

INGLES MARKETS INC  
Form 10-Q  
January 29, 2010  
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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 December 26, 2009**

**..    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)**

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**North Carolina**  
(State or other jurisdiction of

incorporation or organization)

**56-0846267**  
(I.R.S. Employer

Identification No.)

**P.O. Box 6676, Asheville NC**  
(Address of principal executive offices)

**28816**  
(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 ☒ No ☐.

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

Large accelerated filer ☐ Accelerated filer ☒

Non-accelerated filer ☐ (Do not check if a smaller reporting company.) Smaller reporting company ☐

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or 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 shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ☐ No ☒.

As of January 25, 2010, the Registrant had 12,888,608 shares of Class A Common Stock, \$0.05 par value per share, outstanding and 11,623,651 shares of Class B Common Stock, \$0.05 par value per share, outstanding.

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**Table of Contents****Part I. Financial Information****Item 1. Interim Financial Statements****INGLES MARKETS, INCORPORATED AND SUBSIDIARIES****CONDENSED CONSOLIDATED BALANCE SHEETS (UNAUDITED)**

|                                                                                                                                                                           | DECEMBER 26,<br>2009 | SEPTEMBER<br>26,<br>2009 |
|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------|----------------------|--------------------------|
| <b>ASSETS</b>                                                                                                                                                             |                      |                          |
| Current Assets:                                                                                                                                                           |                      |                          |
| Cash and cash equivalents                                                                                                                                                 | \$ 50,177,486        | \$ 77,035,848            |
| Receivables-net                                                                                                                                                           | 60,364,326           | 50,401,639               |
| Inventories                                                                                                                                                               | 282,568,281          | 271,744,736              |
| Other current assets                                                                                                                                                      | 12,251,209           | 24,537,514               |
| Total Current Assets                                                                                                                                                      | 405,361,302          | 423,719,737              |
| Property and Equipment Net                                                                                                                                                | 1,070,209,095        | 1,072,937,349            |
| Other Assets                                                                                                                                                              | 21,263,301           | 20,951,979               |
| Total Assets                                                                                                                                                              | \$ 1,496,833,698     | \$ 1,517,609,065         |
| <b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>                                                                                                                               |                      |                          |
| Current Liabilities:                                                                                                                                                      |                      |                          |
| Current portion of long-term debt                                                                                                                                         | \$ 59,533,204        | \$ 31,314,776            |
| Accounts payable - trade                                                                                                                                                  | 124,893,757          | 118,378,264              |
| Accrued expenses and current portion of other long-term liabilities                                                                                                       | 57,605,217           | 78,868,836               |
| Total Current Liabilities                                                                                                                                                 | 242,032,178          | 228,561,876              |
| Deferred Income Taxes                                                                                                                                                     | 66,085,000           | 67,223,000               |
| Long-Term Debt                                                                                                                                                            | 782,209,364          | 817,999,569              |
| Other Long-Term Liabilities                                                                                                                                               | 6,196,673            | 5,660,664                |
| Total Liabilities                                                                                                                                                         | 1,096,523,215        | 1,119,445,109            |
| 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; 12,888,608 shares issued and outstanding at December 26, 2009 and at September 26, 2009                         | 644,430              | 644,430                  |
| Class B, convertible to Class A, \$0.05 par value; 100,000,000 shares authorized; 11,623,651 shares issued and outstanding at December 26, 2009 and at September 26, 2009 | 581,183              | 581,183                  |
| Paid-in capital in excess of par value                                                                                                                                    | 118,184,132          | 118,184,132              |
| Retained earnings                                                                                                                                                         | 280,900,738          | 278,754,211              |
| Total Stockholders' Equity                                                                                                                                                | 400,310,483          | 398,163,956              |
| Total Liabilities and Stockholders' Equity                                                                                                                                | \$ 1,496,833,698     | \$ 1,517,609,065         |

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See notes to unaudited interim financial statements.

**Table of Contents****INGLES MARKETS, INCORPORATED AND SUBSIDIARIES****CONDENSED CONSOLIDATED STATEMENTS OF INCOME (UNAUDITED)**

|                                       | <b>THREE MONTHS ENDED</b>    |                              |
|---------------------------------------|------------------------------|------------------------------|
|                                       | <b>DECEMBER 26,<br/>2009</b> | <b>DECEMBER 27,<br/>2008</b> |
| Net sales                             | <b>\$ 840,953,201</b>        | <b>\$ 804,864,666</b>        |
| Cost of goods sold                    | <b>655,692,544</b>           | <b>619,309,658</b>           |
| Gross profit                          | <b>185,260,657</b>           | <b>185,555,008</b>           |
| Operating and administrative expenses | <b>160,600,998</b>           | <b>156,290,930</b>           |
| Rental income, net                    | <b>273,710</b>               | <b>808,176</b>               |
| Loss from sale or disposal of assets  | <b>(200,024)</b>             | <b>(113,666)</b>             |
| Income from operations                | <b>24,733,345</b>            | <b>29,958,588</b>            |
| Other income, net                     | <b>853,554</b>               | <b>1,187,592</b>             |
| Interest expense                      | <b>16,150,889</b>            | <b>12,977,877</b>            |
| Income before income taxes            | <b>9,436,010</b>             | <b>18,168,303</b>            |
| Income taxes:                         |                              |                              |
| Current                               | <b>4,309,000</b>             | <b>6,963,000</b>             |
| Deferred                              | <b>(890,000)</b>             | <b>77,000</b>                |
|                                       | <b>3,419,000</b>             | <b>7,040,000</b>             |
| Net income                            | <b>\$ 6,017,010</b>          | <b>\$ 11,128,303</b>         |
| Per share amounts:                    |                              |                              |
| Class A Common Stock                  |                              |                              |
| Basic earnings per common share       | <b>\$ 0.26</b>               | <b>\$ 0.47</b>               |
| Diluted earnings per common share     | <b>\$ 0.25</b>               | <b>\$ 0.45</b>               |
| Class B Common Stock                  |                              |                              |
| Basic earnings per common share       | <b>\$ 0.23</b>               | <b>\$ 0.43</b>               |
| Diluted earnings per common share     | <b>\$ 0.23</b>               | <b>\$ 0.43</b>               |
| Cash dividends per common share:      |                              |                              |
| Class A Common Stock                  | <b>\$ 0.165</b>              | <b>\$ 0.165</b>              |
| Class B Common Stock                  | <b>\$ 0.150</b>              | <b>\$ 0.150</b>              |

See notes to unaudited interim financial statements.

**Table of Contents****INGLES MARKETS, INCORPORATED AND SUBSIDIARIES****CONDENSED CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY (UNAUDITED)****THREE MONTHS ENDED DECEMBER 26, 2009 AND DECEMBER 27, 2008**

|                                   | CLASS A<br>COMMON STOCK |                   | CLASS B<br>COMMON STOCK |                   | PAID-IN<br>CAPITAL IN<br>EXCESS OF<br>PAR VALUE | RETAINED<br>EARNINGS  | TOTAL                 |
|-----------------------------------|-------------------------|-------------------|-------------------------|-------------------|-------------------------------------------------|-----------------------|-----------------------|
|                                   | SHARES                  | AMOUNT            | SHARES                  | AMOUNT            |                                                 |                       |                       |
| Balance, September 27, 2008       | 12,818,608              | \$ 640,930        | 11,693,651              | \$ 584,683        | \$ 118,184,132                                  | \$ 265,404,700        | \$ 384,814,445        |
| Net income                        |                         |                   |                         |                   |                                                 | 11,128,303            | 11,128,303            |
| Cash dividends                    |                         |                   |                         |                   |                                                 | (3,869,432)           | (3,869,432)           |
| Balance, December 27, 2008        | 12,818,608              | \$ 640,930        | 11,693,651              | \$ 584,683        | \$ 118,184,132                                  | \$ 272,663,571        | \$ 392,073,316        |
| Balance, September 26, 2009       | 12,888,608              | \$ 644,430        | 11,623,651              | \$ 581,183        | \$ 118,184,132                                  | \$ 278,754,211        | \$ 398,163,956        |
| Net income                        |                         |                   |                         |                   |                                                 | 6,017,010             | 6,017,010             |
| Cash dividends                    |                         |                   |                         |                   |                                                 | (3,870,483)           | (3,870,483)           |
| <b>Balance, December 26, 2009</b> | <b>12,888,608</b>       | <b>\$ 644,430</b> | <b>11,623,651</b>       | <b>\$ 581,183</b> | <b>\$ 118,184,132</b>                           | <b>\$ 280,900,738</b> | <b>\$ 400,310,483</b> |

See notes to unaudited interim financial statements.

**Table of Contents****INGLES MARKETS, INCORPORATED AND SUBSIDIARIES****CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)**

|                                                                                             | THREE MONTHS ENDED<br>DECEMBER 26,<br>2009 | DECEMBER 27,<br>2008 |
|---------------------------------------------------------------------------------------------|--------------------------------------------|----------------------|
| <b>Cash Flows from Operating Activities:</b>                                                |                                            |                      |
| Net income                                                                                  | \$ 6,017,010                               | \$ 11,128,303        |
| Adjustments to reconcile net income to net cash (used in) provided by operating activities: |                                            |                      |
| Depreciation and amortization expense                                                       | 21,600,028                                 | 19,003,710           |
| Losses on disposals of property and equipment                                               | 200,024                                    | 113,666              |
| Receipt of advance payments on purchases contracts                                          | 750,000                                    | 500,000              |
| Recognition of advance payments on purchases contracts                                      | (927,980)                                  | (1,070,288)          |
| Deferred income taxes                                                                       | (890,000)                                  | 77,000               |
| Changes in operating assets and liabilities:                                                |                                            |                      |
| Receivables                                                                                 | (9,962,686)                                | (1,873,937)          |
| Inventory                                                                                   | (10,823,545)                               | (8,808,743)          |
| Other assets                                                                                | 10,616,878                                 | 11,135,505           |
| Accounts payable and accrued expenses                                                       | (15,510,449)                               | (3,042,522)          |
| <b>Net Cash Provided by Operating Activities</b>                                            | <b>1,069,280</b>                           | <b>27,162,694</b>    |
| <b>Cash Flows from Investing Activities:</b>                                                |                                            |                      |
| Proceeds from sales of property and equipment                                               | 1,195,386                                  |                      |
| Capital expenditures                                                                        | (17,680,769)                               | (60,204,064)         |
| <b>Net Cash Used in Investing Activities</b>                                                | <b>(16,485,383)</b>                        | <b>(60,204,064)</b>  |
| <b>Cash Flows from Financing Activities:</b>                                                |                                            |                      |
| Proceeds from line of credit borrowings                                                     |                                            | 215,137,000          |
| Payments on line of credit borrowings                                                       |                                            | (218,698,000)        |
| Proceeds from long-term borrowings                                                          |                                            | 52,275,350           |
| Principal payments on long-term borrowings                                                  | (7,571,776)                                | (12,424,552)         |
| Dividends paid                                                                              | (3,870,483)                                | (3,869,432)          |
| <b>Net Cash (Used) Provided By Financing Activities</b>                                     | <b>(11,442,259)</b>                        | <b>32,420,366</b>    |
| <b>Net (Decrease) Increase in Cash and Cash Equivalents</b>                                 | <b>(26,858,362)</b>                        | <b>(621,004)</b>     |
| Cash and cash equivalents at beginning of period                                            | 77,035,848                                 | 4,178,897            |
| <b>Cash and Cash Equivalents at End of Period</b>                                           | <b>\$ 50,177,486</b>                       | <b>\$ 3,557,893</b>  |

See notes to unaudited interim financial statements.



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**INGLES MARKETS, INCORPORATED AND SUBSIDIARIES**

**NOTES TO INTERIM FINANCIAL STATEMENTS (UNAUDITED)**

**Three Months Ended December 26, 2009 and December 27, 2008**

**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 December 26, 2009, and the results of operations, changes in stockholders' equity and cash flows for the three months ended December 26, 2009 and December 27, 2008. 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 26, 2009, filed by the Company under the Securities Exchange Act of 1934 on December 7, 2009.

The results of operations for the three-month period ended December 26, 2009 are not necessarily indicative of the results to be expected for the full fiscal year.

Certain amounts for the three months ended December 27, 2008 have been reclassified to conform to the current year presentation in the accompanying financial statements. Beginning with the fiscal quarter ended September 26, 2009 the Company began including the costs of its distribution network in the line item "Cost of goods sold" on the Condensed Consolidated Statements of Income. These costs previously were included in the line item "Operating and administrative expenses" on the Condensed Consolidated Statements of Income. While this is an accounting policy election, management believes the new presentation is more closely aligned with industry practice. The amounts for the three months ended December 27, 2008 have been reclassified to conform to the current year presentation in the accompanying consolidated financial statements.

**B. NEW ACCOUNTING PRONOUNCEMENTS**

In June 2009, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 168 "The FASB Accounting Standards Codification and the Hierarchy of Generally Accepted Accounting Principles" a replacement of FASB Standard No. 162 (SFAS 168). SFAS 168 replaces the Generally Accepted Accounting Principles (GAAP) with two levels of GAAP: authoritative and non-authoritative. On July 1, 2009, the FASB Accounting Standards Codification (FASB ASC) became the single source of authoritative nongovernmental GAAP, except for rules and interpretive releases of the Securities and Exchange Commission. All other non-grandfathered accounting literature became non-authoritative. The adoption of SFAS 168 did not have a material impact on the Company's condensed consolidated financial statements. As a result of the adoption of SFAS 168, all references to GAAP now refer to the codified FASB ASC topic.

In September 2006, FASB ASC Topic 820 was issued which defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. FASB ASC Topic 820 does not require any new fair value measurements, but provides guidance on how to measure fair value by providing a fair value hierarchy used to classify the source of the information. FASB ASC Topic 820 was effective for the Company as of the year ending September 26, 2009. The adoption of FASB ASC Topic 820 did not have a significant impact on the Company's condensed consolidated financial statements.

In April 2009, FASB ASC Topic 855 was issued which establishes general standards of accounting for and disclosure of events that occur after the balance sheet date but before financial statements are issued or available to be issued. The Company adopted FASB ASC Topic 855 for the quarter ending June 27, 2009. The adoption did not have a material impact on the Company's condensed consolidated financial statements.

**C. ALLOWANCE FOR DOUBTFUL ACCOUNTS**

Receivables are presented net of an allowance for doubtful accounts of \$639,000 at December 26, 2009 and September 26, 2009.

**D. INCOME TAXES**

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The Company's continuing practice is to recognize interest and penalties related to uncertain tax positions and related matters in income tax expense. As of December 26, 2009, the Company had approximately \$167,000 accrued for interest and penalties.

The Company's effective tax rate differs from the federal statutory rate primarily as a result of state income taxes and tax credits. As of December 26, 2009, the Company had gross unrecognized tax benefits of approximately \$353,000, all of which, if recognized, would affect the effective tax rate. The Company does not expect that the total amounts of unrecognized tax benefits will significantly increase or decrease within the next twelve months.

**Table of Contents****INGLES MARKETS, INCORPORATED AND SUBSIDIARIES****NOTES TO INTERIM FINANCIAL STATEMENTS (UNAUDITED) (Continued)****Three Months Ended December 26, 2009 and December 27, 2008**

The Company files income tax returns with federal and various state jurisdictions. With few exceptions, the Company is no longer subject to state income tax examinations by tax authorities for the years before 2004. Additionally, the Internal Revenue Service has completed its examination of the Company's U.S. Federal income tax returns filed through fiscal year 2005.

At September 26, 2009 the Company had approximately \$12.5 million of refundable income taxes included in the caption "Other current assets" in the Condensed Consolidated Balance Sheets. The Company applied for early refund of federal income taxes and received the refund during the fiscal quarter ended December 26, 2009.

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

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

|                                            | DECEMBER 26,<br>2009 | SEPTEMBER 26,<br>2009 |
|--------------------------------------------|----------------------|-----------------------|
| Property, payroll, and other taxes payable | \$ 10,796,725        | \$ 15,783,416         |
| Salaries, wages and bonuses payable        | 17,935,741           | 22,203,640            |
| Self-insurance liabilities                 | 13,547,742           | 14,156,543            |
| Interest                                   | 6,963,023            | 20,414,995            |
| Income taxes                               | 2,465,650            |                       |
| Other                                      | 5,896,336            | 6,310,242             |
| <b>Total</b>                               | <b>\$ 57,605,217</b> | <b>\$ 78,868,836</b>  |

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 \$300,000 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 \$7.6 million and \$5.5 million for each of the three-month periods ended December 26, 2009 and December 27, 2008, respectively.

**F. LONG-TERM DEBT**

In May 2009, the Company issued \$575.0 million aggregate principal amount of senior notes due in 2017 (the "Notes") in a private placement. The Notes bear an interest rate of 8.875% per annum and were issued at a discount to yield 9.5% per annum.

The Company may redeem all or a portion of the Notes at any time on or after May 15, 2013 at the following redemption prices (expressed as percentages of the principal amount), if redeemed during the 12-month period beginning May 15 of the years indicated below:

| <b>Year</b>         |          |
|---------------------|----------|
| 2013                | 104.438% |
| 2014                | 102.219% |
| 2015 and thereafter | 100.000% |

In connection with the offering of the Notes, the Company entered into a new three-year \$175.0 million line of credit and terminated three other lines of credit. At December 26, 2009, the Company has \$185.0 million of total commitments under lines of credit, with no borrowings.

outstanding.

The lines of credit provide the Company with various interest rate options generally at rates less than prime. The lines allow the Company to issue up to \$30.0 million in unused letters of credit, of which \$9.4 million of unused letters of credit were issued at December 26, 2009. The Company is not required to maintain compensating balances in connection with these lines of credit.

The Notes and 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 December 26, 2009.

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.

**Table of Contents****INGLES MARKETS, INCORPORATED AND SUBSIDIARIES****NOTES TO INTERIM FINANCIAL STATEMENTS (UNAUDITED) (Continued)****Three Months Ended December 26, 2009 and December 27, 2008****G. 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 October 22, 2009 to stockholders of record on October 8, 2009.

**H. 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. 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 on Class B Common Stock.

The Company calculates earnings per share for its Class A Common Stock and Class B Common Stock using the two-class method in accordance with FASB ASC Topic 260.

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 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 and prior periods.

|                                                         | <b>THREE MONTHS ENDED<br/>DECEMBER 26, 2009</b> |                | <b>THREE MONTHS ENDED<br/>DECEMBER 27, 2008</b> |                |
|---------------------------------------------------------|-------------------------------------------------|----------------|-------------------------------------------------|----------------|
|                                                         | <b>CLASS A</b>                                  | <b>CLASS B</b> | <b>CLASS A</b>                                  | <b>CLASS B</b> |
| <i>Numerator: Allocated net income</i>                  |                                                 |                |                                                 |                |
| Net income allocated, basic                             | \$ 3,306,370                                    | \$ 2,710,640   | \$ 6,083,417                                    | \$ 5,044,886   |
| Conversion of Class B to Class A shares                 | 2,710,640                                       |                | 5,044,886                                       |                |
| Net income allocated, diluted                           | \$ 6,017,010                                    | \$ 2,710,640   | \$ 11,128,303                                   | \$ 5,044,886   |
| <i>Denominator: Weighted average shares outstanding</i> |                                                 |                |                                                 |                |
| Weighted average shares outstanding, basic              | 12,888,608                                      | 11,623,651     | 12,818,608                                      | 11,693,651     |
| Conversion of Class B to Class A shares                 | 11,623,651                                      |                | 11,693,651                                      |                |
| Weighted average shares outstanding, diluted            | 24,512,259                                      | 11,623,651     | 24,512,259                                      | 11,693,651     |
| <i>Earnings per share</i>                               |                                                 |                |                                                 |                |
| Basic                                                   | \$ 0.26                                         | \$ 0.23        | \$ 0.47                                         | \$ 0.43        |
| Diluted                                                 | \$ 0.25                                         | \$ 0.23        | \$ 0.45                                         | \$ 0.43        |

**I. LINES OF BUSINESS**

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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   |                      |
|--------------------------------------------|----------------------|----------------------|
|                                            | DECEMBER 26,<br>2009 | DECEMBER 27,<br>2008 |
| Revenues from unaffiliated customers:      |                      |                      |
| Grocery sales                              | \$ 814,199           | \$ 775,739           |
| Shopping center rentals                    | 2,280                | 2,781                |
| Fluid dairy                                | 26,754               | 29,126               |
| Total revenues from unaffiliated customers | \$ 843,233           | \$ 807,646           |
| Income from operations:                    |                      |                      |
| Grocery sales                              | \$ 21,273            | \$ 25,790            |
| Shopping center rentals                    | 274                  | 808                  |
| Fluid dairy                                | 3,186                | 3,361                |
| Total income from operations               | \$ 24,733            | \$ 29,959            |

**Table of Contents****INGLES MARKETS, INCORPORATED AND SUBSIDIARIES****NOTES TO INTERIM FINANCIAL STATEMENTS (UNAUDITED) (Continued)****Three Months Ended December 26, 2009 and December 27, 2008**

|                                        | DECEMBER 26,<br>2009 | SEPTEMBER 26,<br>2009 |
|----------------------------------------|----------------------|-----------------------|
| Assets:                                |                      |                       |
| Grocery sales                          | \$ 1,343,191         | \$ 1,366,248          |
| Shopping center rentals                | 126,853              | 126,853               |
| Fluid dairy                            | 29,158               | 26,450                |
| Elimination of intercompany receivable | (2,368)              | (1,942)               |
| Total assets                           | \$ 1,496,834         | \$ 1,517,609          |

Sales by product category (amounts in thousands) are as follows:

|                       | THREE MONTHS ENDED   |                      |
|-----------------------|----------------------|----------------------|
|                       | DECEMBER 26,<br>2009 | DECEMBER 27,<br>2008 |
| Grocery               | \$ 348,590           | \$ 344,574           |
| Non-foods             | 169,675              | 161,118              |
| Perishables           | 190,301              | 188,917              |
| Gasoline              | 105,633              | 81,130               |
| Total grocery segment | \$ 814,199           | \$ 775,739           |

The grocery category includes grocery, dairy, and frozen foods.

The non-foods category includes alcoholic beverages, tobacco, pharmacy, health and video.

The perishables category includes meat, produce, deli and bakery.

Revenue from shopping center rentals is included in the caption Rental income, net in the Condensed Consolidated Statements of Income. Grocery and fluid dairy revenues comprise net sales reported in the Condensed Consolidated Statements of Income.

For the three months ended December 26, 2009 and December 27, 2008, the fluid dairy segment had \$13.7 million and \$14.8 million, respectively, in sales to the grocery sales segment. These sales have been eliminated in consolidation and are excluded from the amounts in the table above.

**J. FAIR VALUES OF FINANCIAL INSTRUMENTS**

The carrying amounts for cash and cash equivalents, accounts receivable, and accounts payable approximate fair value due to the short-term maturity of these instruments. At December 26, 2009 and September 26, 2009, the fair value of the Company's debt was estimated at \$878.9 million and \$884.2 million, respectively, primarily using market yields and taking into consideration the underlying terms of the debt. Such fair value was more than the carrying value of debt at December 26, 2009 by \$37.0 million and more than the carrying value of debt at September 26, 2009 by \$34.9 million.

**K. SUBSEQUENT EVENTS**

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We have evaluated subsequent events and transactions for potential recognition or disclosure in the financial statements through January 29, 2010, the day the financial statements were issued.

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

#### ***Overview***

Ingles, a leading supermarket chain in the Southeastern United States, operates 201 supermarkets in Georgia (73), North Carolina (68), South Carolina (36), Tennessee (21), 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. Non-food products include health and beauty care products and general merchandise. The Company also offers quality private label items. As of December 26, 2009, the Company operated 70 in-store pharmacies and 66 fuel centers.

Ingles also operates two other lines of business, fluid dairy processing and shopping center rentals. The fluid dairy processing segment sells approximately 34% of its products to the retail grocery segment and approximately 66% 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 benefits.



**Table of Contents*****Critical Accounting Policies***

Critical accounting policies are those accounting policies that management believes are important to the portrayal of the Company's 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. Estimates are based on historical experience and other factors believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Management estimates, by their nature, involve judgments regarding future uncertainties, and actual results may therefore differ materially from these estimates.

***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 of \$750,000 per occurrence for workers compensation and \$300,000 per covered person for medical care benefits for a policy year. 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. These estimates can fluctuate if historical trends are not predictive of the future. The majority of the Company's properties are self-insured for casualty losses and business interruption; however, liability coverage is maintained. At December 26, 2009, the Company's self insurance reserves totaled \$13.5 million for employee group insurance, workers' compensation insurance and general liability insurance.

***Asset Impairments***

The Company accounts for the impairment of long-lived assets in accordance with Financial Accounting Standards Board Accounting Standards Codification (FASB ASC) Topic 360. 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 closed properties under long-term lease agreements, a 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, in accordance with FASB ASC Topic 420. The Company's estimates of market rates are based on its experience, knowledge and 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 the line item Accrued expenses and current portion of other long-term liabilities on the Condensed Consolidated Balance Sheets.

***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 vendor consideration received is sold. Vendor allowances applied as a reduction of merchandise costs totaled \$24.9 million and \$23.6 million for the fiscal years ended December 26, 2009 and December 27, 2008, 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 \$2.6 million and \$3.3 million for the fiscal years ended December 26, 2009 and December 27, 2008, respectively.



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If vendor advertising allowances were substantially reduced or eliminated, the Company would likely consider other methods of advertising as well as the volume and frequency of the Company's product advertising, which could increase or decrease the Company's expenditures.

Similarly, the Company is not able to assess the impact of vendor advertising allowances on creating additional revenue, as such allowances do not directly generate revenue for the Company's stores.

*Uncertain Tax Positions*

Despite the Company's belief that its tax positions are consistent with applicable tax laws, the Company believes that certain positions are likely to be challenged by taxing authorities. Settlement of any challenge can 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 positions. The Company's positions are evaluated 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 position provisions for and changes to uncertain tax positions as the Company considers appropriate. Unfavorable settlement of any particular position would require use of cash. Favorable resolution would be recognized as a reduction to income tax expense at the time of resolution.

*Results of Operations*

Ingles operates on a 52 or 53-week fiscal year ending on the last Saturday in September. The unaudited condensed consolidated statements of income for the three-month periods ended December 26, 2009 and December 27, 2008 both include 13 weeks of operations. 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-month periods ended December 26, 2009 and December 27, 2008, comparable store sales include 196 and 195 stores, respectively.

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 I Lines of Business to the Unaudited Condensed Consolidated Financial Statements.

|                                       | THREE MONTHS ENDED   |                      |
|---------------------------------------|----------------------|----------------------|
|                                       | DECEMBER 26,<br>2009 | DECEMBER 27,<br>2008 |
| Net sales                             | 100.0%               | 100.0%               |
| Gross profit                          | 22.0%                | 23.1%                |
| Operating and administrative expenses | 19.1%                | 19.4%                |
| Rental income, net                    | %                    | 0.1%                 |
| Income from operations                | 2.9%                 | 3.7%                 |
| Other income, net                     | 0.1%                 | 0.2%                 |
| Interest expense                      | 1.9%                 | 1.6%                 |
| Income before income taxes            | 1.1%                 | 2.3%                 |
| Income taxes                          | 0.4%                 | 0.9%                 |
| Net income                            | 0.7%                 | 1.4%                 |

**Three Months Ended December 26, 2009 Compared to the Three Months Ended December 27, 2008**

Net income for the first quarter of fiscal 2010 totaled \$6.0 million, 45.9% lower than net income of \$11.1 million earned for the first quarter of fiscal 2009. Total and comparable store sales increases were offset by a lower gross margin and by higher interest, depreciation and insurance expenses.

*Net Sales.* Net sales increased 4.5% to \$841.0 million for the three months ended December 26, 2009 from \$804.9 million for the three months ended December 27, 2008. Ingles operated 201 stores at December 26, 2009 and at 199 stores at December 27, 2008. Retail square footage was approximately 10.8 million at December 26, 2009 and 10.4 million at December 27, 2008. Excluding gasoline sales, grocery segment sales increased 2.0% for the three months ended December 26, 2009 compared with the three months ended December 27, 2008.



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Grocery segment comparable store sales grew \$26.5 million, or 3.4%, in the first quarter of fiscal 2010 compared to the first quarter of fiscal 2009. Excluding gasoline sales, comparable store sales increased \$5.6 million, or 0.8%. Comparable store sales growth excluding gasoline continues to be affected by price deflation and the effect of the economic recession on consumer spending. The number of customer transactions (excluding gasoline) increased 11.6%, while the average transaction size (excluding gasoline) decreased by 9.8%.

Sales by product category (amounts in thousands) are as follows:

|                              | THREE MONTHS ENDED   |                      |
|------------------------------|----------------------|----------------------|
|                              | DECEMBER 26,<br>2009 | DECEMBER 27,<br>2008 |
| Grocery                      | \$ 348,590           | \$ 344,574           |
| Non-foods                    | 169,675              | 161,118              |
| Perishables                  | 190,301              | 188,917              |
| Gasoline                     | 105,633              | 81,130               |
| <b>Total grocery segment</b> | <b>\$ 814,199</b>    | <b>\$ 775,739</b>    |

The grocery category includes grocery, dairy, and frozen foods.

The non-foods category includes alcoholic beverages, tobacco, pharmacy, health and video.

The perishables category includes meat, produce, deli and bakery.

Changes in grocery segment sales for the quarter ended December 26, 2009 are summarized as follows (in thousands):

|                                                                         |                   |
|-------------------------------------------------------------------------|-------------------|
| Total grocery sales for the three months ended December 27, 2008        | <b>\$ 775,739</b> |
| Comparable store sales increase (including gasoline)                    | <b>26,543</b>     |
| Impact of stores opened in fiscal 2009 and 2010                         | <b>12,913</b>     |
| Impact of stores closed in fiscal 2009 and 2010                         | <b>(997)</b>      |
| Other                                                                   | <b>1</b>          |
| <b>Total grocery sales for the three months ended December 26, 2009</b> | <b>\$ 814,199</b> |

Net sales to outside parties for the Company's milk processing subsidiary decreased \$2.4 million, or 8.1%, in the December 2009 quarter compared to the December 2008 quarter. The sales decrease is attributable to lower raw milk costs in the December 2009 quarter compared to the December 2008 quarter. The case volume of products sold increased.

*Gross Profit.* Gross profit for the three-month period ended December 26, 2009 decreased \$0.3 million to \$185.3 million, or 22.0% of sales, compared to \$185.6 million, or 23.1% of sales, for the three-month period ended December 27, 2008.

Grocery segment gross profit as a percentage of total sales was affected by lower margins on gasoline, competitive factors and the effect of price deflation on certain of the Company's products. The Company's emphasis on sales growth, market share and customer satisfaction has affected its prices and margins. Excluding gasoline sales, grocery segment gross profit as a percentage of sales was relatively constant at 25.0% for the three months ended December 26, 2009 compared with 24.9% for the three months ended December 27, 2008.

Gross profit for the Company's milk processing subsidiary for the December 2009 quarter decreased \$0.2 million, or 3.6%, to \$5.5 million, or 13.6% of sales, compared to \$5.7 million, or 13.0% of sales, for the December 2008 quarter. Raw milk costs were substantially lower and the cents-per-gallon margin were affected by the competitive environment comparing the three months ended December 2009 with the three months ended December 2008.

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In addition to the direct product cost, the cost of goods sold line item for the grocery segment includes inbound freight charges and the costs related to the Company's distribution network. Distribution network costs for the grocery segment were previously included in operating and administrative expenses and totaled \$11.7 million and \$11.6 million for the quarters ended December 2009 and December 2008, respectively. 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 goods sold line item, while these items are included in operating and administrative expenses by the grocery segment.

*Operating and Administrative Expenses.* Operating and administrative expenses increased \$4.3 million, or 2.8%, to \$160.6 million for the three months ended December 26, 2009, from \$156.3 million for the three months ended December 27, 2008. As a percentage of sales, operating and administrative expenses were 19.1% and 19.4% for the three months ended December 26, 2009 and December 27,

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2008, respectively. Excluding gasoline sales and associated gasoline operating expenses (primarily payroll), operating expenses were 21.7% of sales for the first fiscal 2010 quarter compared with 21.5% for the first fiscal quarter of 2009. The increased number of new and remodeled stores opened by the Company during fiscal years 2008 and 2009 contributed to higher expenses, while the economic recession has resulted in a longer sales growth time period to cover such expenses.

The major increases (decreases) in operating and administrative expenses were as follows:

|                                   | INCREASE<br>(DECREASE)<br>IN<br>MILLIONS | INCREASE<br>(DECREASE)<br>AS A %<br>OF SALES |
|-----------------------------------|------------------------------------------|----------------------------------------------|
| Depreciation and amortization     | \$ 2.6                                   | 0.31%                                        |
| Insurance expense                 | \$ 2.0                                   | 0.24%                                        |
| Salaries and wages                | \$ 1.6                                   | 0.19%                                        |
| Bank charges                      | \$ 0.7                                   | 0.09%                                        |
| Advertising and promotion expense | \$ (1.3)                                 | (0.15)%                                      |

Depreciation and amortization expense increased as a result of the Company's increased capital expenditures in fiscal years 2008 and 2009 to improve its store base.

Insurance expense increased due to an increased number of employees and due to higher claims under the Company's self insurance programs.

Salaries and wages expenses increased due to the additional labor hours required to support the increased sales volume and the increased number of new and remodeled stores.

Bank charges increased as result of increased interchange fees charged by processing companies and by an increase in the proportion of sales settled with debit and credit cards.

Advertising and promotion expenses decreased due to more targeted programs and due to higher vendor reimbursements for cooperative advertising.

*Rental Income, Net.* Rental income, net totaling \$0.3 million decreased \$0.5 million for the December 2009 quarter compared to the December 2008 quarter. The Company's expansion and relocation activities have resulted in less tenant space available for lease, and the economic recession has increased tenant vacancies.

*Other Income, Net.* Other income, net decreased \$0.3 million to \$0.9 million for the three-month period ended December 26, 2009 from \$1.2 million for the three-month period ended December 27, 2008. The decrease is principally due to lower income from waste paper and packaging sales and lower service rebates.

*Interest Expense.* Interest expense increased \$3.2 million for the three-month period ended December 26, 2009 to \$16.2 million from \$13.0 million for the three-month period ended December 27, 2008. Total debt at December 26, 2009 was \$841.7 million compared to \$753.4 million at December 27, 2008.

*Income Taxes.* Income tax expense as a percentage of pre-tax income was 36.2% in the December 2009 quarter compared to 38.8% in the December 2008 quarter. The decreased percentage is primarily attributable to lower state income taxes and higher tax credits.

*Net Income.* Net income decreased \$5.1 million or 45.9% for the three-month period ended December 26, 2009 to \$6.0 million compared to \$11.1 million for the three-month period ended December 27, 2008. Net income, as a percentage of sales, was 0.7% for the December 2009 quarter and 1.4% for the December 2008 quarter. Basic and diluted earnings per share for Class A Common Stock were \$0.26 and \$0.25, respectively, for the December 2009 quarter, compared to \$0.47 and \$0.45, respectively, for the December 2008 quarter. Basic and diluted earnings per share for Class B Common Stock were each \$0.23 for the December 2009 quarter compared to \$0.43 for the December 2008 quarter.

**Liquidity and Capital Resources**

*Capital Expenditures*

The Company believes that a key to its ability to increase sales and develop a loyal customer base is providing conveniently located, clean and modern stores that provide customers with good service and a broad selection of competitively priced products. Accordingly, the Company has invested and plans to 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, and the relocation of selected existing stores to larger, more convenient locations.



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Capital expenditures totaled \$17.7 million for the three-month period ended December 26, 2009, including the opening of one new store and one remodeled store. 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 scheduled to open later in fiscal 2010 and in fiscal 2011.

Ingles' capital expenditure plans for fiscal 2010 include investments of approximately \$120 to \$150 million. The timing and extent of current year development projects will be influenced by Company financial performance and overall economic conditions and the availability of financing. At the present time, for the remainder of fiscal 2010 the Company intends to open seven new, replacement or remodeled stores and add approximately four new fuel stations at either new or existing stores.

The Company expects that its net annual capital expenditures will be in the range of approximately \$120 to \$170 million going forward in order to maintain a modern store base. Planned expenditures for any given future fiscal year will be influenced by the Company's financial performance, overall economic conditions and the availability of financing. In general, the Company is increasing the average size of stores being built, which could affect both the number of projects pursued at any given time and the cost of these projects. The number of projects may also fluctuate due to the varying costs of the types of projects pursued and the availability of suitable financing. 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. Construction commitments at December 26, 2009 totaled \$29.2 million.

### *Liquidity*

The Company had cash on hand of \$50.2 million at December 26, 2009. This cash balance resulted primarily from financings accomplished during fiscal 2009 and a lower level of capital expenditures. The Company is being cautious with its liquidity until economic conditions improve and stores developed in fiscal years 2008 and 2009 have an opportunity to mature in a more typical operating environment. Interest earned on this cash balance is much lower than the Company's average borrowing rate, resulting in a short-term decrease in earnings until the cash can be profitably deployed.

The Company generated \$1.1 million of net cash from operations in the December 2009 quarter compared to \$27.2 million of net cash provided by operations in the December 2008 quarter. Most of the change is attributable to a decrease in operating income and inventory growth.

Cash used in investing activities for the December 2009 quarter totaled \$16.5 million (primarily made up of \$17.7 million in capital expenditures), compared to \$60.2 million of cash used in investing activities (substantially all capital expenditures) for the December 2008 quarter. The Company is being more cautious in its development plans until economic conditions improve.

Cash used by financing activities during the December 2009 quarter totaled \$11.4 million, compared with cash provided by financing activities (including new borrowings) totaling \$32.4 million during the December 2008 quarter. For the December 2009 quarter, principal payments on long-term debt and lines of credit were \$7.6 million and dividend payments were \$3.9 million.

In May 2009, the Company issued \$575.0 million aggregate principal amount of senior notes due in 2017 (the "Notes") in a private placement. The Notes bear an interest rate of 8.875% per annum and were issued at a discount to yield 9.5% per annum. Note proceeds were used to pay off \$349.8 million aggregate principal amount of senior subordinated debt maturing in 2011, pay off \$45.3 million outstanding indebtedness under the Company's committed lines of credit, pay off \$77.7 million of secured indebtedness, and pay costs related to the offering of the Notes. Remaining Note proceeds are being used for general corporate purposes, including current and future capital expenditures. As a result of these transactions, the Company has extended the average maturity of its total debt outstanding. The Company believes that availability of suitable financing may be sporadic in the future, as it has been for the past twelve to eighteen months, and opportunistically accessed the capital markets.

In connection with the offering of the Notes, the Company entered into a new three-year \$175.0 million line of credit and terminated three other lines of credit. After giving effect to these transactions, the Company has \$185.0 million of total commitments under lines of credit. There are no borrowings outstanding under lines of credit at December 26, 2009.

The lines of credit provide the Company with various interest rate options generally at rates less than prime. The lines allow the Company to issue up to \$30.0 million in unused letters of credit, of which \$9.4 million of unused letters of credit were issued at December 26, 2009. The Company is not required to maintain compensating balances in connection with these lines of credit.

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The Notes and 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

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its respective loan documents. The Company was in compliance with all financial covenants related to these lines of credit at December 26, 2009.

The Company's 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. These covenants have the effect of restricting certain types of transactions, including the payment of cash dividends in excess of current quarterly per share amounts. As of December 26, 2009, the Company was in compliance with these covenants.

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 the Notes 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 December 26, 2009, the Company had unencumbered real property and equipment with a net book value of approximately \$696.8 million. The Company believes, based on its current results of operations and financial condition, that its 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, there is no assurance that any such sources of financing will be available to the Company when needed 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 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 26, 2009.

### *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, the Notes and the lines of credit contain provisions that, based on certain financial parameters, restrict the ability of the Company to pay additional cash dividends in excess of current quarterly per share amounts. Further, the Company is prevented from declaring dividends at any time that it is in default under the indenture governing the Notes.

### *Seasonality*

Sales in the grocery segment of the Company's business are subject to a slight seasonal variance due to holiday related sales and 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 the Company's 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.

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|                    | THREE MONTHS ENDED   |                      |
|--------------------|----------------------|----------------------|
|                    | DECEMBER 26,<br>2009 | DECEMBER 27,<br>2008 |
| All items          | 0.8%                 | (12.7)%              |
| Food and beverages | 0.4%                 | 1.7%                 |
| Energy             | 6.8%                 | (76.6)%              |

*Forward Looking Statements*

This Quarterly Report contains certain forward-looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended (the Exchange Act). The words expect, anticipate, intend, plan, likely, goal, believe, seek and similar expressions are used to identify forward-looking statements. While these forward-looking statements and the related assumptions are made in good faith and reflect 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; sudden or significant changes in the availability of gasoline and retail gasoline prices; the maturation of new and expanded stores; general concerns about food safety; 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 other risks and uncertainties, including those contained in the Company's Annual Report on Form 10-K for the year ended September 26, 2009, as updated or supplemented by subsequent quarterly reports on Form 10-Q and current reports of Form 8-K filed with the Securities and Exchange Commission.

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. The Company does not undertake and specifically declines any obligation to update any such statements or to publicly announce the results of any revisions to any of such statements to reflect future events or developments.

**Item 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

The Company does not typically utilize financial instruments for trading or other speculative purposes, nor does it typically utilize leveraged financial instruments. Following the comprehensive refinancing undertaken by the Company during the third quarter of fiscal year 2009, the Company may consider derivative instruments such as interest rate swaps to manage its overall interest rate risk. There have been no material changes in the market risk factors from those disclosed in the Company's Annual Report on Form 10-K for the year ended September 26, 2009.

**Item 4. CONTROLS AND PROCEDURES***(a) Evaluation of Disclosure 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 Rule 13a-15(b) under the Exchange Act, 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 December 26, 2009, 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 2009. After consideration of the

matters discussed above, management has concluded that the Company's controls and procedures were effective as of December 26, 2009.

***(b) Changes in Internal Control over Financial Reporting***

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The Company has set the timing and scope of its fiscal year 2010 testing of internal controls over financial reporting and has begun performing tests for fiscal year 2010.

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)/15d-14(a) Certification
- 2) Exhibit 31.2 Rule 13a-14(a)/15d-14(a) Certification
- 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 the report to be signed on its behalf by the undersigned thereunto duly authorized.

**INGLES MARKETS, INCORPORATED**

Date: January 29, 2010

/s/ ROBERT P. INGLE  
**Robert P. Ingle**

**Chief Executive Officer**

Date: January 29, 2010

/s/ RONALD B. FREEMAN  
**Ronald B. Freeman**

**Vice President-Finance and**

**Chief Financial Officer**