

CROWN CRAFTS INC
Form 10-Q
August 09, 2018

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended July 1, 2018

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

For the transition period from _____ to _____

Commission File No. 1-7604

Crown Crafts, Inc.

(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of incorporation)

58-0678148
(IRS Employer Identification No.)

916 South Burnside Avenue, Gonzales, LA
(Address of principal executive offices)

70737
(Zip Code)

Registrant's telephone number, including area code: **(225) 647-9100**

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

Indicate by check mark whether the Registrant has submitted electronically and posted on its corporate Website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the Registrant was required to submit and post such files). Yes No

Indicate by check mark whether the Registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company" and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer		Accelerated filer
Non-Accelerated filer	(Do not check if a smaller reporting company)	Smaller Reporting Company
Emerging Growth Company		

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

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

The number of shares of common stock, \$0.01 par value, of the registrant outstanding as of August 7, 2018 was 10,069,558.

PART I – FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

CROWN CRAFTS,
INC. AND
SUBSIDIARIES
CONDENSED
CONSOLIDATED
BALANCE
SHEETS
JULY 1, 2018
AND APRIL 1,
2018
(amounts in
thousands, except
share and per share
amounts)

	July 1, 2018 (Unaudited)	April 1, 2018
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 199	\$215
Accounts receivable (net of allowances of \$543 at July 1, 2018 and \$565 at April 1, 2018):		
Due from factor	10,772	15,447
Other	3,789	3,051
Inventories	20,759	19,788
Prepaid expenses	1,264	1,253
Total current assets	36,783	39,754
Property, plant and equipment - at cost:		
Vehicles	257	268
Leasehold improvements	273	272
Machinery and equipment	4,065	4,010
Furniture and fixtures	799	799
Property, plant and equipment - gross	5,394	5,349
Less accumulated depreciation	3,652	3,571
Property, plant and equipment - net	1,742	1,778

Finite-lived intangible assets - at cost:		
Tradename and trademarks	3,667	3,667
Customer relationships	7,374	7,374
Other finite-lived intangible assets	3,159	3,159
Finite-lived intangible assets - gross	14,200	14,200
Less accumulated amortization	7,128	6,928
Finite-lived intangible assets - net	7,072	7,272
Goodwill	7,125	7,125
Deferred income taxes	512	532
Other	120	120
Total Assets	\$ 53,354	\$56,581
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	\$ 7,067	\$3,766
Accrued wages and benefits	1,052	842
Accrued royalties	156	793
Dividends payable	806	807
Income taxes payable	81	40
Other accrued liabilities	516	540
Total current liabilities	9,678	6,788
Non-current liabilities:		
Long-term debt	3,840	9,458
Reserve for unrecognized tax liabilities	1,045	1,017
Total non-current liabilities	4,885	10,475
Shareholders' equity:		
Common stock - \$0.01 par value per share; Authorized 40,000,000 shares at July 1, 2018 and April 1, 2018; Issued 12,493,789 shares at July 1, 2018 and April 1, 2018	125	125
Additional paid-in capital	52,984	52,874
Treasury stock - at cost - 2,424,231 shares at July 1, 2018 and 2,408,025 shares at April 1, 2018	(12,326)	(12,231)
Accumulated Deficit	(1,992)	(1,450)
Total shareholders' equity	38,791	39,318
Total Liabilities and Shareholders' Equity	\$ 53,354	\$56,581

*See notes to
unaudited
condensed
consolidated
financial
statements.*

CROWN CRAFTS,
 INC. AND
 SUBSIDIARIES
 UNAUDITED
 CONDENSED
 CONSOLIDATED
 STATEMENTS OF
 INCOME
 THREE-MONTH
 PERIODS ENDED
 JULY 1, 2018
 AND JULY 2,
 2017
 (amounts in
 thousands, except
 per share amounts)

	Three-Month Periods Ended	
	July 1, 2018	July 2, 2017
Net sales	\$15,460	\$13,647
Cost of products sold	11,332	10,045
Gross profit	4,128	3,602
Marketing and administrative expenses	3,685	2,901
Income from operations	443	701
Other income (expense):		
Interest expense	(99)	(20)
Interest income	-	41
Foreign exchange loss	-	(2)
Other - net	-	1
Income before income tax expense	344	721
Income tax expense	80	203
Net income	\$264	\$518
Weighted average shares outstanding:		
Basic	10,070	10,044
Effect of dilutive securities	2	11
Diluted	10,072	10,055
Earnings per share:		
Basic	\$0.03	\$0.05
Diluted	\$0.03	\$0.05

Cash dividends declared per share	\$0.08	\$0.08
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*See notes to
unaudited
condensed
consolidated
financial
statements.*

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CROWN CRAFTS,
 INC. AND
 SUBSIDIARIES
 UNAUDITED
 CONDENSED
 CONSOLIDATED
 STATEMENTS OF
 CASH FLOWS
 THREE-MONTH
 PERIODS ENDED
 JULY 1, 2018
 AND JULY 2,
 2017
 (amounts in
 thousands)

	Three-Month Periods Ended	
	July 1, 2018	July 2, 2017
Operating activities:		
Net income	\$264	\$518
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation of property, plant and equipment	138	36
Amortization of intangibles	200	189
Deferred income taxes	20	40
Reserve for unrecognized tax benefits	28	30
Stock-based compensation	110	142
Changes in assets and liabilities:		
Accounts receivable	3,937	2,528
Inventories	(971)	263
Prepaid expenses	(11)	(19)
Other assets	-	(1)
Accounts payable	3,301	266
Accrued liabilities	(410)	934
Net cash provided by operating activities	6,606	4,926
Investing activities:		
Capital expenditures for property, plant and equipment	(102)	(56)
Net cash used in investing activities	(102)	(56)
Financing activities:		
Repayments under revolving line of credit	(16,778)	-
Borrowings under revolving line of credit	11,160	-
Purchase of treasury stock	(95)	(56)
Dividends paid	(807)	(803)

Net cash used in financing activities	(6,520)	(859)
Net (decrease) increase in cash and cash equivalents	(16)	4,011
Cash and cash equivalents at beginning of period	215	7,892
Cash and cash equivalents at end of period	\$ 199	\$ 11,903

Supplemental cash flow information:

Income taxes paid	\$3	\$3
Interest paid	75	-

Noncash financing activities:

Dividends declared but unpaid	(806)	(805)
Compensation paid as common stock	-	116

*See notes to
unaudited
condensed
consolidated
financial
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CROWN CRAFTS, INC. AND SUBSIDIARIES

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

FOR THE THREE-MONTH PERIODS ENDED JULY 1, 2018 AND JULY 2, 2017

Note 1 – Summary of Significant Accounting Policies

Basis of Presentation: The accompanying unaudited consolidated financial statements include the accounts of Crown Crafts, Inc. (the “Company”) and its subsidiaries and have been prepared in accordance with accounting principles generally accepted in the United States (“GAAP”) applicable to interim financial information as promulgated by the Financial Accounting Standards Board (“FASB”). Accordingly, they do not include all of the information and disclosures required by GAAP for complete financial statements. References herein to GAAP are to topics within the FASB Accounting Standards Codification (the “FASB ASC”), which has been established by the FASB as the authoritative source for GAAP to be applied by nongovernmental entities.

In the opinion of management, the interim unaudited consolidated financial statements contained herein include all adjustments necessary to present fairly the financial position of the Company as of July 1, 2018 and the results of its operations and cash flows for the period presented. Such adjustments include normal, recurring accruals, as well as the elimination of all significant intercompany balances and transactions. Operating results for the three-month period ended July 1, 2018 are not necessarily indicative of the results that may be expected by the Company for its fiscal year ending March 31, 2019. For further information, refer to the Company’s consolidated financial statements and notes thereto included in the Company’s annual report on Form 10-K for the fiscal year ended April 1, 2018.

Fiscal Year: The Company’s fiscal year ends on the Sunday that is nearest to or on March 31. References herein to “fiscal year 2019” or “2019” represent the 52-week period ending March 31, 2019 and references herein to “fiscal year 2018” or “2018” represent the 52-week period ended April 1, 2018.

Use of Estimates: The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities as of the date of the accompanying condensed consolidated balance sheets and the reported amounts of revenues and expenses during the periods presented on the accompanying unaudited consolidated statements of income and cash flows. Significant estimates are made with respect to the allowances related to accounts receivable for customer deductions for returns, allowances and disputes. The Company also has a certain amount of discontinued finished products which necessitates the establishment of inventory reserves and allocates indirect costs

to inventory based on an estimated percentage of the supplier purchase price, each of which is highly subjective. The Company has also established estimated reserves in connection with the uncertainty concerning the amount of income tax recognized. Actual results could differ from those estimates.

Cash and Cash Equivalents: The Company considers highly-liquid investments, if any, purchased with original maturities of three months or less to be cash equivalents.

The Company's credit facility consists of a revolving line of credit under a certain Financing Agreement between the Company, its wholly-owned subsidiaries (together with the Company, the "Borrowers") and The CIT Group/Commercial Services, Inc. ("CIT"), a subsidiary of CIT Group, Inc. (as amended from time to time, the "CIT Financing Agreement"). The Company classifies a negative balance outstanding under the revolving line of credit as cash, as these amounts are legally owed to the Company and are immediately available to be drawn upon by the Company. There are no compensating balance requirements or other restrictions on the transfer of amounts associated with the Company's depository accounts.

Financial Instruments: For short-term instruments such as cash and cash equivalents, accounts receivable and accounts payable, the Company uses carrying value as a reasonable estimate of the fair value.

Advertising Costs: The Company's advertising costs are primarily associated with cooperative advertising arrangements with certain of the Company's customers and are recognized using the straight-line method based upon aggregate annual estimated amounts for those customers, with periodic adjustments to the actual amounts of authorized agreements. Costs associated with advertising on websites such as Facebook and Google and which are related to the Company's online business are recorded as incurred. Advertising expense is included in marketing and administrative expenses in the accompanying unaudited condensed consolidated statements of income and amounted to \$325,000 and \$219,000 for the three-month periods ended July 1, 2018 and July 2, 2017, respectively.

Revenue Recognition: Revenue is recognized upon the satisfaction of all contractual performance obligations and the transfer of control of the products sold to the customer. The majority of the Company's sales consists of single performance obligation arrangements for which the transaction price for a given product sold is equivalent to the price quoted for the product, net of any stated discounts applicable at a point in time. Each sales transaction results in an implicit contract with the customer to deliver a product as directed by the customer. Shipping and handling costs that are charged to customers are included in net sales, and the Company's costs associated with shipping and handling activities are included in cost of products sold.

A provision for anticipated returns, which are based upon historical returns and claims, is provided through a reduction of net sales and cost of products sold in the reporting period within which the related sales are recorded. Actual returns and claims experienced in a future period may differ from historical experience, and thus, the Company's provision for anticipated returns at any given point in time may be over-funded or under-funded.

The Company recognizes revenue associated with unredeemed store credits and gift certificates at the earlier of their redemption by customers, their expiration or when their likelihood of redemption becomes remote, which is generally two years from the date of issuance.

Revenue from sales made directly to consumers is recorded when the shipped products have been received by customers, and excludes sales taxes collected on behalf of governmental entities. Revenue from sales made to retailers is recorded when legal title has been passed to the customer based upon the terms of the customer's purchase order, the Company's sales invoice, or other associated relevant documents. Such terms usually stipulate that legal title will pass when the shipped products are no longer under the control of the Company, such as when the products are picked up at the Company's facility by the customer or by a common carrier. A disaggregation of the Company's revenue is set forth below under the heading "*Segment and Related Information*" in this Note 1 disclosure.

Allowances Against Accounts Receivable: Revenue from sales made to retailers is reported net of allowances for anticipated returns and other allowances, including cooperative advertising allowances, warehouse allowances, placement fees, volume rebates, coupons and discounts. Such allowances are recorded commensurate with sales activity or using the straight-line method, as appropriate, and the cost of such allowances is netted against sales in reporting the results of operations. The provision for the majority of the Company's allowances occurs on a per-invoice basis. When a customer requests to have an agreed-upon deduction applied against the customer's outstanding balance due to the Company, the allowances are correspondingly reduced to reflect such payments or credits issued against the customer's account balance. The Company analyzes the components of the allowances for customer deductions monthly and adjusts the allowances to the appropriate levels. The timing of funding requests for advertising support can cause the net balance in the allowance account to fluctuate from period to period. The timing of such funding requests should have no impact on the consolidated statements of income since such costs are accrued commensurate with sales activity or using the straight-line method, as appropriate.

Uncollectible Accounts: To reduce the exposure to credit losses and to enhance the predictability of its cash flows, the Company assigns the majority of its trade accounts receivable under factoring agreements with CIT. In the event a factored receivable becomes uncollectible due to creditworthiness, CIT bears the risk of loss. For reporting periods beginning on or after April 2, 2018, the Company recognizes revenue net of the amount of its non-factored accounts receivable that is expected to be uncollectible, which is estimated by specifically analyzing accounts receivable, historical trends of uncollected accounts, customer concentrations, customer creditworthiness, current economic trends and changes in its customers' payment terms. For reporting periods that ended prior to April 2, 2018, the Company instead recorded a provision for its expected uncollectible accounts in the form of a bad debt expense, which was included in marketing and administrative expenses in the unaudited condensed consolidated statements of income. However, the Company did not record such a charge for bad debt expense during the three-month period ended July 2, 2017.

Credit Concentration: The Company's accounts receivable as of July 1, 2018 was \$14.5 million, net of allowances of \$543,000. Of this amount, \$10.7 million was due from CIT under the factoring agreements, which represents the maximum loss that the Company could incur if CIT failed completely to perform its obligations thereunder.

Other Accrued Liabilities: An amount of \$516,000 was recorded as other accrued liabilities as of July 1, 2018. Of this amount, \$293,000 reflected unearned revenue recorded for payments from customers that were received before products were shipped. Other accrued liabilities as of July 1, 2018 also includes a reserve for anticipated returns of \$9,000 and unredeemed store credits and gift certificates totaling \$19,000.

Segment and Related Information: The Company operates primarily in one principal segment, infant, toddler and juvenile products. These products consist of infant and toddler bedding, bibs, soft bath products, disposable products and accessories. Net sales of bedding, blankets and accessories and net sales of bibs, bath, developmental toy, feeding, baby care and disposable products for the three-month periods ended July 1, 2018 and July 2, 2017 are as follows (in thousands):

	Three-Month Periods Ended	
	July 1, 2018	July 2, 2017
Bedding, blankets and accessories	\$8,521	\$8,424
Bibs, bath, developmental toy, feeding, baby care and disposable products	6,939	5,223
Total net sales	\$15,460	\$13,647

Inventory Valuation: The preparation of the Company's financial statements requires careful determination of the appropriate value of the Company's inventory balances. Such amounts are presented as a current asset in the accompanying condensed consolidated balance sheets and are a direct determinant of cost of products sold in the accompanying unaudited consolidated statements of income and, therefore, have a significant impact on the amount of net income in the accounting periods reported. The basis of accounting for inventories is cost, which includes the direct supplier acquisition cost, duties, taxes and freight, and the indirect costs incurred to design, develop, source and store the products until they are sold. Once cost has been determined, the Company's inventory is then stated at the lower of cost or net realizable value, with cost determined using the first-in, first-out ("FIFO") method, which assumes that inventory quantities are sold in the order in which they are acquired, and the average cost method for a portion of the Company's inventory.

The indirect charges and their allocation to the Company's finished goods inventory are determined as a percentage of projected annual supplier purchases and can impact the Company's results of operations as purchase volumes fluctuate from quarter to quarter and year to year. The difference between indirect costs incurred and the indirect costs allocated to inventory creates a burden variance, which is generally favorable when actual inventory purchases exceed planned inventory purchases, and is generally unfavorable when actual inventory purchases are lower than planned inventory purchases.

On a periodic basis, management reviews the Company's inventory quantities on hand for obsolescence, physical deterioration, changes in price levels and the existence of quantities on hand which may not reasonably be expected to be sold within the normal operating cycle of the Company's operations. To the extent that any of these conditions is believed to exist or the market value of the inventory expected to be realized in the ordinary course of business is otherwise no longer as great as its carrying value, an allowance against the inventory value is established. To the extent that this allowance is established or increased during an accounting period, an expense is recorded in cost of products sold in the Company's consolidated statements of income. Only when inventory for which an allowance has

been established is later sold or is otherwise disposed of is the allowance reduced accordingly. Significant management judgment is required in determining the amount and adequacy of this allowance. In the event that actual results differ from management's estimates or these estimates and judgments are revised in future periods, the Company may not fully realize the carrying value of its inventory or may need to establish additional allowances, either of which could materially impact the Company's financial position and results of operations.

Royalty Payments: The Company has entered into agreements that provide for royalty payments based on a percentage of sales with certain minimum guaranteed amounts. These royalties are accrued based upon historical sales rates adjusted for current sales trends by customers. Royalty expense is included in cost of products sold in the accompanying unaudited condensed consolidated statements of income and amounted to \$974,000 and \$1.3 million for the three-month periods ended July 1, 2018 and July 2, 2017, respectively.

Depreciation and Amortization: The accompanying condensed consolidated balance sheets reflect property, plant and equipment, and certain intangible assets at cost less accumulated depreciation or amortization. The Company capitalizes additions and improvements and expenses maintenance and repairs as incurred. Depreciation and amortization are computed using the straight-line method over the estimated useful lives of the assets, which are three to eight years for property, plant and equipment, and five to twenty years for amortizable intangible assets. The Company amortizes improvements to its leased facilities over the term of the lease or the estimated useful life of the asset, whichever is shorter.

Valuation of Long-Lived Assets and Identifiable Intangible Assets: In addition to the depreciation and amortization procedures set forth above, the Company reviews for impairment long-lived assets and certain identifiable intangible assets whenever events or changes in circumstances indicate that the carrying amount of any asset may not be recoverable. In the event of impairment, the asset is written down to its fair market value.

Patent Costs: The Company incurs certain legal and associated costs in connection with applications for patents, which are classified within other finite-lived intangible assets in the accompanying condensed consolidated balance sheets. The Company capitalizes such costs to be amortized over the expected life of the patent to the extent that an economic benefit is anticipated from the resulting patent or an alternative future use for the underlying product is available to the Company. The Company also capitalizes legal and other costs incurred in the protection or defense of the Company's patents to the extent that it is believed that the future economic benefit of the patent will be maintained or increased and a successful outcome of the litigation is probable. Capitalized patent protection or defense costs are amortized over the remaining expected life of the related patent. The Company's assessment of the future economic benefit of its patents involves considerable management judgment, and a different conclusion could result in a material impairment charge up to the carrying value of these assets.

Purchase Price Allocations and the Resulting Goodwill: The Company's strategy includes, when appropriate, entering into transactions accounted for as business combinations. In connection with a business combination, the Company prepares an allocation of the cost of the acquisition to the identifiable assets acquired and liabilities assumed, based on estimated fair values as of the acquisition date. The excess of the purchase price over the estimated fair value of the identifiable net assets acquired is recorded as goodwill.

The amount of goodwill recorded in a business combination can vary significantly depending upon the values attributed to the assets acquired and liabilities assumed. Although goodwill has no useful life and is not subject to a systematic annual amortization against earnings, the Company performs a measurement for impairment of the carrying value of its goodwill annually on the first day of the Company's fiscal year. An additional impairment test is performed during the year whenever an event or change in circumstances suggest that the fair value of the goodwill of either of the reporting units of the Company has more likely than not fallen below its carrying value. The annual or interim measurement for impairment of goodwill is performed at the reporting unit level. A reporting unit is either an operating segment or one level below an operating segment. In its annual or interim measurement for impairment of goodwill, the Company conducts a qualitative assessment by examining relevant events and circumstances which could have a negative impact on the Company's goodwill, which includes macroeconomic conditions, industry and market conditions, commodity prices, cost factors, overall financial performance, reporting unit dispositions and acquisitions, the market capitalization of the Company and other relevant events specific to the Company.

If, after assessing the totality of events or circumstances described above, the Company determines that it is more likely than not that the fair value of either of the Company's reporting units is less than its carrying amount, the two-step goodwill test is performed. The two-step goodwill impairment test is also performed whenever events or changes in circumstances indicate that the carrying value may not be recoverable. If, after performing the two-step goodwill test, it is determined that the carrying value of goodwill is impaired, the amount of goodwill is reduced and a corresponding charge is made to earnings in the period in which the goodwill is determined to be impaired.

Provision for Income Taxes: The Company's provision for income taxes includes all currently payable federal, state, local and foreign taxes and is based upon the Company's estimated annual effective tax rate ("ETR"), which is based on the Company's forecasted annual pre-tax income, as adjusted for certain expenses within the consolidated statements

of income that will never be deductible on the Company's tax returns and certain charges expected to be deducted on the Company's tax returns that will never be deducted on the consolidated statements of income, multiplied by the statutory tax rates for the various jurisdictions in which the Company operates. The Company's provisions for income taxes for the three-month periods ended July 1, 2018 and July 2, 2017 are based upon an estimated annual ETR from continuing operations of 24.0% and 35.0%, respectively. The Company provides for deferred income taxes based on the difference between the financial statement and tax bases of assets and liabilities using enacted tax rates that will be in effect when the differences are expected to reverse. The Company's policy is to recognize the effect that a change in enacted tax rates would have on net deferred income tax assets and liabilities in the period in which the tax rates are changed.

The Company files income tax returns in the many jurisdictions within which it operates, including the U.S., several U.S. states and the People's Republic of China. The statute of limitations for the Company's filed income tax returns varies by jurisdiction; tax years open to federal or state examination or other adjustment as of July 1, 2018 were the fiscal years ended April 1, 2018, April 2, 2017, April 3, 2016, March 29, 2015, March 30, 2014, March 31, 2013, April 1, 2012 and April 3, 2011.

Management evaluates items of income, deductions and credits reported on the Company's various federal and state income tax returns filed and recognizes the effect of positions taken on those income tax returns only if those positions are more likely than not to be sustained. The Company applies the provisions of FASB ASC Sub-topic 740-10-25, which requires a minimum recognition threshold that a tax benefit must meet before being recognized in the financial statements. Recognized income tax positions are measured at the largest amount that has a greater than 50% likelihood of being realized. Changes in recognition or measurement are reflected in the period in which the change in judgment occurs.

During fiscal year 2016, an evaluation was made of the Company's process regarding the calculation of the state portion of its income tax provision. This evaluation resulted in the Company taking a tax position that reflected opportunities for the application of more favorable state apportionment percentages for several prior fiscal years. After considering all relevant information, the Company believes that the technical merits of this tax position would more likely than not be sustained. However, the Company also believes that the ultimate resolution of the tax position will result in a tax benefit that is less than the full amount being sought. Therefore, the Company's measurement regarding the tax impact of the revised state apportionment percentages resulted in the Company recording a reserve for unrecognized tax benefits during the three-month periods ended July 1, 2018 and July 2, 2017 of \$3,000 and \$11,000, respectively, in the accompanying unaudited condensed consolidated statements of income.

The Company's policy is to accrue interest expense and penalties as appropriate on estimated unrecognized tax benefits as a charge to interest expense in the Company's consolidated statements of income. Interest expense and penalties are not accrued with respect to estimated unrecognized tax benefits that are associated with claims for income tax refunds as long as the overpayments are receivable. The Company accrued interest and penalties associated with its reserve for unrecognized tax benefits during the three-month periods ended July 1, 2018 and July 2, 2017 of \$25,000 and \$20,000, respectively, in the accompanying unaudited condensed consolidated statements of income.

During the three-month periods ended July 1, 2018 and July 2, 2017, the Company recorded discrete income tax benefits of \$5,000 and \$60,000, respectively, to reflect the effect of excess tax benefits arising from the vesting of non-vested stock during the periods.

The ETR on continuing operations and the discrete income tax charges and benefits set forth above resulted in an overall provision for income taxes of 23.3% and 28.2% for the three-month periods ended July 1, 2018 and July 2, 2017, respectively.

Earnings Per Share: The Company calculates basic earnings per share by using a weighted average of the number of shares outstanding during the reporting periods. Diluted shares outstanding are calculated in accordance with the treasury stock method, which assumes that the proceeds from the exercise of all exercisable options would be used to repurchase shares at market value. The net number of shares issued after the exercise proceeds are exhausted represents the potentially dilutive effect of the options, which are added to basic shares to arrive at diluted shares.

Recently-Issued Accounting Standards: In 2014, the FASB issued Accounting Standards Update ("ASU") No. 2014-09, *Revenue from Contracts with Customers (Topic 606)*, which has replaced most previous GAAP guidance on revenue recognition, and which now requires the use of more estimates and judgments. When issued, ASU No. 2014-09 was to become effective in the fiscal year beginning after December 15, 2016, but on August 12, 2015 the FASB issued ASU No. 2015-14, *Revenue from Contracts with Customers (Topic 606): Deferral of the Effective Date*, which provided for a one-year deferral of the effective date to apply the guidance of ASU No. 2014-09. Thus, the Company adopted ASU

No. 2014-09 effective as of April 2, 2018 on a modified retrospective basis.

ASU No. 2014-09 requires that revenue be recognized by an entity when a customer obtains control of promised products in an amount that reflects the consideration that the entity expects to receive in exchange for those products. A further description of the GAAP guidance in effect subsequent to the Company's adoption of ASU No. 2014-09 is set forth above under the headings "*Revenue Recognition*," "*Allowances Against Accounts Receivable*" and "*Uncollectible Accounts*" in this Note 1 disclosure. The Company performed an evaluation of its revenue contract arrangements and determined that, although the disclosures related to the Company's accounting policies and practices associated with the amount and timing of revenue recognition have been enhanced, the adoption of ASU No. 2014-09 did not have a material effect on the Company's financial position or results of operations.

On February 25, 2016, the FASB issued ASU No. 2016-02, *Leases (Topic 842)*, which will increase transparency and comparability by requiring an entity to recognize lease assets and lease liabilities on its balance sheet and by requiring the disclosure of key information about leasing arrangements. Under the provisions of ASU No. 2016-02, the Company will be required to capitalize most of its current operating lease obligations as right-of-use assets with corresponding liabilities based upon the present value of the future cash outflows associated with such operating lease obligations. ASU No. 2016-02 will become effective for the first interim period of the fiscal year beginning after December 15, 2018.

When issued, ASU No. 2016-02 was to have been applied using a modified retrospective approach, but on July 30, 2018 the FASB issued ASU No. 2018-11, *Leases (Topic 842): Targeted Improvements*, which will allow an alternative optional transition method with which to adopt ASU No. 2016-02. Upon adoption, in lieu of the modified retrospective approach, an entity will be allowed to recognize a cumulative-effect adjustment to the opening balance of retained earnings in the period of adoption.

Although early adoption of ASU No. 2016-02 (as modified by ASU No. 2018-11) is permitted, the Company intends to adopt ASU No. 2016-02 effective as of April 1, 2019. The Company has not yet decided whether it will use the modified retrospective approach or the cumulative-effect adjustment approach and is currently evaluating the effect that the adoption of ASU No. 2016-02 will have on its financial position, results of operations and related disclosures.

On June 16, 2016, the FASB issued ASU No. 2016-13, *Financial Instruments – Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments*, the objective of which is to provide financial statement users with more information about the expected credit losses on financial instruments and other commitments to extend credit held by an entity. Current GAAP requires an “incurred loss” methodology for recognizing credit losses that delays recognition until it is probable that a loss has been incurred. Because this methodology restricted the recognition of credit losses that are expected, but did not yet meet the “probable” threshold, ASU No. 2016-13 was issued to require the consideration of a broader range of reasonable and supportable information when determining estimates of credit losses. The ASU will become effective for the first interim period of the fiscal year beginning after December 15, 2019. The ASU is to be applied using a modified retrospective approach, and the ASU may be early-adopted as of the first interim period of the fiscal year beginning after December 15, 2018.

Although the Company has not yet decided whether to adopt ASU No. 2016-13 early or determined the full impact of the adoption of the ASU, because the Company assigns the majority of its trade accounts receivable under factoring agreements with CIT, the Company does not believe that its adoption of ASU No. 2016-13 will have a material impact on the Company’s financial position, results of operations and related disclosures.

On June 20, 2018, the FASB issued ASU No. 2018-07, *Compensation – Stock Compensation (Topic 718): Improvements to Nonemployee Share-Based Payment Accounting*, the objective of which is to expand the scope of Topic 718 to clarify the accounting treatment to be applied for share-based payments made to acquire goods and services from nonemployees. Under existing GAAP guidance, such nonemployee share-based payment awards are to be measured at the fair value of the goods or services provided by the nonemployee, or the fair value of the equity instruments issued, whichever can be more easily measured. ASU No. 2018-07 will simplify this accounting to require that nonemployee share-based payment awards are to be measured at the grant-date fair value of the equity instruments that an entity is obligated to issue when the good has been delivered or the service has been rendered. The Company routinely awards grants of non-vested stock to its nonemployee directors and measures such awards in a manner consistent with the provisions of ASU No. 2018-07.

ASU No. 2018-07 will become effective for the first interim period of the fiscal year beginning after December 15, 2018. Thus, the Company intends to adopt ASU No. 2018-07 effective as of April 1, 2019 and does not believe that its adoption of the ASU will have a material impact on the Company’s financial position, results of operations and related disclosures.

The Company has determined that all other ASUs which had become effective as of July 1, 2018, or which will become effective at some future date, are not expected to have a material impact on the Company's consolidated financial statements.

Note 2 – Acquisitions

Carousel: On August 4, 2017, Carousel Acquisition, LLC, a wholly-owned subsidiary of the Company, acquired substantially all of the assets and business, and assumed certain specified liabilities, of a privately held manufacturer and online retailer of premium infant and toddler bedding and nursery décor based in Douglasville, Georgia, which was at the time named Carousel Designs, LLC (the “Carousel Acquisition”). On August 11, 2017, the seller of such assets having relinquished its rights to its name under the terms of the acquisition, Carousel Acquisition, LLC changed its name to Carousel Designs, LLC (“Carousel”).

The Company anticipates that certain synergies, including administrative and capital efficiencies, may be achieved as a result of the Company's control of the combined assets and that the Company will benefit from the direct-to-consumer opportunities that will result from the Carousel Acquisition. Carousel paid an acquisition cost of \$8.7 million from cash on hand and assumed certain specified liabilities relating to the business. In connection with the Carousel Acquisition, Carousel paid off capital leases amounting to \$845,000 that were associated with certain fixed assets that were acquired.

The Carousel Acquisition has been accounted for as a business combination in accordance with FASB ASC Topic 805, *Business Combinations*. The Company has determined the preliminary allocation of the acquisition cost with the assistance of an independent third party. The identifiable assets acquired were recorded at their estimated fair value, which has been preliminarily determined based on available information and the use of multiple valuation approaches. The estimated useful lives of the identifiable intangible assets acquired was determined based upon the remaining time that these assets are expected to directly or indirectly contribute to the future cash flow of the Company.

The Company expects to complete the acquisition cost allocation during the 12-month period following the acquisition date, during which time the values of the assets acquired and liabilities assumed, including the goodwill, may need to be revised as appropriate. Based upon the preliminary allocation of the acquisition cost, the Company has recognized of \$5.7 million of goodwill, the entirety of which has been assigned to the reporting unit of the Company that produces and markets infant and toddler bedding, blankets and accessories, and the entirety of which is expected to be deductible for income tax purposes.

The following table represents the Company's preliminary allocation of the acquisition cost (in thousands) to the identifiable assets acquired and the liabilities assumed based on their respective estimated fair values as of the acquisition date. The excess of the acquisition cost over the estimated fair value of the identifiable net assets acquired is reflected as goodwill.

Tangible assets:	
Inventory	\$967
Prepaid expenses	5
Fixed assets	1,068
Total tangible assets	2,040
Amortizable intangible assets:	
Tradename	1,100
Developed technology	1,100
Non-compete covenants	360
Total amortizable intangible assets	2,560
Goodwill	5,679
Total acquired assets	10,279
Liabilities assumed:	
Accounts payable	319
Accrued wages and benefits	59
Unearned revenue	271
Other accrued liabilities	60
Capital leases	845
Total liabilities assumed	1,554
Net acquisition cost	\$8,725

The Carousel Acquisition resulted in net sales of \$1.8 million of infant and toddler bedding, blankets and accessories during the three-month period ended July 1, 2018. Carousel recorded amortization expense associated with the acquired amortizable intangible assets of \$50,000 during the three-month period ended July 1, 2018, which is included in marketing and administrative expenses in the accompanying unaudited condensed consolidated statements of income. Amortization is computed for the acquired amortizable intangible assets using the straight-line method over the estimated useful lives of the assets, which are 15 years for the tradename, 10 years for the developed technology, 5 years for the non-compete agreements and 11 years on a weighted-average basis for the grouping taken together.

Sassy: On December 15, 2017, Hamco, Inc. (“Hamco”), a wholly-owned subsidiary of the Company, acquired certain assets associated with the Sassy®-branded developmental toy, feeding and baby care product line from Sassy 14, LLC and assumed certain related liabilities (the “Sassy Acquisition”). Hamco paid an acquisition cost of \$6.5 million from a combination of cash on hand and the revolving line of credit. The Company has achieved certain administrative and capital efficiencies as a result of its acquisition of the Sassy product line. For example, synergies were attained in April 2018 when the Company transferred the remaining inventory acquired in the Sassy Acquisition from Grand Rapids, Michigan to the Company’s distribution facility in Compton, California. The Company anticipates that it will benefit from the diversity added to the Company’s portfolio of products and that the Sassy Acquisition will strengthen the Company’s overall position in the infant and juvenile products market.

The Sassy Acquisition has been accounted for as a business combination in accordance with FASB ASC Topic 805, *Business Combinations*. The Company is currently determining the allocation of the acquisition cost with the assistance of an independent third party. The identifiable assets acquired were recorded at their estimated fair value, which has been preliminarily determined based on available information and the use of multiple valuation approaches. The estimated useful lives of the identifiable intangible assets acquired was determined based upon the remaining time that these assets are expected to directly or indirectly contribute to the future cash flow of the Company. Certain data necessary to complete the acquisition cost allocation is not yet available, including the valuation of pre-acquisition contingencies and the final appraisals and valuations of assets acquired and liabilities assumed.

The following table represents the Company's preliminary allocation of the acquisition cost (in thousands) to the identifiable assets acquired and the liabilities assumed based on their respective estimated fair values as of the acquisition date. The excess of the acquisition cost over the estimated fair value of the identifiable net assets acquired is reflected as goodwill.

Tangible assets:	
Inventory	\$3,297
Prepaid expenses	120
Fixed assets	383
Total tangible assets	3,800
Amortizable intangible assets:	
Tradename	580
Customer relationships	1,840
Total amortizable intangible assets	2,420
Goodwill	320
Total acquired assets	6,540
Liabilities assumed:	
Accrued wages	20
Net acquisition cost	\$6,520

The Company expects to complete the acquisition cost allocation during the 12-month period following the acquisition date, during which time the values of the assets acquired and liabilities assumed, including the goodwill, may need to be revised as appropriate.

Based upon the preliminary allocation of the acquisition cost, the Company has recognized \$320,000 of goodwill, the entirety of which has been assigned to the reporting unit of the Company that produces and markets infant and toddler bibs, bath, developmental toys, feeding, baby care and disposable products, and the entirety of which is expected to be deductible for income tax purposes. The Sassy Acquisition resulted in net sales of \$2.2 million of developmental toy, feeding and baby care products during the three-month period ended July 1, 2018. Hamco recorded amortization expense associated with the amortizable intangible assets acquired in the Sassy Acquisition in the amount of \$56,000 during the three-month period ended July 1, 2018, which is included in marketing and administrative expenses in the accompanying unaudited condensed consolidated statements of income. Amortization is computed for the acquired amortizable intangible assets using the straight-line method over the estimated useful lives of the assets, which are 15 years for the tradename, 10 years for the customer relationships and 11 years on a weighted-average basis for the grouping taken together.

Note 3 – Goodwill, Customer Relationships and Other Intangible Assets

Goodwill: Goodwill represents the excess of the purchase price over the fair value of net identifiable assets acquired in business combinations. For the purpose of presenting and measuring for the impairment of goodwill, the Company has two reporting units: one that produces and markets infant and toddler bedding, blankets and accessories and another that produces and markets infant and toddler bibs, bath, developmental toys, feeding, baby care and disposable products. The goodwill of the reporting units of the Company as of July 1, 2018 and April 1, 2018 amounted to \$30.0 million, which is reflected in the accompanying condensed consolidated balance sheets net of accumulated impairment charges of \$22.9 million, for a net reported balance of \$7.1 million.

The Company measures for impairment the goodwill within its reporting units annually as of the first day of the Company's fiscal year. An additional interim measurement for impairment is performed during the year whenever an event or change in circumstances occurs that suggests that the fair value of either of the reporting units of the Company has more likely than not (defined as having a likelihood of greater than 50%) fallen below its carrying value. The annual or interim measurement for impairment is performed by first assessing qualitative factors to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount. If such qualitative factors so indicate, then the measurement for impairment is continued by calculating an estimate of the fair value of each reporting unit and comparing the estimated fair value to the carrying value of the reporting unit. If the carrying value exceeds the estimated fair value of the reporting unit, then an impairment charge is calculated as the difference between the carrying value of the reporting unit and its estimated fair value, not to exceed the goodwill of the reporting unit.

On April 2, 2018, the Company performed the annual measurement for impairment of the goodwill of its reporting units and concluded that the estimated fair value of each of the Company's reporting units exceeded their carrying values, and thus the goodwill of the Company's reporting units was not impaired as of that date.

Other Intangible Assets: Other intangible assets as of July 1, 2018 and April 1, 2018 consisted primarily of the fair value of identifiable assets acquired in business combinations other than tangible assets and goodwill. The gross amount and accumulated amortization of the Company's other intangible assets as of July 1, 2018 and April 1, 2018, the amortization expense for the three-month periods ended July 1, 2018 and July 2, 2017 and the classification of such amortization expense within the accompanying unaudited condensed consolidated statements of income are as follows (in thousands):

	Gross Amount		Accumulated Amortization		Amortization Expense Three-Month Periods Ended	
	July 1, 2018	April 1, 2018	July 1, 2018	April 1, 2018	July 1, 2018	July 2, 2017
Tradename and trademarks	\$3,667	\$3,667	\$1,318	\$1,270	\$48	\$34
Developed technology	1,100	1,100	100	73	27	-
Non-compete covenants	458	458	142	122	20	2
Patents	1,601	1,601	700	673	27	27
Customer relationships	7,374	7,374	4,868	4,790	78	126
Total other intangible assets	\$14,200	\$14,200	\$7,128	\$6,928	\$200	\$189

Classification within the accompanying unaudited condensed consolidated statements of income:

Cost of products sold	\$2	\$2
Marketing and administrative expenses	198	187
Total amortization expense	\$200	\$189

Note 4 – Inventories

Major classes of inventory were as follows (in thousands):

	July 1, 2018	April 1, 2018
Raw Materials	\$844	\$875
Work in Process	66	134
Finished Goods	19,849	18,779
Total inventory	\$20,759	\$19,788

Note 5 – Financing Arrangements

Master Stand-by Claims Purchase Agreements: On May 16, 2017, the Company entered into an agreement (the “First Agreement”) with JPMorgan Chase Bank, N.A. (“Chase”) wherein the Company had the right to sell, and Chase had the obligation to purchase, certain claims that could arise if accounts receivable amounts owed by Toys “R” Us-Delaware, Inc. (“Toys-Delaware”), an affiliated company of Toys “R” Us, Inc. (“TRU”), to the Company became uncollectible. The First Agreement would have expired on September 20, 2018 and carried a fee of 1.65% per month of the limit of \$1.8 million of accounts receivable due from Toys-Delaware. On September 18, 2017, TRU and Toys-Delaware filed voluntary petitions for relief under Chapter 11 of the U.S. Bankruptcy Code (the “Bankruptcy Filing”). Pursuant to the terms of the First Agreement, the Bankruptcy Filing allowed the Company to exercise its right to sell to Chase the claim that arose as a result of the Bankruptcy Filing, which amounted to \$866,000 payable to the Company (the “First Exercise”). Of this amount, \$746,000 remained payable to the Company by Chase as of July 1, 2018 under customary closing procedures and has been classified as other accounts receivable in the accompanying condensed consolidated balance sheets. The First Exercise resulted in the acceleration of the recognition of the remaining unpaid fees owed under the First Agreement. During the three-month period ended July 2, 2017, the Company recorded \$64,000 in fees under the First Agreement, which are included in marketing and administrative expenses in the accompanying unaudited condensed consolidated statements of income.

On September 19, 2017, the Company entered into an agreement (the “Second Agreement”) with Chase wherein the Company has the right to sell, and Chase has the obligation to purchase, certain accounts receivable claims that could arise if TRU converts its Chapter 11 case to Chapter 7 of the U.S. Bankruptcy Code or takes other specified actions. The Second Agreement would have expired on March 31, 2018 and carried a fee of 1.50% per month of the limit of \$1.8 million of accounts receivable due from Toys-Delaware. On March 14, 2018, TRU filed a motion with the Court seeking authority to close the remaining Toys-Delaware stores and distribution centers in the U.S., and to otherwise discontinue, liquidate and wind-down all U.S. operations of Toys-Delaware.

Pursuant to the terms of the Second Agreement, the liquidation filing allowed the Company to exercise its right to sell to Chase the claim that arose as a result of the liquidation filing, which amounted to \$1.8 million payable to the Company, the entirety of which remained payable to the Company by Chase as of July 1, 2018 under customary closing procedures and has been classified as other accounts receivable in the accompanying condensed consolidated balance sheets.

Factoring Agreements: The Company assigns the majority of its trade accounts receivable to CIT under factoring agreements whose expiration dates are coterminous with that of the CIT Financing Agreement. Under the terms of the factoring agreements, CIT remits customer payments to the Company as such payments are received by CIT.

CIT bears credit losses with respect to assigned accounts receivable from approved customers that are within approved credit limits, while the Company bears the responsibility for adjustments from customers related to returns, allowances, claims and discounts. CIT may at any time terminate or limit its approval of shipments to a particular customer. If such a termination or limitation occurs, the Company either assumes (and may seek to mitigate) the credit risk for shipments after the date of such termination or limitation or discontinues shipments to such customer. Factoring fees, which are included in marketing and administrative expenses in the accompanying unaudited condensed consolidated statements of income, amounted to \$56,000 and \$65,000 for the three-month periods ended July 1, 2018 and July 2, 2017, respectively.

Credit Facility: The Company's credit facility at July 1, 2018 consisted of a revolving line of credit under the CIT Financing Agreement of up to \$26.0 million, which includes a \$1.5 million sub-limit for letters of credit, with an interest rate of prime minus 0.5% or LIBOR plus 2.0%, and which is secured by a first lien on all assets of the Company. The CIT Financing Agreement was scheduled to mature on July 11, 2019, but on August 7, 2018 the CIT Financing Agreement was amended to extend the maturity date to July 11, 2022 and to lower the interest rate margin under the LIBOR option to 1.75%, effective as of August 1, 2018. As of July 1, 2018, the Company had elected to pay interest on balances owed under the revolving line of credit under the LIBOR option, which was 4.0% as of July 1, 2018. The CIT Financing Agreement also provides for the payment by CIT to the Company of interest at the rate of prime as of the beginning of the calendar month minus 2.0% on daily cash balances held at CIT.

At July 1, 2018, there was a balance due on the revolving line of credit of \$3.8 million, the entirety of which will mature during fiscal year 2023. There was no letter of credit outstanding and \$17.9 million was available under the revolving line of credit based on the Company's eligible accounts receivable and inventory balances. At April 1, 2018, there was a balance due on the revolving line of credit of \$9.5 million, there was no letter of credit outstanding and \$13.2 million was available under the revolving line of credit based on the Company's eligible accounts receivable and inventory balances. The CIT Financing Agreement for the revolving line of credit contains usual and customary covenants for agreements of that type, including limitations on other indebtedness, liens, transfers of assets, investments and acquisitions, merger or consolidation transactions, transactions with affiliates and changes in or amendments to the organizational documents for the Company and its subsidiaries. The Company was in compliance with these covenants as of July 1, 2018.

Note 6 – Stock-based Compensation

The Company has two incentive stock plans, the 2006 Omnibus Incentive Plan (the “2006 Plan”) and the 2014 Omnibus Equity Compensation Plan (the “2014 Plan”). As a result of the approval of the 2014 Plan by the Company’s stockholders at the Company’s 2014 annual meeting, grants may no longer be issued under the 2006 Plan.

The Company believes that awards of long-term, equity-based incentive compensation will attract and retain directors, officers and employees of the Company and will encourage these individuals to contribute to the successful performance of the Company, which will lead to the achievement of the Company’s overall goal of increasing stockholder value. Awards granted under the 2014 Plan may be in the form of incentive stock options, non-qualified stock options, shares of restricted or unrestricted stock, stock units, stock appreciation rights or other stock-based awards. Awards may be granted subject to the achievement of performance goals or other conditions, and certain awards may be payable in stock or cash, or a combination of the two. The 2014 Plan is administered by the Compensation Committee of the Company’s Board of Directors (the “Board”), which selects eligible employees, non-employee directors and other individuals to participate in the 2014 Plan and determines the type, amount, duration (not to exceed ten (10) years for grants of options) and other terms of individual awards. Grants under the 2014 Plan are settled primarily through the issuance of new shares of the Company’s common stock, 562,000 shares of which were available for future issuance under the 2014 Plan as of July 1, 2018.

Stock-based compensation expense is calculated according to FASB ASC Topic 718, *Compensation – Stock Compensation*, which requires stock-based compensation expense to be accounted for using a fair-value-based measurement. The Company recorded stock-based compensation expense of \$110,000 and \$142,000 for the three months ended July 1, 2018 and July 2, 2017, respectively. The Company records the compensation expense related to stock-based awards granted to individuals in the same classifications in the accompanying unaudited condensed consolidated statements of income as the cash compensation paid to those same individuals. No stock-based compensation costs have been capitalized as part of the cost of an asset as of July 1, 2018.

Stock Options: The following table represents stock option activity for the three-month periods ended July 1, 2018 and July 2, 2017:

	Three-Month Period Ended July 1, 2018		Three-Month Period Ended July 2, 2017	
	Weighted- Average Price	Number of Options Outstanding	Weighted- Average Price	Number of Options Outstanding
Outstanding at Beginning of Period	\$7.93	395,000	\$8.35	322,500
Granted	5.90	110,000	7.75	110,000
Forfeited	-	-	9.19	(15,000)
Outstanding at End of Period	7.48	505,000	8.17	417,500
Exercisable at End of Period	8.15	315,000	8.03	252,500

As of July 1, 2018, the intrinsic value of the outstanding and exercisable stock options was \$13,000 and \$10,000, respectively. There were no options exercised during either of the three-month periods ended July 1, 2018 or July 2, 2017.

To determine the estimated fair value of stock options granted, the Company uses the Black-Scholes-Merton valuation formula, which is a closed-form model that uses an equation to estimate fair value. The following table sets forth the assumptions used to determine the fair value of the non-qualified stock options that were awarded to certain employees during the three-month periods ended July 1, 2018 and July 2, 2017, which options vest over a two-year period, assuming continued service.

	Three-Month Periods Ended	
	July 1, 2018	July 2, 2017
Number of options issued	110,000	110,000

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Grant date	June 13, 2018	June 8, 2017
Dividend yield	5.42 %	4.13 %
Expected volatility	25.00 %	25.00 %
Risk free interest rate	2.78 %	1.47 %
Contractual term (years)	10.00	10.00
Expected term (years)	4.00	3.00
Forfeiture rate	5.00 %	5.00 %
Exercise price (grant-date closing price) per option	\$5.90	\$7.75
Fair value per option	\$0.49	\$0.85

For the three-month periods ended July 1, 2018 and July 2, 2017, the Company recorded compensation expense associated with stock options as follows (in thousands):

<u>Options Granted in Fiscal Year</u>	Three-Month Period Ended July 1, 2018			Three-Month Period Ended July 2, 2017		
	Cost of Product Sold	Marketing & Administrative Expenses	Total Expense	Cost of Product Sold	Marketing & Administrative Expenses	Total Expense
2016	\$-	\$ -	\$ -	\$6	\$ 1	\$ 7
2017	6	5	11	10	2	12
2018	7	8	15	2	1	3
2019	-	1	1	-	-	-
Total stock option compensation	\$13	\$ 14	\$ 27	\$18	\$ 4	\$ 22

As of July 1, 2018, total unrecognized stock option compensation expense amounted to \$103,000, which will be recognized as the underlying stock options vest over a weighted-average period of 1.2 years. The amount of future stock option compensation expense could be affected by any future stock option grants and by the separation from the Company of any individual who has received stock options that are unvested as of such individual's separation date.

Non-vested Stock Granted to Nonemployee Directors: The Board granted the following shares of non-vested stock to the Company's nonemployee directors:

Number of Shares	Fair Value per Share	Grant Date
28,000	\$5.50	August 9, 2017
28,000	10.08	August 10, 2016
28,000	8.20	August 12, 2015

These shares vest over a two-year period, assuming continued service. The fair value of the non-vested stock granted to the Company's nonemployee directors was based on the closing price of the Company's common stock on the date of each grant.

Performance Bonus Plan: The Company maintains a performance bonus plan for certain executive officers that provides for awards of shares of common stock in the event that the aggregate average market value of the common stock during the relevant fiscal year, plus the amount of cash dividends paid in respect of the common stock during such period, increases. These individuals may instead be awarded cash, if and to the extent that insufficient shares of common stock are available for issuance from all shareholder-approved, equity-based plans or programs of the Company in effect. The performance bonus plan also imposes individual limits on awards and provides that shares of common stock that may be awarded will vest over a two-year period. Compensation expense associated with performance bonus plan awards are recognized over a three-year period – the fiscal year in which the award is earned, plus the two-year vesting period.

In connection with the performance bonus plan, the Company granted shares of common stock and recognized or will recognize compensation expense as set forth below:

Fiscal Year	Fiscal Year	Fiscal Year	Fair Value Per Share	Compensation expense recognized during fiscal year			
Earned	Granted	Granted	Share	2016	2017	2018	2019
2016	41,205	2017	\$7.865	\$108,000	\$108,000	\$108,000	\$-
2017	42,250	2018	8.271	-	116,000	116,000	116,000

The table below sets forth the vesting of shares issued in connection with the grants of shares set forth in the above table. Each of the individuals holding shares that vested surrendered to the Company the number of shares necessary

to satisfy the income tax withholding obligations that arose from the vesting of the shares. The table below also sets forth the taxes remitted to the appropriate taxing authorities on behalf of such individuals.

Fiscal Year	Shares Granted	Vesting of shares during the three-month periods ended					
		July 1, 2018			July 2, 2017		
		Shares Vested	Aggregate Value	Taxes Remitted	Shares Vested	Aggregate Value	Taxes Remitted
2017	41,205	20,601	\$ 122,000	\$ 39,000	20,604	\$ 167,000	\$ 56,000
2018	42,250	21,125	124,000	56,000	-	-	-
	Total	41,726	\$ 246,000	\$ 95,000	20,604	\$ 167,000	\$ 56,000

For the three-month periods ended July 1, 2018 and July 2, 2017, the Company recorded compensation expense associated with stock grants, which is included in marketing and administrative expenses in the accompanying unaudited condensed consolidated statements of income, as follows (in thousands):

Stock Granted in Fiscal Year	Three-Month Period Ended July 1, 2018			Three-Month Period Ended July 2, 2017		
	Employee	Nonemployee Directors	Total Expense	Employee	Nonemployee Directors	Total Expense
2016	\$-	\$ -	\$ -	\$-	\$ 29	\$ 29
2017	-	35	35	27	35	62
2018	29	19	48	29	-	29
Total stock grant compensation	\$29	\$ 54	\$ 83	\$56	\$ 64	\$ 120

As of July 1, 2018, total unrecognized compensation expense related to the Company's non-vested stock grants amounted to \$183,000, which will be recognized over the respective vesting terms associated with each block of non-vested stock indicated above, such grants having an aggregate weighted-average vesting term of 151 days. The amount of future compensation expense related to the Company's non-vested stock grants could be affected by any future non-vested stock grants and by the separation from the Company of any individual who has non-vested stock grants as of such individual's separation date.

Note 7 – Related Party Transaction

On August 4, 2017, Carousel entered into a lease of the Carousel facilities in Douglasville, Georgia with JST Capital, LLC ("JST"), a wholly-owned subsidiary of Pritech, Inc., which is owned by the Chief Executive Officer and former President of Carousel. Carousel made lease payments of \$24,000 to JST for the three-month period ended July 1, 2018. Of this amount, \$20,000 was included in cost of products sold and \$4,000 was included in marketing and administrative expenses in the accompanying unaudited condensed consolidated statements of income.

Note 8 – Subsequent Events

As set forth in the Note 5 disclosure, on August 7, 2018, the CIT Financing Agreement was amended to extend the maturity date to July 11, 2022 and to lower the interest rate margin under the LIBOR option to 1.75%, effective as of August 1, 2018. The Company has evaluated events which have occurred between July 1, 2018 and the date that the accompanying consolidated financial statements were issued, and has determined that there are no other material subsequent events that require disclosure.

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

FORWARD-LOOKING INFORMATION

This report contains forward-looking statements within the meaning of the Securities Act of 1933, the Securities Exchange Act of 1934 and the Private Securities Litigation Reform Act of 1995. Such statements are based upon management's current expectations, projections, estimates and assumptions. Words such as "expects," "believes,"

“anticipates” and variations of such words and similar expressions identify such forward-looking statements. Forward-looking statements involve known and unknown risks and uncertainties that may cause future results to differ materially from those suggested by the forward-looking statements. These risks include, among others, general economic conditions, including changes in interest rates, in the overall level of consumer spending and in the price of oil, cotton and other raw materials used in the Company’s products, changing competition, changes in the retail environment, the Company’s ability to successfully integrate newly acquired businesses, the level and pricing of future orders from the Company’s customers, the Company’s dependence upon third-party suppliers, including some located in foreign countries with unstable political situations, the Company’s ability to successfully implement new information technologies, customer acceptance of both new designs and newly-introduced product lines, actions of competitors that may impact the Company’s business, disruptions to transportation systems or shipping lanes used by the Company or its suppliers, and the Company’s dependence upon licenses from third parties. Reference is also made to the Company’s periodic filings with the Securities and Exchange Commission (the “SEC”) for additional factors that may impact the Company’s results of operations and financial condition. The Company does not undertake to update the forward-looking statements contained herein to conform to actual results or changes in the Company’s expectations, whether as a result of new information, future events or otherwise.

DESCRIPTION OF BUSINESS

The Company operates indirectly through its wholly-owned subsidiaries, Crown Crafts Infant Products, Inc. (“CCIP”), Hamco and Carousel, in the infant, toddler and juvenile products segment within the consumer products industry. The infant and toddler products segment consists of infant and toddler bedding and blankets, bibs, soft bath products, disposable products, developmental toys and accessories. Sales of the Company’s products are made directly to retailers, such as mass merchants, large chain stores, juvenile specialty stores, value channel stores, grocery and drug stores, restaurants, wholesale clubs and internet-based retailers, as well as directly to consumers through www.babybedding.com.

The Company’s products are marketed to retailers through a national sales force consisting of salaried sales executives and employees located in Compton, California; Gonzales, Louisiana; Grand Rapids, Michigan; and Bentonville, Arkansas and by independent commissioned sales representatives located throughout the United States. Products are also marketed directly to consumers from a Company facility in Douglasville, Georgia. Sales outside the United States are made primarily through distributors.

Foreign and domestic contract manufacturers produce most of the Company's products, with the largest concentration being in China. The Company makes sourcing decisions based on quality, timeliness of delivery and price, including the impact of ocean freight and duties. Although the Company maintains relationships with a limited number of suppliers, the Company believes that its products may be readily manufactured by several alternative sources in quantities sufficient to meet the Company's requirements. The Company also produces some of its products domestically at a Company facility in Douglasville, Georgia.

A summary of certain factors that management considers important in reviewing the Company's results of operations, financial position, liquidity and capital resources is set forth below, which should be read in conjunction with the accompanying consolidated financial statements and related notes included in the preceding sections of this report.

RESULTS OF OPERATIONS

The following table contains the results of operations for the three-month periods ended July 1, 2018 and July 2, 2017 and the dollar and percentage changes for those periods (in thousands, except percentages):

	Three-Month Periods Ended		Change	
	July 1, 2018	July 2, 2017	\$	%
Net sales by category:				
Bedding, blankets and accessories	\$8,521	\$8,424	\$97	1.2 %
Bibs, bath, developmental toy, feeding, baby care and disposable products	6,939	5,223	1,716	32.9 %
Total net sales	15,460	13,647	1,813	13.3 %
Cost of products sold	11,332	10,045	1,287	12.8 %
Gross profit	4,128	3,602	526	14.6 %
<i>% of net sales</i>	26.7 %	26.4 %		
Marketing and administrative expenses	3,685	2,901	784	27.0 %
<i>% of net sales</i>	23.8 %	21.3 %		
Interest expense	99	20	79	395.0 %
Other income	-	40	(40)	-100.0 %
Income tax expense	80	203	(123)	-60.6 %
Net income	264	518	(254)	-49.0 %
<i>% of net sales</i>	1.7 %	3.8 %		

Net Sales: Sales increased by \$1.8 million, or 13.3%, for the three-month period ended July 1, 2018 compared with the same period in the prior year. The increase is due to sales that resulted from the Sassy Acquisition and the Carousel Acquisition, which added \$2.2 million and \$1.8 million, respectively, of sales during the three-month period ended July 1, 2018. These increases were offset by the elimination of all sales to Toys-Delaware in the current year

quarter, which were \$3.4 million during the three-month period ended July 2, 2017. Most of the sales previously made to Toys-Delaware had not yet shifted to other customers of the Company in the current year quarter, as Toys-Delaware actually became a major competitor of the Company as it conducted liquidation sales during the entire quarter, which included deep discounts on in-line merchandise.

Gross Profit: Gross profit increased by \$526,000 and increased from 26.4% of net sales for the three-month period ended July 2, 2017 to 26.7% of net sales for the three-month period ended July 1, 2018. The increase in amount is primarily due to the net higher sales levels in the current year quarter.

Marketing and Administrative Expenses: Marketing and administrative expenses increased in amount by \$784,000 and increased from 21.3% of net sales for the three-month period ended July 2, 2017 to 23.8% of net sales for the three-month period ended July 1, 2018. Contributing to the increase in amount is \$904,000 in costs during the current year quarter that were associated with Carousel and which were not incurred in the same period of the prior year. The current year quarter also included \$210,000 in charges associated with transferring the remaining inventory acquired in the Sassy Acquisition from Grand Rapids, Michigan to the Company's distribution facility in Compton, California. Offsetting these increases were lower advertising costs incurred by CCIP and Hamco in the current year quarter, which were \$163,000 lower than the prior year.

Income Tax Expense: The Company's provision for income taxes is based upon an estimated annual ETR from continuing operations of 24.0% for the three-month period ended July 1, 2018. On December 22, 2017, the President of the United States signed into law comprehensive tax legislation commonly referred to as the Tax Cuts and Jobs Act (the "TCJA"), which includes a provision to lower the federal corporate income tax rate from 34% to 21% effective as of January 1, 2018. As the Company's fiscal year 2018 ended on April 1, 2018, the lower corporate income tax rate was phased in, resulting in a blended federal statutory rate of 30.75% for fiscal year 2018. Because the TCJA had not yet been enacted, the Company's provision for income taxes was based upon an estimated ETR from continuing operations of 35.0% for the three-month period ended July 2, 2017.

Management evaluates items of income, deductions and credits reported on the Company's various federal and state income tax returns filed and recognizes the effect of positions taken on those income tax returns only if those positions are more likely than not to be sustained. The Company applies the provisions of FASB ASC Sub-topic 740-10-25, which requires a minimum recognition threshold that a tax benefit must meet before being recognized in the financial statements. Recognized income tax positions are measured at the largest amount that has a greater than 50% likelihood of being realized. Changes in recognition or measurement are reflected in the period in which the change in judgment occurs.

During fiscal year 2016, an evaluation was made of the Company's process regarding the calculation of the state portion of its income tax provision. This evaluation resulted in the Company taking a tax position that reflected opportunities for the application of more favorable state apportionment percentages for several prior fiscal years. After considering all relevant information, the Company believes that the technical merits of this tax position would more likely than not be sustained. However, the Company also believes that the ultimate resolution of the tax position will result in a tax benefit that is less than the full amount being sought. Therefore, the Company's measurement regarding the tax impact of the revised state apportionment percentages resulted in the Company recording a reserve for unrecognized tax benefits during the three-month periods ended July 1, 2018 and July 2, 2017 of \$3,000 and \$11,000, respectively, in the accompanying unaudited condensed consolidated statements of income.

During the three-month periods ended July 1, 2018 and July 2, 2017, the Company recorded discrete income tax benefits of \$5,000 and \$60,000, respectively, to reflect the effect of excess tax benefits arising from the vesting of non-vested stock during the periods.

The ETR on continuing operations and the discrete income tax charges and benefits set forth above resulted in an overall provision for income taxes of 23.3% and 28.2% for the three-month periods ended July 1, 2018 and July 2, 2017, respectively.

Although the Company does not anticipate a material change to the ETR from continuing operations for the balance of fiscal year 2019, several factors could impact the ETR, including variations from the Company's estimates of the amount and source of its pre-tax income.

FINANCIAL POSITION, LIQUIDITY AND CAPITAL RESOURCES

Net cash provided by operating activities increased from \$4.9 million for the three-month period ended July 2, 2017 to \$6.6 million for the three-month period ended July 1, 2018. Increases of net cash provided by operating activities in the current year period included an increase in the Company's accounts payable balances that was \$3.0 million higher than the increase in the prior year period. Also, the current year period included a decrease in the Company's accounts receivable balances that was \$1.4 million higher than the decrease in the prior year period. Decreases of net cash provided by operating activities that offset these increases included a net decrease in the Company's accrued liabilities balances in the current year period that was \$1.3 million lower than the increase in the prior year period. The current year decrease in accrued liabilities was primarily due to a \$637,000 decrease in accrued royalties, compared with a \$632,000 increase in accrued royalties in the prior year. The Company also experienced in the current year period an increase in its inventory balances that was \$1.2 million higher than the increase in the prior year period.

Net cash used in investing activities increased to \$102,000 in the current year from \$56,000 in the prior year, due to higher capital expenditures in the current year for property, plant and equipment compared with the prior year.

Net cash used in financing activities increased by \$5.7 million to \$6.5 million in the current year. The increase was due primarily to net repayments under the revolving line of credit in the current year.

From July 2, 2017 to July 1, 2018, the Company decreased its cash balances from \$11.9 million to \$199,000. During that period, the Company made combined payments of \$15.2 million for the Carousel Acquisition and the Sassy Acquisition and paid \$3.2 million in dividends. Offsetting these decreases in cash was an increase in the Company's revolving line of credit of \$3.8 million and net income of \$2.8 million.

At July 1, 2018, there was a balance of \$3.8 million owed on the revolving line of credit, there was no letter of credit outstanding and \$17.9 million was available under the revolving line of credit based on the Company's eligible accounts receivable and inventory balances.

To reduce its exposure to credit losses and to enhance the predictability of its cash flow, the Company assigns the majority of its trade accounts receivable to CIT under factoring agreements. Under the terms of the factoring agreements, CIT remits customer payments to the Company as such payments are received by CIT and bears credit losses with respect to assigned accounts receivable from approved customers that are within approved credit limits, while the Company bears the responsibility for adjustments from customers related to returns, allowances, claims and discounts. CIT may at any time terminate or limit its approval of shipments to a particular customer. If such a termination were to occur, the Company must either assume the credit risk for shipments after the date of such termination or limitation or cease shipments to such customer. There were no advances from the factor at either July 1, 2018 or April 1, 2018.

The Company's future performance is, to a certain extent, subject to general economic, financial, competitive, legislative, regulatory and other factors beyond its control. Based upon the current level of operations, the Company believes that its cash flow from operations and its availability from the revolving line of credit will be adequate to meet its liquidity needs.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

For a detailed discussion of market risk, refer to the risk factors disclosed in Item 1A. of Part 1 of the Company's annual report on Form 10-K for the year ended April 1, 2018.

INTEREST RATE RISK

As of July 1, 2018, the Company had \$3.8 million of indebtedness that bears interest at a variable rate, comprised of borrowings under the revolving line of credit. Based upon this level of outstanding debt, the Company's net income would decrease by approximately \$29,000 for each increase of one percentage point in the interest rate applicable to the debt.

COMMODITY RATE RISK

The Company sources its products primarily from foreign contract manufacturers, with the largest concentration being in China. The Company's exposure to commodity price risk primarily relates to changes in the prices in China of cotton, oil and labor, which are the principal inputs used in a substantial number of the Company's products. Also, although the Company's purchases of its products from its Chinese suppliers are paid in U.S. dollars, an arbitrary strengthening of the rate of the Chinese currency versus the U.S. dollar could result in an increase in the cost of the prices at which the Company purchases its finished goods. There can be no assurance that the Company could timely respond to such increases by proportionately increasing the prices at which its products are sold to the Company's customers.

MARKET CONCENTRATION RISK

The Company's financial results are closely tied to sales to its top three customers, which represented approximately 65% of the Company's gross sales in fiscal year 2018, including 15% of sales to Toys-Delaware. On September 18, 2017, TRU and Toys-Delaware filed petitions for relief under Chapter 11 of Title 11 of the U.S. Bankruptcy Code with the U.S. Bankruptcy Court for the Eastern District of Virginia. On March 14, 2018, TRU filed a motion with the Court seeking authority to close all of the remaining Toys-Delaware stores and distribution centers in the U.S., and to otherwise discontinue, liquidate and wind-down all U.S. operations of Toys-Delaware. The Company had ceased all shipments to Toys-Delaware shortly before the liquidation filing was made. The Company anticipates that the loss of future business with Toys-Delaware may be mitigated by a shift to other customers of the Company. A significant downturn experienced by either or both of the Company's two remaining top customers could lead to pressure on the Company's revenues.

For the fiscal year ended April 1, 2018, 52% of the Company's gross sales consisted of licensed products, which included 34% of sales associated with the Company's license agreements with affiliated companies of the Walt Disney Company. The Company's results could be materially impacted by the loss of one or more of these licenses.

ITEM 4. CONTROLS AND PROCEDURES

The Company's Chief Executive Officer and Chief Financial Officer have evaluated the effectiveness of the Company's disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the "Exchange Act")), as of the end of the period covered by this report, as required by paragraph (b) of Rules 13a-15 or 15d-15 of the Exchange Act. Based on such evaluation, such officers have concluded that, as of the end of the period covered by this report, the Company's disclosure controls and procedures are effective.

In the Company's evaluation of whether there was any change in the Company's internal control over financial reporting ("ICFR") during the three-month period ended July 1, 2018, the Company has excluded an evaluation of the ICFR related to the operations of Carousel, which consummated the Carousel Acquisition on August 4, 2017. For the three-month period ended July 1, 2018, the net sales of Carousel were \$1.8 million, which was 11.9% of the Company's total net sales. The total assets of Carousel as of July 1, 2018 amounted to \$10.2 million (including \$5.7 million in goodwill), which was 19.1% of the Company's total assets.

During the three-month period ended July 1, 2018, notwithstanding the exclusion of evaluations of the ICFR related to the operations of Carousel, there was not any change in the Company's ICFR identified in connection with the evaluation required by paragraph (d) of Rules 13a-15 or 15d-15 of the Exchange Act that has materially affected, or is reasonably likely to materially affect, the Company's ICFR.

PART II - OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

The Company is, from time to time, involved in various legal and regulatory proceedings relating to claims arising in the ordinary course of its business. Neither the Company nor any of its subsidiaries is a party to any such proceeding the outcome of which, individually or in the aggregate, is expected to have a material adverse effect on the Company's financial condition, results of operations or cash flow.

ITEM 1A. RISK FACTORS

There have been no material changes to the risk factors disclosed in Item 1A. of Part 1 of the Company's annual report on Form 10-K for the year ended April 1, 2018.

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

(c) Issuer Purchases of Equity Securities.

The table below sets forth information regarding the Company's repurchase of its outstanding common stock during the three-month period ended July 1, 2018.

Period	Total Number of Shares Purchased (1)	Average Price Paid Per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Approximate Dollar Value of Shares That May Yet be Purchased Under the Plans or Programs
April 2, 2018 through May 6, 2018	16,206	\$ 5.87	0	\$ 0
May 7, 2018 through June 3, 2018	0	\$ 0	0	\$ 0
June 4, 2018 through July 1, 2018	0	\$ 0	0	\$ 0
Total	16,206	\$ 5.87	0	\$ 0

(1) The shares purchased from April 2, 2018 through May 6, 2018 consist of shares of common stock surrendered to the Company in payment of the income tax withholding obligations relating to the vesting of non-vested stock.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

ITEM 5. OTHER INFORMATION

On August 7, 2018, the Borrowers entered into a Thirteenth Amendment to Financing Agreement with CIT, amending the CIT Financing Agreement to extend its maturity date to July 11, 2022 and to lower the interest rate margin under the LIBOR option to 1.75%, effective as of August 1, 2018.

ITEM 6. EXHIBITS

Exhibits required to be filed by Item 601 of Regulation S-K are included as Exhibits to this report as follows:

Exhibit Number	Description of Exhibit
10.1	<u>Thirteenth Amendment to Financing Agreement dated as of August 7, 2018 by and among the Company, Hamco, CCIP, Carousel and CIT (1)</u>
31.1	<u>Rule 13a-14(a)/15d-14(a) Certification by the Company's Chief Executive Officer (1)</u>
31.2	<u>Rule 13a-14(a)/15d-14(a) Certification by the Company's Chief Financial Officer (1)</u>
32.1	<u>Section 1350 Certification by the Company's Chief Executive Officer (1)</u>
32.2	<u>Section 1350 Certification by the Company's Chief Financial Officer (1)</u>

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The following information from the Registrant's Form 10-Q for the quarterly period ended July 1, 2018, formatted as interactive data files in XBRL (eXtensible Business Reporting Language):

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- (i) Unaudited Condensed Consolidated Statements of Income;
 - (ii) Unaudited Condensed Consolidated Balance Sheets;
 - (iii) Unaudited Condensed Consolidated Statements of Cash Flows; and
 - (iv) Notes to Unaudited Condensed Consolidated Financial Statements.

(1) Filed herewith.

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.

CROWN CRAFTS, INC.

Date: August 9, 2018 /s/ Olivia W. Elliott
OLIVIA W. ELLIOTT

Vice President and
Chief Financial Officer
(Principal Financial Officer
and Principal Accounting Officer)