INGLES MARKETS INC
Form 10-Q
August 03, 2007
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

x **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the quarterly period ended June 30, 2007

¨ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the transition period from ______ to ______

Commission file number 0-14706.

INGLES MARKETS, INCORPORATED

(Exact name of registrant as specified in its charter)

North Carolina	**56-0846267**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**
P.O. Box 6676, Asheville NC	**28816**
(Address of principal executive offices)	**(Zip Code)**

(828) 669-2941

Registrant s telephone number, including area code

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (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 x 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 x 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 x.

As of July 30, 2007, the Registrant had 12,346,410 shares of Class A Common Stock, $0.05 par value per share, outstanding and 12,164,851 shares of Class B Common Stock, $0.05 par value per share, outstanding.

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INGLES MARKETS, INCORPORATED

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Part I. FINANCIAL INFORMATION

Item 1. FINANCIAL STATEMENTS
INGLES MARKETS, INCORPORATED AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEETS (UNAUDITED)

	JUNE 30, 2007	SEPTEMBER 30, 2006
ASSETS		
Current Assets:		
Cash and Cash Equivalents	**$ 17,244,597**	$ 17,540,306
Receivables	**44,934,700**	43,593,653
Inventories	**231,570,736**	215,368,516
Other Current Assets	**9,855,915**	9,315,413
Total Current Assets	**303,605,948**	285,817,888
Property and Equipment Net	**820,222,868**	771,627,871
Other Assets	**12,419,911**	17,527,783
Total Assets	**$ 1,136,248,727**	$ 1,074,973,542
LIABILITIES AND STOCKHOLDERS EQUITY		
Current Liabilities:		
Current portion of long-term debt	**$ 52,361,755**	$ 33,665,969
Accounts payable - trade	**140,930,864**	112,269,275
Accrued expenses and current portion of other long-term liabilities	**64,328,269**	72,925,571
Total Current Liabilities	**257,620,888**	218,860,815
Deferred Income Taxes	**37,268,578**	22,672,578
Long-Term Debt	**498,251,565**	522,649,069
Other Long-Term Liabilities	**5,337,852**	6,118,193
Total Liabilities	**798,478,883**	770,300,655
Stockholders Equity		
Preferred stock, $0.05 par value; 10,000,000 shares authorized; no shares issued		
Common stocks:		
Class A, $0.05 par value; 150,000,000 shares authorized; 12,346,408 shares issued and outstanding June 30, 2007; 12,176,485 shares issued and outstanding September 30, 2006	**617,320**	608,824
Class B, $0.05 par value; 100,000,000 shares authorized; 12,164,851 shares issued and outstanding June 30, 2007; 12,321,774 shares issued and outstanding September 30, 2006	**608,243**	616,089
Paid-in capital in excess of par value	**118,165,637**	117,911,423
Retained earnings	**218,378,644**	185,536,551
Total Stockholders Equity	**337,769,844**	304,672,887
Total Liabilities and Stockholders Equity	**$ 1,136,248,727**	$ 1,074,973,542

See notes to unaudited interim financial statements.

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INGLES MARKETS, INCORPORATED AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF INCOME (UNAUDITED)

	THREE MONTHS ENDED JUNE 30, 2007	JUNE 24, 2006
Net sales	**$ 738,695,131**	$ 659,212,015
Cost of goods sold	**563,466,947**	495,018,993
Gross profit	**175,228,184**	164,193,022
Operating and administrative expenses	**141,786,968**	132,164,105
Rental income, net	**1,248,327**	1,431,531
Income from operations	**34,689,543**	33,460,448
Other income, net	**8,460,820**	445,850
Interest expense	**11,861,469**	12,184,329
Income before income taxes	**31,288,894**	21,721,969
Income tax expense (benefit):		
Current	**(6,906,000)**	9,170,000
Deferred	**18,449,000**	(1,290,000)
	11,543,000	7,880,000
Net income	**$ 19,745,894**	$ 13,841,969
Per share amounts:		
Class A Common Stock		
Basic earnings per common share	**$ 0.84**	$ 0.59
Diluted earnings per common share	**$ 0.81**	$ 0.57
Class B Common Stock		
Basic earnings per common share	**$ 0.77**	$ 0.54
Diluted earnings per common share	**$ 0.77**	$ 0.54
Cash dividends per common share:		
Class A Common Stock	**$ 0.165**	$ 0.165
Class B Common Stock	**$ 0.150**	$ 0.150

See notes to unaudited interim financial statements.

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INGLES MARKETS, INCORPORATED AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF INCOME (UNAUDITED)

	NINE MONTHS ENDED JUNE 30, 2007	NINE MONTHS ENDED JUNE 24, 2006
Net sales	**$ 2,105,557,730**	$ 1,889,255,406
Cost of goods sold	**1,598,898,669**	1,414,999,962
Gross profit	**506,659,061**	474,255,444
Operating and administrative expenses	**417,749,019**	392,647,333
Rental income, net	**3,551,833**	4,016,501
Income from operations	**92,461,875**	85,624,612
Other income, net	**9,315,944**	1,265,643
Interest expense	**35,802,596**	36,736,831
Income before income taxes	**65,975,223**	50,153,424
Income tax expense (benefit):		
Current	**7,214,000**	26,170,000
Deferred	**14,341,000**	(7,070,000)
	21,555,000	19,100,000
Net income	**$ 44,420,223**	$ 31,053,424
Per share amounts:		
Class A Common Stock		
Basic earnings per common share	**$ 1.90**	$ 1.33
Diluted earnings per common share	**$ 1.81**	$ 1.27
Class B Common Stock		
Basic earnings per common share	**$ 1.73**	$ 1.21
Diluted earnings per common share	**$ 1.73**	$ 1.21
Cash dividends per common share:		
Class A Common Stock	**$ 0.495**	$ 0.495
Class B Common Stock	**$ 0.450**	$ 0.450

See notes to unaudited interim financial statements.

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INGLES MARKETS, INCORPORATED AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS EQUITY (UNAUDITED)

NINE MONTHS ENDED JUNE 30, 2007 AND JUNE 24, 2006

	CLASS A COMMON STOCK		CLASS B COMMON STOCK		PAID-IN CAPITAL IN EXCESS OF PAR VALUE	RETAINED EARNINGS	TOTAL
	SHARES	AMOUNT	SHARES	AMOUNT			
Balance, September 24, 2005	12,080,718	$ 604,036	12,364,991	$ 618,250	$ 117,259,716	$ 158,366,661	$ 276,848,663
Net income						31,053,424	31,053,424
Cash dividends						(11,554,298)	(11,554,298)
Exercise of stock options	52,550	2,628			651,707		654,335
Common stock conversions	41,867	2,093	(41,867)	(2,093)			
Balance, June 24, 2006	12,175,135	$ 608,757	12,323,124	$ 616,157	$ 117,911,423	$ 177,865,787	$ 297,002,124
Balance, September 30, 2006	12,176,485	$ 608,824	12,321,774	$ 616,089	$ 117,911,423	$ 185,536,551	$ 304,672,887
Net income						44,420,223	44,420,223
Cash dividends						(11,578,130)	(11,578,130)
Exercise of stock options	13,000	650			254,214		254,864
Common stock conversions	156,923	7,846	(156,923)	(7,846)			
Balance, June 30, 2007	**12,346,408**	**$ 617,320**	**12,164,851**	**$ 608,243**	**$ 118,165,637**	**$ 218,378,644**	**$ 337,769,844**

See notes to unaudited interim financial statements.

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INGLES MARKETS, INCORPORATED AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)

	NINE MONTHS ENDED JUNE 30, 2007	JUNE 24, 2006
Cash Flows from Operating Activities:		
Net income	**$ 44,420,223**	$ 31,053,424
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization expense	**44,794,403**	44,380,418
Amortization of deferred gain on sale/leasebacks	**(38,079)**	(83,771)
(Gain) loss on disposals of property and equipment	**(6,930,568)**	41,627
Receipt of advance payments on purchase contracts	**3,645,153**	1,674,403
Recognition of advance payments on purchase contracts	**(2,936,750)**	(1,930,825)
Deferred income taxes	**14,341,000**	(7,070,000)
Changes in operating assets and liabilities:		
Receivables	**(3,441,047)**	(438,067)
Inventory	**(16,202,220)**	(12,641,382)
Other assets	**5,856,370**	(2,341,666)
Accounts payable and accrued expenses	**15,561,177**	10,103,027
Net Cash Provided by Operating Activities	**99,069,662**	62,747,188
Cash Flows from Investing Activities:		
Proceeds from sales of property and equipment	**14,060,732**	628,586
Capital expenditures	**(96,401,120)**	(66,838,102)
Net Cash Used in Investing Activities	**(82,340,388)**	(66,209,516)
Cash Flows from Financing Activities:		
Proceeds from short-term borrowings	**324,038,400**	
Payments on short-term borrowings	**(302,838,400)**	
Principal payments on long-term debt	**(26,901,717)**	(13,983,106)
Proceeds from exercise of stock options	**254,864**	654,335
Dividends paid	**(11,578,130)**	(11,554,298)
Net Cash Used in Financing Activities	**(17,024,983)**	(24,883,069)
Net Decrease in Cash and Cash Equivalents	**(295,709)**	(28,345,397)
Cash and cash equivalents at beginning of period	**17,540,306**	50,626,448
Cash and Cash Equivalents at End of Period	**$ 17,244,597**	$ 22,281,051

See notes to unaudited interim financial statements.

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INGLES MARKETS, INCORPORATED AND SUBSIDIARIES

NOTES TO UNAUDITED INTERIM FINANCIAL STATEMENTS

Nine Months Ended June 30, 2007 and June 24, 2006

A. BASIS OF PREPARATION

In the opinion of management, the accompanying unaudited interim financial statements contain all adjustments necessary to present fairly the Company s financial position as of June 30, 2007, the results of operations for the three-month and nine-month periods ended June 30, 2007 and June 24, 2006, and the changes in stockholders equity and cash flows for the nine-month periods ended June 30, 2007 and June 24, 2006. The adjustments made are of a normal recurring nature. Certain information and footnote disclosures normally included in the annual financial statements prepared in accordance with accounting principles generally accepted in the United States have been condensed or omitted pursuant to the rules and regulations of the Securities and Exchange Commission for Form 10-Q. It is suggested that these unaudited interim financial statements be read in conjunction with the audited financial statements and the notes thereto included in the Annual Report on Form 10-K for the year ended September 30, 2006 and the Form 10-Q for the fiscal quarter ended June 24, 2006, filed by the Company under the Securities Exchange Act of 1934 on December 1, 2006, and July 31, 2006, respectively.

The results of operations for the three-month and nine-month periods ended June 30, 2007 are not necessarily indicative of the results to be expected for the full fiscal year.

Certain amounts for the three-month and nine-month periods ended June 24, 2006 have been reclassified to conform to the current year presentation in the accompanying financial statements.

B. NEW ACCOUNTING PRONOUNCEMENTS

In July 2006, the Financial Accounting Standards Board (FASB) issued Interpretation No. 48, Accounting for Uncertainty in Income Taxes, an interpretation of FAS 109, Accounting for Income Taxes (FIN 48), to create a single model to address accounting for uncertainty in tax positions. FIN 48 clarifies the accounting for income taxes, by prescribing a minimum recognition threshold a tax position is required to meet before being recognized in the financial statements. FIN 48 also provides guidance on derecognition, measurement, classification, interest and penalties, accounting in interim periods, disclosure and transition of tax provisions. FIN 48 is effective for fiscal years beginning after December 15, 2006. The Company will adopt FIN 48 as of September 30, 2007, as required. The Company is currently evaluating the impact of FIN 48 on its consolidated financial statements.

C. ALLOWANCE FOR DOUBTFUL ACCOUNTS

Receivables are presented net of an allowance for doubtful accounts of $959,000 and $845,000 at June 30, 2007 and September 30, 2006, respectively.

D. ACCRUED EXPENSES AND CURRENT PORTION OF OTHER LONG-TERM LIABILITIES

Accrued expenses and current portion of other long-term liabilities consist of the following:

	JUNE 30, 2007	**SEPTEMBER 30, 2006**
Property, payroll, and other taxes payable	**$ 15,342,640**	$ 17,865,518
Salaries, wages and bonuses payable	**19,466,863**	19,602,902
Self-insurance liabilities	**9,571,766**	8,524,499
Interest	**3,837,250**	11,855,031
Income taxes	**3,088,365**	2,175,447
Other	**13,021,385**	12,902,174
	$ 64,328,269	$ 72,925,571

Self-insurance liabilities are established for workers compensation and employee group medical and dental benefits based on claims filed and estimates of claims incurred but not reported. The Company is insured for covered costs in excess of $750,000 per occurrence for workers compensation and $250,000 per covered person for medical care benefits for a policy year. Employee insurance expense, including workers compensation and medical care benefits, net of employee contributions, totaled $5.6 million and $4.2 million for each of the three-month periods ended June 30, 2007 and June 24, 2006, respectively. For the nine-month periods ended June 30, 2007 and June 24, 2006, employee insurance expense, net of employee contributions, totaled $17.2 million and $15.5 million, respectively.

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E. LONG-TERM DEBT

At June 30, 2007, the Company had lines of credit with six banks totaling $150.0 million, of which $25.1 million was outstanding at June 30, 2007. The lines of credit mature between October 2007 and February 2010. At June 30, 2007, the Company had issued $21.3 million in unused letters of credit that reduced the amounts available to be drawn under its lines of credit. The letters of credit mature from September 2007 to May 2008. The lines provide the Company with various interest rate options generally at rates less than prime. The Company is not required to maintain compensating balances in connection with these lines of credit. The lines of credit contain provisions that under certain circumstances would permit lending institutions to terminate or withdraw their respective extensions of credit to the Company. Included among the triggering factors permitting the termination or withdrawal of lines of credit to the Company are certain events of default, including both monetary and non-monetary defaults, the initiation of bankruptcy or insolvency proceedings, and the failure of the Company to meet certain financial covenants designated in its respective loan documents. The Company was in compliance with all financial covenants related to these lines of credit at June 30, 2007.

Long-term debt and lines of credit agreements contain various restrictive covenants requiring, among other things, minimum levels of net worth and maintenance of certain financial ratios. One of the covenants has the effect of restricting funds available for dividends to approximately $130.1 million, based on tangible net worth at June 30, 2007. As of June 30, 2007, the Company was in compliance with these covenants.

F. DIVIDENDS

The Company paid cash dividends of $0.165 for each share of Class A Common Stock and $0.15 for each share of Class B Common Stock on April 26, 2007, January 30, 2007 and October 26, 2006 to stockholders of record on April 12, 2007, January 16, 2007 and October 12, 2006, respectively.

G. COMMON STOCK AND CALCULATION OF EARNINGS PER COMMON SHARE

The Company has two classes of common stock: Class A which is publicly traded, and Class B, which has no public market. The Class B Common Stock has restrictions on transfer; however, each share is convertible into one share of Class A Common Stock at any time. During the nine months ended June 30, 2007, 156,923 shares of Class B Common Stock were converted to Class A Common Stock, including 125,000 shares of Class B Common Stock owned by the Ingles Investment/Profit Sharing Plan (the Plan). The Plan then sold the Class A Common Stock to meet distribution and asset diversification requests from Plan participants. Each share of Class A Common Stock has one vote per share and each share of Class B Common Stock has ten votes per share. Each share of Class A Common Stock is entitled to receive cash dividends equal to 110% of any cash dividend paid on Class B Common Stock.

The Company has determined that, under Emerging Issues Task Force (EITF) Issue 03-6, Participating Securities and the Two-Class Method under FASB Statement No. 128, Earnings per Share, the two-class method of computing earnings per share is required.

The two-class method of computing basic earnings per share for each period reflects the cash dividends paid per share for each class of stock, plus the amount of allocated undistributed earnings per share computed using the participation percentage which reflects the dividend rights of each class of stock. Diluted earnings per share is calculated assuming the exercise of dilutive stock options outstanding and the conversion of all shares of Class B Common Stock to shares of Class A Common Stock on a share-for-share basis. The tables below reconcile the numerators and denominators of basic and diluted earnings per share for current periods.

	THREE MONTHS ENDED JUNE 30, 2007		NINE MONTHS ENDED JUNE 30, 2007	
	CLASS A	CLASS B	CLASS A	CLASS B
Numerator: Allocated net income				
Net income allocated, basic	$ 10,412,733	$ 9,333,161	$ 23,283,816	$ 21,136,407
Conversion of Class B to Class A shares	9,332,311		21,134,423	
Effect of assumed stock options exercised on allocated net income	850	(850)	1,984	(1,984)
Net income allocated, diluted	$ 19,745,894	$ 9,332,311	$ 44,420,223	$ 21,134,423

Denominator: Weighted average shares outstanding				
Weighted average shares outstanding, basic	12,342,335	12,167,761	12,255,288	12,247,610
Conversion of Class B to Class A shares	12,167,761		12,247,610	
Assumed stock options exercised	2,652		2,614	
Weighted average shares outstanding, diluted	24,512,748	12,167,761	24,505,512	12,247,610
Earnings per share				
Basic	$ 0.84	$ 0.77	$ 1.90	$ 1.73
Diluted	$ 0.81	$ 0.77	$ 1.81	$ 1.73

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The per share amounts for the third quarter of fiscal 2006 and the nine months ended June 24, 2006 are based on the following amounts:

	THREE MONTHS ENDED JUNE 24, 2006		NINE MONTHS ENDED JUNE 24, 2006	
	CLASS A	**CLASS B**	**CLASS A**	**CLASS B**
Numerator: Allocated net income				
Net income allocated, basic	$ 7,206,366	$ 6,635,603	$ 16,128,524	$ 14,924,900
Conversion of Class B to Class A shares	6,634,395		14,918,417	
Effect of assumed stock options exercised on allocated net income	1,208	(1,208)	6,483	(6,483)
Net income allocated, diluted	$ 13,841,969	$ 6,634,395	$ 31,053,424	$ 14,918,417
Denominator: Weighted average shares outstanding				
Weighted average shares outstanding, basic	12,169,462	12,324,944	12,123,493	12,346,868
Conversion of Class B to Class A shares	12,324,944		12,346,868	
Assumed stock options exercised	5,901		5,402	
Weighted average shares outstanding, diluted	24,500,307	12,324,944	24,475,763	12,346,868
Earnings per share				
Basic	$ 0.59	$ 0.54	$ 1.33	$ 1.21
Diluted	$ 0.57	$ 0.54	$ 1.27	$ 1.21

H. LINES OF BUSINESS

The Company operates three lines of business: retail grocery sales, shopping center rentals, and a fluid dairy processing plant. All of the Company s operations are domestic. Information about the Company s operations by lines of business (in thousands) is as follows:

	THREE MONTHS ENDED		NINE MONTHS ENDED	
	JUNE 30, 2007	**JUNE 24, 2006**	**JUNE 30, 2007**	**JUNE 24, 2006**
Revenues from unaffiliated customers:				
Grocery sales	**$ 706,908**	$ 632,196	**$ 2,017,341**	$ 1,807,174
Shopping center rentals	**3,193**	3,244	**9,586**	9,613
Fluid dairy	**31,787**	27,016	**88,217**	82,081
Total revenues from unaffiliated customers	**$ 741,888**	$ 662,456	**$ 2,115,144**	$ 1,898,868
Income from operations:				
Grocery sales	**$ 30,085**	$ 29,047	**$ 79,188**	$ 73,409
Shopping center rentals	**1,248**	1,432	**3,552**	4,017
Fluid dairy	**3,357**	2,981	**9,722**	8,199
Total income from operations	**$ 34,690**	$ 33,460	**$ 92,462**	$ 85,625

	JUNE 30, 2007	SEPTEMBER 30, 2006
Assets:		
Grocery sales	**$ 989,983**	$ 927,510
Shopping center rentals	**120,626**	121,083
Fluid dairy	**27,777**	28,125
Elimination of intercompany receivable	**(2,137)**	(1,744)
Total assets	**$ 1,136,249**	$ 1,074,974

Revenue from shopping center rentals is reported on the rental income, net line of the income statements. The other revenues comprise the net sales reported.

For the three-month periods ended June 30, 2007 and June 24, 2006, respectively, the fluid dairy segment had $14.1 million and $11.9 million in sales to the grocery sales segment. The fluid dairy segment had $40.3 million and $36.4 million in sales to the grocery sales segment for the nine-month periods ended June 30, 2007 and June 24, 2006, respectively. These sales have been eliminated in consolidation and are excluded from the amounts in the table above.

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I. TAX CONTINGENCY SETTLEMENT

During the quarter ended March 31, 2007 the Company settled a tax position under an initiative offered by one of the states in which the Company conducts its operations. As a result of this settlement, the Company reduced its reserve for contingent income tax liabilities by $3.2 million. This reduction is reflected as a reduction of income tax expense for the nine-month period ended June 30, 2007. Without this reduction, the effective tax rate would have been 38.2% for the nine months ended June 30, 2007.

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

Overview

Ingles, a leading supermarket chain in the Southeast, operates 196 supermarkets in Georgia (73), North Carolina (65), South Carolina (35), Tennessee (20), Virginia (2) and Alabama (1). The Company locates its supermarkets primarily in suburban areas, small towns and rural communities. Ingles supermarkets offer customers a wide variety of nationally advertised food products, including grocery, meat and dairy products, produce, frozen foods and other perishables and non-food products, including health and beauty care products and general merchandise, as well as quality private label items. In addition, the Company focuses on selling high-growth, high-margin products to its customers through the development of book sections, media centers, floral departments, premium coffee kiosks, certified organic products, bakery departments and prepared foods including delicatessen sections. During fiscal 2000, the Company began adding fuel centers and pharmacies at select store locations. As of June 30, 2007, the Company operated 49 in-store pharmacies and 42 fuel centers.

Ingles also operates two other lines of business, fluid dairy processing and shopping center rentals. The fluid dairy processing segment sells approximately 31% of its products to the retail grocery segment and approximately 69% of its products to third parties. Real estate ownership (including the shopping center rental segment) is an important component of the Company s operations, providing both operational and economic benefit.

Critical Accounting Policies

Critical accounting policies are those accounting policies that management believes are important to the portrayal of Ingles financial condition and results of operations, and require management s most difficult, subjective or complex judgments, often as a result of the need to make estimates about the effect of matters that are inherently uncertain.

Self-Insurance

The Company is self-insured for workers compensation and group medical and dental benefits. Risks and uncertainties are associated with self-insurance; however, the Company has limited its exposure by maintaining excess liability coverage. Self-insurance liabilities are established based on claims filed and estimates of claims incurred but not reported. The estimates are based on data provided by the respective claims administrators. The majority of the Company s properties are self-insured for casualty losses and business interruption; however, liability coverage is maintained.

Asset Impairments

The Company accounts for the impairment of long-lived assets in accordance with Statement of Financial Accounting Standards No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets. For assets to be held and used, the Company tests for impairment using undiscounted cash flows and calculates the amount of impairment using discounted cash flows. For assets held for sale, impairment is recognized based on the excess of remaining book value over expected recovery value. The recovery value is the fair value as determined by independent quotes or expected sales prices developed by internal associates. Estimates of future cash flows and expected sales prices are judgments based upon the Company s experience and knowledge of local operations and cash flows that are projected for several years into the future. These estimates can fluctuate significantly due to changes in real estate market conditions, the economic environment, capital spending decisions and inflation. The Company monitors the carrying value of long-lived assets for potential impairment each quarter based on whether any indicators of impairment have occurred.

Closed Store Accrual

For properties closed prior to December 31, 2002 that were under long-term lease agreements, the present value of any remaining liability under the lease, discounted using risk-free rates and net of expected sublease recovery, is recognized as a liability and expensed. For all store closures subsequent to the adoption of Statement of Financial Accounting Standards No. 146, Accounting for Costs Associated with Exit or Disposal Activities, effective December 31, 2002, the liability is recognized and expensed based on the difference between the present value of any remaining liability under the lease and the present value of the estimated market rate at which the Company expects to be able to sublease the properties. The Company s estimates of market rates are based on its experience, knowledge and typical third-party advice or market data. If the real estate and leasing markets change, sublease recovery could vary significantly from the recoveries originally assumed, resulting in a material change in the Company s recorded liability. The closed store accrual is included in accrued expenses on the consolidated balance sheet.

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Vendor Allowances

The Company receives funds for a variety of merchandising activities from the many vendors whose products the Company buys for resale in its stores. These incentives and allowances are primarily comprised of volume or purchase based incentives, advertising allowances, slotting fees, and promotional discounts. The purpose of these incentives and allowances is generally to help defray the costs incurred by the Company for stocking, advertising, promoting and selling the vendor s products. These allowances generally relate to short term arrangements with vendors, often relating to a period of a month or less, and are negotiated on a purchase-by-purchase or transaction-by-transaction basis. Whenever possible, vendor discounts and allowances that relate to buying and merchandising activities are recorded as a component of item cost in inventory and recognized in merchandise costs when the item is sold. Due to system constraints and the nature of certain allowances, it is sometimes not practicable to apply allowances to the item cost of inventory. In those instances, the allowances are applied as a reduction of merchandise costs using a rational and systematic methodology, which results in the recognition of these incentives when the inventory related to the initial purchase is sold. Vendor allowances applied as a reduction of merchandise costs totaled $23.3 million and $22.3 million for the fiscal quarters ended June 30, 2007 and June 24, 2006, respectively. For the nine-month periods ended June 30, 2007 and June 24, 2006, vendor allowances applied as a reduction of merchandise costs totaled $69.1 million and $68.5 million, respectively. Vendor advertising allowances that represent a reimbursement of specific identifiable incremental costs of advertising the vendor s specific products are recorded as a reduction to the related expense in the period that the related expense is incurred. Vendor advertising allowances recorded as a reduction of advertising expense totaled $2.8 million and $2.9 million for the fiscal quarters ended June 30, 2007 and June 24, 2006, respectively. For the nine-month periods ended June 30, 2007 and June 24, 2006, vendor advertising allowances recorded as a reduction of advertising expense totaled $7.6 million and $7.5 million, respectively.

Tax Contingencies

Despite the Company s belief that its tax positions are consistent with applicable tax laws, the Company believes that certain positions it has taken are likely to be challenged by taxing authorities. Settlement of any challenge may result in no change, a complete disallowance, or some partial adjustment reached through negotiations or litigation. Significant judgment is required in evaluating the Company s tax contingencies. The Company s contingencies are adjusted in light of changing facts and circumstances, such as the progress of its tax audits as well as evolving case law. Income tax expense includes the impact of contingency provisions and changes to contingencies that the Company considers appropriate. Unfavorable settlement of any particular issue would require use of cash. Favorable resolution would be recognized as a reduction to income tax expense at the time of resolution.

During the quarter ended March 31, 2007 the Company settled a tax position under an initiative offered by one of the states in which the Company conducts its operations. As a result of this settlement, the Company reduced its reserve for contingent income tax liabilities by $3.2 million. This reduction is reflected as a reduction of income tax expense for the nine-month period ended June 30, 2007.

Results of Operations

Ingles operates on a 52 or 53-week fiscal year ending on the last Saturday in September. There are 13 and 39 weeks of operations included in the unaudited condensed consolidated statements of income for the three and nine-month periods ended June 30, 2007 and June 24, 2006. Comparable store sales are defined as sales by grocery stores in operation for the entire duration of the previous and current fiscal periods. Sales from replacement stores, major remodels, minor remodels and the addition of fuel stations to existing stores are included in the comparable store sales calculation from the date thereof. A replacement store is a new store that is opened to replace an existing nearby store that is closed. A major remodel entails substantial remodeling of an existing store and may include additional retail square footage. A minor remodel includes repainting, remodeling and updating the lighting and equipment throughout an existing store. For the three and nine-month periods ended June 30, 2007 and June 24, 2006, comparable store sales include 194 stores.

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The following table sets forth, for the periods indicated, selected financial information as a percentage of net sales. For information regarding the various segments of the business, see Note H Lines of Business to the Unaudited Consolidated Financial Statements.

	THREE MONTHS ENDED		NINE MONTHS ENDED	
	JUNE 30, 2007	JUNE 24, 2006	JUNE 30, 2007	JUNE 24, 2006
Net sales	**100.0%**	100.0%	**100.0%**	100.0%
Gross profit	**23.7%**	24.9%	**24.0%**	25.1%
Operating and administrative expenses	**19.2%**	20.0%	**19.8%**	20.8%
Rental income, net	**0.2%**	0.2%	**0.2%**	0.2%
Income from operations	**4.7%**	5.1%	**4.4%**	4.5%
Other income, net	**1.2%**	0.1%	**0.4%**	0.1%
Interest expense	**1.6%**	1.9%	**1.7%**	2.0%
Income taxes	**1.6%**	1.2%	**1.0%**	1.0%
Net income	**2.7%**	2.1%	**2.1%**	1.6%

Three Months Ended June 30, 2007 Compared to the Three Months Ended June 24, 2006

Net income for the third quarter of fiscal 2007 totaled $19.7 million, 42.6% higher than net income of $13.8 million earned for the third quarter of fiscal 2006. Total and comparable store sales increases were strong and gross profit dollars grew despite a decrease in gross profit as a percentage of sales. During the current quarter, the Company also sold a shopping center in which it no longer operated a store and recognized an after-tax gain of approximately $4.9 million.

Net Sales. Net sales increased 12.1% to $738.7 million for the three months ended June 30, 2007 from $659.2 million for the three months ended June 24, 2006. Ingles operated 196 stores at June 30, 2007, compared to 197 stores at June 24, 2006. Retail square footage was approximately 9.6 million at June 30, 2007 and at June 24, 2006. Sales improved in each department except video, with the largest percentage increases in the gasoline, produce, deli and bakery departments. The Company operated eight additional fuel centers at June 30, 2007 compared to June 24, 2006. Produce sales increased due to increased customer demand for fresh and organic produce and due to general increases in the cost of produce. Increases in the Company s deli and bakery departments reflect its customers desire for convenience and quality in prepared foods.

Grocery segment comparable store sales grew $74.7 million, or 11.9%, in the third quarter of fiscal 2007 compared to the third quarter of fiscal 2006. Excluding gasoline sales, comparable store sales increased $53.3 million, or 9.4%, for the three months ended June 30, 2007. Total gasoline gallons sold increased approximately 27% while the average price per gas gallon was approximately 16 cents higher comparing the June fiscal 2007 quarter to the same period of fiscal 2006.

Changes in grocery segment sales for the quarter ended June 30, 2007 are summarized as follows (dollars in thousands):

Total grocery sales for the three months ended June 24, 2006	**$ 632,196**
Comparable store sales increase (including gasoline)	**74,715**
Impact of stores opened in fiscal 2006 and 2007	**2,110**
Impact of stores closed in fiscal 2006 and 2007	**(2,192)**
Other	**79**
Total grocery sales for the three months ended June 30, 2007	**$ 706,908**

Net sales to outside parties for the Company s milk processing subsidiary increased $4.8 million or 17.7% in the June 2007 quarter compared to the June 2006 quarter. The sales increase is primarily attributable to a sharp increase in raw milk costs, which are generally passed on to customers in the pricing of milk products. Sales volume growth in gallons was approximately 1%.

Gross Profit. Gross profit for the three-month period ended June 30, 2007 increased $11.0 million or 6.7% to $175.2 million, or 23.7% of sales, compared to $164.2 million, or 24.9% of sales, for the three-month period ended June 24, 2006.

The increase in grocery segment gross profit dollars was primarily due to the higher sales volume. Grocery segment gross profit as a percentage of total sales was lower for the June 2007 quarter due primarily to higher relative sales growth in the gasoline department that has lower gross margins. Excluding gasoline sales, grocery segment gross profit as a percentage of sales was 26.6% for the three months ended June 30, 2007 compared to 27.2% for the same quarter of last fiscal year. Increased competitive pressures and food cost increases also contributed to lower grocery segment margins. The Company elected to accept lower margins in order to increase sales, maintain market share and keep prices low for its customers.

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Gross profit for the Company s milk processing subsidiary for the June 2007 quarter increased $0.4 million or 7.2% to $6.0 million, or 13.1% of sales, compared to $5.6 million, or 14.4% of sales for the June 2006 quarter. Per gallon margins were somewhat level, resulting in a lower gross profit as a percentage of sales as the sales price per gallon increased.

In addition to the direct product cost, the cost of goods sold line item for the grocery segment includes inbound freight charges. The milk processing segment is a manufacturing process; therefore, the costs mentioned above as well as purchasing and receiving costs, production costs, inspection costs, warehousing costs, internal transfer costs, and other costs of distribution incurred by the milk processing segment are included in the cost of sales line item, while these items are included in operating and administrative expenses by the grocery segment.

The Company s gross margins may not be comparable to those of other retailers, since some retailers include all of the costs related to their distribution network in cost of goods sold and others, like the Company, exclude a portion of the costs from gross profit, including the costs instead in a line item such as operating and administrative expenses.

Operating and Administrative Expenses. Operating and administrative expenses increased $9.6 million or 7.3% to $141.8 million for the three months ended June 30, 2007, from $132.2 million for the three months ended June 24, 2006. As a percentage of sales, operating and administrative expenses decreased to 19.2% for the three months ended June 30, 2007 compared to 20.0% for the three months ended June 24, 2006.

A breakdown of the major increases (decreases) in operating and administrative expenses is as follows:

	Increase (decrease) in millions	Increase (decrease) as a % of sales
Salaries and wages	$ 5.3	(0.22)%
Insurance	$ 1.2	0.08 %
Building and land rent expense	$ (1.1)	(0.23)%
Utilities and fuel	$ 0.7	(0.06)%
Warehouse expense	$ 0.7	(0.04)%
Store supplies	$ 0.5	(0.02)%

Salaries and wages increased in dollars due to additional labor hours required for the increased sales volume, but decreased slightly as a percentage of sales due to the allocation of management salaries over higher sales dollars and sales growth in less labor-intensive departments, such as gasoline.

Insurance expense increased due to a higher level of employee health insurance and workers compensation claims.

Building and land rent expense decreased due to the expiration, cancellation or sublease of lease obligations on former store properties.

Utility and fuel expenses increased due to increases in market energy prices.

Warehouse expense increased due to additional labor costs needed to process increased volume of both incoming and outgoing product shipments and due to additional depreciation expense on replacement vehicles in the Company s delivery fleet.

Store supplies increased due to upgraded packaging used in perishables departments and the higher cost of plastic used in bags and wrapping materials.

Rental Income, Net. Rental income, net decreased $0.2 million to $1.2 million for the June 2007 quarter from $1.4 million for the June 2006 quarter due to a decrease in gross rental income and an increase in shopping center expenses.

Other Income, Net. Other income, net totaled $8.5 million for the three-month period ended June 30, 2007, including a pre-tax gain of approximately $7.9 million on the sale of a shopping center in which the Company no longer operated a store. Other income totaled $0.4 million for the three-month period ended June 24, 2006.

Interest Expense. Interest expense decreased $0.3 million for the three-month period ended June 30, 2007 to $11.9 million from $12.2 million for the three-month period ended June 24, 2006. Total debt at June 2007 was $550.6 million compared to $555.4 million at June 2006.

Income Taxes. Income tax expense as a percentage of pre-tax income increased to 36.9% in the June 2007 quarter compared to 36.3% in the June 2006 quarter due to lower amounts of tax exempt interest income and lower deductions related to the exercise of employee stock options.

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Net Income. Net income increased $5.9 million or 42.6% for the three-month period ended June 30, 2007 to $19.7 million compared to $13.8 million for the three-month period ended June 24, 2006. Net income, as a percentage of sales, was 2.7% for the June 2007 quarter and 2.1% for the June 2006 quarter. The increase in net income is attributed to the gain on sale on the former store property, increased sales and gross profit, and a decrease in expenses as a percentage of sales. Basic and diluted earnings per share for Class A Common Stock were $0.84 and $0.81 for the June 2007 quarter compared to $0.59 and $0.57, respectively, for the June 2006 quarter. Basic and diluted earnings per share for Class B Common Stock were each $0.77 for the June 2007 quarter compared to $0.54 for the June 2006 quarter.

Nine Months Ended June 30, 2007 Compared to the Nine Months Ended June 24, 2006

Net income for the first nine months of fiscal 2007 totaled $44.4 million, 43.0% higher than net income of $31.1 million earned for the first nine months of fiscal 2006. The $44.4 million of nine-month net income exceeds total net income of $42.6 million for the entire fiscal year ended September, 2006. Total and comparable store sales increases were strong and gross profit dollars grew despite a decrease in gross profit as a percentage of sales. Gross profit dollar growth exceeded operating expense growth by approximately $7.3 million. Settlement of a state income tax position during the second quarter of fiscal 2007 and the previously disclosed property gain during the third quarter of fiscal 2007 also contributed to increased net income.

Net Sales. Net sales for the nine months ended June 30, 2007 increased 11.5% to $2.11 billion, compared to $1.89 billion for the nine months ended June 24, 2006. Sales improved in each department except video, with the largest percentage increases in the gasoline, pharmacy, and deli departments, as noted above in the three-month discussion. Pharmacy revenues increased due to an increase in the number of prescriptions.

Grocery segment comparable store sales for the period grew $208.4 million, or 11.6%. Excluding gasoline sales, comparable store sales increased $142.4 million, or 8.6%, for the nine months ended June 30, 2007. Total gasoline gallons sold increased approximately 50% while the average price per gallon was somewhat level comparing the June fiscal 2007 nine months to the same period of fiscal 2006.

Changes in grocery segment sales for the nine months ended June 30, 2007 can be summarized as follows (dollars in thousands):

Total grocery sales for the nine months ended June 24, 2006	**$ 1,807,174**
Comparable store sales increase (including gasoline)	**208,351**
Impact of stores opened in fiscal 2006 and 2007	**6,633**
Impact of stores closed in fiscal 2006 and 2007	**(5,235)**
Other	**418**
Total grocery sales for the nine months ended June 30, 2007	**$ 2,017,341**

Net sales to outside parties for the Company s milk processing subsidiary increased $6.1 million or 7.5% in the June 2007 nine-month period compared to the June 2006 nine-month period. The increase is attributable to both volume growth and the increase in the price of raw milk which began during the third quarter of fiscal year 2007.

The Company expects continued weekly sales growth for the remainder of fiscal year 2007 to approximate sales growth achieved during the first three quarters of the current fiscal year. The Company s fourth fiscal 2007 quarter will have 13 weeks compared to 14 weeks in the fourth quarter of fiscal 2006.

Gross Profit. Gross profit for the nine months ended June 30, 2007 increased $32.4 million or 6.8% to $506.7 million compared to $474.3 million, for the nine months ended June 24, 2006. As a percentage of sales, gross profit decreased to 24.1% for the nine months ended June 30, 2007 from 25.1% for the nine months ended June 24, 2006.

The increase in grocery segment gross profit dollars was primarily due to the higher sales volume. Grocery segment gross profit as a percentage of total sales was lower for the June 2007 nine month period due primarily to higher sales growth in the gasoline and pharmacy departments. These departments generally have lower gross margins. Excluding gasoline sales, grocery segment gross profit as a percentage of sales was 26.7% for the nine months ended June 30, 2007 compared to 27.0% for the same period of last fiscal year. Increased competitive pressures and food cost increases also contributed to lower grocery segment margins. The Company elected to accept lower margins in order to increase sales, maintain market share and keep prices low for its customers.

Gross profit for the Company s milk processing subsidiary increased $2.2 million or 14.3% for the June 2007 nine-month period compared to the June 2006 nine-month period. Gross profit dollars increased due to higher case sales volume and increases per gallon margins during the first six months of fiscal 2007.

Operating and Administrative Expenses. Operating and administrative expenses increased $25.1 million or 6.4% to $417.7 million for the nine months ended June 30, 2007, from $392.6 million for the nine months ended June 24, 2006. As a percentage of sales, operating and administrative expenses decreased to 19.8% for the June 2007 nine-month period from 20.8% for the same period last year.

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A breakdown of the major increases (decreases) in operating and administrative expenses is as follows:

	Increase (decrease) in millions	Increase (decrease) as a % of sales
Salaries and wages	$ 14.8	(0.21)%
Equipment rent expense	$ (2.3)	(0.12)%
Warehouse expense	$ 2.3	(0.03)%
Repairs and maintenance	$ 2.2	(0.01)%
Bank charges	$ 1.8	0.02 %
Building and land rent expense	$ (1.8)	(0.16)%

Salaries and wages increased in dollars due to additional labor hours required for the increased sales volume, but decreased slightly as a percentage of sales due to the allocation of management salaries over higher sales dollars and sales growth in less labor-intensive departments, such as gasoline.

Equipment rent expense decreased due to the expiration of operating leases on equipment used in the Company s distribution facility and in its stores. Much of this equipment was purchased by the Company at the expiration of the lease term.

Warehouse expenses increased due to additional labor costs needed to process increased volume of both incoming and outgoing product shipments.

Repairs and maintenance increased due to the replacement and upgrade of refrigeration equipment, product display and other store fixtures.

Bank charges rose primarily due to increased fees for processing debit and credit cards. The increase is a result of both increased usage of cards and increased transaction fees related to the usage.

Building and land rent expense decreased due to the expiration, cancellation or sublease of lease obligations on former store properties.

Rental Income, Net. Rental income, net decreased $0.5 million to $3.5 million in the June 2007 nine-month period from $4.0 million in the June 2006 comparable period due to a decrease in gross rental income and an increase in shopping center expenses.

Other Income, Net. Other income, net totaled $9.3 million for the nine-month period ended June 30, 2007, including a pre-tax gain of approximately $7.9 million on the sale of a shopping center in which the Company no longer operated a store. Increased sales of waste paper and packaging also contributed to the increase.

Interest Expense. Interest expense decreased $0.9 million to $35.8 million for the nine months ended June 30, 2007 from $36.7 million for the nine months ended June 24, 2006. Principal repayments on higher-rate mortgage debt totaled $26.9 million for the nine months ended June 30, 2007, somewhat offset by net borrowings under line of credit agreements totaling $21.2 million for the same period.

Income Taxes. Income tax expense as a percentage of pre-tax income was 32.7% in the June 2007 nine-month period compared to 38.1% in the June 2006 nine-month period. During the second quarter of fiscal 2007, the Company settled a tax position under an initiative offered by one of the states in which the Company conducts its operations. As a result of this settlement the Company reduced its reserve for contingent income taxes by $3.2 million and reduced income tax expense by the same amount during that quarter. Without this reduction, the effective tax rate would have been 38.2% for the nine months ended June 30, 2007.

Net Income. Net income increased $13.3 million or 43.0% for the nine-month period ended June 30, 2007 to $44.4 million compared to $31.1 million for the nine-month period ended June 24, 2006. Net income, as a percentage of sales, was 2.1% for the June 2007 nine-month period and 1.6% for the June 2006 nine-month period. Basic and diluted earnings per share for Class A Common Stock were $1.90 and $1.81 for the nine months ended June 2007 compared to $1.33 and $1.27, respectively, for the nine months ended June 2006. Basic and diluted earnings per share for Class B Common Stock were each $1.73 for the nine months ended June 2007 compared to $1.21 of basic and diluted earnings per share for the nine months ended June 2006.

Liquidity and Capital Resources

Capital Expenditures

The Company believes that a key to its ability to continue to develop a loyal customer base is providing conveniently located, clean and modern stores which provide customers with good service and a broad selection of competitively priced products. As such, the

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Company has invested and will continue to invest significant amounts of capital toward the modernization of its store base. The Company s modernization program includes the opening of new stores, the completion of major remodels and expansion of selected existing stores, the relocation of selected existing stores to larger, more convenient locations and the completion of minor remodeling of its remaining existing stores. The Company will also add fuel centers and other products complementary to grocery sales where market conditions and real estate considerations warrant.

Capital expenditures totaled $96.4 million for the nine-month period ended June 30, 2007, including the completion of one new store, two remodeled stores, one replacement store, one convenience store/fuel center, and the purchase of 11 land parcels for future store and distribution development. In addition, the Company added three pharmacies and six fuel centers either in conjunction with the store development mentioned above or to existing locations. Capital expenditures also included the costs of upgrading and replacing store equipment, technology investments, capital expenditures related to the Company s distribution operation and its milk processing plant, and expenditures for stores to open later in fiscal 2007 and in fiscal 2008.

Ingles capital expenditure plans for all of fiscal 2007 include investments of approximately $120 million. For the balance of fiscal 2007, the Company plans to complete one owned remodeled store, one new owned store, one leased replacement store and purchase two sites for future store and fluid dairy expansion. Expenditure plans also include the addition of two fuel stations and one pharmacy to existing stores. Further expenditures include investments in stores expected to open in fiscal 2008 as well as technology improvements, upgrading and replacing existing store equipment and warehouse and transportation equipment, and improvements to the Company s milk processing plant.

The Company expects that its net annual capital expenditures will remain in the range of approximately $100 to $110 million going forward in order to maintain a modern store base. The number of projects may fluctuate due to the varying costs of the types of projects pursued including new stores, major remodel/expansions or minor remodels. The Company makes decisions on the allocation of capital expenditure dollars based on many factors including the competitive environment, other Company capital initiatives and its financial condition.

The Company does not generally enter into commitments for capital expenditures other than on a store-by-store basis at the time it begins construction on a new store or begins a major or minor remodeling project. The Company generally engages in major remodeling and new store development on not more than three or four locations at a time. Construction commitments at June 30, 2007 totaled $31.1 million.

Liquidity

The Company generated net cash from operations of $99.0 million in the June 2007 nine-month period compared to $62.7 million for the comparable 2006 period. In addition to the $13.4 million increase in net income over the comparative nine-month periods, inventory increased $16.2 million during the nine months ended June 30, 2007 to support increased growth.

Cash used by investing activities for the June 2007 nine-month period totaled $82.3 million comprised primarily of $96.4 million of capital expenditures during the period, partially offset by $14.1 million of proceeds from the sale of assets.

Cash used by financing activities during the June 2007 nine-month period totaled $17.0 million including principal payments on long-term debt of $26.9 million and dividend payments of $11.6 million offset primarily by net borrowings under committed lines of credit totaling $21.2 million.

At June 30, 2007, the Company had committed lines of credit with six banks totaling $150.0 million. $25.1 million was borrowed under the lines of credit at June 30, 2007; in addition, unused letters of credit totaling $21.3 million reduced the amount available to be drawn under these lines to $103.6 million at June 30, 2007. The lines of credit mature in October 2007 and February 2010. The lines provide the Company with various interest rate options generally at rates less than prime. The Company is not required to maintain compensating balances in connection with these lines of credit. The Company was in compliance with all financial covenants related to these lines of credit at June 30, 2007.

At June 30, 2007, the Company had $349.8 million principal amount of senior subordinated notes (the Notes) outstanding to mature in December 2011. The indenture governing the Notes contains certain restrictive covenants relating to, among other things, the issuance of indebtedness and the payment of dividends. The Notes are currently redeemable by the Company at a redemption premium of 104.438%. The redemption premium decreases to 102.903% on December 1, 2007 and to 101.369% on December 1, 2008. Beginning December 1, 2009 the Notes can be redeemed at par. The Company was in compliance with all financial covenants related to the Notes at June 30, 2007.

The Company s long term debt agreements generally have cross-default provisions which could result in the acceleration of payments due under the Company s lines of credit and Notes indenture in the event of default under any one instrument.

The Company s principal sources of liquidity are expected to be cash flow from operations, borrowings under its lines of credit and long-term financing. As of June 30, 2007, the Company had unencumbered real property and equipment with a net book value of approximately $555.0 million. The Company believes, based on its current results of operations and financial condition, that its

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financial resources, including existing bank lines of credit, short- and long-term financing expected to be available to it and internally generated funds, will be sufficient to meet planned capital expenditures and working capital requirements for the foreseeable future, including any debt service requirements of additional borrowings. However, such sources of financing may not be available to the Company on acceptable terms, or at all.

It is possible that, in the future, the Company s results of operations and financial condition will be different from that described in this report based on a number of intangible factors. These factors may include, among others, increased competition, changing regional and national economic conditions, adverse climatic conditions affecting food production and delivery and changing demographics as well as the additional factors discussed below under Forward Looking Statements. It is also possible, for such reasons, that the results of operations from the new, expanded, remodeled and/or replacement stores will not meet or exceed the results of operations from existing stores that are described in this report.

Contractual Obligations and Commercial Commitments

There have been no material changes in contractual obligations and commercial commitments subsequent to September 30, 2006.

Off Balance Sheet Arrangements

The Company is not a party to any off-balance sheet arrangements that have, or are reasonably likely to have, a current or future material effect on the Company s financial condition, revenues, expenses, results of operations, liquidity, capital expenditures or capital resources.

Quarterly Cash Dividends

Since December 27, 1993, the Company has paid regular quarterly cash dividends of $0.165 (sixteen and one-half cents) per share on its Class A Common Stock and $0.15 (fifteen cents) per share on its Class B Common Stock for an annual rate of $0.66 and $0.60 per share, respectively.

The Company expects to continue paying regular cash dividends on a quarterly basis. However, the Board of Directors periodically reconsiders the declaration of dividends. The Company pays these dividends at the discretion of the Board of Directors and the continuation of these payments, the amount of such dividends, and the form in which the dividends are paid (cash or stock) depends upon the results of operations, the financial condition of the Company and other factors which the Board of Directors deems relevant. In addition, certain loan agreements containing provisions outlining minimum tangible net worth requirements restrict the ability of the Company to pay additional dividends to approximately $130.1 million based on tangible net worth at June 30, 2007. Further, the Company is prevented from declaring dividends at any time that it is in default under the indenture governing the Notes. In addition, the terms of the indenture may restrict the ability of the Company to pay additional dividends based on certain financial parameters.

Seasonality

Sales in the grocery segment of the Company s business are subject to a slight seasonal variance due to holiday related sales and due to sales in areas where seasonal homes are located. Sales are traditionally higher in the Company s first fiscal quarter due to the inclusion of sales related to Thanksgiving and Christmas. The Company s second fiscal quarter traditionally has the lowest sales of the year. In the third and fourth quarter, sales are affected by the return of customers to seasonal homes in our market area. The fluid dairy segment of the Company s business has slight seasonal variation to the extent of its sales into the grocery industry. The Company s real estate segment is not subject to seasonal variations.

Impact of Inflation

The following table from the United States Bureau of Labor Statistics lists annualized changes in the Consumer Price Index that could have an effect on the Company s operations. One of the Company s significant costs is labor, which increases with general inflation. Inflation in energy costs affects both the Company s gasoline sales and distribution expenses.

	THREE MONTHS ENDED		TWELVE MONTHS ENDED	
	JUNE 30, 2007	JUNE 24, 2006	JUNE 30, 2007	JUNE 24, 2006
All items	**5.2%**	5.1%	**2.7%**	4.3%

Food and beverages	**4.9%**	1.9%	**4.0%**	2.2%
Energy	**32.9%**	23.8%	**4.6%**	23.3%

Forward Looking Statements

This Quarterly Report contains certain forward-looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934. The words expect, anticipate, intend, plan, believe, seek and similar expressions are intended to identify forward-looking statements. Whi forward-looking statements and the related assumptions are made in good faith and reflect

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the Company s current judgment regarding the direction of the Company s business, actual results will almost always vary, sometimes materially, from any estimates, predictions, projections, assumptions or other future performance suggested herein. Such statements are based upon a number of assumptions and estimates which are inherently subject to significant risks and uncertainties many of which are beyond the Company s control. Some of these assumptions inevitably will not materialize, and unanticipated events will occur which will affect the Company s results. Some important factors (but not necessarily all factors) that affect the Company s revenues, growth strategies, future profitability and operating results, or that otherwise could cause actual results to differ materially from those expressed in or implied by any forward-looking statement, include business and economic conditions generally in the Company s operating area; the Company s ability to successfully implement its expansion and operating strategies and to manage rapid expansion; pricing pressures and other competitive factors; the Company s ability to reduce costs and achieve improvements in operating results; the availability and terms of financing; increases in labor and utility costs; success or failure in the ownership and development of real estate; changes in the laws and government regulations applicable to the Company; and changes in accounting policies, standards, guidelines or principles as may be adopted by regulatory agencies as well as the Financial Accounting Standards Board.

Consequently, actual events affecting the Company and the impact of such events on the Company s operations may vary significantly from those described in this report or contemplated or implied by statements in this report.

Item 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

There have been no material changes in market interest rates subsequent to September 30, 2006.

Item 4. CONTROLS AND PROCEDURES

The Company maintains disclosure controls and procedures designed to provide reasonable assurance of achieving the objective that information in its Exchange Act reports is recorded, processed, summarized and reported within the time periods specified and pursuant to the regulations of the Securities and Exchange Commission. Disclosure controls and procedures, as defined in Rule 13a-15(e) and 15d-15(e) under the Exchange Act, include controls and procedures designed to ensure the information required to be disclosed by the Company in the reports it files or submits under the Exchange Act is accumulated and communicated to the Company s management, including its Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure. It should be noted that the Company s system of controls, however well designed and operated, can provide only reasonable, and not absolute, assurance that the objectives of the system are met.

As required by SEC Rule 13a-15(b), the Company carried out an evaluation, under the supervision and with participation of its management including its Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of its disclosure controls and procedures as of June 30, 2007, the end of the period covered by this report. In making this evaluation, it considered matters previously identified and disclosed in connection with the filing of its Form 10-K for fiscal 2006. After consideration of the matters discussed above, the Company has concluded that its controls and procedures were effective as of June 30, 2007.

(b) Changes in Internal Control over Financial Reporting

No other change in internal control over financial reporting occurred during the Company s last fiscal quarter that materially affected, or is reasonably likely to materially affect, the company s internal control over financial reporting.

Part II. OTHER INFORMATION

Item 6. EXHIBITS

(a) Exhibits.

1) Exhibit 31.1 Rule 13a-14(a) Certificate

2) Exhibit 31.2 Rule 13a-14(a) Certificate

3) Exhibit 32.1 Certification Pursuant to 18 U.S.C. Section 1350

4) Exhibit 32.2 Certification Pursuant to 18 U.S.C. Section 1350

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SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this Form 10-Q to be signed on its behalf by the undersigned thereunto duly authorized.

	INGLES MARKETS, INCORPORATED
Date: August 3, 2007	/s/ Robert P. Ingle Robert P. Ingle Chief Executive Officer
Date: August 3, 2007	/s/ Ronald B. Freeman Ronald B. Freeman Vice President-Finance and Chief Financial Officer