, we used \$20,755 of cash in investing activities, primarily consisting of our \$15,556 investment in Lane Venture and capital expenditures of \$7,662 which included retail store relocations, retail store remodels, in-process spending on new stores, expanding and upgrading our manufacturing capabilities and additional material handling equipment for our logistical services operation, partially offset by \$2,463 of proceeds from the sale of our retail location in Spring, Texas. Net cash used in financing activities was \$10,475, including dividend payments of \$6,124 and the final \$3,000 installment payment on our Zenith acquisition note payable. With cash and cash equivalents and short-term investments totaling \$45,674 on hand at May 26, 2018, we believe we have sufficient liquidity to fund operations for the foreseeable future.

Debt and Other Obligations

Our credit facility with our bank 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 26, 2018, we had \$2,249 outstanding under standby letters of credit against our line, leaving availability under our credit line of \$12,751. In addition, we have outstanding standby letters of credit with another bank totaling \$381.

At May 26, 2018 we have outstanding principal totaling \$541 under real estate notes payable of which \$432 matures within one year of the balance sheet date. See Note 8 to our condensed consolidated financial statements for additional details regarding these notes, including collateral and future maturities. We expect to satisfy these obligations as they mature using cash flow from operations or our available cash on hand.

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. We had obligations of \$180,384 at May 26, 2018 for future minimum lease payments under non-cancelable operating leases having remaining terms in excess of one year. We also have guaranteed certain lease obligations of licensee operators. Remaining terms under these lease guarantees range from approximately one to five years. We were contingently liable under licensee lease obligation guarantees in the amount of \$2,360 at May 26, 2018. See Note 11 to our condensed consolidated financial statements for additional details regarding our leases and lease guarantees.

Investment in Retail Real Estate

We have a substantial investment in real estate acquired for use as retail locations. To the extent such real estate is occupied by Company-owned retail stores, it is included in property and equipment, net, in the accompanying condensed consolidated balance sheets and is considered part of our retail segment. The net book value of such retail real estate occupied by Company-owned stores was \$20,303 at May 26, 2018. All other retail real estate that we own, consisting of locations formerly leased to our licensees and now leased to others, is included in other assets in the accompanying condensed consolidated balance sheets. The net book value of such real estate, which is considered part of our wholesale segment, was \$1,706 at May 26, 2018.

PART I-FINANCIAL INFORMATION-CONTINUED

BASSETT FURNITURE INDUSTRIES, INCORPORATED AND SUBSIDIARIES

MAY 26, 2018

(Dollars in thousands except share and per share data)

The following table summarizes our total investment in retail real estate owned at May 26, 2018:

| | Number of Locations | Aggregate Square Footage | Net Book Value |
|--|---------------------------|--------------------------------|----------------------|
| Real estate occupied by Company-owned and operated stores, included in property and equipment, net (1) | 9 | 223,570 | \$20,303 |
| Investment real estate leased to others, included in other assets | 2 | 41,021 | 1,706 |
| Total Company investment in retail real estate | 11 | 264,591 | \$22,009 |

(1)Includes two properties encumbered under mortgages totalling \$541 at May 26, 2018.

Critical Accounting Policies and Estimates

There have been no material changes to our critical accounting policies and estimates from the information provided in Item 7, “Management’s Discussion and Analysis of Financial Condition and Results of Operations”, included in our Annual Report on Form 10-K for the fiscal year ended November 25, 2017.

Off-Balance Sheet Arrangements

We utilize stand-by letters of credit in the procurement of certain goods in the normal course of business. We lease land and buildings that are primarily used in the operation of both Company-owned and licensee stores as well as land

and buildings used in our logistical services segment. We also lease transportation equipment used in our logistical services segment. We have guaranteed certain lease obligations of licensee operators of the stores as part of our retail expansion strategy. See Note 11 to our condensed consolidated financial statements for further discussion of operating leases and lease guarantees, including descriptions of the terms of such commitments and methods used to mitigate risks associated with these arrangements.

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, it is our opinion that the final resolution of these matters will not have a material adverse effect on our financial position or future results of operations. See Note 11 to our condensed consolidated financial statements for further information regarding certain contingencies as of May 26, 2018.

PART I-FINANCIAL INFORMATION-CONTINUED

BASSETT FURNITURE INDUSTRIES, INCORPORATED AND SUBSIDIARIES

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(Dollars in thousands except share and per share data)

Item 3. Quantitative and Qualitative Disclosure about Market Risk:

We are exposed to market risk from changes in the value of foreign currencies. Substantially all of our imports purchased outside of North America are denominated in U.S. dollars. Therefore, we believe that gains or losses resulting from changes in the value of foreign currencies relating to foreign purchases not denominated in U.S. dollars would not be material to our results from operations in fiscal 2018.

We are exposed to market risk from changes in the cost of raw materials used in our manufacturing processes, principally wood, woven fabric, and foam products. A continued recovery in home construction could result in increases in wood and fabric costs from current levels, and the cost of foam products, which are petroleum-based, is sensitive to changes in the price of oil.

We are also exposed to commodity price risk related to diesel fuel prices for fuel used in our logistical services segment. We manage our exposure to that risk primarily through the application of fuel surcharges to our customers.

We have potential exposure to market risk related to conditions in the commercial real estate market. Our retail real estate holdings of \$1,706 at May 26, 2018 for stores formerly operated by licensees as well as our holdings of \$20,303 at May 26, 2018 for Company-owned stores could suffer significant impairment in value if we are forced to close additional stores and sell or lease the related properties during periods of weakness in certain markets. Additionally, if we are required to assume responsibility for payment under the lease obligations of \$2,360 which we have guaranteed on behalf of licensees as of May 26, 2018, we may not be able to secure sufficient sub-lease income in the current market to offset the payments required under the guarantees.

Item 4. Controls and Procedures:

The Company's principal executive officer and principal accounting officer have evaluated the Company's disclosure controls and procedures (as defined in Exchange Act Rule 13a-15(e)) as of the end of the period covered by this Quarterly Report on Form 10-Q. Based upon their evaluation, the principal executive officer and principal accounting officer concluded that the Company's disclosure controls and procedures are effective. There has been no change in the Company's internal control over financial reporting during the Company's most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

PART I-FINANCIAL INFORMATION-CONTINUED

BASSETT FURNITURE INDUSTRIES, INCORPORATED AND SUBSIDIARIES

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(Dollars in thousands except share and per share data)

Safe-harbor, forward-looking statements:

The discussion in items 2 and 3 above contains certain forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995 with respect to the financial condition, results of operations and business of Bassett Furniture Industries, Incorporated and subsidiaries. Such forward-looking statements are identified by use of forward-looking words such as “*anticipates*”, “*believes*”, “*plans*”, “*estimates*”, “*expects*”, “*aims*” and “*intends*” or words or phrases of similar expression. These forward-looking statements involve certain risks and uncertainties. No assurance can be given that any such matters will be realized. Important factors that could cause actual results to differ materially from those contemplated by such forward-looking statements include:

• competitive conditions in the home furnishings industry

• general economic conditions, including the strength of the housing market in the United States

• overall retail traffic levels and consumer demand for home furnishings

• ability of our customers and consumers to obtain credit

• Bassett store openings and store closings and the profitability of the stores (independent licensees and Company-owned retail stores)

• ability to implement our Company-owned retail strategies and realize the benefits from such strategies as they are implemented

fluctuations in the cost and availability of raw materials, fuel, labor and sourced products

results of marketing and advertising campaigns

effectiveness and security of our information and technology systems

future tax legislation, or regulatory or judicial positions

ability to efficiently manage the import supply chain to minimize business interruption

concentration of domestic manufacturing, particularly of upholstery products, and the resulting exposure to business interruption from accidents, weather and other events and circumstances beyond our control

general risks associated with providing freight transportation and other logistical services through our wholly-owned subsidiary, Zenith Freight Lines, LLC

Additionally, other risks that could cause actual results to differ materially from those contemplated by such forward-looking statements are set forth in Item 1A. Risk Factors in the Company's Annual Report on Form 10-K for fiscal 2017.

You should keep in mind that any forward-looking statement made by us in this report or elsewhere speaks only as of the date on which such forward-looking statement is made. New risks and uncertainties arise from time to time, and it is impossible for us to predict these events or how they may affect us. We have no duty to, and do not intend to, update or revise the forward-looking statements in this discussion after the date hereof, except as may be required by law. In light of these risks and uncertainties, you should keep in mind that the events described in any forward-looking statement made in this report or elsewhere, might not occur.

PART II - OTHER INFORMATIONBASSETT FURNITURE INDUSTRIES INCORPORATED AND SUBSIDIARIESMAY 26, 2018

(Dollars in thousands except share and per share data)

Item 1. Legal Proceedings

None

Item 2. Unregistered Sales of Equity Securities, Use of Proceeds and Issuer Purchases of Equity Securities

The following table summarizes the stock repurchase activity for the three months ended May 26, 2018 and the approximate dollar value of shares that may yet be purchased pursuant to our stock repurchase program:

| | Total Shares Purchased | Average Price Paid | Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs (1) | Approximate Dollar Value of Shares that May Yet Be Purchased Under the Plans or Programs (1) |
|------------------------------|---------------------------------------|-----------------------------------|---|---|
| February 25 - March 31, 2018 | 500 | \$ 28.98 | 500 | \$ 11,195 |
| April 1 - April 28, 2018 | 2,834 | \$ 29.21 | 2,834 | \$ 11,112 |
| April 29 - May 26, 2018 | 17,000 | \$ 28.33 | 17,000 | \$ 10,630 |

The Company is authorized to repurchase Company stock under a plan which was originally announced in 1998. (1) On October 9, 2014, the Board of Directors increased the remaining limit of the repurchase plan to \$20,000. At May 26, 2018, \$10,630 remains available for stock repurchases under the plan.

Item 3. Defaults Upon Senior Securities

None.

Item 6. Exhibits

a. Exhibits:

Exhibit 3a – Articles of Incorporation as amended to date are incorporated herein by reference to the Exhibit to Form 10-Q for the fiscal quarter ended February 28, 1994.

Exhibit 3b – By-laws as amended to date are incorporated herein by reference to Exhibit 3 to Form 8-K filed with the SEC on March 13, 2018.

Exhibit 4 – Registrant hereby agrees to furnish the SEC, upon request, other instruments defining the rights of holders of long-term debt of the Registrant.

Exhibit 31a – Chief Executive Officer’s certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

Exhibit 31b – Chief Financial Officer’s certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

Exhibit 32a – Chief Executive Officer’s certification pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

Exhibit 32b – Chief Financial Officer’s certification pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

PART II - OTHER INFORMATION-CONTINUED

BASSETT FURNITURE INDUSTRIES INCORPORATED AND SUBSIDIARIES

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Exhibit 101.INS XBRL Instance

Exhibit 101.SCH XBRL Taxonomy Extension Schema

Exhibit 101.CAL XBRL Taxonomy Extension Calculation

Exhibit 101.DEF XBRL Taxonomy Extension Definition

Exhibit 101.LAB XBRL Taxonomy Extension Labels

Exhibit 101.PRE XBRL Taxonomy Extension Presentation

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SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this Report to be signed on its behalf by the undersigned thereunto duly authorized.

BASSETT FURNITURE INDUSTRIES, INCORPORATED

/s/ Robert H. Spilman, Jr.

Robert H. Spilman, Jr., Chairman and Chief Executive Officer

June 28, 2018

/s/ J. Michael Daniel

J. Michael Daniel, Senior Vice President and Chief Financial Officer

June 28, 2018

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