





UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549-1004

**FORM 10-Q**

Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934  
FOR QUARTERLY PERIOD ENDED OCTOBER 27, 2007  
COMMISSION FILE NUMBER 1-9656

**LA-Z-BOY INCORPORATED**

(Exact name of registrant as specified in its charter)

MICHIGAN

(State or other jurisdiction of incorporation or organization)

38-0751137

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

1284 North Telegraph Road, Monroe, Michigan

(Address of principal executive offices)

48162-3390

(Zip Code)

Registrant's telephone number, including area code (734) 242-1444

None

(Former name, former address and former fiscal year, if changed since last report.)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by section 13 or 15 (d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports) and (2) has been subject to such filing requirements for the past 90 days.

Yes  No

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

Large accelerated filer  Accelerated filer  Non-accelerated filer

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes  No

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date:

| Class                           | Outstanding at October 27, 2007 |
|---------------------------------|---------------------------------|
| Common Shares, \$1.00 par value | 51,416,118                      |

LA-Z-BOY INCORPORATED  
FORM 10-Q SECOND QUARTER OF FISCAL 2008

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PART I  
FINANCIAL INFORMATION  
**Item 1. Financial Statements**  
**LA-Z-BOY INCORPORATED**  
**CONSOLIDATED STATEMENT OF OPERATIONS**

| <i>(Unaudited, amounts in thousands, except per share data)</i> | Second Quarter Ended |                 |                   | Percent of Sales |          |
|---|----------------------|-----------------|-------------------|------------------|----------|
|   | 10/27/07             | 10/28/06        | % Over<br>(Under) | 10/27/07         | 10/28/06 |
| Sales   | \$ 365,434           | \$ 414,614      | -11.9%            | 100.0%           | 100.0%   |
| Cost of sales   |                      |                 |                   |                  |          |
| Cost of goods sold  | 266,658              | 306,351         | -13.0%            | 73.0%            | 73.9%    |
| Restructuring   | 518                  | (400)           | -229.5%           | 0.1%             | -0.1%    |
| Total cost of sales   | 267,176              | 305,951         | -12.7%            | 73.1%            | 73.8%    |
| Gross profit  | 98,258               | 108,663         | -9.6%             | 26.9%            | 26.2%    |
| Selling, general and administrative                             | 98,098               | 99,887          | -1.8%             | 26.8%            | 24.1%    |
| Write-down of intangibles                                       | 5,809                | —               | N/M               | 1.6%             | —        |
| Restructuring   | 449                  | 2,265           | -80.2%            | 0.1%             | 0.5%     |
| Operating income (loss)   | (6,098)              | 6,511           | -193.7%           | -1.7%            | 1.6%     |
| Interest expense  | 2,120                | 2,614           | -18.9%            | 0.6%             | 0.6%     |
| Other income, net   | 1,374                | 1,348           | 1.9%              | 0.4%             | 0.3%     |
| Income (loss) from continuing operations before income taxes    | (6,844)              | 5,245           | -230.5%           | -1.9%            | 1.3%     |
| Income tax expense (benefit)                                    | (3,192)              | 1,949           | -263.8%           | 46.6%*           | 37.2%*   |
| Income (loss) from continuing operations                        | (3,652)              | 3,296           | -210.8%           | -1.0%            | 0.8%     |
| Loss from discontinued operations (net of tax)                  | (6,282)              | (1,342)         | -368.1%           | -1.7%            | -0.3%    |
| Net income (loss)   | <u>\$ (9,934)</u>    | <u>\$ 1,954</u> | -608.4%           | -2.7%            | 0.5%     |
| Basic average shares  | 51,410               | 51,373          |                   |                  |          |
| Basic income (loss) from continuing operations per share        | \$ (0.07)            | \$ 0.06         |                   |                  |          |
| Discontinued operations per share (net of tax)                  | \$ (0.12)            | \$ (0.02)       |                   |                  |          |
| Basic net income (loss) per share                               | <u>\$ (0.19)</u>     | <u>\$ 0.04</u>  |                   |                  |          |
| Diluted average shares  | 51,410               | 51,639          |                   |                  |          |
| Diluted income (loss) from continuing operations per share      | \$ (0.07)            | \$ 0.06         |                   |                  |          |
| Discontinued operations per share (net of tax)                  | \$ (0.12)            | \$ (0.02)       |                   |                  |          |
| Diluted net income (loss) per share                             | <u>\$ (0.19)</u>     | <u>\$ 0.04</u>  |                   |                  |          |
| Dividends paid per share  | \$ 0.12              | \$ 0.12         |                   |                  |          |

\* As a percent of pretax income, not sales.

N/M = not meaningful

The accompanying Notes to Consolidated Financial Statements are an integral part of these statements.

**LA-Z-BOY INCORPORATED**  
**CONSOLIDATED STATEMENT OF OPERATIONS**

| <i>(Unaudited, amounts in thousands, except per share data)</i> | Six Months Ended   |                 |                   | Percent of Sales |          |
|---|--------------------|-----------------|-------------------|------------------|----------|
|   | 10/27/07           | 10/28/06        | % Over<br>(Under) | 10/27/07         | 10/28/06 |
| Sales   | \$ 709,830         | \$ 808,537      | -12.2%            | 100.0%           | 100.0%   |
| Cost of sales   |                    |                 |                   |                  |          |
| Cost of goods sold  | 525,801            | 602,359         | -12.7%            | 74.1%            | 74.5%    |
| Restructuring   | 3,079              | (400)           | -869.8%           | 0.4%             | —        |
| Total cost of sales   | 528,880            | 601,959         | -12.1%            | 74.5%            | 74.5%    |
| Gross profit  | 180,950            | 206,578         | -12.4%            | 25.5%            | 25.5%    |
| Selling, general and administrative                             | 192,606            | 194,570         | -1.0%             | 27.1%            | 24.1%    |
| Write-down of intangibles                                       | 5,809              | —               | N/M               | 0.8%             | —        |
| Restructuring   | 1,569              | 2,265           | -30.7%            | 0.2%             | 0.3%     |
| Operating income (loss)   | (19,034)           | 9,743           | -295.4%           | -2.7%            | 1.2%     |
| Interest expense  | 4,217              | 5,140           | -18.0%            | 0.6%             | 0.6%     |
| Other income, net   | 2,822              | 1,618           | 74.4%             | 0.4%             | 0.2%     |
| Income (loss) from continuing operations before income taxes    | (20,429)           | 6,221           | -428.4%           | -2.9%            | 0.8%     |
| Income tax expense (benefit)                                    | (8,235)            | 1,833           | -549.3%           | 40.3%*           | 29.5%*   |
| Income (loss) from continuing operations                        | (12,194)           | 4,388           | -377.9%           | -1.7%            | 0.5%     |
| Loss from discontinued operations (net of tax)                  | (6,434)            | (139)           | N/M%              | -0.9%            | —        |
| Net income (loss)   | <u>\$ (18,628)</u> | <u>\$ 4,249</u> | -538.4%           | -2.6%            | 0.5%     |
| Basic average shares  | 51,395             | 51,580          |                   |                  |          |
| Basic income (loss) from continuing operations per share        | \$ (0.24)          | \$ 0.08         |                   |                  |          |
| Discontinued operations per share (net of tax)                  | \$ (0.12)          | —               |                   |                  |          |
| Basic net income (loss) per share                               | <u>\$ (0.36)</u>   | <u>\$ 0.08</u>  |                   |                  |          |
| Diluted average shares  | 51,395             | 51,806          |                   |                  |          |
| Diluted income (loss) from continuing operations per share      | \$ (0.24)          | \$ 0.08         |                   |                  |          |
| Discontinued operations per share (net of tax)                  | \$ (0.12)          | —               |                   |                  |          |
| Diluted net income (loss) per share                             | <u>\$ (0.36)</u>   | <u>\$ 0.08</u>  |                   |                  |          |
| Dividends paid per share  | \$ 0.24            | \$ 0.24         |                   |                  |          |

\* As a percent of pretax income, not sales.

N/M = not meaningful

The accompanying Notes to Consolidated Financial Statements are an integral part of these statements.

**LA-Z-BOY INCORPORATED**  
**CONSOLIDATED BALANCE SHEET**

| <i>(Unaudited, amounts in thousands)</i>       | 10/27/07         | 10/28/06         | Increase/(Decrease) |         | 4/28/07          |
|--|------------------|------------------|---------------------|---------|------------------|
|  |                  |                  | Dollars             | Percent |                  |
| <b>Current assets</b>                          |                  |                  |                     |         |                  |
| Cash and equivalents                           | \$ 32,692        | \$ 20,529        | \$ 12,163           | 59.2%   | \$ 51,721        |
| Receivables, net                               | 215,275          | 253,519          | (38,244)            | -15.1%  | 230,399          |
| Inventories, net                               | 190,985          | 237,885          | (46,900)            | -19.7%  | 197,790          |
| Deferred income taxes—current                  | 14,337           | 16,043           | (1,706)             | -10.6%  | 17,283           |
| Assets of discontinued operations              | 3,634            | —                | 3,634               | N/M     | 24,278           |
| Other current assets                           | 27,073           | 29,076           | (2,003)             | -6.9%   | 19,327           |
| Total current assets                           | <u>483,996</u>   | <u>557,052</u>   | <u>(73,056)</u>     | -13.1%  | 540,798          |
| Property, plant and equipment, net             | 180,912          | 204,904          | (23,992)            | -11.7%  | 183,218          |
| Deferred income taxes—long term                | 25,608           | 3,451            | 22,157              | N/M     | 15,380           |
| Goodwill                                       | 49,850           | 62,736           | (12,886)            | -20.5%  | 55,659           |
| Trade names                                    | 9,006            | 18,794           | (9,788)             | -52.1%  | 9,472            |
| Other long-term assets                         | 76,545           | 80,166           | (3,621)             | -4.5%   | 74,164           |
| Total assets                                   | <u>\$825,917</u> | <u>\$927,103</u> | <u>\$(101,186)</u>  | -10.9%  | <u>\$878,691</u> |
| <b>Current liabilities</b>                     |                  |                  |                     |         |                  |
| Short-term borrowings                          | \$ —             | \$ 35,000        | \$ (35,000)         | -100.0% | \$ —             |
| Current portion of long-term debt              | 38,353           | 3,295            | 35,058              | N/M     | 37,688           |
| Accounts payable                               | 54,194           | 72,308           | (18,114)            | -25.1%  | 68,089           |
| Liabilities of discontinued operations         | 1,664            | —                | 1,664               | N/M     | 3,843            |
| Accrued expenses and other current liabilities | 103,130          | 114,762          | (11,632)            | -10.1%  | 118,590          |
| Total current liabilities                      | <u>197,341</u>   | <u>225,365</u>   | <u>(28,024)</u>     | -12.4%  | 228,210          |
| Long-term debt                                 | 110,774          | 147,799          | (37,025)            | -25.1%  | 111,714          |
| Income taxes payable — long term               | 7,084            | —                | 7,084               | N/M     | —                |
| Other long-term liabilities                    | 56,474           | 54,920           | 1,554               | 2.8%    | 53,419           |
| Contingencies and commitments                  | —                | —                | —                   | —       | —                |
| <b>Shareholders' equity</b>                    |                  |                  |                     |         |                  |
| Common shares, \$1 par value                   | 51,416           | 51,364           | 52                  | 0.1%    | 51,377           |
| Capital in excess of par value                 | 206,636          | 206,145          | 491                 | 0.2%    | 208,283          |
| Retained earnings                              | 193,681          | 236,635          | (42,954)            | -18.2%  | 223,896          |
| Accumulated other comprehensive income         | 2,511            | 4,875            | (2,364)             | -48.5%  | 1,792            |
| Total shareholders' equity                     | <u>454,244</u>   | <u>499,019</u>   | <u>(44,775)</u>     | -9.0%   | <u>485,348</u>   |
| Total liabilities and shareholders' equity     | <u>\$825,917</u> | <u>\$927,103</u> | <u>\$(101,186)</u>  | -10.9%  | <u>\$878,691</u> |

The accompanying Notes to Consolidated Financial Statements are an integral part of these statements.

**LA-Z-BOY INCORPORATED**  
**CONSOLIDATED STATEMENT OF CASH FLOWS**

| <i>(Unaudited, amounts in thousands)</i>   | Second Quarter Ended |           | Six Months Ended |           |
|--|----------------------|-----------|------------------|-----------|
|  | 10/27/07             | 10/28/06  | 10/27/07         | 10/28/06  |
| <b>Cash flows from operating activities</b>                                      |                      |           |                  |           |
| Net income (loss)  | \$ (9,934)           | \$ 1,954  | \$ (18,628)      | \$ 4,249  |
| Adjustments to reconcile net income (loss) to cash used for operating activities |                      |           |                  |           |
| Loss (gain) on sale of discontinued operations (net of tax)                      | 3,990                | —         | 3,990            | (1,280)   |
| Write-down of businesses held for sale (net of tax)                              | 2,159                | —         | 2,159            | —         |
| Write-down of intangibles (net of tax)   | 3,689                | —         | 3,689            | —         |
| Restructuring  | 967                  | 1,865     | 4,648            | 1,865     |
| Provision for doubtful accounts  | 1,505                | 1,643     | 3,619            | 2,807     |
| Depreciation and amortization  | 6,093                | 6,809     | 12,313           | 13,889    |
| Stock-based compensation expense   | 1,001                | 1,861     | 1,862            | 2,732     |
| Change in receivables  | (13,409)             | (24,228)  | 9,188            | (2,945)   |
| Change in inventories  | 15,323               | 873       | 9,252            | (17,117)  |
| Change in payables   | 1,000                | (2,060)   | (14,414)         | (9,379)   |
| Change in other assets and liabilities   | 6,568                | (8,623)   | (16,678)         | (15,570)  |
| Change in deferred taxes   | (4,671)              | (3,110)   | (6,146)          | (6,766)   |
| Total adjustments  | 24,215               | (24,970)  | 13,482           | (31,764)  |
| Net cash provided by (used for) operating activities                             | 14,281               | (23,016)  | (5,146)          | (27,515)  |
| <b>Cash flows from investing activities</b>                                      |                      |           |                  |           |
| Proceeds from disposals of assets  | 867                  | 3,633     | 7,282            | 24,962    |
| Proceeds from sale of discontinued operations                                    | 4,019                | 3,184     | 4,019            | 33,166    |
| Capital expenditures   | (5,970)              | (5,767)   | (15,599)         | (15,010)  |
| Purchases of investments   | (6,648)              | (2,760)   | (13,270)         | (8,392)   |
| Proceeds from sales of investments   | 7,801                | 2,320     | 14,593           | 8,017     |
| Change in other long-term assets   | 365                  | (701)     | 385              | (196)     |
| Net cash provided by (used for) investing activities                             | 434                  | (91)      | (2,590)          | 42,547    |
| <b>Cash flows from financing activities</b>                                      |                      |           |                  |           |
| Proceeds from debt   | 171                  | 56,276    | 817              | 78,675    |
| Payments on debt   | (192)                | (31,266)  | (1,092)          | (78,680)  |
| Stock issued for stock and employee benefit plans                                | (94)                 | (342)     | (116)            | 766       |
| Repurchases of common stock  | —                    | (3,261)   | —                | (6,947)   |
| Dividends paid   | (6,232)              | (6,213)   | (12,441)         | (12,462)  |
| Net cash provided by (used for) financing activities                             | (6,347)              | 15,194    | (12,832)         | (18,648)  |
| Effect of exchange rate changes on cash and equivalents                          | 538                  | 49        | 1,539            | 56        |
| Change in cash and equivalents   | 8,906                | (7,864)   | (19,029)         | (3,560)   |
| Cash and equivalents at beginning of period                                      | 23,786               | 28,393    | 51,721           | 24,089    |
| Cash and equivalents at end of period  | \$ 32,692            | \$ 20,529 | \$ 32,692        | \$ 20,529 |
| Cash paid (net of refunds) during period — income taxes                          | \$ 758               | \$ 16,889 | \$ 3,893         | \$ 17,097 |
| Cash paid during period — interest   | \$ 1,495             | \$ 1,748  | \$ 3,405         | \$ 4,660  |

The accompanying Notes to Consolidated Financial Statements are an integral part of these statements.

**LA-Z-BOY INCORPORATED**  
**CONSOLIDATED STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY**

| <i>(Unaudited, amounts in thousands)</i>   | Common<br>Shares | Capital in<br>Excess of Par<br>Value | Retained<br>Earnings | Unearned<br>Compensation | Accumulated<br>Other<br>Comprehensive<br>Income(Loss) | Total             |
|--|------------------|--------------------------------------|----------------------|--------------------------|---|-------------------|
| At April 29, 2006  | \$ 51,782        | \$ 210,826                           | \$ 246,387           | (\$ 3,083)               | \$ 4,433  | \$ 510,345        |
| Reclassification of unearned<br>compensation due to adoption of SFAS<br>No. 123(R)       |                  | (3,083)                              |                      | 3,083                    |   | —                 |
| Repurchases of common stock  | (540)            |                                      | (6,407)              |                          |   | (6,947)           |
| Stock issued for stock and employee<br>benefit plans                                     | 135              | (3,458)                              | 4,663                |                          |   | 1,340             |
| Stock option and restricted stock expense  |                  | 3,959                                |                      |                          |   | 3,959             |
| Tax benefit from exercise of options   |                  | 39                                   |                      |                          |   | 39                |
| Dividends paid   |                  |                                      | (24,886)             |                          |   | (24,886)          |
| Comprehensive income (loss)  |                  |                                      |                      |                          |   |                   |
| Net income   |                  |                                      | 4,139                |                          |   |                   |
| Unrealized gain on marketable<br>securities (net of tax of \$0.5 million)                |                  |                                      |                      |                          | 1,145   |                   |
| Realized gain on marketable securities<br>(net of tax of \$0.3 million)                  |                  |                                      |                      |                          | (458)   |                   |
| Translation adjustment   |                  |                                      |                      |                          | 1,418   |                   |
| Change in fair value of cash flow<br>hedges (net of tax)                                 |                  |                                      |                      |                          | (118)   |                   |
| Change in additional minimum pension<br>liability (net of tax of \$0.1 million)          |                  |                                      |                      |                          | 319   |                   |
| Total comprehensive income   |                  |                                      |                      |                          |   | 6,445             |
| Adjustment upon adoption of SFAS<br>No. 158 for pension (net of tax of<br>\$3.2 million) |                  |                                      |                      |                          | (4,947)   | (4,947)           |
| At April 28, 2007  | <u>\$ 51,377</u> | <u>\$ 208,283</u>                    | <u>\$ 223,896</u>    | <u>\$ —</u>              | <u>\$ 1,792</u>                                       | <u>\$ 485,348</u> |
| Stock issued for stock and employee<br>benefit plans                                     | 39               | (3,509)                              | 3,354                |                          |   | (116)             |
| Stock option and restricted stock expense  |                  | 1,862                                |                      |                          |   | 1,862             |
| Dividends paid   |                  |                                      | (12,441)             |                          |   | (12,441)          |
| Comprehensive income (loss)  |                  |                                      |                      |                          |   |                   |
| Net loss   |                  |                                      | (18,628)             |                          |   |                   |
| Unrealized gain on marketable<br>securities (net of tax of \$0.2 million)                |                  |                                      |                      |                          | 409   |                   |
| Realized gain on marketable securities<br>(net of tax of \$0.1 million)                  |                  |                                      |                      |                          | (165)   |                   |
| Translation adjustment   |                  |                                      |                      |                          | 443   |                   |
| Change in the fair value of cash flow<br>hedges (net of tax)                             |                  |                                      |                      |                          | 32  |                   |
| Total comprehensive loss   |                  |                                      |                      |                          |   | (17,909)          |
| Impact of adoption of FIN 48   |                  |                                      | (2,500)              |                          |   | (2,500)           |
| At October 27, 2007  | <u>\$ 51,416</u> | <u>\$ 206,636</u>                    | <u>\$ 193,681</u>    | <u>\$ —</u>              | <u>\$ 2,511</u>                                       | <u>\$ 454,244</u> |

The accompanying Notes to Consolidated Financial Statements are an integral part of these statements.



**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)****Note 1: Basis of Presentation**

The interim financial information is prepared in conformity with generally accepted accounting principles and such principles are applied on a basis consistent with those reflected in our fiscal 2007 Annual Report on Form 10-K, filed with the Securities and Exchange Commission, but does not include all the disclosures required by generally accepted accounting principles. In the opinion of management, the interim financial information includes all adjustments and accruals, consisting only of normal recurring adjustments, which are necessary for a fair presentation of results for the respective interim period.

**Note 2: Interim Results**

The foregoing interim results are not necessarily indicative of the results of operations which will occur for the full fiscal year ending April 26, 2008.

**Note 3: Reclassification**

Certain prior year information has been reclassified to be comparable with the current year presentation.

**Note 4: Inventories**

A summary of inventory follows:

| <i>(Amounts in thousands)</i> | <b>10/27/07</b>   | <b>10/28/06</b>   | <b>4/28/07</b>    |
|-------------------------------|-------------------|-------------------|-------------------|
| Raw materials                 | \$ 71,742         | \$ 80,331         | \$ 69,562         |
| Work in process               | 17,652            | 23,115            | 19,972            |
| Finished goods                | 126,014           | 156,245           | 132,679           |
| FIFO inventories              | 215,408           | 259,691           | 222,213           |
| Excess of FIFO over LIFO      | (24,423)          | (21,806)          | (24,423)          |
| Inventories, net              | <u>\$ 190,985</u> | <u>\$ 237,885</u> | <u>\$ 197,790</u> |

[Table of Contents](#)**Note 5: Goodwill and Other Intangible Assets**

In accordance with Statement of Financial Accounting Standards No. 142, *Goodwill and Other Intangible Assets*, (“SFAS No. 142”), trade names are tested at least annually for impairment by comparing their fair value to their carrying values. The fair value for each trade name is established based upon a royalty savings approach. Additionally, goodwill is tested for impairment by comparing the fair value of our operating units to their carrying values. The fair value for each operating unit is established based upon a combination of the discounted cash flows and the projected profitability of the market in which the entity operates.

With the decline in the housing market affecting Florida greater than the rest of the country, we have delayed our store growth in the market. The double-digit decline in sales over the past twelve months coupled with our change in the timing of our store build-out triggered us to evaluate our goodwill in South Florida in advance of our normal testing in the fourth quarter of each fiscal year. We have not experienced as dramatic a sales decline and have not made any strategic decisions to delay store build-out in our other retail markets that have goodwill. As a result of the significant change in our valuation model for this business, we recorded an impairment charge of \$5.8 million, \$3.7 million after tax, in the second quarter of fiscal 2008.

In the first quarter of fiscal 2008, we reevaluated our tax reserves relating to an acquisition in fiscal 2000. Due primarily to the lapsing of statutes of limitations, a reduction of the tax reserves was recorded. This reduction in the tax reserves was recorded as a reduction in the remaining acquired intangible assets, which consisted of trade names and totaled \$0.7 million. Of this reduction \$0.3 million related to trade names of our discontinued operations and is not shown in the table that follows.

The following table summarizes the changes to goodwill and trade names during the first half of fiscal 2008:

| <i>(Amounts in thousands)</i> | <b>Balance<br/>as of<br/>4/28/07</b> | <b>Impairments<br/>and<br/>Dispositions</b> | <b>Balance<br/>as of<br/>10/27/07</b> |
|-------------------------------|--------------------------------------|---|---------------------------------------|
| <b>Goodwill</b>               |                                      |   |                                       |
| Upholstery Group              | \$ 19,632                            | \$ —  | \$ 19,632                             |
| Retail Group                  | 27,905                               | (5,809)                                     | 22,096                                |
| Corporate and Other           | 8,122                                | —   | 8,122                                 |
| Consolidated                  | <u>\$ 55,659</u>                     | <u>\$ (5,809)</u>                           | <u>\$ 49,850</u>                      |
| <b>Trade names</b>            |                                      |   |                                       |
| Casegoods Group               | <u>\$ 9,472</u>                      | <u>\$ (466)</u>                             | <u>\$ 9,006</u>                       |

**Note 6: Debt**

| <i>(Amounts in thousands)</i> | <b>Fiscal<br/>Year<br/>Maturity</b> | <b>10/27/07</b>   | <b>4/28/07</b>    |
|-------------------------------|-------------------------------------|-------------------|-------------------|
| Revolving credit facility     | 2010                                | \$ —              | \$ —              |
| Industrial revenue bonds      | 2010-2023                           | 16,851            | 16,851            |
| Private placement notes       | 2008                                | 35,000            | 35,000            |
|                               | 2010                                | 36,000            | 36,000            |
|                               | 2013                                | 50,000            | 50,000            |
| Other debt                    | 2008-2011                           | 9,948             | 9,768             |
| Capital leases                | 2008-2011                           | 1,328             | 1,783             |
| Total debt                    |                                     | 149,127           | 149,402           |
| Less: current portion         |                                     | (38,353)          | (37,688)          |
| Long-term debt                |                                     | <u>\$ 110,774</u> | <u>\$ 111,714</u> |

Certain of our debt agreements require that certain financial covenants be met. As of the end of the second quarter, we were not in compliance with the fixed charge coverage ratio requirement under our revolving credit facility. We obtained an amendment to our fixed charge coverage ratio from our revolving credit facility lenders, dated November 6, 2007, to amend the ratio for our quarter ended October 27, 2007 so that we were in compliance. Although we were in compliance with our other financial covenants, we believe that we will not be in compliance with the fixed charge coverage ratio requirements relating to both our revolving credit facility and private placement notes as of the end of the third quarter, and therefore we have engaged our lead bank to begin structuring a new secured credit facility. We had no unamortized debt issue costs as of the end of the second quarter of fiscal 2008.

We believe that by the end of our fiscal 2008 third quarter, we will be successful in negotiating a long-term credit facility, which we will utilize to pay off our private placement notes. There can be no assurance that an agreement can be reached; however, we consider this scenario unlikely. If an agreement cannot be reached and the lenders were to exercise their right to accelerate the maturity of their notes, this could result in an adverse effect on us unless the lenders were to agree to forbearance or restructuring of the debt.

In order to repay our private placement notes, we will be required to pay a 'make-whole' premium which is currently in the range of \$2.5 — \$3.0 million. We anticipate that the interest rate on the new debt, which is expected to be collateralized by accounts receivable and inventory, will be greater than the average interest rate for the private placement notes.

[Table of Contents](#)**Note 7: Pension Plans**

Net periodic pension costs were as follows:

| <i>(Amounts in thousands)</i>       | <b>Second Quarter Ended</b> |                 | <b>Six Months Ended</b> |                 |
|-------------------------------------|-----------------------------|-----------------|-------------------------|-----------------|
|                                     | <b>10/27/07</b>             | <b>10/28/06</b> | <b>10/27/07</b>         | <b>10/28/06</b> |
| Service cost                        | \$ 441                      | \$ 578          | \$ 882                  | \$ 1,154        |
| Interest cost                       | 1,346                       | 1,338           | 2,692                   | 2,676           |
| Expected return on plan assets      | (1,839)                     | (1,719)         | (3,678)                 | (3,438)         |
| Net amortization and deferral       | —                           | 9               | —                       | 18              |
| Net periodic pension cost (benefit) | <u>\$ (52)</u>              | <u>\$ 206</u>   | <u>\$ (104)</u>         | <u>\$ 410</u>   |

We are not required to make any contributions to the defined benefit plans in fiscal year 2008, however we may make discretionary contributions. We did not make any contributions to the plans during the first six months of fiscal 2008.

**Note 8: Financial Guarantees and Product Warranties**

We have provided financial guarantees relating to leases in connection with certain La-Z-Boy Furniture Galleries® stores which are not operated by the company. The lease guarantees are generally for real estate leases and have terms lasting from five to ten years. These lease guarantees enhance the credit of these dealers. The dealer is required to make periodic fee payments to compensate us for our guarantees. We have recognized liabilities for the fair values of the lease agreements that we have entered into, but they are not material to our financial position.

We would be required to perform under these agreements only if the dealer were to default on the lease. The maximum amount of potential future payments under lease guarantees was \$15.5 million as of October 27, 2007.

We have, from time to time, entered into agreements which resulted in indemnifying third parties against certain liabilities, mainly environmental obligations. We believe that judgments, if any, against us related to such agreements would not have a material effect on our business or financial condition.

Our accounting policy for product warranties is to accrue an estimated liability at the time the revenue is recognized. This estimate is based on historical claims and adjusted for currently known warranty issues.

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A reconciliation of the changes in our product warranty liability is as follows:

| <i>(Amounts in thousands)</i>             | Second Quarter Ended |                  | Six Months Ended |                  |
|---|----------------------|------------------|------------------|------------------|
|   | 10/27/07             | 10/28/06         | 10/27/07         | 10/28/06         |
| Balance as of the beginning of the period | \$ 13,960            | \$ 17,816        | \$ 13,983        | \$ 19,655        |
| Accruals during the period                | 4,148                | 3,574            | 8,331            | 7,007            |
| Adjustments for discontinued operations   | —                    | —                | —                | (956)            |
| Other adjustments during the period       | —                    | (1,496)          | —                | (2,267)          |
| Settlements during the period             | (4,198)              | (3,503)          | (8,404)          | (7,048)          |
| Balance as of the end of the period       | <u>\$ 13,910</u>     | <u>\$ 16,391</u> | <u>\$ 13,910</u> | <u>\$ 16,391</u> |

Other adjustments of \$1.5 million and \$2.3 million for the quarter and six months ended October 28, 2006, respectively, reflected a trend of lower warranty costs incurred beyond one year after the sale of the product. Our current trends show that a majority of our claims were from product sold in the past twelve months thus reducing our liability, along with changes in estimated amounts required for currently known warranty issues.

### **Note 9: Stock-Based Compensation**

We account for share-based compensation transactions in accordance with the provisions of Statement of Financial Accounting Standards No. 123 (Revised 2004), *Share-Based Payment* ("SFAS 123R"). SFAS 123R requires all companies to measure and recognize compensation expense at an amount equal to the fair value of share-based payments granted under compensation arrangements. The fair value for the employee stock options granted during the respective periods were estimated at the date of grant using the Black-Scholes option-pricing model and are amortized on a straight-line basis as compensation expense over the vesting periods of the options. For the three and six months ended October 27, 2007, we recorded total stock-based compensation expense of approximately \$1.0 million and approximately \$1.9 million, respectively. For the three and six months ended October 28, 2006, we recorded total stock-based compensation expense of approximately \$1.9 million and approximately \$2.7 million, respectively.

As of October 27, 2007, there was approximately \$4.0 million of total unrecognized compensation expense related to restricted stock, which we expect to recognize on a straight-line basis over an average remaining service period of approximately 2.5 years.

### **Note 10: Segment Information**

Our reportable operating segments are the Upholstery Group, the Casegoods Group and the Retail Group.

*Upholstery Group.* The operating units in the Upholstery Group are Bauhaus, England, La-Z-Boy and La-Z-Boy UK. This group primarily manufactures and sells upholstered furniture to furniture retailers. Upholstered furniture includes recliners and motion furniture, sofas, loveseats, chairs, ottomans and sleeper sofas.

*Casegoods Group.* The operating units in the Casegoods Group are American Drew/Lea, Hammary and Kincaid. This group primarily sells manufactured or imported wood furniture to furniture retailers. Casegoods product includes tables, chairs, entertainment centers, headboards, dressers, accent pieces and some upholstered furniture.

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*Retail Group.* The Retail Group consists of 70 company-owned La-Z-Boy Furniture Galleries® stores (“the retail network”). The Retail Group sells mostly upholstered furniture to end consumers.

| <i>(Amounts in thousands)</i>  | Second Quarter Ended   |                        | Six Months Ended       |                        |
|--------------------------------|------------------------|------------------------|------------------------|------------------------|
|                                | 10/27/07<br>(13 weeks) | 10/28/06<br>(13 weeks) | 10/27/07<br>(26 weeks) | 10/28/06<br>(26 weeks) |
| <b>Sales</b>                   |                        |                        |                        |                        |
| Upholstery Group               | \$ 269,749             | \$ 304,598             | \$ 524,506             | \$ 599,995             |
| Casegoods Group                | 58,892                 | 74,164                 | 112,466                | 135,190                |
| Retail Group                   | 46,163                 | 52,485                 | 91,394                 | 104,689                |
| VIEs/Eliminations              | (9,370)                | (16,633)               | (18,536)               | (31,337)               |
| Consolidated                   | <u>\$ 365,434</u>      | <u>\$ 414,614</u>      | <u>\$ 709,830</u>      | <u>\$ 808,537</u>      |
| <b>Operating income (loss)</b> |                        |                        |                        |                        |
| Upholstery Group               | \$ 19,036              | \$ 20,162              | \$ 27,903              | \$ 37,787              |
| Casegoods Group                | 3,577                  | 6,200                  | 6,177                  | 9,442                  |
| Retail Group                   | (9,119)                | (8,769)                | (19,193)               | (16,484)               |
| Corporate and Other*           | (12,816)               | (9,217)                | (23,464)               | (19,137)               |
| Intangible write-down          | (5,809)                | —                      | (5,809)                | —                      |
| Restructuring                  | (967)                  | (1,865)                | (4,648)                | (1,865)                |
|                                | <u>\$ (6,098)</u>      | <u>\$ 6,511</u>        | <u>\$ (19,034)</u>     | <u>\$ 9,743</u>        |

\* Variable Interest Entities (“VIEs”) are included in corporate and other.

### **Note 11: Restructuring**

In the fourth quarter of fiscal 2007, we committed to a restructuring plan which included the closures of our Lincolnton, North Carolina and Iuka, Mississippi upholstery manufacturing facilities, the closure of our rough mill lumber operation in North Wilkesboro, North Carolina, the consolidation of operations at our Kincaid Taylorsville, North Carolina upholstery operation and the elimination of a number of positions throughout the remainder of the organization. The Lincolnton and Iuka facility closures occurred in the first quarter of fiscal 2008 and impacted approximately 250 and 150 employees, respectively. The closure of our North Wilkesboro lumber operation, the consolidation of operations at Kincaid’s Taylorsville operation and the remaining activities occurred in the fourth quarter of fiscal 2007 and impacted approximately 100 positions. These decisions were made to help align our company with the current business environment and strengthen our positioning going forward.

During the second quarter and first half of fiscal 2008, we recorded pre-tax restructuring charges in cost of sales of \$0.5 million and \$3.1 million, respectively which equates to \$0.01 and \$0.04 per diluted share, respectively, covering severance and benefits and other restructuring costs. During fiscal 2007, we recorded pre-tax restructuring charges of \$4.3 million or \$0.05 per diluted share covering severance and benefits, write-down of certain fixed assets in addition to other restructuring costs. Of these costs \$4.0 million was reported as a component of Cost of Sales with the remainder in Selling, General and Administrative. The write-down was accounted for in accordance with Statement of Financial Accounting Standards No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets* (“SFAS No. 144”). All other costs were accounted for in accordance with Statement of Financial Accounting Standards No. 146, *Accounting for Costs Associated with Exit or Disposal Activities* (“SFAS No. 146”).

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During fiscal 2007, several of our Retail warehouses were consolidated into larger facilities and several underperforming stores were closed. Approximately 100 jobs were eliminated as a result of these closures. During the second quarter and first half of fiscal 2008, we recorded pre-tax restructuring charges of \$0.4 million and \$1.5 million, respectively, which equates to \$0.01 and \$0.02 per diluted share, respectively, covering contract termination costs for the leases on these facilities, severance and benefits, write-down of certain leasehold improvements in addition to other relocation costs which were expensed as incurred. In fiscal 2007, we recorded pre-tax restructuring charges of \$7.3 million or \$0.08 per diluted share covering contract termination costs for the leases on these facilities, severance and benefits, write-down of certain leasehold improvements in addition to other relocation costs which were expensed as incurred. These costs were reported as a component of Selling, General and Administrative costs. The write-down was accounted for in accordance with SFAS No. 144. All other costs were accounted for in accordance with SFAS No. 146.

As of October 27, 2007, we had a remaining restructuring liability of \$3.2 million which is expected to be paid out or written off as follows: \$2.2 million in fiscal 2008, \$0.5 million in fiscal 2009, \$0.4 million in fiscal 2010 and \$0.1 million thereafter. Contract terminations resulting from the closure of several of our retail stores and warehouses resulted in our restructuring liability being paid out over an extended length of time.

Restructuring liabilities along with charges to expense, cash payments or asset write-downs were as follows:

|                                       | Fiscal 2008        |                       |  |                     |
|---------------------------------------|--------------------|-----------------------|--|---------------------|
|                                       | 4/28/07<br>Balance | Charges to<br>Expense | Cash<br>Payments<br>or Asset<br>Write-Offs | 10/27/07<br>Balance |
| <i>(Amounts in thousands)</i>         |                    |                       |  |                     |
| Severance and benefit-related costs   | \$2,177            | \$1,828               | \$(1,988)                                  | \$2,017             |
| Fixed asset write-downs, net of gains | —                  | (144)                 | 144  | —                   |
| Contract termination costs            | 1,257              | 1,197                 | (1,277)                                    | 1,177               |
| Other                                 | —                  | 1,767                 | (1,767)                                    | —                   |
| Total restructuring                   | \$3,434            | \$4,648               | \$(4,888)                                  | \$3,194             |

|                                       | Fiscal 2007        |                       |  |                    |
|---------------------------------------|--------------------|-----------------------|--|--------------------|
|                                       | 4/29/06<br>Balance | Charges to<br>Expense | Cash<br>Payments<br>or Asset<br>Write-Offs | 4/28/07<br>Balance |
| <i>(Amounts in thousands)</i>         |                    |                       |  |                    |
| Severance and benefit-related costs   | \$891              | \$ 2,537              | \$(1,251)                                  | \$2,177            |
| Fixed asset write-downs, net of gains | —                  | 1,091                 | (1,091)                                    | —                  |
| Contract termination costs            | —                  | 3,441                 | (2,184)                                    | 1,257              |
| Other                                 | —                  | 3,964                 | (3,964)                                    | —                  |
| Total restructuring                   | \$891              | \$11,033              | \$(8,490)                                  | \$3,434            |

**Note 12: Uncertain Tax Positions**

We adopted FASB interpretation No. 48, *Accounting for Uncertainty in Income Taxes — an interpretation of FASB 109* (“FIN 48”), effective as of April 29, 2007. As a result of the implementation of FIN 48, we recognized a \$2.5 million decrease to beginning retained earnings. We elected to continue to classify interest and penalties, accrued as required by FIN 48, as a part of income tax expense. As of April 29, 2007, the gross amount of interest and penalties due to unrecognized tax benefits was \$3.1 million which was included as a part of the unrecognized tax benefit discussed below. An additional \$0.3 million of interest and penalties was accrued during the second quarter of fiscal 2008.

The total amount of unrecognized tax benefits as of the end of the second quarter of fiscal 2008 was \$9.4 million, which includes \$1.7 million attributable to timing differences that, once resolved, will have no impact on our effective tax rate. If recognized, \$7.4 million of unrecognized tax benefits would decrease our effective tax rate.

We believe that it is reasonably possible that the amount of unrecognized tax benefits will decrease by about \$2.4 million within the next twelve months. The amount of the expected reduction is comprised of gross unrecognized tax benefits of \$2.0 million and interest and penalties of \$1.4 million, net of deferred taxes of \$1.0 million. This decrease relates to anticipated settlements of several outstanding issues with various taxing authorities, including cash payments of about \$1.2 million.

United States federal income tax returns filed by us remain subject to examination for tax years 2004 and subsequent. In addition, our State returns remain subject to examination for tax years 2003 and subsequent. Canadian federal and provincial returns remain subject to examination for tax years 2002 and subsequent.

**Note 13: Variable Interest Entities**

Financial Accounting Standards Board Interpretation No. 46R, *Consolidation of Variable Interest Entities* (“FIN 46”), requires the “primary beneficiary” of a VIE to include the VIE’s assets, liabilities and operating results in its consolidated financial statements. In general, a VIE is a corporation, partnership, limited-liability corporation, trust or any other legal structure used to conduct activities or hold assets that either (a) has an insufficient amount of equity to carry out its principal activities without additional subordinated financial support, (b) has a group of equity owners that are unable to make significant decisions about its activities, or (c) has a group of equity owners that do not have the obligation to absorb losses or the right to receive returns generated by its operations.

La-Z-Boy Furniture Galleries® stores that are not operated by us are operated by independent dealers. These stores sell La-Z-Boy manufactured products as well as various accessories purchased from approved La-Z-Boy vendors. In some cases we have extended credit beyond normal trade terms to the independent dealers, made direct loans and/or guaranteed certain leases. Most of these independent dealers have sufficient equity to carry out their principal operating activities without subordinated financial support. However, there are certain independent dealers that we have determined may not have sufficient equity.

We have consolidated several dealers where we were the primary beneficiary based on the fair value of our variable interests. All of our consolidated VIEs were recorded at fair value on the date we became the primary beneficiary. Because these entities are accounted for as if the entities were consolidated based on voting interests, we absorb all net losses of the VIEs in excess of the equity at the dealerships. We recognize all net earnings of these VIEs to the extent of recouping the losses we recorded. Earnings in excess of our losses are attributed to equity owners of the dealers and are shown as minority interest on our financial statements. We had four consolidated VIEs throughout the second quarter of fiscal 2008 and 2007.



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Our consolidated VIEs recognized \$12.2 million and \$10.2 million in sales, net of intercompany eliminations, in the second quarter of fiscal 2008 and the second quarter of fiscal 2007, respectively. Additionally, we recognized a net loss per share of \$0.04 in the second quarter of fiscal 2008 and the second quarter of fiscal 2007, resulting from the operating results of these VIEs. Our consolidated VIEs recognized \$24.0 million and \$21.9 million in sales, net of intercompany eliminations, in the first half of fiscal 2008 and fiscal 2007, respectively. Additionally, we recognized a net loss per share of \$0.07 and \$0.06 in the first half of fiscal 2008 and fiscal 2007, respectively, resulting from the operating results of these VIEs. The VIEs had \$0.6 million, \$4.9 million and \$2.8 million of assets net of elimination of intercompany balances at the end of the second quarter of fiscal 2008, the second quarter of fiscal 2007 and at the end of fiscal 2007, respectively.

### **Note 14: Discontinued Operations**

During the third quarter of fiscal 2007, we committed to a plan to sell Sam Moore, which was a part of our Upholstery Group, and to sell Clayton Marcus and Pennsylvania House, which were part of our Casegoods Group. As we have continued to assess our long-term strategic direction, we have determined that these operating units do not align with our current strategic plan. Due to this decision these operating units were presented as discontinued operations beginning in the third quarter of fiscal 2007 and segment data was reclassified. Accordingly, our Consolidated Statement of Operations for the prior year has been reclassified to reflect the results of these operations as discontinued operations, with taxes allocated based on the operating units' estimated effective tax rate and no corporate expenses or interest allocated.

As a result of the decision to sell Sam Moore, Clayton Marcus and Pennsylvania House and subsequent testing of the fair value of the assets remaining to be sold, we recorded a \$17.5 million (\$13.7 million net of taxes) impairment charge in the third quarter of fiscal 2007 that is included in discontinued operations on our Consolidated Statement of Operations. The pretax impairment charge was comprised of \$3.6 million for impairment of the trade names, \$7.3 million for impairment of goodwill, \$0.2 million of other intangibles, \$1.7 million for write-down of LIFO inventory relating to the APB 16 acquisition adjustment, \$1.0 million for allowance for inventory and \$3.7 million for the write down of fixed assets. During the fourth quarter of fiscal 2007, current market data indicated the fixed assets for Clayton Marcus and Pennsylvania House were recorded above fair value, which resulted in an additional \$1.3 million impairment of their fixed assets.

During the second quarter of fiscal 2008, we completed the sale of our Clayton Marcus operating unit and we completed the sale of our Pennsylvania House trade name. The stock of Clayton Marcus was sold to Rowe Fine Furniture, Incorporated and resulted in a loss of about \$5.8 million (\$3.6 million net of taxes), of which about \$3.4 million related to the intangible assets of Clayton Marcus. The Pennsylvania House trade name was sold to Universal Furniture for \$1.7 million resulting in a pre-tax charge of about \$0.6 million (\$0.4 million net of taxes). We are in the process of liquidating the remaining Pennsylvania House inventory at discounted prices, and as a result have recorded an additional loss of \$3.0 million to write the inventory down to fair value.

On April 27, 2007, we completed the sale of our Sam Moore operating unit, an upholstered chair manufacturer. We sold the business for \$9.9 million, consisting of \$9.5 million in cash and a receivable of \$0.4 million, recognizing a loss in the fourth quarter of \$0.3 million. The receivable was subsequently collected in the first quarter of fiscal 2008.

During the first quarter of fiscal 2007, we completed the sale of our American of Martinsville operating unit, which supplied contract furniture to the hospitality, assisted-living and governmental markets. This operating unit was not a strategic fit with our current business model, which is centered on providing comfortable and stylish furnishings for the home, and was not a large enough component of our overall business (about 5% of sales) to justify our continued corporate focus and resources. We sold the business for \$33.2 million, recognizing a pre-tax gain in the first quarter of \$2.1 million. This disposition qualified as discontinued

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operations. Accordingly, our Consolidated Statement of Operations for the prior year has been reclassified to reflect the results of operations of this divested business as discontinued operations with taxes allocated based on the operating units' estimated effective tax rate and no corporate expenses or interest allocated. The business unit was previously included in the Casegoods Group, which was reclassified to reflect the discontinued operations.

For Clayton Marcus and Pennsylvania House, the assets and liabilities have been reclassified as assets and liabilities of discontinued operations. For the quarter ended October 27, 2007, the assets and liabilities mainly reflect the remaining accounts of Pennsylvania House, most of which will be liquidated or paid during our third fiscal quarter of 2008:

| <i>(Amounts in thousands)</i>                  | 10/27/07        | 4/28/07          |
|--|-----------------|------------------|
| <b>Assets of discontinued operations:</b>      |                 |                  |
| Receivables, net                               | \$ 2,038        | \$ 7,140         |
| Inventories, net                               | 1,596           | 10,978           |
| Trade names                                    | —               | 5,740            |
| Other assets                                   | —               | 420              |
|  | <u>\$ 3,634</u> | <u>\$ 24,278</u> |
| <b>Liabilities of discontinued operations:</b> |                 |                  |
| Accounts payable                               | \$ 84           | \$ 1,591         |
| Accrued expenses                               | 1,298           | 2,057            |
| Non-current liabilities                        | 282             | 195              |
|  | <u>\$ 1,664</u> | <u>\$ 3,843</u>  |

The results of the discontinued operations for Clayton Marcus and Pennsylvania House for the second quarter ended fiscal 2008 and for Sam Moore, Clayton Marcus, Pennsylvania House, and American of Martinsville for the second quarter ended fiscal 2007 were as follows:

| <i>(Amounts in thousands)</i>                              | Second Quarter Ended |            | Six Months Ended |            |
|--|----------------------|------------|------------------|------------|
|  | 10/27/07             | 10/28/06   | 10/27/07         | 10/28/06   |
| Net sales  | \$10,323             | \$26,910   | \$21,058         | \$76,309   |
| Loss from discontinued operations, net of tax              | \$ (2,292)           | \$ (1,342) | \$ (2,444)       | \$ (1,419) |
| Gain (loss) on sale of discontinued operations, net of tax | \$ (3,990)           | \$ —       | \$ (3,990)       | \$ 1,280   |

In the Consolidated Statement of Cash Flows, the cash flows of discontinued operations were not reclassified for fiscal 2008 and fiscal 2007. The assets and liabilities of these operating units were not reclassified for second quarter of fiscal 2007. They are reported in the respective categories of the Consolidated Balance Sheet and Statement of Cash Flows along with those of our continuing operations.

**Note 15: Earnings per Share**

Basic earnings per share is computed using the weighted average number of shares outstanding during the period. Diluted net income per share uses the weighted average number of shares outstanding during the period plus the additional common shares that would be outstanding if the dilutive potential common shares issuable under employee stock options were issued. A reconciliation of basic and diluted weighted average common shares outstanding follows:

| <i>(Amounts in thousands)</i>                        | Second Quarter<br>Ended |          | Six Months<br>Ended |          |
|--|-------------------------|----------|---------------------|----------|
|  | 10/27/07                | 10/28/06 | 10/27/07            | 10/28/06 |
| Weighted average common shares outstanding (basic)   | 51,410                  | 51,373   | 51,395              | 51,580   |
| Effect of options and unvested restricted stock      | —                       | 266      | —                   | 226      |
| Weighted average common shares outstanding (diluted) | 51,410                  | 51,639   | 51,395              | 51,806   |

The weighted average common shares outstanding (diluted) at October 27, 2007 excludes the effect of options to purchase 0.2 million shares because the net loss in the second quarter and first six months of fiscal 2008 would cause the effect of options to be anti-dilutive.

The effect of additional options to purchase 2.7 million and 1.1 million shares for the quarters ended October 27, 2007 and October 28, 2006 with a weighted average exercise price of \$15.52 and \$20.10 respectively, were excluded from the diluted share calculation because the exercise prices of these options were higher than the weighted average share price for the quarters and would have been anti-dilutive.

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

Our Management's Discussion and Analysis is an integral part of understanding our financial results. This Management's Discussion and Analysis should be read in conjunction with the accompanying Consolidated Financial Statements and related Notes to Consolidated Financial Statements. We begin the Management's Discussion and Analysis with an introduction to La-Z-Boy Incorporated's key businesses, strategies and significant operational events in fiscal 2008. We then provide a discussion of our results of operations, liquidity and capital resources, quantitative and qualitative disclosures about market risk, and critical accounting policies.

### Cautionary Statement Concerning Forward-Looking Statements

We are making forward-looking statements in this report. Generally, forward-looking statements include information concerning possible or assumed future actions, events or results of operations. More specifically, forward-looking statements include the information in this document regarding:

future income, margins and cash flows  
future growth  
adequacy and cost of financial resources

future economic performance  
industry and importing trends  
management plans

Forward-looking statements also include those preceded or followed by the words "anticipates," "believes," "estimates," "hopes," "plans," "intends" and "expects" or similar expressions. With respect to all forward-looking statements, we claim the protection of the safe harbor for forward-looking statements contained in the Private Securities Litigation Reform Act of 1995.

Actual results could differ materially from those anticipated or projected due to a number of factors. These factors include, but are not limited to: (a) changes in consumer confidence; (b) changes in demographics; (c) changes in housing sales; (d) the impact of terrorism or war; (e) continued energy price changes; (f) the impact of logistics on imports; (g) the impact of interest rate changes; (h) changes in currency exchange rates; (i) competitive factors; (j) operating factors, such as supply, labor or distribution disruptions including changes in operating conditions or costs; (k) effects of restructuring actions; (l) changes in the domestic or international regulatory environment; (m) ability to implement global sourcing organization strategies; (n) fair value changes to our intangible assets due to actual results differing from projected; (o) the impact of adopting new accounting principles; (p) the impact from natural events such as hurricanes, earthquakes and tornadoes; (q) the impact of retail store relocation costs, the success of new stores or the timing of converting stores to the New Generation format; (r) the ability to procure fabric rolls or cut and sewn fabric sets domestically or abroad; (s) the ability to sell the remaining assets of our discontinued operations for their recorded fair value; (t) those matters discussed under "Risk Factors" in our most recent Annual Report of Form 10-K and subsequent Quarterly Reports on Form 10-Q and factors relating to acquisitions and other factors identified from time to time in our reports filed with the Securities and Exchange Commission. We undertake no obligation to update or revise any forward-looking statements, either to reflect new developments or for any other reason.

## INTRODUCTION

### Our Business

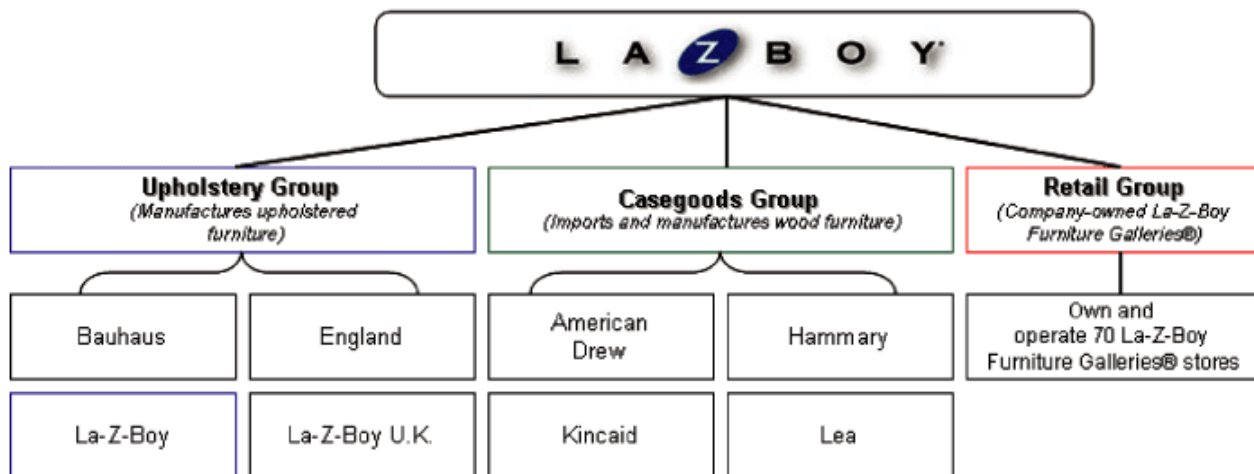
La-Z-Boy Incorporated manufactures, markets, imports, distributes and retails upholstery products and casegoods (wood) furniture products. Our La-Z-Boy brand is the most recognized brand in the furniture industry, and we are the leading global producer of reclining chairs. We own 70 La-Z-Boy Furniture Galleries® stores, which are retail locations dedicated to marketing our La-Z-Boy branded product. These 70 stores are part of the larger network of La-Z-Boy Furniture Galleries® stores, which includes a total of 338 stores, the balance

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of which are independently owned and operated. The network constitutes the industry’s largest single-branded upholstered furniture retailer in North America. These stores combine the style, comfort and quality of La-Z-Boy furniture with our in-home design service to help consumers furnish certain rooms in their homes.

In addition to our company-owned stores, we consolidate certain of our independent dealers who did not have sufficient equity to carry out their principal business activities without our financial support. These dealers are referred to as Variable Interest Entities (“VIEs”). During the second quarter of fiscal 2007 we had four VIEs, operating 28 stores, consolidated into our Statement of Operations. During the fiscal 2008 second quarter, we had four VIEs, operating 30 stores, in our Consolidated Statement of Operations.

Our reportable operating segments are the Upholstery Group, the Casegoods Group and the Retail Group. Below is a chart that shows the organizational structure of La-Z-Boy segments.



In terms of revenue, our largest segment is the Upholstery Group, which includes La-Z-Boy, our largest operating unit. We import cut and sewn fabric kits to complement our leather kits that allow us to take full advantage of both the cost-saving opportunities presented in Asia and the speed to market advantages of a United States manufacturing base. The Upholstery Group sells furniture mainly to La-Z-Boy Furniture Galleries® stores, general dealers and department stores.

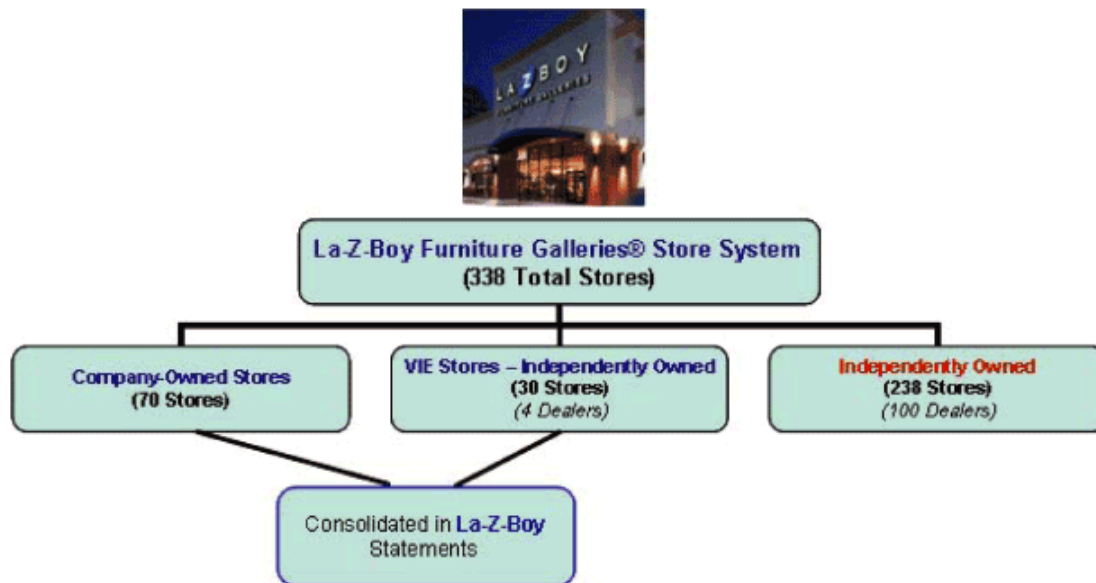
Our Casegoods Group today is primarily an importer, marketer and distributor of casegoods (wood) furniture as well as operates two manufacturing facilities in North Carolina. In order to compete globally, we have significantly changed the cost structure from fixed to highly variable.

The Retail Group consists of 70 company-owned La-Z-Boy Furniture Galleries® stores in eight markets ranging from the Midwest to the East Coast of the United States and also including southeastern Florida.

According to the May, 2007 Top 100 ranking by *Furniture Today*, an industry trade publication, the La-Z-Boy Furniture Galleries® stores network ranks as the largest retailer of upholstered single-brand furniture in the U.S. One of our major strategic initiatives is to expand the retail opportunities of the La-Z-Boy brand name in the United States and Canada by opening new stores, relocating stores to better locations and converting existing stores to our New Generation store format. Slightly more than half of the 338 stores in the network—the majority of which are independently owned—are concentrated in the top 25 markets in the U.S. We will attempt to increase our market penetration over the next few years in the top 25 markets, allowing our dealers and company-owned stores to create operating efficiencies, particularly in the areas of advertising, distribution and

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administration. Additionally, we have an extensive La-Z-Boy in-store gallery program with 215 in-store galleries. During the first quarter, we began rolling out a new model for our in-store galleries referred to as our Comfort Studios. Comfort Studios are less expensive than the current in-store gallery model and provide a better presentation to our consumer. During the second quarter of fiscal 2008 we opened 117 Comfort Studios, and we expect to open 173 Comfort Studios during the remainder of fiscal 2008. Kincaid, England and Lea also have in-store gallery programs. The chart below shows the current structure of the La-Z-Boy Furniture Galleries® store network.



**Highlights of Our Current Quarter**

All of our segments experienced a degradation in sales resulting from the weak consumer demand. We continue to aggressively focus on advertising and merchandising of our product in an attempt to reverse this trend. In addition, we have focused on cutting costs and will continue to do so as needed to keep our expenses in line with revenue.

For the remainder of fiscal 2008, we plan to continue to take the following actions to grow sales and improve the operating results for the Retail Group as well as to take advantage of synergies between the company-owned markets:

- Centralize certain of our advertising and marketing functions, and take advantage of the efficiencies gained as we continue the warehouse consolidation we began during the second quarter of fiscal 2007.
- Continue to consolidate information systems and eliminate redundant processes. We are currently in the process of consolidating our information systems into one system and expect to complete this process by the end of this fiscal year.
- Expand our in-home design service, which has increased the average sale per customer where employed. Currently, 71% of our company-owned locations have this service available.
- Improve our gross margins based on better merchandising and pricing of product and services.

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During the second quarter of fiscal 2008, we evaluated the goodwill at our South Florida retail market as a result of a decision to delay our planned store openings in this market. These delays are the result of a slow housing market causing double-digit declines in sales in the market over the past twelve months. We recognized a \$5.8 million impairment charge for the full amount of goodwill of this retail market in the second quarter of fiscal 2008.

Certain of our debt agreements require that certain financial covenants be met. As of the end of the second quarter, we were not in compliance with the fixed charge coverage ratio requirements under our revolving credit facility. We obtained an amendment to our fixed charge coverage ratio from our revolving credit facility lenders, dated November 6, 2007, to amend the ratio for our quarter ended October 27, 2007 so that we were in compliance. Although we were in compliance with our other debt covenants, we believe that we will not be in compliance with the fixed charge coverage ratio requirements relating to both our revolving credit facility and private placement notes as of the end of the third quarter, and therefore we have engaged our lead bank to begin structuring a new secured credit facility. We had no unamortized debt issue costs as of the end of the second quarter of fiscal 2008.

We believe that by the end of our fiscal 2008 third quarter, we will be successful in negotiating a long-term credit facility, which we will utilize to pay off our private placement notes. There can be no assurance that an agreement can be reached; however, we consider this scenario unlikely. If an agreement cannot be reached and the lenders were to exercise their right to accelerate the maturity of their notes, this could result in an adverse effect on us unless the lenders were to agree to forbearance or restructuring of the debt. For more information about the risks and anticipated costs associated with our financing plans, see "Liquidity and Capital Resources."

During the second quarter of fiscal 2008, we completed the sale of our Clayton Marcus operating unit and the sale of our Pennsylvania House trade name. The stock of Clayton Marcus was sold to Rowe Fine Furniture, Incorporated for \$2.9 million, resulting in a pre-tax loss of about \$5.8 million, of which about \$3.4 million related to the intangible assets of Clayton Marcus. The Pennsylvania House trade name was sold to Universal Furniture for \$1.7 million, resulting in a pre-tax charge of about \$0.6 million. We are in the process of liquidating the remaining Pennsylvania House inventory at discounted prices, and as a result have recorded an additional pre-tax loss of \$3.0 million to adjust the inventory to fair value.

[Table of Contents](#)**Results of Operations****Analysis of Operations: Quarter Ended October 27, 2007****(Second Quarter 2008 compared with 2007)**

| <i>(Amounts in thousands, except per share amounts and percentages)</i> | Quarter Ended     |                   | Percent change |
|---|-------------------|-------------------|----------------|
|   | 10/27/07          | 10/28/06          |                |
| Upholstery sales  | \$269,749         | \$304,598         | -11.4%         |
| Casegoods sales   | 58,892            | 74,164            | -20.6%         |
| Retail sales  | 46,163            | 52,485            | -12.0%         |
| Other/eliminations*   | (9,370)           | (16,633)          | 43.7%          |
| <b>Consolidated sales</b>   | <b>\$365,434</b>  | <b>\$414,614</b>  | <b>-11.9%</b>  |
| Consolidated gross profit   | \$ 98,258         | \$108,663         | -9.6%          |
| <b>Consolidated gross margin</b>  | <b>26.9%</b>      | <b>26.2%</b>      |                |
| Consolidated S,G&A  | \$ 98,098         | \$ 99,887         | -1.8%          |
| <b>S,G&amp;A as a percent of sales</b>                                  | <b>26.8%</b>      | <b>24.1%</b>      |                |
| Upholstery operating income   | \$ 19,036         | \$ 20,162         | -5.6%          |
| Casegoods operating income  | 3,577             | 6,200             | -42.3%         |
| Retail operating loss   | (9,119)           | (8,769)           | -4.0%          |
| Corporate and other   | (12,816)          | (9,217)           | -39.0%         |
| Intangible write-down   | (5,809)           | —                 | N/M            |
| Restructuring   | (967)             | (1,865)           | 48.2%          |
| <b>Consolidated operating income (loss)</b>                             | <b>\$ (6,098)</b> | <b>\$ 6,511</b>   | <b>-193.7%</b> |
| Upholstery operating margin   | 7.1%              | 6.6%              |                |
| Casegoods operating margin  | 6.1%              | 8.4%              |                |
| Retail operating margin   | -19.8%            | -16.7%            |                |
| <b>Consolidated operating margin</b>                                    | <b>-1.7%</b>      | <b>1.6%</b>       |                |
| <b>Income (loss) from continuing operations</b>                         | <b>\$ (3,652)</b> | <b>\$ 3,296</b>   |                |
| <b>Diluted income (loss) per share from continuing operations</b>       | <b>\$ (0.07)</b>  | <b>\$ 0.06</b>    |                |
| <b>Loss from discontinued operations</b>                                | <b>\$ (6,282)</b> | <b>\$ (1,342)</b> |                |
| <b>Diluted loss per share from discontinued operations</b>              | <b>\$ (0.12)</b>  | <b>\$ (0.02)</b>  |                |

\* Includes sales from our VIEs.

N/M = Not Meaningful



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### **Sales**

**Consolidated sales** were down 11.9% when compared with second quarter of fiscal 2007. Our Upholstery, Caseloads and Retail Group sales decreased, while our VIEs' sales increased.

**Upholstery Group** sales were down 11.4% compared with the second quarter of fiscal 2007. Sales price increases resulted in a 2.3% increase in sales; however this was offset by a decrease in sales volume due to an overall weak consumer demand.

Our **Caseloads Group** sales decreased 20.6% compared with the second quarter of fiscal 2007. Sales price increases resulted in a 1.0% increase in sales; however, this was offset by a decrease in sales volume which occurred across all of our Caseloads operating units due to weak consumer demand.

**Retail Group** sales decreased 12.0% when compared with the second quarter of fiscal 2007. About 8% of this decline was the result of exiting the Pittsburgh, Pennsylvania and Rochester, New York markets in the second half of fiscal 2007; however, we added 10 stores in our remaining markets during the past twelve months but have not realized our anticipated additional sales in these remaining markets. The decrease in sales was related to the negative effect that housing sales declines have had on the home furnishings market and the weak consumer demand.

Intercompany sales eliminations and sales of VIEs increased \$7.3 million, net, during the second quarter of fiscal 2008 when compared with the second quarter of fiscal 2007. The majority of this increase was attributable to a \$5.3 million decrease in intercompany sales eliminations. The reduction of intercompany sales eliminations was a result of a decrease in same store sales to company-owned stores due to the weak consumer demand. Sales of our VIEs increased in the second quarter of fiscal 2008 compared to the second quarter of fiscal 2007 as the result of having 2 additional stores in fiscal 2008.

### **Gross Margin**

Gross margin increased 0.7 percentage points in the second quarter of fiscal 2008 in comparison to the second quarter of fiscal 2007. Our sales price increases impacted our gross margin by 2.1 percentage points thus increasing the margin on our La-Z-Boy branded product; however, most of our other operating units experienced lower gross margins due to the decline in volume. Restructuring expense in the second quarter of fiscal 2008 decreased our gross margin by 0.1 percentage points. Restructuring expense in the second quarter of fiscal 2007 increased the gross margin by 0.1 percentage points due to a gain on the sale of a property held for sale as a result of a previous restructuring.

### **Selling, General and Administrative Expenses**

Selling, general and administrative expenses (S,G&A) were down slightly in dollars when compared to the prior year's second quarter, but as a percent of sales increased 2.7 percentage points. The higher level of S,G&A as a percent of sales was mainly attributable to:

- In the second quarter of fiscal 2007, we recognized a gain of \$2.6 million relating to the sale of several properties which was not repeated in fiscal 2008.
- In the second quarter of fiscal 2007, we reduced our warranty reserve by \$1.5 million due to a trend of lower warranty costs incurred beyond one year after the sale of the product. Our current trends show that a majority of our claims were from product sold in the past twelve months thus reducing our

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liability, along with changes in estimated amounts required for currently known warranty issues. This adjustment was not repeated in fiscal 2008.

- During the second quarter of fiscal 2008, we continued to have consulting costs related to our strategic planning for retail excellence and other company initiatives. These costs were about \$1.3 million greater in the second quarter of fiscal 2008 when compared to the second quarter of fiscal 2007. We expect this activity to come to a close during the 2008 third quarter.

Offsetting these increases, we have focused on cost containment efforts and taking cost out of the business, which have reduced S,G&A in commissions, advertising and other variable costs.

### ***Restructuring***

Restructuring costs totaled \$1.0 million for the second quarter of fiscal 2008 as compared with \$1.9 million of restructuring expense in the second quarter of fiscal 2007. The restructuring costs in fiscal 2008 related to our closure of several manufacturing facilities, consolidation of retail warehouses and closure of underperforming retail stores. These costs were comprised mainly of fixed asset impairments and lease termination, severance and other restructuring costs. Of the \$1.0 million in restructuring costs during the second quarter of fiscal 2008, \$0.5 million was classified in Cost of Goods Sold. This expense relating to the closure of several manufacturing facilities was partially offset by a gain on the sale of a property held for sale relating to a previous restructuring. The remaining restructuring costs of \$0.5 million were reclassified as an operating expense line item below S,G&A related to Retail operations.

### ***Intangible Write-down***

During the second quarter of fiscal 2008, we evaluated the goodwill at our South Florida retail market as a result of a decision to delay our planned store openings in this market. This delay was the result of a slow housing market causing double-digit declines in sales in the market over the past twelve months. We recognized a \$5.8 million impairment charge for the full amount of goodwill of this retail market in the second quarter of fiscal 2008.

### ***Operating Margin***

Our consolidated operating margin was (1.7)% for the second quarter of fiscal 2008 and included 1.6 percentage points for the impairment of goodwill and 0.3 percentage points for restructuring costs. Operating margin for the second quarter of fiscal 2007 was 1.6% and included 0.4 percentage points of restructuring charges offset by a 0.6 percentage point gain on sales of properties. While we have increased our gross margin as compared to the second quarter of fiscal 2007, our S,G&A expenses have only decreased slightly. With the significant decline in sales as compared to the second quarter of fiscal 2007, we have been unable to absorb the fixed S,G&A expenses to maintain our operating margin.

The **Upholstery Group** operating margin increased 0.5 percentage points for the second quarter of fiscal 2008 when compared with the prior year. Our higher gross margins in the second quarter of fiscal 2008 as compared to the prior year somewhat offset the impact of our fixed S,G&A costs to increase our operating margin. Selling price increases accounted for a 2.6 percentage point increase in our operating margin over the prior year. Additionally, the prior year operating margin included a 0.4 percentage point favorable impact relating to warranty adjustments. This reduction in our warranty reserve was the result of a trend of lower aggregate warranty costs incurred beyond one year after the sale of the product.

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Our **Casegoods Group** operating margin decreased 2.3 percentage points during the second quarter of fiscal 2008 versus the second quarter of fiscal 2007. With the continued decline in sales volume, we were not able to absorb our fixed costs to maintain our operating margin.

Our **Retail Group** operating margin decreased by 3.1 percentage points during the second quarter of fiscal 2008 in comparison to the second quarter of fiscal 2007. As we continued to convert, relocate or build new stores in our Retail markets and our net sales continued to decline in light of the weak furniture retail environment, we were not able to absorb our fixed costs. We have completed the consolidation of our warehouses in the northeast, have increased our Retail gross margins and eliminated duplicate jobs as we have consolidated functions throughout the organization, but will need to increase sales volumes to realize those savings in our Retail operating margins. Over the next two quarters, we believe that the consolidation of the remaining warehouses in Retail will be complete.

**Corporate and Other** operating loss increased \$3.6 million during the second quarter of fiscal 2008 when compared with the second quarter of fiscal 2007. During the second quarter of fiscal 2007, we recognized a gain of \$2.6 million relating to the sale of several properties which was not repeated in fiscal 2008. Additionally, during the second quarter of fiscal 2008, we continued a retail test marketing program at the corporate level, which increased our expense by \$0.8 million.

### ***Interest Expense***

Interest expense for the second quarter of fiscal 2008 was less than the second quarter of fiscal 2007 due to a \$34.6 million decrease in our average debt.

### ***Income Tax Expense***

Our effective tax rate was 46.6% in the second quarter of fiscal 2008 compared to 37.2% in second quarter of fiscal 2007. In fiscal 2008, our expected tax rate was impacted by several discrete items, the most significant being the reversal of \$0.9 million of valuation allowance related to a portion of net operating loss carryforward benefits of our European joint venture.

### ***Discontinued Operations***

During the second quarter of fiscal 2008, our discontinued operations recognized a loss of \$6.3 million after tax. During the quarter, we completed the sale of our Clayton Marcus operating unit and we completed the sale of our Pennsylvania House trade name. The stock of Clayton Marcus was sold to Rowe Fine Furniture, Incorporated, resulting in a loss of about \$5.8 million or \$3.6 million after tax. Of this loss, about \$3.4 million pre-tax related to the intangible assets of Clayton Marcus. The Pennsylvania House trade name was sold to Universal Furniture for \$1.7 million, resulting in a pre-tax charge of about \$0.6 million. We are in the process of liquidating the remaining inventory at discounted prices, and as a result have recorded an additional loss of \$3.0 million to adjust the inventory to fair value. During the second quarter of fiscal 2007, our discontinued operations recognized a loss of \$1.3 million from operations.

[Table of Contents](#)**Results of Operations****Analysis of Operations: Six Months Ended October 27, 2007****(First Six Months of 2008 compared with 2007)**

| <i>(Amounts in thousands, except per share amounts and percentages)</i> | Six Months Ended   |                  | Percent change |
|---|--------------------|------------------|----------------|
|   | 10/27/07           | 10/28/06         |                |
| Upholstery sales  | \$524,506          | \$599,995        | -12.6%         |
| Casegoods sales   | 112,466            | 135,190          | -16.8%         |
| Retail sales  | 91,394             | 104,689          | -12.7%         |
| Other/eliminations*   | (18,536)           | (31,337)         | 40.8%          |
| <b>Consolidated sales</b>   | <b>\$709,830</b>   | <b>\$808,537</b> | <b>-12.2%</b>  |
| Consolidated gross profit   | \$180,950          | \$206,578        | -12.4%         |
| <b>Consolidated gross margin</b>  | <b>25.5%</b>       | <b>25.5%</b>     |                |
| Consolidated S,G&A  | \$192,606          | \$194,570        | -1.0%          |
| <b>S,G&amp;A as a percent of sales</b>                                  | <b>27.1%</b>       | <b>24.1%</b>     |                |
| Upholstery operating income   | \$ 27,903          | \$ 37,787        | -26.2%         |
| Casegoods operating income  | 6,177              | 9,442            | -34.6%         |
| Retail operating loss   | (19,193)           | (16,484)         | -16.4%         |
| Corporate and other   | (23,464)           | (19,137)         | -22.6%         |
| Intangible write-down   | (5,809)            | —                | —              |
| Restructuring   | (4,648)            | (1,865)          | -149.2%        |
| <b>Consolidated operating income (loss)</b>                             | <b>\$ (19,034)</b> | <b>\$ 9,743</b>  | <b>-295.4%</b> |
| Upholstery operating margin   | 5.3%               | 6.3%             |                |
| Casegoods operating margin  | 5.5%               | 7.0%             |                |
| Retail operating margin   | -21.0%             | -15.7%           |                |
| <b>Consolidated operating margin</b>                                    | <b>-2.7%</b>       | <b>1.2%</b>      |                |
| <b>Income (loss) from continuing operations</b>                         | <b>\$ (12,194)</b> | <b>\$ 4,388</b>  |                |
| <b>Diluted income (loss) per share from continuing operations</b>       | <b>\$ (0.24)</b>   | <b>\$ 0.08</b>   |                |
| <b>Loss from discontinued operations</b>                                | <b>\$ (6,434)</b>  | <b>\$ (139)</b>  |                |
| <b>Diluted income (loss) per share from discontinued operations</b>     | <b>\$ (0.12)</b>   | <b>—</b>         |                |

\* Includes sales from our VIEs.

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### **Sales**

**Consolidated sales** were down 12.2% compared to the first six months of fiscal 2007 due in large part to a weak retail environment attributable to weak consumer demand.

**Upholstery Group** sales decreased 12.6% compared to the first six months of fiscal 2007. The Upholstery Group benefited by a 1.9% sales increase due to sales price increases; however, this increase in sales was offset by the decline in sales volume due to an overall weak consumer demand.

Our **Casegoods Group** sales decreased 16.8% compared to the prior year first six months. The decrease in sales occurred across all of our Casegoods operating units and was mainly due to the weak consumer demand.

**Retail Group** sales decreased 12.7% when compared to the first half of fiscal 2007. About 7% of this decrease was the result of exiting the Pittsburgh, Pennsylvania and Rochester, New York markets in the second half of fiscal 2007; however, we added 10 stores in the past twelve months but have not realized our anticipated additional sales in these remaining markets. The remaining decrease in sales was related to the negative effect of housing sales declines impacting the home furnishings market and the weak consumer demand.

The net total of intercompany sales eliminations and sales to VIEs increased \$12.8 million during the first six months of fiscal 2008 when compared to the first six months of fiscal 2007. The majority of this increase was attributable to a decrease in intercompany sales eliminations resulting from a decrease in same store sales to company-owned stores due to the weak consumer demand.

### **Gross Margin**

Gross margin for the first six months of fiscal 2008 was flat in comparison to the prior year margin. Sales price increases positively affected our gross margin by 1.6 percentage points; however, this increase was offset by the lower sales volume. The first six months of fiscal 2008 were impacted by restructuring charges totaling \$3.1 million relating to the closure of several manufacturing facilities. The first six months of 2007 were impacted by a restructuring gain of \$0.4 million.

### **Selling, General and Administrative Expenses**

Selling, general and administrative expenses (S,G&A) were down slightly in dollar amount but increased as a percent of sales in fiscal 2008 compared to the prior year.

- In the first six months of fiscal 2007, we recognized a gain of \$2.6 million relating to the sale of several properties which was not repeated in fiscal 2008.
- In the first six months of fiscal 2007, we reduced our warranty reserve by \$2.3 million due to a trend of lower warranty costs incurred beyond one year after the sale of the product. Our current trends show that a majority of our claims were from product sold in the past twelve months thus reducing our liability, along with changes in estimated amounts required for currently known warranty issues. This adjustment was not repeated in fiscal 2008.
- The remaining increase as a percent of sales was a result of a reduction in sales volume during the first six months, when compared to the high fixed costs associated with the business, especially as it relates to our Retail operations.

## **Restructuring**

Restructuring costs totaled \$4.6 million for the first half of fiscal 2008 as compared with \$1.9 million of restructuring expense in the first half of fiscal 2007. The restructuring costs in fiscal 2008 related to our closure of several manufacturing facilities, consolidation of retail warehouses and the closure of underperforming retail stores. These costs were comprised mainly of fixed asset impairments and lease termination, severance and other restructuring costs. Of the \$4.6 million in restructuring costs during the first half of fiscal 2008, \$3.1 million was classified in Cost of Goods Sold. This expense relating to the closure of several manufacturing facilities was partially offset by a gain on the sale of a property held for sale relating to a previous restructuring. The remaining restructuring costs of \$1.6 million were reclassified as an operating expense line item below S,G&A related to Retail operations. Of the restructuring costs in fiscal 2007, a gain of \$0.4 million was recognized in cost of sales relating to the sale of a property held as part of a previous restructuring. The remaining cost of \$2.3 million related to the consolidation of our retail warehouses and the closure of certain of our retail facilities.

## **Operating Margin**

Our consolidated operating margin was (2.7)% for the first six months of fiscal 2008 and included 0.8 percentage points for our intangible write-down and 0.7 percentage points of restructuring charges. Operating margin for the prior year six months was 1.2% and included 0.2 percentage points of restructuring charges.

The **Upholstery Group** operating margin decreased 1.0 percentage points for the first six months of fiscal 2008 over the prior year. Our sales price increases impacted our gross margin by 2.1 percentage points thus increasing the margin on our La-Z-Boy branded product; however, most of our other operating units experienced lower gross margins due to the decline in volume.

Our **Casegoods Group** operating margin decreased 1.5 percentage points during the first half of fiscal 2008 versus the first half of fiscal 2007. With the 16.8% decline in sales volume, we were unable to absorb some of our fixed costs creating a degradation in our margin.

Our **Retail Group** operating margin decreased by 5.3 percentage points during the first six months of fiscal 2008 in comparison to the first six months of fiscal 2007. As we continued to convert, relocate or build new stores in our Retail markets and our net sales continued to decline in light of the weak furniture retail environment, we were not able to absorb our fixed costs. We have completed the consolidation of our warehouses in the northeast, have increased our Retail gross margins and eliminated duplicate jobs as we have consolidated functions throughout the organization, but will need to increase sales volumes to realize those savings in our Retail operating margins. Over the next quarter, we believe that the consolidation of the remaining warehouses in Retail will be complete.

**Corporate and Other** operating loss increased \$4.3 million during the first six months of fiscal 2008 when compared to the first six months of fiscal 2007. Gains recognized in S,G&A in the prior year on long-lived assets that we sold were \$2.6 million higher than the same period of the current year. Additionally, during the first half of fiscal 2008, we continued a retail test marketing program which increased our expenses by \$2.5 million.

## **Interest Expense**

Interest expense for the first half of fiscal 2008 was less than the first half of fiscal 2007. The decrease in interest expense was due to our weighted average debt being down \$31.5 million for the first six months of the

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current year when compared to the same period last year. This decrease was slightly offset by a 0.1 percentage point increase in our interest rate as most of our debt has fixed interest rates.

### ***Other Income***

Other income increased in the first six months of fiscal 2008 when compared with the first six months of fiscal 2007 due to a decrease in realized foreign currency exchange losses, increased royalty income and increased investment income.

### ***Income Tax Expense***

Our effective tax rate from continuing operations was 40.3% in the first six months of fiscal 2008 compared to 29.5% in fiscal 2007. The fiscal 2007 expected rate was reduced to reflect a change in Canadian tax law that increased the carry-forward period for net operating losses from ten to 20 years. The fiscal 2008 expected tax rate was impacted by several discrete items, the most significant being the reversal of \$0.9 million of valuation allowance related to a portion of net operating loss carryforward benefits of our European joint venture.

### ***Discontinued Operations***

During the first six months of fiscal 2008, our discontinued operations recognized a loss of \$6.4 million after tax. During the second quarter, we completed the sale of our Clayton Marcus operating unit and we completed the sale of our Pennsylvania House trade name. The stock of Clayton Marcus was sold to Rowe Fine Furniture, Incorporated, resulting in a loss of about \$5.8 million, of which about \$3.4 million related to the intangible assets of Clayton Marcus. The Pennsylvania House trade name was sold to Universal Furniture for \$1.7 million, resulting in a pre-tax charge of about \$0.6 million. We are in the process of liquidating the remaining inventory at discounted prices, and as a result have recorded an additional loss of \$3.0 million to adjust the inventory to fair value. During the first six months of fiscal 2007, our discontinued operations recognized a loss of \$0.1 million. Our gain on the sale of American of Martinsville of \$1.3 million after tax was offset by the operational losses of our remaining businesses held for sale.

## **Liquidity and Capital Resources**

Our total assets at the end of the second quarter of fiscal 2008 decreased \$52.8 million compared with the end of fiscal 2007. The majority of this decline was attributable to declines in assets of our businesses held for sale, accounts receivable and cash.

Our sources of cash liquidity include cash and equivalents, cash from operations and amounts available under credit facilities. These sources have been adequate for day-to-day operations, dividends to shareholders and capital expenditures. We expect these sources of liquidity to continue to be adequate for the foreseeable future. Capital expenditures for the first half of fiscal 2008 were \$15.6 million compared with \$15.0 million during the first half of fiscal 2007. During the first half of fiscal 2008 we exercised a \$5.2 million option to purchase property, which we subsequently sold and leased back. Similarly during the first half of fiscal 2007 we exercised a \$3.0 million option to purchase property, which we subsequently sold and leased back. There are no material purchase commitments for capital expenditures, which are expected to be in the range of \$25 to \$28 million in fiscal 2008 including the previously mentioned sale leaseback.

We have a committed bank credit facility of \$100 million. As part of an amendment to this facility, borrowings are based on an asset-based formula. As of October 27, 2007, \$48 million was available under this facility. We are also allowed an additional \$5.0 million from other sources.

Certain of our debt agreements require that certain financial covenants be met. As of the end of the second quarter, we were not in compliance with the fixed charge coverage ratio requirement under our revolving credit facility. We obtained an amendment to our fixed charge coverage ratio from our revolving credit facility lenders, dated November 6, 2007, to amend the ratio for our quarter ended October 27, 2007 so that we were in compliance. Although we were in compliance with our other financial covenants, we believe that we will not be in compliance with the fixed charge coverage ratio requirements relating to both our revolving credit facility and our private placement notes as of the end of the third quarter, and therefore we have engaged our lead bank to begin structuring a new secured credit facility. We had no unamortized debt issue costs as of the end of the second quarter of fiscal 2008.

We believe that by the end of our fiscal 2008 third quarter, we will be successful in negotiating a long-term credit facility, which we will utilize to pay off our private placement notes. There can be no assurance that an agreement can be reached; however, we consider this scenario unlikely. If an agreement cannot be reached and the lenders were to exercise their right to accelerate the maturity of their notes, this could result in an adverse effect on us unless the lenders were to agree to forbearance or restructuring of the debt.

In order to repay our private placement notes, we will be required to pay a 'make-whole' premium which is currently in the range of \$2.5 — \$3.0 million. We anticipate that the interest rate on the new debt, which is expected to be collateralized by accounts receivable and inventory, will be greater than the average interest rate for the private placement notes.



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The following table illustrates the main components of our cash flows:

| Cash Flows Provided From (Used For)<br>(Amounts in thousands) | Six Months Ended   |                   |
|---|--------------------|-------------------|
|   | 10/27/07           | 10/28/06          |
| <b>Operating activities</b>                                   |                    |                   |
| Net income (loss), depreciation and deferred taxes            | \$ (12,461)        | \$ 11,372         |
| Loss/(gain) on sales of discontinued operations (net of tax)  | 3,990              | (1,280)           |
| Write-down of businesses held for sale                        | 2,159              | —                 |
| Write-down of intangibles                                     | 3,689              | —                 |
| Restructuring   | 4,648              | 1,865             |
| Working capital and other                                     | (7,171)            | (39,472)          |
| <b>Cash used for operating activities</b>                     | <b>(5,146)</b>     | <b>(27,515)</b>   |
| <b>Investing activities</b>                                   | <b>(2,590)</b>     | <b>42,547</b>     |
| <b>Financing activities</b>                                   |                    |                   |
| Repurchase of common stock                                    | —                  | (6,947)           |
| Net decrease in debt  | (275)              | (5)               |
| Other financing activities                                    | (12,557)           | (11,696)          |
| <b>Cash used for financing activities</b>                     | <b>(12,832)</b>    | <b>(18,648)</b>   |
| Exchange rate changes   | 1,539              | 56                |
| Net decrease in cash and equivalents                          | <u>\$ (19,029)</u> | <u>\$ (3,560)</u> |

### **Operating Activities**

During the first half of fiscal 2008, net cash used for operating activities was \$5.1 million, compared with \$27.5 million used for the first half of fiscal 2007. The decrease in 2008 operating cash flows used was due mainly to cash provided by a reduction in inventory and receivables. Discontinued operations did not have a significant impact on the cash provided by operating activities for the second quarter of fiscal 2008 or fiscal 2007.

### **Investing Activities**

During the first half of fiscal 2008, net cash used for investing activities was \$2.6 million, whereas \$42.5 million was provided by investing activities during the first half of fiscal 2007. During the first half of fiscal 2008, \$6.4 million in proceeds was generated by a sale-leaseback transaction we entered into with a third party. We exercised an option to purchase a property, sold it to a third party and then subsequently leased it back. During the second quarter of fiscal 2008, \$4.0 million of proceeds were received for the sale of Clayton Marcus and the sale of our Pennsylvania House trade name. These proceeds were offset by our capital expenditures of \$15.6 million during the first half of fiscal 2008. In the second quarter of fiscal 2007, \$33.2 million of proceeds were received for the sale of our operating unit American of Martinsville, along with \$25.0 million in proceeds for the sale of six properties, offset by \$15.0 million of capital expenditures.

### **Financing Activities**

Our financing activities included borrowings and payments on our debt facilities, dividend payments, issuances of stock and stock repurchases. We used \$12.8 million of cash in financing activities in the first six months of fiscal 2008 compared with \$18.6 million of cash used in financing activities during the first six months of fiscal 2007. In our first half of fiscal 2007, we used \$6.9 million to repurchase stock. Our discontinued operations did not have a material impact on cash flows from financing activities for fiscal 2008 or 2007.

In the first quarter of fiscal 2008 we adopted FIN 48 and as a consequence, the balance sheet at the end of the second quarter reflected a \$7.8 million liability for uncertain income tax positions. We reasonably expect that a portion of this liability will be settled within the next 12 months. This amount expected to be resolved within the next 12 months is comprised of gross unrecognized tax benefits of \$2.0 million and interest and penalties of \$1.4 million, net of deferred taxes of \$1.0 million. The remaining balance, to the extent it is ever paid, will be paid as tax audits are completed or settled.

There were no material changes to our contractual obligations table during the quarter.

Our debt-to-capitalization ratio was 24.7% at October 27, 2007, 23.5% at April 28, 2007, and 27.2% at October 28, 2006.

Our Board of Directors has authorized the repurchase of company stock. As of October 27, 2007, 5.4 million additional shares could be purchased pursuant to this authorization. We did not purchase any shares during the first half of fiscal 2008.

We have guaranteed various leases of dealers with proprietary stores. The total amount of these guarantees is \$15.5 million. Of this, \$3.4 million will expire within one year, \$4.5 million in one to three years, \$3.2 million in four to five years, and \$4.4 million thereafter. In recent years, we have increased our imports of casegoods product and leather and fabric for upholstery product. At the end of the second quarter of fiscal 2008, we had \$51.1 million in open purchase orders with foreign casegoods, leather and fabric sources. Some of these open purchase orders are cancelable. We are not required to make any contributions to our defined benefit plans; however, we may make discretionary contributions.

Continuing compliance with existing federal, state and local statutes dealing with protection of the environment is not expected to have a material effect upon our capital expenditures, earnings, competitive position or liquidity.

### **Critical Accounting Policies**

Our critical accounting policies are disclosed in our Form 10-K for the year ended April 28, 2007.

### **Restructuring**

In the fourth quarter of fiscal 2007, we committed to a restructuring plan which included the closures of our Lincolnton, North Carolina and Iuka, Mississippi upholstery manufacturing facilities, the closure of our rough mill lumber operation in North Wilkesboro, North Carolina, the consolidation of operations at our Kincaid Taylorsville, North Carolina upholstery operation and the elimination of a number of positions throughout the remainder of the organization. The Lincolnton and Iuka facility closures occurred in the first quarter of fiscal 2008 and impacted approximately 250 and 150 employees, respectively. The closure of our North Wilkesboro

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lumber operation, the consolidation of operations at Kincaid's Taylorsville operation and the remaining activities occurred in the fourth quarter of fiscal 2007 and impacted approximately 100 positions. These decisions were made to help align our company with the current business environment and strengthen our positioning going forward.

During the second quarter and first half of fiscal 2008, we recorded pre-tax restructuring charges in Cost of Sales of \$0.5 million and \$3.1 million, respectively which equates to \$0.01 and \$0.04 per diluted share, respectively, covering severance and benefits and other restructuring costs. During fiscal 2007, we recorded pre-tax restructuring charges of \$4.3 million or \$0.05 per diluted share covering severance and benefits, write-down of certain fixed assets in addition to other restructuring costs. Of these costs \$4.0 million was reported as a component of Cost of Sales with the remainder in Selling, General and Administrative. The write-down was accounted for in accordance with SFAS No. 144. All other costs were accounted for in accordance with SFAS No. 146.

During fiscal 2007, several of our Retail warehouses were consolidated into larger facilities and several underperforming stores were closed. Approximately 100 jobs were eliminated as a result of these closures. During the second quarter and first half of fiscal 2008, we recorded pre-tax restructuring charges of \$0.4 million and \$1.5 million, respectively, which equates to \$0.01 and \$0.02 per diluted share, respectively, covering contract termination costs for the leases on these facilities, severance and benefits, write-down of certain leasehold improvements in addition to other relocation costs which were expensed as incurred. In fiscal 2007, we recorded pre-tax restructuring charges of \$7.3 million or \$0.08 per diluted share covering contract termination costs for the leases on these facilities, severance and benefits, write-down of certain leasehold improvements in addition to other relocation costs which were expensed as incurred. These costs were reported as a component of Selling, General and Administrative costs. The write-down was accounted for in accordance with SFAS No. 144. All other costs were accounted for in accordance with SFAS No. 146.

As of October 27, 2007, we had a remaining restructuring liability of \$3.2 million which is expected to be paid out or written off as follows: \$2.2 million in fiscal 2008, \$0.5 million in fiscal 2009, \$0.4 million in fiscal 2010 and \$0.1 million thereafter. Contract terminations resulting from the closure of several of our retail stores and warehouses resulted in our restructuring liability being paid out over an extended length of time.

### **Regulatory Developments**

The Continued Dumping and Subsidy Offset Act of 2000 ("CDSOA") provides for distribution of monies collected by U.S. Customs and Border Protection ("CBP") from anti-dumping cases to domestic producers that supported the anti-dumping petition. CBP has reported that approximately \$57.4 million in preliminary CDSOA amounts were available as of April 30, 2007 for distribution to eligible domestic manufacturers in connection with the case involving wooden bedroom furniture imported from China. These funds are subject to adjustment. We have not received any CDSOA payments during the first six months of fiscal 2008. In view of the uncertainties associated with this program, we are unable to predict the amounts, if any, we may receive during the remainder of calendar 2007 or thereafter under CDSOA. However, assuming CDSOA distributions continue, these distributions could be material depending on the results of legal appeals and administrative reviews and our actual percentage allocation.

## **Recent Accounting Pronouncements**

### ***FASB Statement of Financial Accounting Standards No. 157***

The FASB issued Statement of Financial Accounting Standards No. 157, *Fair Value Measurements* (“SFAS No. 157”). SFAS No. 157 clarifies the principle that fair value should be based on the assumptions market participants would use when pricing an asset or liability and establishes a fair value hierarchy that prioritizes the information used to develop those assumptions. This statement is effective for financial statements issued for fiscal years beginning after November 15, 2007 and interim periods within those fiscal years, with early adoption permitted.

We are currently in the process of determining the impact this pronouncement may have on our financial statements.

### ***FASB Statement of Financial Accounting Standards No. 159***

The FASB issued Statement of Financial Accounting Standards No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities* (“SFAS No. 159”), which allows a company to choose to measure selected financial assets and financial liabilities at fair value. Unrealized gains and losses on items for which the fair value option has been elected are reported in earnings. SFAS No. 159 is effective for fiscal years beginning after November 15, 2007.

We are currently evaluating the impact SFAS No. 159 will have on our financial statements. This statement will be effective for our fiscal 2009 year end.

## **Business Outlook**

With the continued weak demand at retail for furniture, the decline in consumer confidence and the overall uncertain economic environment, our previously reported guidance will not be attainable. Since there are a number of unusual items in the first half of the year, the company feels that updated guidance for the second half of the year would be more prudent at this time and would give investors better perspective for the remainder of the year. At this point, we expect sales for the second half of fiscal year 2008 to be down 4% to 8% and earnings per share to be in the range of \$0.06 to \$0.14 per share compared with \$0.30 per share from continuing operations in the second half of 2007, which included an \$0.11 per share charge for restructuring, a \$0.14 per share gain on property sales and \$0.04 per share in income from anti-dumping monies. The 2008 estimate does not include restructuring charges, potential income from anti-dumping monies, or any further effect from discontinued operations.

### **ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

We are exposed to market risk from changes in interest rates. Our exposure to interest rate risk results from our lines of credit and our floating rate \$100 million revolving credit facility under which we had no borrowings at October 27, 2007. Management estimates that a one percentage point change in interest rates would not have a material impact on our results of operations for fiscal 2008 based upon the current levels of exposed liabilities.

We are exposed to market risk from changes in the value of foreign currencies. Our exposure to changes in the value of foreign currencies is reduced through our use of foreign currency forward contracts from time to time. At October 27, 2007, we had an insignificant amount of foreign exchange forward contracts outstanding. Substantially all of our imports purchased outside of North America are denominated in U.S. dollars. However, a change in the value of Chinese currency could be one of several factors that could inflate costs in the future. We believe that gains or losses resulting from changes in the value of foreign currencies will not be material to our results from operations in fiscal year 2008.

### **ITEM 4. CONTROLS AND PROCEDURES**

We maintain a system of disclosure controls and procedures that are designed to provide reasonable assurance that information that is required to be timely disclosed is accumulated and communicated to management in a timely fashion. An evaluation of the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rule 13a-15(e) of the Securities Exchange Act of 1934, as amended) was performed as of the end of the period covered by this report. This evaluation was performed under the supervision and with the participation of management, including our Chief Executive Officer and Chief Financial Officer. Based upon that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures are effective to provide reasonable assurance that information we are required to disclose in the reports that we file or submit under the Exchange Act is accumulated and communicated to management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure and are effective to provide reasonable assurance that such information is recorded, processed, summarized and reported within the time periods specified by the SEC's rules and forms.

There was no change in the Company's internal controls over financial reporting that occurred during the quarter covered by this report that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

**PART II — OTHER INFORMATION**

**ITEM 1A. RISK FACTORS**

In addition to the risk factors disclosed in our Form 10-K for the year ended April 28, 2007, you should consider the following risk:

*If we are unable to complete the refinancing of our debt obligation, we would be unable to repay our private placement debt if the lenders were to accelerate the maturity of this debt.*

During November 2007, we signed an engagement letter with our lead bank to refinance our current debt obligations. Due to current business conditions, we could be in noncompliance with the third quarter fixed charge coverage ratio requirements in our existing revolving credit facility (under which no borrowings are outstanding) and in the agreement governing our private placement notes (under which \$121.0 million is outstanding). Although we consider this unlikely, if our private placement noteholders were to accelerate the maturity of our debt and we were unable to complete the refinancing of a new credit facility during our fiscal 2008 third quarter, we would be unable to satisfy our repayment obligations and would default under our private placement debt agreement. As a result, the private placement noteholders would have certain rights including the acceleration of principal and interest payments, which could have an adverse effect on our results of operation and financial condition.

**ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS**

During the second quarter of fiscal 2008, we sold shares of our common stock to our non-employee directors pursuant to our Restricted Stock Plan for Non-Employee Directors without registration under the Securities Act of 1933 in reliance on the exemption provided in Section 4(2) of the Act. In accordance with the terms of the plan, we sold these shares to our non-employee directors upon their acceptance of awards granted to them to purchase shares at 25% of their fair market value on the date of grant. The following table shows the date of these sales, the number of shares sold, and the per share and aggregate sales price.

| <b>Date of Sale</b> | <b>Number of Shares Sold</b> | <b>Per Share Price</b> | <b>Aggregate Price</b> |
|---------------------|------------------------------|------------------------|------------------------|
| August 2007         | 18,000                       | \$2.16                 | \$38,925               |

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### ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

The Annual Meeting of Shareholders of La-Z-Boy Incorporated was held on August 15, 2007. The shareholders elected three directors for three-year terms expiring in 2010, elected one director to serve the remainder of a three-year term expiring in 2008 and ratified the selection of the independent registered public accounting firm for fiscal year 2008.

| <b>Proposal</b>  | <b>Shares Voted<br/>In Favor</b> | <b>Percent<br/>Shares<br/>In Favor</b> | <b>Shares<br/>Withheld</b>  |
|--|----------------------------------|--|-----------------------------|
| <b>Election of Directors for terms expiring in 2010:</b>                               |                                  |  |                             |
| David K. Hehl  | 37,997,979                       | 89.7%                                  | 4,382,460                   |
| Rocque E. Lipford  | 27,411,899                       | 64.7%                                  | 14,968,540                  |
| Jack L. Thompson   | 38,015,635                       | 89.7%                                  | 4,364,804                   |
| <b>Election of Director for term expiring in 2008:</b>                                 |                                  |  |                             |
| W. Alan McCollough   | 41,597,469                       | 98.2%                                  | 782,970                     |
| <b>Proposal</b>  | <b>Shares Voted<br/>In Favor</b> | <b>Shares<br/>Voted<br/>Against</b>    | <b>Shares<br/>Abstained</b> |
| Ratify the selection of the independent registered public accounting firm for FYE 2008 | 42,163,666                       | 89,461                                 | 127,310                     |

### ITEM 6. EXHIBITS

| <b>Exhibit<br/>Number</b> | <b>Description</b>   |
|---------------------------|--|
| (4.1)                     | Third Amendment dated as of November 13, 2007 to Credit Agreement dated as of March 30, 2004 |
| (31.1)                    | Certifications of Chief Executive Officer pursuant to Rule 13a-14(a)                         |
| (31.2)                    | Certifications of Chief Financial Officer pursuant to Rule 13a-14(a)                         |
| (32)                      | Certifications of Executive Officers pursuant to 18 U.S.C. Section 1350(b)                   |
| (99.1)                    | Press Release dated November 13, 2007  |

**SIGNATURE**

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.

**LA-Z-BOY INCORPORATED**

\_\_\_\_\_  
(Registrant)

Date: November 13, 2007

BY: /s/ Louis M. Riccio, Jr.

\_\_\_\_\_  
Louis M. Riccio, Jr.

Chief Financial Officer

On behalf of the registrant and as

Chief Financial Officer



**THIRD AMENDMENT TO CREDIT AGREEMENT**

**THIS THIRD AMENDMENT TO CREDIT AGREEMENT** (this "Amendment"), dated as of November 13, 2007, is by and among **LA-Z-BOY INCORPORATED**, a Michigan corporation, (the "Borrower"), those Subsidiaries of the Borrower identified as a "Guarantor" on the signature pages hereto (individually a "Guarantor" and collectively the "Guarantors"), and **WACHOVIA BANK, NATIONAL ASSOCIATION**, as administrative agent for the Lenders (in such capacity, the "Administrative Agent").

**WITNESSETH**

**WHEREAS**, the Borrower, the Guarantors, the several banks and other financial institutions as may from time to time become parties thereto (the "Lenders"), and the Administrative Agent have entered into that certain Credit Agreement dated as of March 30, 2004 (as previously amended and/or modified and as further amended, modified, supplemented, restated or amended and restated from time to time, the "Credit Agreement"; capitalized terms used but not otherwise defined herein shall have the meaning ascribed thereto in the Credit Agreement);

**WHEREAS**, the Borrower has requested certain amendments to the Credit Agreement as more fully set forth herein; and

**WHEREAS**, the Required Lenders have agreed to such amendments, subject to the terms and conditions set forth herein.

**NOW, THEREFORE**, in consideration of the agreements hereinafter set forth, and for other good and valuable consideration, the receipt and adequacy of which are hereby acknowledged, the parties hereto agree as follows:

**ARTICLE I  
AMENDMENTS TO CREDIT AGREEMENT**

**1.1 New Definitions.** The following definitions are hereby added to Section 1.1 of the Credit Agreement in the appropriate alphabetical order:

"Accounts Receivable" means, as of any date of determination, the amount representing accounts receivable of the Borrower and the Subsidiaries that would appear on a consolidated balance sheet of the Borrower and its Subsidiaries at such time prepared in accordance with GAAP.

"Asset Coverage Ratio" shall mean, as of the last day of any fiscal month of the Borrower and its Subsidiaries on a consolidated basis, the ratio (a) the numerator of which shall be equal to the sum of (i) 85% of Eligible Accounts Receivable plus (ii) 60% of Eligible

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Finished Goods Inventory plus (iii) 35% of Eligible Raw Materials Inventory and (b) the denominator of which shall be equal to all Funded Debt of the Borrower and its Subsidiaries on a consolidated basis.

“Eligible Accounts Receivable” shall mean 90% of all Accounts Receivable.

“Eligible Finished Goods Inventory” shall mean 85% of all Finished Goods Inventory.

“Eligible Raw Materials Inventory” shall mean 70% of all Raw Materials Inventory.

“Finished Goods Inventory” means, as of any date of determination, the amount representing finished goods inventory of the Borrower and the Subsidiaries that would appear on a consolidated balance sheet of the Borrower and its Subsidiaries at such time prepared in accordance with GAAP.

“Raw Materials Inventory” means, as of any date of determination, the amount representing raw materials inventory of the Borrower and the Subsidiaries that would appear on a consolidated balance sheet of the Borrower and its Subsidiaries at such time prepared in accordance with GAAP.

“Third Amendment Effective Date” shall mean November 13, 2007.

**1.2 Definition of Applicable Percentage.** The pricing grid set forth in the definition of “Applicable Percentage” in Section 1.1 of the Credit Agreement is hereby amended and restated in its entirety to read as follows:

| <i>Level</i> | <i>Funded Debt to Total Capitalization Ratio</i> | <i>Alternate Base Rate Margin for Revolving Loans</i> | <i>LIBOR Rate Margin for Revolving Loans and Standby Letter of Credit Fee</i> | <i>Commercial and Trade Letters of Credit Fee</i> | <i>Facility Fee</i> |
|--------------|--|---|---|---|---------------------|
| <i>I</i>     | <i>≥ .400 to 1.0</i>                             | <i>0.475%</i>   | <i>1.475%</i>   | <i>1.075%</i>                                     | <i>0.325%</i>       |
| <i>II</i>    | <i>&lt; .400 to 1.0 but ≥ .250 to 1.0</i>        | <i>0.225%</i>   | <i>1.225%</i>   | <i>0.950%</i>                                     | <i>0.275%</i>       |
| <i>III</i>   | <i>&lt; .250 to 1.0</i>                          | <i>0.150%</i>   | <i>1.150%</i>   | <i>0.9125%</i>                                    | <i>0.250%</i>       |

**1.3 Fixed Charge Coverage Ratio.** Section 6.7(b) of the Credit Agreement is hereby amended by adding the following proviso to the end of Section 6.7(b):

*; provided that, notwithstanding the foregoing, the Fixed Charge Coverage Ratio as of the end of the fiscal quarter ended October 27, 2007 shall be greater than or equal to 2.00 to 1.0.*

**1.4 Asset Coverage Ratio.** Section 6.7 of the Credit Agreement is hereby amended by adding the following clause (c):

*(c) Asset Coverage Ratio. The Asset Coverage Ratio measured as of the last day of the twelve month period ending as of each fiscal month end shall be greater than*

or equal to 1.10 to 1.0 at all times; provided that it is acknowledged and agreed that Credit Parties shall not be required to show such calculations except in connection with the delivery of the financial statements referred to in Sections 6.1(a) and 6.1(b) in accordance with Section 6.2(a).

**1.5 Indebtedness.** Section 7.1(b) and (c) of the Credit Agreement is hereby amended and restated in its entirety to read as follows:

(b) Priority Debt existing as of the Third Amendment Effective Date; and

(c) Indebtedness existing as of the Third Amendment Effective Date plus other Indebtedness (other than Priority Debt) in an aggregate amount not to exceed \$5,000,000 at any time outstanding; provided that the Credit Parties are in compliance with the financial covenants set forth in Section 6.7 on a Pro Forma Basis.

**1.6 Liens.** Section 7.2(a) of the Credit Agreement is hereby amended and restated in its entirety to read as follows:

(a) (i) purchase money security interests in fixed assets granted prior to the Third Amendment Effective Date (including such security interests granted in connection with the issuance of industrial development revenue bonds issued to permit the Borrower or any of its Subsidiaries to acquire fixed assets) and (ii) purchase money security interests in fixed assets granted after the Third Amendment Effective Date in an aggregate amount not to exceed \$4,000,000 at any time outstanding (including such security interests granted in connection with the issuance of industrial development revenue bonds issued to permit the Borrower or any of its Subsidiaries to acquire fixed assets), provided that each such security interest is created substantially contemporaneously with the acquisition of such fixed assets and does not extend to any property other than the fixed assets so financed;

**1.7 Mergers, Sale of Assets and Indebtedness of Subsidiaries.** Section 7.4(v) of the Credit Agreement is hereby amended and restated in its entirety to read as follows:

(v) in addition to the foregoing, the sale, lease or transfer of property or assets to Persons other than the Borrower and its Subsidiaries not to exceed 10% of Consolidated Assets (determined as of the end of the most recently ended fiscal quarter prior to the Closing Date) in the aggregate during the term of this Credit Agreement; or

**1.8 Advances, Investments and Loans.** Section 7.5(c) of the Credit Agreement is hereby amended and restated in its entirety to read as follows:

(c) consummate any acquisition except for Permitted Acquisitions that are dealer acquisitions in an aggregate amount not to exceed \$6,000,000 from the Third Amendment Effective Date through the end of this Agreement;

*provided that after giving effect to the making of any Investment, loan or advance permitted by this Section 7.5, no Default or Event of Default shall have occurred and be continuing.*

**1.9 Restricted Payments.** Section 7.9 of the Credit Agreement is hereby amended and restated in its entirety to read as follows:

**7.9 Restricted Payments.**

*Directly or indirectly, declare, order, make or set apart any sum for or pay any Restricted Payment, except (a) to make dividends payable solely in the same class of Capital Stock of such Person, (b) to make dividends or other distributions payable to the Borrower (directly or indirectly through Subsidiaries) and (c) the Borrower may pay cash dividends to the shareholders of the Borrower so long as, after giving effect thereto on a Pro Forma Basis, no Default or Event of Default shall exist.*

## **ARTICLE II CONDITIONS TO EFFECTIVENESS**

**2.1 Closing Conditions.** This Amendment shall become effective as of the day and year set forth above upon satisfaction of the following conditions (in form and substance reasonably acceptable to the Administrative Agent):

(a) **Executed Amendment.** The Administrative Agent shall have received a copy of this Amendment duly executed by each of the Credit Parties, the Required Lenders and the Administrative Agent.

(b) **New Facility.** The Borrower shall be actively engaged in obtaining a new credit facility for the purpose of terminating all Credit Party Obligations under the Credit Documents.

(c) **Fees and Expenses.** The Administrative Agent shall have received from the Borrower, on behalf of each Lender that executes and delivers a Lender Consent to the Administrative Agent by 2:00 p.m. (Charlotte, NC time) on November 6, 2007, an amendment fee in an amount equal to 5.0 basis points on the aggregate Revolving Commitments of such approving Lenders. In addition, the Administrative Agent shall have received from the Borrower such other fees and expenses that are payable in connection with the consummation of the transactions contemplated hereby, including, without limitation, the reasonable fees and expenses of Moore & Van Allen PLLC.

(d) **Miscellaneous.** All other documents and legal matters in connection with the transactions contemplated by this Amendment shall be reasonably satisfactory in form and substance to the Administrative Agent and its counsel.

**ARTICLE III  
MISCELLANEOUS**

**3.1 Amended Terms.** All references to the Credit Agreement in each of the Credit Documents shall hereafter mean the Credit Agreement as amended by this Amendment. Except as specifically amended hereby or otherwise agreed, all of the terms and provisions and conditions of each of the Credit Documents shall remain unchanged and are hereby ratified and confirmed and shall remain in full force and effect according to their respective terms. The amendments to the Credit Agreement set forth in this Amendment shall be effective from and after the date of this Amendment and shall not be applied retroactively.

**3.2 Representations and Warranties of Credit Parties.** Each of the Credit Parties represents and warrants as follows:

(a) It has taken all necessary action to authorize the execution, delivery and performance of this Amendment.

(b) This Amendment has been duly executed and delivered by such Person and constitutes such Person's legal, valid and binding obligations, enforceable in accordance with its terms, except as such enforceability may be subject to (i) bankruptcy, insolvency, reorganization, fraudulent conveyance or transfer, moratorium or similar laws affecting creditors' rights generally and (ii) general principles of equity (regardless of whether such enforceability is considered in a proceeding at law or in equity).

(c) No consent, approval, authorization or order of, or filing, registration or qualification with, any court or governmental authority or third party is required in connection with the execution, delivery or performance by such Person of this Amendment.

(d) The representations and warranties set forth in Section 5 of the Credit Agreement are true and correct as of the date hereof (except for those which expressly relate to an earlier date).

(e) No Default or Event of Default exists after giving effect to this Amendment.

(f) Both before and after giving effect to this Amendment, the Borrower is in compliance with all representations, warranties, covenants and other terms and conditions set forth in the definitive documentation for the Private Shelf Facility.

**3.3 Acknowledgment of Guarantors.** The Guarantors acknowledge and consent to all of the terms and conditions of this Amendment and agree that this Amendment and all documents executed in connection herewith do not operate to reduce or discharge the Guarantors' obligations under the Credit Documents.

**3.4 Credit Document.** This Amendment shall constitute a Credit Document under the terms of the Credit Agreement.

**3.5 Entirety.** This Amendment and the other Credit Documents embody the entire agreement between the parties hereto and supersede all prior agreements and understandings, oral or written, if any, relating to the subject matter hereof.

**3.6 Counterparts; Telecopy.** This Amendment may be executed in any number of counterparts, each of which when so executed and delivered shall be an original, but all of which shall constitute one and the same instrument. Delivery of an executed counterpart to this Amendment by telecopy shall be effective as an original and shall constitute a representation that an original will be delivered. A copy of this Amendment executed by the Borrower and the Administrative Agent shall constitute definitive evidence that this Amendment has been executed by all requisite parties.

**3.7 Successors and Assigns.** This Amendment shall be binding upon and inure to the benefit of the parties hereto and their respective successors and assigns.

**3.8 GOVERNING LAW. THIS AMENDMENT AND THE RIGHTS AND OBLIGATIONS OF THE PARTIES UNDER THIS AMENDMENT SHALL BE GOVERNED BY, AND CONSTRUED AND INTERPRETED IN ACCORDANCE WITH, THE LAW OF THE STATE OF NORTH CAROLINA.**

**3.9 Consent to Jurisdiction; Service of Process.** The jurisdiction and service of process provisions set forth in Section 11.14 of the Credit Agreement are hereby incorporated by reference, *mutatis mutandis*.

**3.10 GENERAL RELEASE. IN CONSIDERATION OF THE REQUIRED LENDERS ENTERING INTO THIS AMENDMENT, THE CREDIT PARTIES HEREBY RELEASE THE ADMINISTRATIVE AGENT, THE LENDERS, AND THE ADMINISTRATIVE AGENT'S AND THE LENDERS' RESPECTIVE OFFICERS, EMPLOYEES, REPRESENTATIVES, AGENTS, COUNSEL AND DIRECTORS FROM ANY AND ALL ACTIONS, CAUSES OF ACTION, CLAIMS, DEMANDS, DAMAGES AND LIABILITIES OF WHATEVER KIND OR NATURE, IN LAW OR IN EQUITY, NOW KNOWN OR UNKNOWN, SUSPECTED OR UNSUSPECTED TO THE EXTENT THAT ANY OF THE FOREGOING ARISES FROM ANY ACTION OR FAILURE TO ACT UNDER THE CREDIT AGREEMENT OR UNDER THE OTHER CREDIT DOCUMENTS ON OR PRIOR TO THE DATE HEREOF.**

LA-Z-BOY INCORPORATED  
THIRD AMENDMENT TO CREDIT AGREEMENT

IN WITNESS WHEREOF the Borrower, the Guarantors and the Administrative Agent, on behalf of the Required Lenders, have caused this Amendment to be duly executed on the date first above written.

**BORROWER:**

LA-Z-BOY INCORPORATED, a Michigan corporation

By: /s/ M. Skrzypczak \_\_\_\_\_

Name: Michael S. Skrzypczak

Title: VP and Treasurer

**GUARANTORS:**

KINCAID FURNITURE COMPANY

INCORPORATED, a Delaware corporation

ENGLAND, INC., a Michigan corporation

BAUHAUS U.S.A., INC., a Mississippi corporation

LA-Z-BOY GREENSBORO, INC., a North Carolina  
corporation

LZB MANUFACTURING, INC., a Michigan corporation

By: /s/ M. Skrzypczak \_\_\_\_\_

Name: Michael S. Skrzypczak

Title: VP and Treasurer

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LA-Z-BOY INCORPORATED  
THIRD AMENDMENT TO CREDIT AGREEMENT

**ADMINISTRATIVE AGENT:**

WACHOVIA BANK, NATIONAL ASSOCIATION,  
as a Lender and as Administrative Agent

By: /s/ Martha M. Winters  
Name: Martha M. Winters  
Title: Director

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LA-Z-BOY INCORPORATED  
THIRD AMENDMENT TO CREDIT AGREEMENT

**LENDERS:**

JPMORGAN CHASE, N.A.,  
as a lender

By: /s/ James M. Sumoski

Name: James M. Sumoski

Title: Vice President

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LA-Z-BOY INCORPORATED  
THIRD AMENDMENT TO CREDIT AGREEMENT

**LENDERS:**

THE NORTHERN TRUST COMPANY,  
as a Lender

By: /s/ J. T. Hall

Name: Jared T. Hall

Title: Vice President

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LA-Z-BOY INCORPORATED  
THIRD AMENDMENT TO CREDIT AGREEMENT

**LENDERS:**

SunTrust Bank,  
as a Lender

By: /s/ William Humphries  
Name: William Humphries  
Title: Managing Director

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LA-Z-BOY INCORPORATED  
THIRD AMENDMENT TO CREDIT AGREEMENT

**LENDERS:**

COMERICA BANK,  
as a Lender

By: /s/ Steven J. McCormack  
Name: Steven J. McCormack  
Title: Vice President

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LA-Z-BOY INCORPORATED  
THIRD AMENDMENT TO CREDIT AGREEMENT

**LENDERS:**

BRANCH BANKING AND TRUST COMPANY,  
as a Lender

By: /s/ Jennifer L. Cudd

Name: Jennifer L. Cudd

Title: Senior Vice President

**Exhibit 31.1**

**CERTIFICATIONS OF CHIEF EXECUTIVE OFFICER  
PURSUANT TO RULE 13a-14(a)**

I, Kurt L. Darrow, certify that:

1. I have reviewed this quarterly report on Form 10-Q of La-Z-Boy Incorporated;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 13, 2007

/s/ Kurt L. Darrow

\_\_\_\_\_  
Kurt L. Darrow  
Chief Executive Officer

**Exhibit 31.2**

**CERTIFICATIONS OF CHIEF FINANCIAL OFFICER  
PURSUANT TO RULE 13a-14(a)**

I, Louis M. Riccio, Jr., certify that:

1. I have reviewed this quarterly report on Form 10-Q of La-Z-Boy Incorporated;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 13, 2007

/s/ Louis M. Riccio, Jr.

\_\_\_\_\_  
Louis M. Riccio, Jr.  
Chief Financial Officer

CERTIFICATION OF EXECUTIVE OFFICERS\*

Pursuant to 18 U.S.C. section 1350, each of the undersigned officers of La-Z-Boy Incorporated (the "Company") hereby certifies, to such officer's knowledge, that the Company's Quarterly Report on Form 10-Q for the period ended October 27, 2007 (the "Report") fully complies with the requirements of section 13(a) or 15(d), as applicable, of the Securities Exchange Act of 1934 and the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ Kurt L. Darrow

\_\_\_\_\_  
Kurt L. Darrow  
President and Chief Executive Officer  
November 13, 2007

/s/ Louis M. Riccio, Jr.

\_\_\_\_\_  
Louis M. Riccio, Jr.  
Senior Vice President and Chief Financial Officer  
November 13, 2007

\* The foregoing certification is being furnished solely pursuant to 18 U.S.C. section 1350 and is not being filed as part of the Report or as a separate disclosure document.



**NEWS RELEASE****Contact:** Kathy Liebmann

(734) 241-2438

[kathy.liebmann@la-z-boy.com](mailto:kathy.liebmann@la-z-boy.com)**LA-Z-BOY REPORTS FISCAL 2008 SECOND-QUARTER RESULTS**

MONROE, MI. November 13, 2007—La-Z-Boy Incorporated (NYSE: LZB) today reported its operating results for the second fiscal quarter ended October 27, 2007. Net sales for the quarter were \$365.4 million, down 12% compared with the prior-year period. The company posted an after-tax loss of \$9.9 million, or \$0.19 per share, which included a \$0.07 per-share charge for a write-down of goodwill, a \$0.12 per—share charge from discontinued operations, a large portion of which was attributable to intangible assets and liquidating inventory of businesses held for sale, and a \$0.01 restructuring charge. La-Z-Boy posted an after-tax loss of \$3.7 million from continuing operations, or a loss of \$0.07 per share, which included the \$0.01 per share restructuring charge and the \$0.07 per share for the goodwill write-down.

Kurt L. Darrow, La-Z-Boy's President and Chief Executive Officer, said: "While we are disappointed that, due to industry headwinds, the improvements we have made in our business model are not clearly evident in our results, we posted reasonable operating margins in each of our wholesale businesses on significantly lower volume. In the midst of what continues to be a challenging environment across the furniture sector, we are executing against our strategy and making the necessary changes to our business model to ensure we remain both a leading and competitive manufacturer, distributor and retailer. During the quarter, we sold our two remaining businesses held for sale and are pleased to have the announced portfolio rationalization process behind us. Going forward, we will continue to address our manufacturing processes, structure our retail operation to run as an integrated entity with increased efficiencies and remain committed to working on the areas of the business we can control and improve given this environment."

**Upholstery**

For the fiscal 2008 second quarter, sales in the company's upholstery segment decreased 11.4% to \$269.7 million compared with \$304.6 million in the prior year's second quarter while the segment's operating margin increased to 7.1% from 6.6% in the year-ago period. Darrow stated, "Our operating margin results this quarter reflect increased capacity utilization at our remaining facilities as well as the benefit we are attaining through the conversion of our La-Z-Boy branded facilities to the cellular production process, which will be completed by the end of this fiscal year. We are confident that when retail conditions improve, the lower operating cost structure we have achieved across our enterprise will position us to improve our financial results."

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For the quarter, the La-Z-Boy Furniture Galleries® store system, which includes both company-owned and independent-licensed stores, opened 6 new stores, relocated and/or remodeled 4 and closed 1, bringing the total store count to 338, of which 205 are in the New Generation format. For the third quarter 2008, the network plans to open 10 New Generation format La-Z-Boy Furniture Galleries® stores, of which 3 will be new stores and 7 will be store remodels or relocations, and will close 3.

System-wide, for the third calendar quarter, including company-owned and independent-licensed stores, same-store written sales, which the company tracks as an indicator of retail activity, were down 9.1%. Total written sales, which includes new stores, were down 9.6%.

### **Casegoods**

For the 2008 second quarter, casegoods sales were \$58.9 million, down 20.6% from the prior year's second quarter and, as a result, the segment's quarterly operating margin decreased to 6.1% from 8.4% in last year's comparable period.

Darrow commented, "The high variable cost structure associated with our casegoods business, which has transitioned to primarily an import model, allowed us to post a 6.1% operating margin on a significant decrease in sales year over year. Furthermore, we moved and downsized the office facilities for our casegoods operations at the end of the quarter, which will further reduce our fixed costs. Going forward, we are focused on increasing revenues in the segment and are pleased our casegoods companies received positive reviews for their new product introductions at the recent High Point Market."

### **Retail**

For the quarter, retail sales were \$46.2 million, down 12% compared with the prior-year period. The retail group posted an operating loss for the quarter and its operating margin was (19.8%). A portion of the sales decline was the result of exiting the Pittsburgh, Pennsylvania and Rochester, New York markets in the second half of fiscal 2007. Additionally, the retail segment did not achieve the anticipated sales increases from opening 10 stores over the past twelve months in its ongoing markets. With the slowing economy and its effect on the home furnishings market, the company continues to experience negative same store sales comparisons across all of its markets. As a result of the decreased volume, the company's operating results were impacted as it was more difficult to absorb fixed costs, particularly the higher occupancy costs associated with the company's new stores.

Given the continued depressed housing market in southeastern Florida and its impact on La-Z-Boy's retail operations, the company has delayed its new store plans for the near term. The downturn in business and the company's decision to delay its expansion has triggered a significant change in its valuation of the southeastern Florida market, resulting in a \$0.07 per share write-down on the goodwill associated with that market.

Darrow stated, "We continue to make substantial changes to our retail model and are reducing costs through the consolidation of systems and operations. These changes did, indeed, improve our cost structure and overall competitiveness; however, that improvement is not clearly demonstrable in an environment of significantly lower volume."

During the second quarter, the company's retail segment opened 2 new company-owned stores and closed 1. At the end of the second quarter, the company owned 70 stores, including 50 in the

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New Generation format, or about 71% versus 68 company-owned stores last year at this time, of which 37, or 54%, were in the new format.

### **Restructuring**

During the quarter, a pre-tax restructuring charge of approximately \$1 million was recorded. The charge is primarily related to transition costs associated with the closure of the company's Lincolnton plant as well as charges in the company's retail operation. These charges were partially offset by a gain from the sale of a small manufacturing facility.

### **Businesses Held for Sale**

In the second quarter, the company completed the sales of its Clayton-Marcus and Pennsylvania House operations. The company recorded a \$5.8 million pre-tax loss in relation to the sale of Clayton-Marcus, a \$0.6 million pre-tax loss for the sale of the Pennsylvania House trade name and wrote down an additional \$3.0 million to mark its remaining Pennsylvania House inventory to market.

### **Balance Sheet**

At the end of the fiscal 2008 second quarter, the company's debt to capitalization ratio was 24.7%. Inventories decreased to \$191.0 million at the end of the second quarter. Cash generated from operations was \$14.3 million, primarily the result of a reduction in working capital.

The company received an amendment from its bank group for a one-quarter adjustment to its fixed charge coverage ratio requirements, but was in compliance with its covenants for its private placement notes. The company is working to finalize an arrangement to renegotiate its bank agreements, refinancing its debt with an asset-based lending arrangement. Darrow stated, "There are a number of moves we are making to improve our business model, including the consolidations in our retail business, our store build out program and the conversion to cellular production at our branded facilities. Our proposed new arrangement, with longer term financing options, will give us the additional flexibility we need to make the necessary adjustments to our business in the short term."

### **Business Outlook**

Commenting on the company's business outlook, Darrow said: "With the continued weak demand at retail for furniture, the decline in consumer confidence and the overall uncertain economic environment, our previously reported annual guidance will not be attainable. Since there are a number of unusual items in the first half of the year, the company feels that updated guidance for the second half of the year would be more prudent at this time and would give investors better perspective for the remainder of the year. At this point, we expect sales for the second half of fiscal year 2008 to be down 4% to 8% and earnings per share to be in the range of \$0.06 to \$0.14 per share compared with \$0.30 per share from continuing operations in the second half of 2007, which included an \$0.11 per share charge for restructuring, a \$0.14 per share gain on property sales and \$0.04 per share in income from anti-dumping monies. The 2008 estimate does not include restructuring charges, potential income from anti-dumping monies, or any further effect from discontinued operations."

### **Forward-looking Information**

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Any forward-looking statements contained in this news release are based on current information and assumptions and represent management's best judgment at the present time. Actual results could differ materially from those anticipated or projected due to a number of factors. These factors include, but are not limited to: (a) changes in consumer confidence; (b) changes in demographics; (c) changes in housing sales; (d) the impact of terrorism or war; (e) continued energy price changes; (f) the impact of logistics on imports; (g) the impact of interest rate changes; (h) changes in currency exchange rates; (i) competitive factors; (j) operating factors, such as supply, labor or distribution disruptions including changes in operating conditions or costs; (k) effects of restructuring actions; (l) changes in the domestic or international regulatory environment; (m) ability to implement global sourcing organization strategies; (n) fair value changes to our intangible assets due to actual results differing from projected; (o) the impact of adopting new accounting principles; (p) the impact from natural events such as hurricanes, earthquakes and tornadoes; (q) the impact of retail store relocation costs, the success of new stores or the timing of converting stores to the New Generation format; (r) the ability to procure fabric rolls or cut and sewn fabric sets domestically or abroad; (s) the ability to sell the remaining assets of our discontinued operations for their recorded fair value; (t) those matters discussed under "Risk Factors" in our most recent Annual Report of Form 10-K and subsequent Quarterly Reports on Form 10-Q and factors relating to acquisitions and other factors identified from time to time in our reports filed with the Securities and Exchange Commission. We undertake no obligation to update or revise any forward-looking statements, either to reflect new developments or for any other reason.

#### Additional Information

This news release is just one part of La-Z-Boy's financial disclosures and should be read in conjunction with other information filed with the Securities and Exchange Commission, which is available at [http://www.la-z-boy.com/about/investorRelations/sec\\_filings.aspx](http://www.la-z-boy.com/about/investorRelations/sec_filings.aspx). Investors and others wishing to be notified of future La-Z-Boy news releases, SEC filings and quarterly investor conference calls may sign up at:

[http://www.la-z-boy.com/about/investorRelations/IR\\_email\\_alerts.aspx](http://www.la-z-boy.com/about/investorRelations/IR_email_alerts.aspx).

#### **Background Information**

La-Z-Boy Incorporated is one of the world's leading residential furniture producers, marketing furniture for every room of the home. The La-Z-Boy Upholstery Group companies are Bauhaus, England, La-Z-Boy and La-Z-Boy, U.K. The La-Z-Boy Casegoods Group companies are American Drew, Hammary, Kincaid and Lea.

The corporation's proprietary distribution network is dedicated exclusively to selling La-Z-Boy Incorporated products and brands, and includes 338 stand-alone La-Z-Boy Furniture Galleries® stores and 215 La-Z-Boy In-Store Galleries, in addition to in-store gallery programs at the company's Kincaid, England and Lea operating units. According to industry trade publication *In Furniture*, the La-Z-Boy Furniture Galleries retail network is North America's largest single-brand furniture retailer. Additional information is available at <http://www.la-z-boy.com/>.

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**LA-Z-BOY INCORPORATED**  
**CONSOLIDATED STATEMENT OF OPERATIONS**

| (Unaudited, amounts in thousands, except<br>per share data)     | Second Quarter Ended |                 |                   | Percent of Sales |          |
|---|----------------------|-----------------|-------------------|------------------|----------|
|   | 10/27/07             | 10/28/06        | % Over<br>(Under) | 10/27/07         | 10/28/06 |
| Sales   | \$ 365,434           | \$ 414,614      | -11.9%            | 100.0%           | 100.0%   |
| Cost of sales   |                      |                 |                   |                  |          |
| Cost of goods sold  | 266,658              | 306,351         | -13.0%            | 73.0%            | 73.9%    |
| Restructuring   | 518                  | (400)           | -229.5%           | 0.1%             | -0.1%    |
| Total cost of sales   | 267,176              | 305,951         | -12.7%            | 73.1%            | 73.8%    |
| Gross profit  | 98,258               | 108,663         | -9.6%             | 26.9%            | 26.2%    |
| Selling, general and administrative                             | 98,098               | 99,887          | -1.8%             | 26.8%            | 24.1%    |
| Write-down of intangibles                                       | 5,809                | —               | N/M               | 1.6%             | —        |
| Restructuring   | 449                  | 2,265           | -80.2%            | 0.1%             | 0.5%     |
| Operating income (loss)   | (6,098)              | 6,511           | -193.7%           | -1.7%            | 1.6%     |
| Interest expense  | 2,120                | 2,614           | -18.9%            | 0.6%             | 0.6%     |
| Other income, net   | 1,374                | 1,348           | 1.9%              | 0.4%             | 0.3%     |
| Income (loss) from continuing operations before income<br>taxes | (6,844)              | 5,245           | -230.5%           | -1.9%            | 1.3%     |
| Income tax expense (benefit)                                    | (3,192)              | 1,949           | -263.8%           | 46.6%*           | 37.2%*   |
| Income (loss) from continuing operations                        | (3,652)              | 3,296           | -210.8%           | -1.0%            | 0.8%     |
| Loss from discontinued operations (net of tax)                  | (6,282)              | (1,342)         | -368.1%           | -1.7%            | -0.3%    |
| Net income (loss)   | <u>\$ (9,934)</u>    | <u>\$ 1,954</u> | -608.4%           | -2.7%            | 0.5%     |
| Basic average shares  | 51,410               | 51,373          |                   |                  |          |
| Basic income (loss) from continuing operations per share        | \$ (0.07)            | \$ 0.06         |                   |                  |          |
| Discontinued operations per share (net of tax)                  | \$ (0.12)            | \$ (0.02)       |                   |                  |          |
| Basic net income (loss) per share                               | <u>\$ (0.19)</u>     | <u>\$ 0.04</u>  |                   |                  |          |
| Diluted average shares  | 51,410               | 51,639          |                   |                  |          |
| Diluted income (loss) from continuing operations per share      | \$ (0.07)            | \$ 0.06         |                   |                  |          |
| Discontinued operations per share (net of tax)                  | \$ (0.12)            | \$ (0.02)       |                   |                  |          |
| Diluted net income (loss) per share                             | <u>\$ (0.19)</u>     | <u>\$ 0.04</u>  |                   |                  |          |
| Dividends paid per share  | \$ 0.12              | \$ 0.12         |                   |                  |          |

\* As a percent of pretax income, not sales.

N/M = not meaningful

**LA-Z-BOY INCORPORATED**  
**CONSOLIDATED STATEMENT OF OPERATIONS**

| <i>(Unaudited, amounts in thousands, except per share data)</i> | Six Months Ended   |                 |                   | Percent of Sales |          |
|---|--------------------|-----------------|-------------------|------------------|----------|
|   | 10/27/07           | 10/28/06        | % Over<br>(Under) | 10/27/07         | 10/28/06 |
| Sales   | \$ 709,830         | \$ 808,537      | -12.2%            | 100.0%           | 100.0%   |
| Cost of sales   |                    |                 |                   |                  |          |
| Cost of goods sold  | 525,801            | 602,359         | -12.7%            | 74.1%            | 74.5%    |
| Restructuring   | 3,079              | (400)           | -869.8%           | 0.4%             | —        |
| Total cost of sales   | 528,880            | 601,959         | -12.1%            | 74.5%            | 74.5%    |
| Gross profit  | 180,950            | 206,578         | -12.4%            | 25.5%            | 25.5%    |
| Selling, general and administrative                             | 192,606            | 194,570         | -1.0%             | 27.1%            | 24.1%    |
| Write-down of intangibles                                       | 5,809              | —               | N/M               | 0.8%             | —        |
| Restructuring   | 1,569              | 2,265           | -30.7%            | 0.2%             | 0.3%     |
| Operating income (loss)   | (19,034)           | 9,743           | -295.4%           | -2.7%            | 1.2%     |
| Interest expense  | 4,217              | 5,140           | -18.0%            | 0.6%             | 0.6%     |
| Other income, net   | 2,822              | 1,618           | 74.4%             | 0.4%             | 0.2%     |
| Income (loss) from continuing operations before income taxes    | (20,429)           | 6,221           | -428.4%           | -2.9%            | 0.8%     |
| Income tax expense (benefit)                                    | (8,235)            | 1,833           | -549.3%           | 40.3%*           | 29.5%*   |
| Income (loss) from continuing operations                        | (12,194)           | 4,388           | -377.9%           | -1.7%            | 0.5%     |
| Loss from discontinued operations (net of tax)                  | (6,434)            | (139)           | N/M%              | -0.9%            | —        |
| Net income (loss)   | <u>\$ (18,628)</u> | <u>\$ 4,249</u> | -538.4%           | -2.6%            | 0.5%     |
| Basic average shares  | 51,395             | 51,580          |                   |                  |          |
| Basic income (loss) from continuing operations per share        | \$ (0.24)          | \$ 0.08         |                   |                  |          |
| Discontinued operations per share (net of tax)                  | \$ (0.12)          | —               |                   |                  |          |
| Basic net income (loss) per share                               | <u>\$ (0.36)</u>   | <u>\$ 0.08</u>  |                   |                  |          |
| Diluted average shares  | 51,395             | 51,806          |                   |                  |          |
| Diluted income (loss) from continuing operations per share      | \$ (0.24)          | \$ 0.08         |                   |                  |          |
| Discontinued operations per share (net of tax)                  | \$ (0.12)          | —               |                   |                  |          |
| Diluted net income (loss) per share                             | <u>\$ (0.36)</u>   | <u>\$ 0.08</u>  |                   |                  |          |
| Dividends paid per share  | \$ 0.24            | \$ 0.24         |                   |                  |          |

\* As a percent of pretax income, not sales.

N/M = not meaningful

**LA-Z-BOY INCORPORATED**  
**CONSOLIDATED BALANCE SHEET**

| <i>(Unaudited, amounts in thousands)</i>       | 10/27/07         | 10/28/06         | Increase/(Decrease) |         | 4/28/07          |
|--|------------------|------------------|---------------------|---------|------------------|
|  |                  |                  | Dollars             | Percent |                  |
| <b>Current assets</b>                          |                  |                  |                     |         |                  |
| Cash and equivalents                           | \$ 32,692        | \$ 20,529        | \$ 12,163           | 59.2%   | \$ 51,721        |
| Receivables, net                               | 215,275          | 253,519          | (38,244)            | -15.1%  | 230,399          |
| Inventories, net                               | 190,985          | 237,885          | (46,900)            | -19.7%  | 197,790          |
| Deferred income taxes—current                  | 14,337           | 16,043           | (1,706)             | -10.6%  | 17,283           |
| Assets of discontinued operations              | 3,634            | —                | 3,634               | N/M     | 24,278           |
| Other current assets                           | 27,073           | 29,076           | (2,003)             | -6.9%   | 19,327           |
| Total current assets                           | <u>483,996</u>   | <u>557,052</u>   | <u>(73,056)</u>     | -13.1%  | 540,798          |
| Property, plant and equipment, net             | 180,912          | 204,904          | (23,992)            | -11.7%  | 183,218          |
| Deferred income taxes—long term                | 25,608           | 3,451            | 22,157              | N/M     | 15,380           |
| Goodwill                                       | 49,850           | 62,736           | (12,886)            | -20.5%  | 55,659           |
| Trade names                                    | 9,006            | 18,794           | (9,788)             | -52.1%  | 9,472            |
| Other long-term assets                         | 76,545           | 80,166           | (3,621)             | -4.5%   | 74,164           |
| Total assets                                   | <u>\$825,917</u> | <u>\$927,103</u> | <u>\$(101,186)</u>  | -10.9%  | <u>\$878,691</u> |
| <b>Current liabilities</b>                     |                  |                  |                     |         |                  |
| Short-term borrowings                          | \$ —             | \$ 35,000        | \$ (35,000)         | -100.0% | \$ —             |
| Current portion of long-term debt              | 38,353           | 3,295            | 35,058              | N/M     | 37,688           |
| Accounts payable                               | 54,194           | 72,308           | (18,114)            | -25.1%  | 68,089           |
| Liabilities of discontinued operations         | 1,664            | —                | 1,664               | N/M     | 3,843            |
| Accrued expenses and other current liabilities | 103,130          | 114,762          | (11,632)            | -10.1%  | 118,590          |
| Total current liabilities                      | <u>197,341</u>   | <u>225,365</u>   | <u>(28,024)</u>     | -12.4%  | 228,210          |
| Long-term debt                                 | 110,774          | 147,799          | (37,025)            | -25.1%  | 111,714          |
| Income taxes payable — long term               | 7,084            | —                | 7,084               | N/M     | —                |
| Other long-term liabilities                    | 56,474           | 54,920           | 1,554               | 2.8%    | 53,419           |
| Contingencies and commitments                  | —                | —                | —                   | —       | —                |
| <b>Shareholders' equity</b>                    |                  |                  |                     |         |                  |
| Common shares, \$1 par value                   | 51,416           | 51,364           | 52                  | 0.1%    | 51,377           |
| Capital in excess of par value                 | 206,636          | 206,145          | 491                 | 0.2%    | 208,283          |
| Retained earnings                              | 193,681          | 236,635          | (42,954)            | -18.2%  | 223,896          |
| Accumulated other comprehensive income         | 2,511            | 4,875            | (2,364)             | -48.5%  | 1,792            |
| Total shareholders' equity                     | <u>454,244</u>   | <u>499,019</u>   | <u>(44,775)</u>     | -9.0%   | 485,348          |
| Total liabilities and shareholders' equity     | <u>\$825,917</u> | <u>\$927,103</u> | <u>\$(101,186)</u>  | -10.9%  | <u>\$878,691</u> |

**LA-Z-BOY INCORPORATED**  
**CONSOLIDATED STATEMENT OF CASH FLOWS**

| <i>(Unaudited, amounts in thousands)</i>   | Second Quarter Ended |           | Six Months Ended |           |
|--|----------------------|-----------|------------------|-----------|
|  | 10/27/07             | 10/28/06  | 10/27/07         | 10/28/06  |
| <b>Cash flows from operating activities</b>                                      |                      |           |                  |           |
| Net income (loss)  | \$ (9,934)           | \$ 1,954  | \$ (18,628)      | \$ 4,249  |
| Adjustments to reconcile net income (loss) to cash used for operating activities |                      |           |                  |           |
| Loss (gain) on sale of discontinued operations (net of tax)                      | 3,990                | —         | 3,990            | (1,280)   |
| Write-down of businesses held for sale (net of tax)                              | 2,159                | —         | 2,159            | —         |
| Write-down of intangibles (net of tax)   | 3,689                | —         | 3,689            | —         |
| Restructuring  | 967                  | 1,865     | 4,648            | 1,865     |
| Provision for doubtful accounts  | 1,505                | 1,643     | 3,619            | 2,807     |
| Depreciation and amortization  | 6,093                | 6,809     | 12,313           | 13,889    |
| Stock-based compensation expense   | 1,001                | 1,861     | 1,862            | 2,732     |
| Change in receivables  | (13,409)             | (24,228)  | 9,188            | (2,945)   |
| Change in inventories  | 15,323               | 873       | 9,252            | (17,117)  |
| Change in payables   | 1,000                | (2,060)   | (14,414)         | (9,379)   |
| Change in other assets and liabilities   | 6,568                | (8,623)   | (16,678)         | (15,570)  |
| Change in deferred taxes   | (4,671)              | (3,110)   | (6,146)          | (6,766)   |
| Total adjustments  | 24,215               | (24,970)  | 13,482           | (31,764)  |
| Net cash provided by (used for) operating activities                             | 14,281               | (23,016)  | (5,146)          | (27,515)  |
| <b>Cash flows from investing activities</b>                                      |                      |           |                  |           |
| Proceeds from disposals of assets  | 867                  | 3,633     | 7,282            | 24,962    |
| Proceeds from sale of discontinued operations                                    | 4,019                | 3,184     | 4,019            | 33,166    |
| Capital expenditures   | (5,970)              | (5,767)   | (15,599)         | (15,010)  |
| Purchases of investments   | (6,648)              | (2,760)   | (13,270)         | (8,392)   |
| Proceeds from sales of investments   | 7,801                | 2,320     | 14,593           | 8,017     |
| Change in other long-term assets   | 365                  | (701)     | 385              | (196)     |
| Net cash provided by (used for) investing activities                             | 434                  | (91)      | (2,590)          | 42,547    |
| <b>Cash flows from financing activities</b>                                      |                      |           |                  |           |
| Proceeds from debt   | 171                  | 56,276    | 817              | 78,675    |
| Payments on debt   | (192)                | (31,266)  | (1,092)          | (78,680)  |
| Stock issued for stock and employee benefit plans                                | (94)                 | (342)     | (116)            | 766       |
| Repurchases of common stock  | —                    | (3,261)   | —                | (6,947)   |
| Dividends paid   | (6,232)              | (6,213)   | (12,441)         | (12,462)  |
| Net cash provided by (used for) financing activities                             | (6,347)              | 15,194    | (12,832)         | (18,648)  |
| Effect of exchange rate changes on cash and equivalents                          | 538                  | 49        | 1,539            | 56        |
| Change in cash and equivalents   | 8,906                | (7,864)   | (19,029)         | (3,560)   |
| Cash and equivalents at beginning of period                                      | 23,786               | 28,393    | 51,721           | 24,089    |
| Cash and equivalents at end of period  | \$ 32,692            | \$ 20,529 | \$ 32,692        | \$ 20,529 |
| Cash paid (net of refunds) during period — income taxes                          | \$ 758               | \$ 16,889 | \$ 3,893         | \$ 17,097 |
| Cash paid during period — interest   | \$ 1,495             | \$ 1,748  | \$ 3,405         | \$ 4,660  |



**LA-Z-BOY INCORPORATED**  
**SEGMENT INFORMATION**

| <i>(Amounts in thousands)</i>  | Second Quarter Ended   |                        | Six Months Ended       |                        |
|--------------------------------|------------------------|------------------------|------------------------|------------------------|
|                                | 10/27/07<br>(13 weeks) | 10/28/06<br>(13 weeks) | 10/27/07<br>(26 weeks) | 10/28/06<br>(26 weeks) |
| <b>Sales</b>                   |                        |                        |                        |                        |
| Upholstery Group               | \$ 269,749             | \$ 304,598             | \$ 524,506             | \$ 599,995             |
| Casegoods Group                | 58,892                 | 74,164                 | 112,466                | 135,190                |
| Retail Group                   | 46,163                 | 52,485                 | 91,394                 | 104,689                |
| VIEs/Eliminations              | (9,370)                | (16,633)               | (18,536)               | (31,337)               |
| Consolidated                   | \$ 365,434             | \$ 414,614             | \$ 709,830             | \$ 808,537             |
| <b>Operating income (loss)</b> |                        |                        |                        |                        |
| Upholstery Group               | \$ 19,036              | \$ 20,162              | \$ 27,903              | \$ 37,787              |
| Casegoods Group                | 3,577                  | 6,200                  | 6,177                  | 9,442                  |
| Retail Group                   | (9,119)                | (8,769)                | (19,193)               | (16,484)               |
| Corporate and Other*           | (12,816)               | (9,217)                | (23,464)               | (19,137)               |
| Intangible write-down          | (5,809)                | —                      | (5,809)                | —                      |
| Restructuring                  | (967)                  | (1,865)                | (4,648)                | (1,865)                |
|                                | \$ (6,098)             | \$ 6,511               | \$ (19,034)            | \$ 9,743               |

\* Variable Interest Entities ("VIEs") are included in corporate and other.