

INSTEEL INDUSTRIES INC
Form 10-Q
July 17, 2014

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the Quarterly Period Ended June 28, 2014

OR

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

For the Transition Period From _____ to _____

Commission File Number: 1-9929

Insteel Industries, Inc.

(Exact name of registrant as specified in its charter)

North Carolina

(State or other jurisdiction of
incorporation or organization)

56-0674867

(I.R.S.
Employer

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Identification
No.)

1373 Boggs Drive, Mount Airy, North Carolina

27030

(Address of principal executive offices)

(Zip Code)

Registrant's telephone number, including area code: **(336) 786-2141**

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

Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate 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 large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer

Accelerated filer

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

Smaller reporting company

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

Yes No

The number of shares outstanding of the registrant's common stock as of July 16, 2014 was 18,307,165.

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PART I – FINANCIAL INFORMATION**Item 1. Financial Statements**

**INSTEEL
INDUSTRIES, INC.
AND
SUBSIDIARIES
CONSOLIDATED
STATEMENTS OF
OPERATIONS AND
COMPREHENSIVE
INCOME**

(In thousands except
for per share data)
(Unaudited)

	Three Months Ended		Nine Months Ended	
	June 28, 2014	June 29, 2013	June 28, 2014	June 29, 2013
Net sales	\$113,227	\$96,946	\$291,881	\$265,706
Cost of sales	98,964	86,036	256,957	235,152
Gross profit	14,263	10,910	34,924	30,554
Selling, general and administrative expense	6,219	5,373	16,908	15,460
Other expense (income), net	(849)	415	(653)	330
Interest expense	56	57	169	182
Interest income	(4)	(11)	(10)	(13)
Earnings before income taxes	8,841	5,076	18,510	14,595
Income taxes	3,044	1,802	6,444	5,205
Net earnings	\$5,797	\$3,274	\$12,066	\$9,390
Net earnings per share:				
Basic	\$0.32	\$0.18	\$0.66	\$0.53
Diluted	0.31	0.18	0.65	0.51
Weighted average shares outstanding:				
Basic	18,267	18,066	18,230	17,879
Diluted	18,683	18,497	18,636	18,290

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Cash dividends declared per share	\$0.03	\$0.03	\$0.09	\$0.34
Comprehensive income	\$5,797	\$3,274	\$12,066	\$9,390

See accompanying notes to consolidated financial statements.

INSTEEL INDUSTRIES, INC. AND SUBSIDIARIES**CONSOLIDATED BALANCE SHEETS**

(In thousands)

	(Unaudited)	(Audited)
	June 28,	September
	2014	28,
		2013
Assets		
Current assets:		
Cash and cash equivalents	\$ 31,449	\$ 15,440
Accounts receivable, net	46,645	41,110
Inventories, net	79,167	58,793
Other current assets	5,682	5,863
Total current assets	162,943	121,206
Property, plant and equipment, net	80,745	83,053
Other assets	8,351	8,390
Total assets	\$ 252,039	\$ 212,649
Liabilities and shareholders' equity		
Current liabilities:		
Accounts payable	\$ 55,276	\$ 30,561
Accrued expenses	9,046	6,854
Total current liabilities	64,322	37,415
Other liabilities	14,378	14,178
Commitments and contingencies		
Shareholders' equity:		
Common stock	18,280	18,185
Additional paid-in capital	57,216	55,452
Retained earnings	99,405	88,981
Accumulated other comprehensive loss	(1,562)	(1,562)
Total shareholders' equity	173,339	161,056
Total liabilities and shareholders' equity	\$ 252,039	\$ 212,649

See accompanying notes to consolidated financial statements.

**INSTEEL
INDUSTRIES,
INC. AND
SUBSIDIARIES
CONSOLIDATED
STATEMENTS
OF CASH
FLOWS**

(In thousands)

(Unaudited)

	Nine Months Ended June 28, 2014	June 29, 2013
Cash Flows From Operating Activities:		
Net earnings	\$ 12,066	\$ 9,390
Adjustments to reconcile net earnings to net cash provided by operating activities:		
Depreciation and amortization	7,481	7,263
Amortization of capitalized financing costs	77	77
Stock-based compensation expense	1,777	1,454
Deferred income taxes	(113)	3,176
Excess tax benefits from stock-based compensation	(222)	(445)
(Gain) loss on sale of property, plant and equipment	(425)	346
Gain from life insurance proceeds	-	(45)
Increase in cash surrender value of life insurance policies over premiums paid	(468)	(293)
Net changes in assets and liabilities:	(5,535)	4,751

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Accounts receivable, net				
Inventories	(20,374)	(2,778)
Accounts payable and accrued expenses	28,122		9,340	
Other changes	(253	)	(173)
Total adjustments	10,067		22,673	
Net cash provided by operating activities	22,133		32,063	

**Cash Flows From
Investing Activities:**

Capital expenditures	(5,801	)	(4,378)
Acquisition of intangible asset	-		(1,887)
Proceeds from life insurance claims	-		577	
Increase in cash surrender value of life insurance policies	(304	)	(54)
Proceeds from surrender of life insurance policies	160		3	
Proceeds from fire loss insurance	1,380		-	
Proceeds from sale of property, plant and equipment	1		100	
Net cash used for investing activities	(4,564	)	(5,639)

**Cash Flows From
Financing Activities:**

Proceeds from long-term debt	331		4,501	
Principal payments on long-term debt	(331	)	(15,976)
Cash dividends paid	(1,642	)	(6,053)
Cash received from exercise of stock options	365		3,380	
Excess tax benefits from stock-based compensation	222		445	
Payment of employee tax withholdings related to net share transactions	(505)	-	
Other	-		(647)
Net cash used for financing activities	(1,560	)	(14,350)

Net increase in cash and cash equivalents	16,009	12,074
Cash and cash equivalents at beginning of period	15,440	10
Cash and cash equivalents at end of period	\$ 31,449	\$ 12,084

Supplemental Disclosures of Cash Flow Information:

Cash paid during the period for:

Interest	\$ 2	\$ 20
Income taxes, net	4,464	1,423
Non-cash investing and financing activities:		
Purchases of property, plant and equipment in accounts payable	45	502
Restricted stock units and stock options surrendered for withholding taxes payable	505	267

See accompanying notes to consolidated financial statements.

**INSTEEL
INDUSTRIES, INC.
AND
SUBSIDIARIES
CONSOLIDATED
STATEMENTS OF
SHAREHOLDERS'
EQUITY**

(In thousands)

(Unaudited)

	Common Stock		Additional	Retained	Accumulated	Total
	Shares	Amount	Paid-In Capital	Earnings	Other Comprehensive Loss	Shareholders' Equity
Balance at September 28, 2013	18,185	\$18,185	\$ 55,452	\$ 88,981	\$ (1,562	) \$ 161,056
Net earnings				12,066		12,066
Stock options exercised, net	59	59	306			365
Vesting of restricted stock units	36	36	(36)		-
Compensation expense associated with stock-based plans			1,777			1,777
Excess tax benefits from stock-based compensation			222			222
Restricted stock units and stock options surrendered for withholding taxes payable			(505	)		(505
Cash dividends declared				(1,642	)	(1,642
Balance at June 28, 2014	18,280	\$18,280	\$ 57,216	\$ 99,405	\$ (1,562	) \$ 173,339

See accompanying notes to consolidated financial statements.

INSTEEL INDUSTRIES, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

(1) Basis of Presentation

The accompanying unaudited interim consolidated financial statements of Insteel Industries, Inc. (“we,” “us,” “our,” “the Company” or “Insteel”) have been prepared pursuant to the rules and regulations of the U.S. Securities and Exchange Commission (“SEC”) for quarterly reports on Form 10-Q. Certain information and note disclosures normally included in the audited financial statements prepared in accordance with accounting principles generally accepted in the United States (“GAAP”) have been condensed or omitted pursuant to such rules and regulations, although the Company believes that the disclosures made are adequate to make the information not misleading. The September 28, 2013 consolidated balance sheet was derived from the audited consolidated financial statements at that date, but does not include all of the information and footnotes required by GAAP for complete financial statements. These financial statements should therefore be read in conjunction with the consolidated financial statements and notes for the fiscal year ended September 28, 2013 included in the Company’s Annual Report on Form 10-K filed with the SEC.

The accompanying unaudited interim consolidated financial statements reflect all adjustments of a normal recurring nature that the Company considers necessary for a fair presentation of results for these interim periods. The results of operations for the nine-month period ended June 28, 2014 are not necessarily indicative of the results that may be expected for the fiscal year ending September 27, 2014 or future periods.

The Company has evaluated subsequent events through the time of filing this Quarterly Report on Form 10-Q and has concluded that there are no significant events that occurred subsequent to the balance sheet date but prior to the filing of this report that would have a material impact on the consolidated financial statements.

(2) Recent Accounting Pronouncements

In February 2013, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) No. 2013-02 “Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income.” ASU No. 2013-02 requires an entity to disaggregate the total change of each component of other comprehensive income either on the face of the income statement or as a separate disclosure in the notes. The Company adopted ASU No. 2013-02 in the first quarter of fiscal 2014. The adoption of this update did not have a material effect on the Company’s consolidated financial statements.

In May 2014, the FASB issued ASU No. 2014-09 "Revenue from Contracts with Customers," which will supersede nearly all existing revenue recognition guidance under GAAP. ASU No. 2014-09 provides that an entity recognize revenue when it transfers promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. This update also requires additional disclosure about the nature, amount, timing and uncertainty of revenue and cash flows arising from customer contracts, including significant judgments and changes in judgments, and assets recognized from costs incurred to obtain or fulfill a contract. ASU No. 2014-09 allows for either full retrospective or modified retrospective adoption and will become effective for the Company in the first quarter of 2018. The Company is evaluating the alternative transition methods and the potential effects of the adoption of this update on its financial statements.

(3) Fair Value Measurements

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The authoritative guidance for fair value measurements establishes a three-level fair value hierarchy that encourages an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The three levels of inputs used to measure fair value are as follows:

Level 1 - Quoted prices in active markets for identical assets or liabilities.

Level 2 - Observable inputs other than quoted prices included in Level 1, such as quoted prices for similar assets and liabilities in active markets.

Level 3 - Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities, including certain pricing models, discounted cash flow methodologies and similar techniques that use significant unobservable inputs.

As of June 28, 2014 and September 28, 2013, the Company held financial assets that are required to be measured at fair value on a recurring basis. The financial assets held by the Company and the fair value hierarchy used to determine their fair values are as follows:

<i>(In thousands)</i>	Total at June 28, 2014	Quoted Prices in Active Markets (Level 1)	Observable Inputs (Level 2)
Current assets:			
Cash equivalents	\$30,989	\$ 30,989	\$ -
Other assets:			
Cash surrender value of life insurance policies	6,718	-	6,718
Total	\$37,707	\$ 30,989	\$ 6,718

<i>(In thousands)</i>	Total at September 28, 2013	Quoted Prices in Active Markets (Level 1)	Observable Inputs (Level 2)
Current assets:			
Cash equivalents	\$ 15,534	\$ 15,534	\$ -
Other assets:			
Cash surrender value of life insurance policies	6,145	-	6,145
Total	\$ 21,679	\$ 15,534	\$ 6,145

Cash equivalents, which include all highly liquid investments with original maturities of three months or less, are classified as Level 1 of the fair value hierarchy. The carrying amount of the Company's cash equivalents, which consist of investments in money market funds, approximates fair value due to their short maturities. Cash surrender value of life insurance policies are classified as Level 2. The fair value of the life insurance policies was determined by the underwriting insurance company's valuation models and represents the guaranteed value the Company would receive upon surrender of these policies as of the reporting date.

As of June 28, 2014 and September 28, 2013, the Company did not have any nonfinancial assets that were required to be measured at fair value on a nonrecurring basis. The carrying amounts of accounts receivable, accounts payable and accrued expenses approximates fair value due to the short-term maturities of these financial instruments.

(4) Stock-Based Compensation

Under the Company's equity incentive plans, employees and directors may be granted stock options, restricted stock, restricted stock units and performance awards. As of June 28, 2014, there were 480,000 shares available for future grants under the plans.

Stock options. Under the Company's equity incentive plans, employees and directors may be granted options to purchase shares of the Company's common stock at the fair market value on the date of the grant. Options granted under these plans generally vest over three years and expire ten years from the date of the grant. Compensation expense and excess tax benefits associated with stock options for the three- and nine-month periods ended June 28, 2014 and June 29, 2013 are as follows:

	Three Months Ended		Nine Months Ended	
	June 28, 2014	June 29, 2013	June 28, 2014	June 29, 2013
<i>(In thousands)</i>				
Stock options:				
Compensation expense	\$221	\$148	\$744	\$634
Excess tax benefits	(31)	(114)	(222)	(445)

As of June 28, 2014, the remaining unamortized compensation cost related to unvested stock option awards was \$360,000, which is expected to be recognized over a weighted average period of 1.25 years.

The fair value of each option grant is estimated on the date of grant using a Monte Carlo valuation model based upon assumptions that are evaluated and revised, as necessary, to reflect market conditions and actual historical experience. The risk-free interest rate for periods within the contractual life of the option is based on the U.S. Treasury yield curve in effect at the time of the grant. The dividend yield is calculated based on the Company's annual dividend as of the option grant date. The expected volatility is derived using a term structure based on historical volatility and the volatility implied by exchange-traded options on the Company's common stock. The expected term for options is based on the results of a Monte Carlo simulation model, using the model's estimated fair value as an input to the Black-Scholes-Merton model, and then solving for the expected term.

The estimated fair value of stock options granted during the three- and nine-month periods ended June 28, 2014 and June 29, 2013 was \$6.93 and \$7.17, respectively, based on the following assumptions:

	Nine Months Ended	
	June 28, 2014	June 29, 2013
Risk-free interest rate	1.56 %	1.25 %
Dividend yield	0.62 %	0.74 %
Expected volatility	41.46 %	48.15 %
Expected term (in years)	4.94	6.47

The following table summarizes stock option activity for the nine-month period ended June 28, 2014:

Options	Exercise Price Per Share	Contractual Aggregate
----------------	---------------------------------	------------------------------

	Outstanding <i>(in thousands)</i>	Range		Weighted Average Average	Term - <i>(in years)</i>	Intrinsic Value <i>(in thousands)</i>
Outstanding at September 28, 2013	918	\$5.43	-\$20.27	\$ 12.65		
Granted	67		19.08 -	19.08	19.08	
Exercised	(113)	)	5.43-	13.06	10.10	\$ 1,074
Outstanding at June 28, 2014	872		5.43-	20.27	13.47	5,589
Vested and anticipated to vest in the future at June 28, 2014	870			13.47	5.91	5,580
Exercisable at June 28, 2014	581			12.70	4.55	4,180

Stock option exercises include “net exercises,” pursuant to which the optionee received shares of common stock equal to the intrinsic value of the options (fair market value of common stock on the date of exercise less exercise price) reduced by any applicable withholding taxes.

Restricted stock units. Restricted stock units (“RSUs”) granted under the Company’s equity incentive plans are valued based upon the fair market value on the date of the grant and provide for a dividend equivalent payment which is included in compensation expense. The vesting period for RSUs is generally one to three years from the date of the grant. RSUs do not have voting rights. RSU compensation expense for the three- and nine-month periods ended June 28, 2014 and June 29, 2013 is as follows:

	Three Months Ended		Nine Months Ended	
	June 28, 2014	June 29, 2013	June 28, 2014	June 29, 2013
<i>(In thousands)</i>				
Restricted stock unit grants:				
Units	-	-	40	43
Market value	\$-	\$-	\$763	\$703
Compensation expense	328	213	1,033	820

As of June 28, 2014, the remaining unrecognized compensation cost related to unvested RSUs was \$752,000, which is expected to be recognized over a weighted average vesting period of 1.36 years.

The following table summarizes RSU activity during the nine-month period ended June 28, 2014:

<i>(Unit amounts in thousands)</i>	Restricted Stock Units Outstanding	Weighted Average Grant Date Fair Value
Balance, September 28, 2013	221	\$ 13.20
Granted	40	19.08
Released	(49)	13.63
Balance, June 28, 2014	212	\$ 14.21

(5) Income Taxes

Effective income tax rate. The Company's effective income tax rate was 34.8% for the nine-month period ended June 28, 2014 compared with 35.7% for the nine-month period ended June 29, 2013. The year-over-year decrease in the effective rate was primarily due to changes in permanent tax differences. The effective income tax rates for both periods were based upon the estimated effective income tax rate applicable for the entire fiscal year after giving effect to any significant items related specifically to interim periods.

Deferred income taxes. As of June 28, 2014, the Company has recorded a current deferred tax asset (net of valuation allowance) of \$2.8 million in other current assets and a non-current deferred tax liability of \$7.3 million in other liabilities on its consolidated balance sheet. The Company has \$22.1 million of state net operating loss carryforwards

(“NOLs”) that begin to expire in 2017, but principally expire between 2017 and 2032. The Company has also recorded \$261,000 of gross deferred tax assets for various state tax credits that begin to expire in 2014, but principally expire between 2014 and 2020.

In accordance with Accounting Standards Codification (“ASC”) Topic 740, the Company evaluates its deferred tax assets to determine if a valuation allowance is required based on the consideration of all available evidence using a “more likely than not” standard, with significant weight being given to evidence that can be objectively verified. The realization of the Company’s deferred tax assets is entirely dependent upon the Company’s ability to generate future taxable income in applicable jurisdictions. Since the Company operates in multiple jurisdictions, it assesses the need for a valuation allowance on a jurisdiction-by-jurisdiction basis, considering the applicable tax laws. The Company recorded a valuation allowance of \$618,000 and \$730,000 as of June 28, 2014 and September 28, 2013, respectively, pertaining to various state NOLs and tax credits that were not expected to be utilized.

The valuation allowance established by the Company is subject to periodic review and adjustment based on changes in facts and circumstances and would be reduced should the Company utilize the state NOLs and tax credits against which an allowance had previously been provided or determine that such utilization was more likely than not.

Uncertainty in income taxes. Based on management’s judgment, as of June 28, 2014, the Company has no material, known tax exposures that require the establishment of a liability for uncertain tax positions.

The Company files U.S. federal income tax returns as well as state and local income tax returns in various jurisdictions. Federal and various state tax returns filed by the Company subsequent to 2009 remain subject to examination together with certain state tax returns filed by the Company subsequent to 2003.

(6) Employee Benefit Plans

Retirement plans. The Company has one defined benefit pension plan, the Insteel Wire Products Company Retirement Income Plan for Hourly Employees, Wilmington, Delaware (the “Delaware Plan”). The Delaware Plan provides benefits for eligible employees based primarily upon years of service and compensation levels. The Delaware Plan was frozen effective September 30, 2008 whereby participants no longer earn additional service benefits. The Company’s funding policy is to contribute amounts at least equal to those required by law. The Company made contributions totaling \$87,000 and \$188,000 to the Delaware Plan during the three- and nine-month periods ended June 28, 2014, respectively, and expects to contribute an additional \$52,000 during the remainder of the current fiscal year.

Net periodic pension costs and related components for the Delaware Plan for the three- and nine-month periods ended June 28, 2014 and June 29, 2013 are as follows:

	Three Months Ended		Nine Months Ended	
	June 28, 2014	June 29, 2013	June 28, 2014	June 29, 2013
<i>(In thousands)</i>				
Interest cost	\$34	\$32	\$102	\$96
Expected return on plan assets	(41)	(36)	(123)	(108)
Recognized net actuarial loss	11	14	33	42
Net periodic pension cost	\$4	\$10	\$12	\$30

Supplemental employee retirement plan. The Company maintains supplemental employee retirement plans (each, a “SERP”) with certain of its employees (each, a “Participant”). Under the SERPs, if the Participant remains in continuous service with the Company for a period of at least 30 years, the Company will pay to the Participant a supplemental retirement benefit for the 15-year period following the Participant’s retirement equal to 50% of the Participant’s highest average annual base salary for five consecutive years in the 10-year period preceding the Participant’s retirement. If the Participant retires prior to the later of age 65 or the completion of 30 years of continuous service with the Company, but has completed at least 10 years of continuous service with the Company, the amount of the supplemental retirement benefit will be reduced by 1/360th for each month short of 30 years that the Participant was employed by the Company.

Net periodic benefit costs and related components for the SERPs for the three- and nine-month periods ended June 28, 2014 and June 29, 2013 are as follows:

	Three Months Ended		Nine Months Ended	
	June 28, 2014	June 29, 2013	June 28, 2014	June 29, 2013
<i>(In thousands)</i>				
Service cost	\$55	\$60	\$165	\$180
Interest cost	79	72	237	216
Amortization of prior service cost	-	57	-	171
Recognized net actuarial loss	13	34	39	102
Net periodic benefit cost	\$147	\$223	\$441	\$669

(7) Long-Term Debt

Revolving Credit Facility. The Company has a revolving credit facility (the “Credit Facility”) that is used to supplement its operating cash flow and fund its working capital, capital expenditure, general corporate and growth requirements. On February 6, 2012, the Company and each of its wholly-owned subsidiaries entered into an amendment agreement that, among other changes, increased the commitment amount of the Credit Facility from \$75.0 million to \$100.0 million and extended the maturity date from June 2, 2015 to June 2, 2016. Advances under the Credit Facility are limited to the lesser of the revolving loan commitment amount (currently \$100.0 million) or a borrowing base amount that is calculated based upon a percentage of eligible receivables and inventories. As of June 28, 2014, no borrowings were outstanding on the Credit Facility, \$91.2 million of borrowing capacity was available and outstanding letters of credit totaled \$1.5 million.

Interest rates on the Credit Facility are based upon (1) an index rate that is established at the highest of the prime rate, 0.50% plus the federal funds rate or the LIBOR rate plus the excess of the then-applicable margin for LIBOR loans over the then-applicable margin for index rate loans, or (2) at the election of the Company, a LIBOR rate, plus in either case, an applicable interest rate margin. The applicable interest rate margins are adjusted on a quarterly basis based upon the amount of excess availability on the Credit Facility within the range of 0.50% - 1.25% for index rate loans and 1.50% - 2.50% for LIBOR loans. In addition, the applicable interest rate margins would be increased by 2.00% upon the occurrence of certain events of default provided for under the terms of the Credit Facility. Based on the Company’s excess availability as of June 28, 2014, the applicable interest rate margins on the Credit Facility were 0.50% for index rate loans and 1.50% for LIBOR loans.

The Company's ability to borrow available amounts under the Credit Facility will be restricted or eliminated in the event of certain covenant breaches, events of default or if the Company is unable to make certain representations and warranties provided for under the terms of the Credit Facility. The Company is required to maintain a fixed charge coverage ratio of not less than 1.10 at the end of each fiscal quarter for the twelve-month period then ended when the amount of liquidity on the Credit Facility is less than \$13.5 million. In addition, the terms of the Credit Facility restrict the Company's ability to, among other things: engage in certain business combinations or divestitures; make investments in or loans to third parties, unless certain conditions are met with respect to such investments or loans; pay cash dividends or repurchase shares of the Company's stock subject to certain minimum borrowing availability requirements; incur or assume indebtedness; issue securities; enter into certain transactions with affiliates of the Company; or permit liens to encumber the Company's property and assets. The terms of the Credit Facility also provide that an event of default will occur with respect to the Company upon the occurrence of, among other things: defaults or breaches under the loan documents, subject in certain cases to cure periods; defaults or breaches by the Company or any of its subsidiaries under any agreement resulting in the acceleration of amounts above certain thresholds or payment defaults above certain thresholds; certain events of bankruptcy or insolvency with respect to the Company; certain entries of judgment against the Company or any of its subsidiaries, which are not covered by insurance; or a change of control of the Company. As of June 28, 2014, the Company was in compliance with all of the financial and negative covenants under the Credit Facility and there have not been any events of default.

Amortization of capitalized financing costs associated with the Credit Facility was \$26,000 for each of the three-month periods ended June 28, 2014 and June 29, 2013 and \$77,000 for each of the nine-month periods ended June 28, 2014 and June 29, 2013. Accumulated amortization of capitalized financing costs was \$4.4 million and \$4.3 million as of June 28, 2014 and September 28, 2013, respectively.

(8) Earnings Per Share

The computations of basic and diluted earnings per share attributable to common shareholders for the three- and nine-month periods ended June 28, 2014 and June 29, 2013 are as follows:

	Three Months Ended		Nine Months Ended	
	June 28, 2014	June 29, 2013	June 28, 2014	June 29, 2013
<i>(In thousands except per share amounts)</i>				
Net earnings available to common shareholders	\$5,797	\$3,274	\$12,066	\$9,390
Basic weighted average shares outstanding	18,267	18,066	18,230	17,879
Dilutive effect of stock-based compensation	416	431	406	411
Diluted weighted average shares outstanding	\$18,683	\$18,497	\$18,636	\$18,290

Net earnings per share:

Basic	\$0.32	\$0.18	\$0.66	\$0.53
Diluted	\$0.31	\$0.18	\$0.65	\$0.51

Options representing 105,000 and 93,000 shares for the three-month periods ended June 28, 2014 and June 29, 2013, respectively, were antidilutive and were not included in the diluted earnings per share calculation. Options and RSUs representing 125,000 and 265,000 shares for the nine-month periods ended June 28, 2014 and June 29, 2013, respectively, were antidilutive and were not included in the diluted earnings per share calculation.

(9) Share Repurchases

On November 18, 2008, the Company's board of directors approved a share repurchase authorization to buy back up to \$25.0 million of the Company's outstanding common stock (the "Authorization"). Under the Authorization, repurchases may be made from time to time in the open market or in privately negotiated transactions subject to market conditions, applicable legal requirements and other factors. The Company is not obligated to acquire any particular amount of common stock and the program may be commenced or suspended at any time at the Company's discretion without prior notice. The Authorization continues in effect until terminated by the Board of Directors. As of June 28, 2014, there was \$24.8 million remaining available for future share repurchases under this authorization. No repurchases of common stock were made during the three- and nine-month periods ended June 28, 2014 and June 29, 2013.

(10) Other Financial Data

Balance sheet information:

<i>(In thousands)</i>	June 28, 2014	September 28, 2013
Accounts receivable, net:		
Accounts receivable	\$47,523	\$ 42,006
Less allowance for doubtful accounts	(878)	(896)
Total	\$46,645	\$ 41,110
Inventories, net:		
Raw materials	\$48,947	\$ 33,842
Work in process	3,250	3,074
Finished goods	26,970	21,877
Total	\$79,167	\$ 58,793
Other current assets:		
Current deferred tax asset	\$2,830	\$ 2,732
Prepaid insurance	1,575	1,332
Other	1,277	1,799
Total	\$5,682	\$ 5,863
Other assets:		
Cash surrender value of life insurance policies	\$6,718	\$ 6,145
Intangible asset, net of accumulated amortization of \$446 and \$163	1,441	1,724
Capitalized financing costs, net	95	171
Other	97	350
Total	\$8,351	\$ 8,390
Property, plant and equipment, net:		
Land and land improvements	\$9,192	\$ 9,175
Buildings	39,843	42,258
Machinery and equipment	130,168	129,861
Construction in progress	4,665	210
	183,868	181,504
Less accumulated depreciation	(103,123)	(98,451)
Total	\$80,745	\$ 83,053
Accrued expenses:		
Salaries, wages and related expenses	\$3,829	\$ 2,790
Accrued income taxes	1,051	-
Customer rebates	958	813

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Property taxes	802	1,155
Pension plan	751	928
Deferred revenues	551	79
Workers' compensation	290	307
Other	814	782
Total	\$9,046	\$ 6,854
Other liabilities:		
Deferred income taxes	\$7,266	\$ 7,281
Deferred compensation	7,112	6,897
Total	\$14,378	\$ 14,178

(11) Business Segment Information

The Company's operations are entirely focused on the manufacture and marketing of concrete reinforcing products for the concrete construction industry. The Company's concrete reinforcing products consist of welded wire reinforcement and prestressed concrete strand ("PC strand"). Based on the criteria specified in ASC Topic 280, *Segment Reporting*, the Company has one reportable segment.

(12) Contingencies

Insurance recoveries. On January 21, 2014, a fire occurred at the Company's Gallatin, Tennessee PC strand manufacturing facility. The fire damaged a portion of the facility, requiring the temporary curtailment of operations until the necessary repairs are completed. The Company has shifted a portion of its production requirements to its other PC strand manufacturing facility located in Sanderson, Florida, which was operating at a reduced utilization level.

The Company maintains general liability, business interruption and replacement cost property insurance coverage on its facilities that it believes is sufficient to cover the currently foreseeable losses arising from the fire. During the three months ended June 28, 2014 the Company received \$2.7 million of insurance proceeds that were used to cover costs incurred to date for additional plant expenses and the replacement of damaged property and equipment. The insurance proceeds attributable to the additional plant expenses were recorded in cost of sales (\$1.4 million) and selling, general and administrative expense (\$73,000) on the consolidated statement of operations and comprehensive income. During the nine months ended June 28, 2014, the Company received \$4.0 million of insurance proceeds which were recorded in cost of sales (\$2.5 million) and selling, general and administrative expense (\$98,000). The insurance proceeds attributable to the property and equipment damaged in the fire are reported in cash flows from investing activities and all other insurance proceeds received are reported in cash flows from operating activities on the consolidated statement of cash flows. The repairs to the damaged portion of the facility are expected to be completed during the fourth quarter of 2014.

Legal proceedings. The Company is involved in legal proceedings, claims, investigations and proceedings, including commercial, environmental and employment matters, which arise in the ordinary course of business. The Company does not expect that the ultimate costs to resolve these matters will have a material adverse effect on its financial position, results of operations or cash flows.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

Cautionary Note Regarding Forward-Looking Statements

This report contains forward-looking statements within the meaning of the safe harbor provisions of the Private Securities Litigation Reform Act of 1995, particularly under the caption “Outlook” below. When used in this report, the words “believes,” “anticipates,” “expects,” “estimates,” “plans,” “intends,” “will,” “may,” “should,” “could” and similar expressions are intended to identify forward-looking statements. Although we believe that our plans, intentions and expectations reflected in or suggested by such forward-looking statements are reasonable, such forward-looking statements are subject to a number of risks and uncertainties, and we can provide no assurances that such plans, intentions or expectations will be implemented or achieved. All forward-looking statements are based on information that is current as of the date of this report. Many of these risks and uncertainties are discussed in detail, and where appropriate, updated in our periodic and other reports and statements, in particular under the caption “Risk Factors” in our Annual Report on Form 10-K for the year ended September 28, 2013, filed with the U.S. Securities and Exchange Commission (“SEC”). You should carefully review these risks and uncertainties.

All forward-looking statements attributable to us or persons acting on our behalf are expressly qualified in their entirety by these cautionary statements. All forward-looking statements speak only to the respective dates on which such statements are made and we do not undertake and specifically decline any obligation to publicly release the results of any revisions to these forward-looking statements that may be made to reflect any future events or circumstances after the date of such statements or to reflect the occurrence of anticipated or unanticipated events, except as may be required by law.

It is not possible to anticipate and list all risks and uncertainties that may affect our future operations or financial performance; however, they would include, but are not limited to, the following:

general economic and competitive conditions in the markets in which we operate;

credit market conditions and the relative availability of financing for us, our customers and the construction industry as a whole;

the continuation of reduced spending for nonresidential and residential construction and the impact on demand for our products;

changes in the amount and duration of transportation funding provided by federal, state and local governments and the impact on spending for infrastructure construction and demand for our products;

the cyclical nature of the steel and building material industries;

fluctuations in the cost and availability of our primary raw material, hot-rolled steel wire rod, from domestic and foreign suppliers;

competitive pricing pressures and our ability to raise selling prices in order to recover increases in wire rod costs;

changes in United States or foreign trade policy affecting imports or exports of steel wire rod or our products;

unanticipated changes in customer demand, order patterns and inventory levels;

the impact of weak demand and reduced capacity utilization levels on our unit manufacturing costs;

our ability to further develop the market for engineered structural mesh (“ESM”) and expand our shipments of ESM;

legal, environmental, economic or regulatory developments that significantly impact our operating costs;

unanticipated plant outages, equipment failures or labor difficulties;

continued escalation in certain of our operating costs;

the adverse impact of the fire at our Gallatin, Tennessee PC strand manufacturing facility, including operational interruptions, higher than anticipated repair costs, reduced production levels and lower than anticipated insurance reimbursements; and

the “Risk Factors” discussed in our Annual Report on Form 10-K for the year ended September 28, 2013 and in other filings that we make with the SEC.

Overview

Insteel Industries, Inc. is the nation's largest manufacturer of steel wire reinforcing products for concrete construction applications. We manufacture and market PC strand and welded wire reinforcement, including ESM, concrete pipe reinforcement and standard welded wire reinforcement. Our products are sold primarily to manufacturers of concrete products that are used in nonresidential construction. We market our products through sales representatives who are our employees. Our products are sold nationwide as well as into Canada, Mexico, and Central and South America, and delivered primarily by truck, using common or contract carriers. Our business strategy is focused on: (1) achieving leadership positions in our markets; (2) operating as the lowest cost producer; and (3) pursuing growth opportunities within our core businesses that further our penetration of the markets we currently serve or expand our geographic footprint.

Results of Operations

Statements of Operations – Selected Data

(Dollars in thousands)

	Three Months Ended			Nine Months Ended		
	June 28, 2014	Change	June 29, 2013	June 28, 2014	Change	June 29, 2013
Net sales	\$113,227	16.8 %	\$96,946	\$291,881	9.9 %	\$265,706
Gross profit	14,263	30.7 %	10,910	34,924	14.3 %	30,554
<i>Percentage of net sales</i>	<i>12.6 %</i>		<i>11.3 %</i>	<i>12.0 %</i>		<i>11.5 %</i>
Selling, general and administrative expense	\$6,219	15.7 %	\$5,373	\$16,908	9.4 %	\$15,460
<i>Percentage of net sales</i>	<i>5.5 %</i>		<i>5.5 %</i>	<i>5.8 %</i>		<i>5.8 %</i>
Other expense (income), net	\$(849)	) N/M	\$415	\$(653)	) N/M	\$330
Interest expense	56	(1.8%)	57	169	(7.1%)	182
Interest income	(4)	) (63.6%)	(11)	(10)	) (23.1%)	(13)
Effective income tax rate	34.4 %		35.5 %	34.8 %		35.7 %
Net earnings	\$5,797	77.1 %	\$3,274	\$12,066	28.5 %	\$9,390

"N/M" = not meaningful

Third Quarter of Fiscal 2014 Compared to Third Quarter of Fiscal 2013

Net Sales

Net sales for the third quarter of 2014 increased 16.8% to \$113.2 million from \$96.9 million in the same year-ago period. Shipments for the quarter increased 16.0% and average selling prices increased 0.7% from the prior year levels. The increase in shipments was primarily due to improved market conditions and increased demand for our products relative to the prior year period. Sales for both periods reflect depressed volumes on an absolute basis relative to prerecession levels in our construction end-markets.

Gross Profit

Gross profit for the third quarter of 2014 increased 30.7% to \$14.3 million, or 12.6% of net sales, from \$10.9 million, or 11.3% of net sales, in the same year-ago period. The year-over-year increase was primarily due to higher shipments (\$1.8 million), higher spreads between average selling prices and raw material costs (\$1.7 million) and lower unit conversion costs (\$0.4 million). The increase in spreads was driven by lower raw material costs (\$1.2 million) and higher average selling prices (\$0.8 million) partially offset by higher freight expense (\$0.3 million). Gross profit for both periods was unfavorably impacted by depressed shipment volumes and elevated unit conversion costs resulting from reduced operating schedules.

Selling, General and Administrative Expense

Selling, general and administrative expense (“SG&A expense”) for the third quarter of 2014 increased 15.7% to \$6.2 million, or 5.5% of net sales, from \$5.4 million, or 5.5% of net sales, in the same year-ago period primarily due to higher compensation expense (\$0.8 million), partially offset by the relative year-over-year change in the cash surrender value of life insurance policies (\$0.1 million). The increase in compensation expense was primarily driven by higher incentive plan expense due to our improved financial results in the current year. The cash surrender value of life insurance policies increased \$110,000 in the current year quarter compared with an increase of \$1,000 in the prior year quarter due to the changes in the value of the underlying investments.

Other Expense (Income)

Other income for the third quarter of 2014 was \$0.8 million compared to other expense of \$0.4 million in the same year-ago period. The income for the current year period was primarily related to the net gain from insurance proceeds attributable to the replacement of property and equipment damaged in the fire at our Gallatin, Tennessee PC strand manufacturing facility. Other expense for the third quarter of 2013 was primarily due to a net loss on the disposal of equipment.

Interest Expense

Interest expense for the third quarter of 2014 was relatively flat year-over-year.

Income Taxes

Our effective income tax rate for the third quarter of 2014 decreased to 34.4% from 35.5% in the same year-ago period primarily due to changes in permanent tax differences.

Net Earnings

Net earnings for the third quarter of 2014 were \$5.8 million (\$0.31 per diluted share) compared to \$3.3 million (\$0.18 per share) in the same year-ago period primarily due to the increase in gross profit partially offset by the increase in SG&A expense.

First Nine Months of Fiscal 2014 Compared to Nine Months of Fiscal 2013

Net Sales

Net sales for the first nine months of 2014 increased 9.9% to \$291.9 million from \$265.7 million in the same year-ago period. Shipments for the period increased 11.9% while average selling prices decreased 1.9% from the prior year levels. The increase in shipments was primarily due to improved market conditions and increased demand for our products during the period. The decrease in average selling prices was driven by competitive pricing pressures. Sales for both periods reflect depressed volumes on an absolute basis relative to prerecession levels in our construction end-markets.

Gross Profit

Gross profit for the first nine months of 2014 increased 14.3% to \$34.9 million, or 12.0% of net sales, from \$30.6 million, or 11.5% of net sales, in the same year-ago period. The year-over-year increase was primarily due to higher shipments (\$3.9 million) and wider spreads between average selling prices and raw material costs (\$2.1 million) partially offset by higher unit conversion costs (\$0.5 million). The increase in spreads was driven by lower raw material costs (\$7.7 million) partially offset by lower average selling prices (\$5.5 million) and higher freight expense (\$0.1 million). Gross profit for both periods was unfavorably impacted by depressed shipment volumes and elevated unit conversion costs resulting from reduced operating schedules.

Selling, General and Administrative Expense

SG&A expense for the first nine months of 2014 increased 9.4% to \$16.9 million, or 5.8% of net sales, from \$15.5 million, or 5.8% of net sales, in the same year-ago period primarily due to increases in incentive compensation (\$0.8 million), bad debt (\$0.2 million), amortization (\$0.1 million) and employee benefit expense (\$0.1 million), partially offset by the relative year-over-year change in the cash surrender value of life insurance policies (\$0.2 million). The increase in compensation expense was primarily driven by higher incentive plan expense due to our improved financial results in the current year. The increase in bad debt expense resulted from an adjustment to the allowance for doubtful accounts that was driven by the increases in sales and accounts receivable. The cash surrender value of life insurance policies increased \$468,000 in the current year period compared with an increase of \$292,000 in the prior year period due to the changes in the value of the underlying investments.

Other Expense (Income)

Other income for the first nine months of 2014 was \$0.7 million compared to other expense of \$0.3 million in the same year-ago period. The income for the current year period was primarily related to the net gain from insurance proceeds attributable to the replacement of property and equipment damaged in the fire at our Gallatin, Tennessee PC strand manufacturing facility. Other expense for the same year-ago period was primarily due to a net loss on the disposal of equipment.

Interest Expense

Interest expense for the first nine months of 2014 was relatively flat year-over-year.

Income Taxes

Our effective income tax rate for the first nine months of 2014 decreased to 34.8% from 35.7% in the prior year period due to changes in permanent tax differences.

Net Earnings

Net earnings for the first nine months of 2014 were \$12.1 million (\$0.65 per diluted share) compared to \$9.4 million (\$0.51 per diluted share) in the same year-ago period primarily due to the increase in gross profit partially offset by the increase in SG&A expense.

Liquidity and Capital Resources**Selected Financial Data**

(Dollars in thousands)

Operating Activities

	Nine Months Ended	
	June 28, 2014	June 29, 2013
Net cash provided by operating activities	\$22,133	\$32,063
Net cash used for investing activities	(4,564)	(5,639)
Net cash used for financing activities	(1,560)	(14,350)
Net working capital	98,621	78,096
Total debt	-	-
<i>Percentage of total capital</i>	-	-
Shareholders' equity	\$173,339	\$157,849
<i>Percentage of total capital</i>	100.0 %	100.0 %
Total capital (total debt + shareholders' equity)	\$173,339	\$157,849

Operating activities provided \$22.1 million of cash during the first nine months of 2014 primarily from net earnings adjusted for non-cash items and a reduction in the net working capital components of accounts receivable, inventories, and accounts payable and accrued expenses. Net working capital provided \$2.2 million of cash due to a \$28.1 million increase in accounts payable and accrued expenses partially offset by a \$20.4 million increase in inventories and a \$5.5 million increase in accounts receivable. The increase in accounts payable and accrued expenses was largely due to higher raw material purchases and changes in the mix of vendor payments and terms. The increase in inventories was primarily driven by higher receipts of imported raw materials which are purchased in larger quantities. The increase in accounts receivable was principally due to the increase in sales.

Operating activities provided \$32.1 million of cash during the first nine months of 2013 primarily from net earnings adjusted for non-cash items and a reduction in the net working capital components of accounts receivable, inventories, and accounts payable and accrued expenses. Net working capital provided \$11.3 million of cash due to a \$4.8 million decrease in accounts receivable and a \$9.3 million increase in accounts payable and accrued expenses partially offset by a \$2.8 million increase in inventories. The decrease in accounts receivable was primarily driven by a reduction in days sales outstanding. The increase in accounts payable and accrued expenses was due to higher raw material purchases and changes in the mix of vendor payments and related terms.

We may elect to make adjustments in our operating activities as there are changes in the conditions in our construction end markets, which could materially impact our cash requirements. While a downturn in the level of construction activity adversely affects sales to our customers, it generally reduces our working capital requirements.

Investing Activities

Investing activities used \$4.6 million of cash during the first nine months of 2014 compared to \$5.6 million during the same period last year. Capital expenditures for the first nine months of 2014 were \$5.8 million, including \$1.9 million of outlays related to the replacement of property and equipment damaged in the fire at our Gallatin, Tennessee PC strand manufacturing facility for which the Company expects to be reimbursed under its insurance coverage, compared with \$4.4 million in the prior year period. Capital expenditures for fiscal 2014 are not expected to exceed \$5.0 million, excluding the outlays related to the Gallatin fire. The current year uses of cash were offset by the receipt of \$1.4 million of insurance proceeds related to the Gallatin fire. Prior year investing activities include the acquisition of an intangible asset for \$1.9 million in connection with the April 2013 acquisition of certain assets from Tatano Wire and Steel, Inc. partially offset by \$0.5 million of proceeds from life insurance claims. Our investing activities are largely discretionary, providing us with the ability to significantly curtail outlays should business conditions warrant that such actions be taken.

Financing Activities

Financing activities used \$1.6 million of cash during the first nine months of 2014 compared to \$14.4 million during the same period last year. Net repayments of borrowings on our revolving credit facility used \$11.5 million of cash in the prior year period. Cash dividend payments were \$1.6 million (\$0.09 per share) in the current year and \$6.1 million in the prior year period, including a special cash dividend of \$4.5 million (\$0.25 per share) and regular cash dividends totaling \$1.6 million (\$0.09 per share). The current year and prior year uses of cash were partially offset by \$0.4 million and \$3.4 million, respectively, of proceeds from the exercise of stock options. While we intend to pay regular quarterly cash dividends for the foreseeable future, the declaration and payment of future dividends, if any, are discretionary and will be subject to determination by the board of directors each quarter after taking into account various factors.

Cash Management

Our cash is concentrated primarily at one financial institution, which at times exceeds federally insured limits. We invest excess cash primarily in money market funds, which are highly liquid securities that bear minimal risk.

Credit Facility

We have a revolving credit facility (the “Credit Facility”) that is used to supplement our operating cash flow and fund our working capital, capital expenditure, general corporate and growth requirements. The Credit Facility provides for up to \$100.0 million of financing and matures in June 2016. As of June 28, 2014, no borrowings were outstanding on the Credit Facility, \$91.2 million of borrowing capacity was available and outstanding letters of credit totaled \$1.5 million.

We believe that, in the absence of significant unanticipated cash demands, cash and cash equivalents, net cash generated by operating activities, and the borrowing availability provided under the Credit Facility will be sufficient to satisfy our expected requirements for working capital, capital expenditures, dividends and share repurchases, if any. We expect to have access to the amounts available under the Credit Facility as required. However, deterioration in our construction end-markets could result in reduced demand from our customers, which would likely reduce our operating cash flows. Under such circumstances, we may need to curtail capital and operating expenditures, delay or restrict share repurchases, cease dividend payments and/or realign our working capital requirements.

Should we determine, at any time, that we required additional short-term liquidity, we would evaluate the alternative sources of financing that were potentially available to provide such funding. There can be no assurance that any such financing, if pursued, would be obtained, or if obtained, would be adequate or on terms acceptable to us. However, we believe that our strong balance sheet, flexible capital structure and borrowing capacity available to us under the Credit Facility position us to meet our anticipated liquidity requirements for the foreseeable future.

Seasonality and Cyclical

Demand in our markets is both seasonal and cyclical, driven by the level of construction activity, but can also be impacted by fluctuations in the inventory positions of our customers. From a seasonal standpoint, the highest level of sales within the year typically occurs when weather conditions are the most conducive to construction activity. As a result, sales and profitability are usually higher in the third and fourth quarters of the fiscal year and lower in the first and second quarters. From a cyclical standpoint, the level of construction activity tends to be correlated with general

economic conditions although there can be significant differences between the relative performance of nonresidential versus residential construction for extended periods.

Impact of Inflation

We are subject to inflationary risks arising from fluctuations in the market prices for our primary raw material, hot-rolled steel wire rod, and, to a much lesser extent, freight, energy and other consumables that are used in our manufacturing processes. We have generally been able to adjust our selling prices to pass through increases in these costs or offset them through various cost reduction and productivity improvement initiatives. However, our ability to raise our selling prices depends on market conditions and competitive dynamics, and there may be periods during which we are unable to fully recover increases in our costs. Inflation did not have a material impact on our sales or earnings during the third fiscal quarter of 2014. The timing and magnitude of any future increases or decreases in the prices for wire rod and the impact on selling prices for our products is uncertain at this time.

Off-Balance Sheet Arrangements

We do not have any material transactions, arrangements, obligations (including contingent obligations), or other relationships with unconsolidated entities or other persons, as defined by Item 303(a)(4) of Regulation S-K of the SEC, that have or are reasonably likely to have a material current or future impact on our financial condition, results of operations, liquidity, capital expenditures, capital resources or significant components of revenues or expenses.

Contractual Obligations

There have been no material changes in our contractual obligations and commitments as disclosed in our Annual Report on Form 10-K as of September 28, 2013 other than those which occur in the ordinary course of business.

Critical Accounting Policies

Our Management's Discussion and Analysis of Financial Condition and Results of Operations is based on our unaudited financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States ("GAAP") for interim financial information. The preparation of our financial statements requires the application of accounting policies in addition to certain estimates and judgments based on current available information, actuarial estimates, historical results and other assumptions believed to be reasonable. Actual results could differ from these estimates. Please refer to "Management's Discussion and Analysis of Financial Condition and Results of Operations – Critical Accounting Policies" included in our Annual Report on Form 10-K for the year ended September 28, 2013 for further information regarding our critical accounting policies and estimates. As of June 28, 2014, there were no changes in the nature of our critical accounting policies or the application of those policies from those reported in our Annual Report on Form 10-K for the year ended September 28, 2013.

Recent Accounting Pronouncements

Refer to Note 2 of the Notes to Consolidated Financial Statements in Item 1 of this Quarterly Report for recently adopted and issued accounting pronouncements since the filing of our Form 10-K for the year ended September 28, 2013, including the expected dates of adoption and estimated effects, if any, on our consolidated financial statements.

Outlook

As we look ahead to the remainder of 2014, we expect continued improvement in the conditions in our construction end-markets following the steep decline in demand that we have experienced in recent years. There are growing indications the recovery in private nonresidential construction, our primary demand driver, is strengthening, which should favorably impact our financial results through higher shipment volumes and operating levels at our facilities. The outlook for infrastructure construction is less clear pending the enactment of a new federal transportation funding authorization.

We continue to focus on the operational fundamentals of our business: closely managing and controlling our expenses; aligning our production schedules with demand in a proactive manner as there are changes in market conditions to minimize our cash operating costs; and pursuing further improvements in the productivity and effectiveness of all of our manufacturing, selling and administrative activities. We expect the contributions from our 2010 acquisition of Ivy Steel and Wire, Inc. will increase during the remainder of the year through the realization of additional operational synergies and the anticipated benefits from the reconfiguration of our combined welded wire reinforcement operations. As market conditions improve, we also expect gradually increasing contributions from the substantial investments we have made in our facilities in the form of reduced operating costs and additional capacity to support future growth (see “Cautionary Note Regarding Forward-Looking Statements” and “Risk Factors”). In addition, we will continue to pursue further potential acquisitions in our existing businesses that expand our penetration of markets we currently serve or expand our geographic footprint.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Our cash flows and earnings are subject to fluctuations resulting from changes in commodity prices, interest rates and foreign exchange rates. We manage our exposure to these market risks through internally established policies and procedures and, when deemed appropriate, through the use of derivative financial instruments. We do not use financial instruments for trading purposes and we are not a party to any leveraged derivatives. We monitor our underlying market risk exposures on an ongoing basis and believe that we can modify or adapt our hedging strategies as necessary.

Commodity Prices

We are subject to significant fluctuations in the cost and availability of our primary raw material, hot-rolled steel wire rod, which we purchase from both domestic and foreign suppliers. We negotiate quantities and pricing for both domestic and foreign wire rod purchases for varying periods (most recently monthly for domestic suppliers), depending upon market conditions, to manage our exposure to price fluctuations and to ensure adequate availability of material consistent with our requirements. We do not use derivative commodity instruments to hedge our exposure to changes in prices as such instruments are not currently available for wire rod. Our ability to acquire wire rod from foreign sources on favorable terms is impacted by fluctuations in foreign currency exchange rates, foreign taxes, duties, tariffs and other trade actions. Although changes in wire rod costs and our selling prices may be correlated over extended periods of time, depending upon market conditions and competitive dynamics, there may be periods during which we are unable to fully recover increased wire rod costs through higher selling prices, which would reduce our gross profit and cash flow from operations. Additionally, should wire rod costs decline, our financial results may be negatively impacted if the selling prices for our products decrease to an even greater degree and to the extent that we are consuming higher cost material from inventory. Based on our shipments and average wire rod cost reflected in cost of sales for the first nine months of 2014, a 10% increase in the price of steel wire rod would have resulted in a \$18.7 million decrease in our pre-tax earnings for the nine months ended June 28, 2014 (assuming there was not a corresponding change in our selling prices).

Interest Rates

Although we did not have any balances outstanding on our revolving credit facility as of June 28, 2014, future borrowings under the facility are subject to a variable rate of interest and are sensitive to changes in interest rates.

Foreign Exchange Exposure

We have not typically hedged foreign currency exposures related to transactions denominated in currencies other than U.S. dollars, as such transactions have not been material historically. We will occasionally hedge firm commitments for certain equipment purchases that are denominated in foreign currencies. The decision to hedge any such transactions is made by us on a case-by-case basis. There were no forward contracts outstanding as of June 28, 2014.

Item 4. Controls and Procedures

We have conducted an evaluation of the effectiveness of our disclosure controls and procedures as of June 28, 2014. This evaluation was conducted under the supervision and with the participation of management, including our principal executive officer and our principal financial officer. Based upon that evaluation, our principal executive officer and our principal financial officer concluded that our disclosure controls and procedures were effective to ensure that information required to be disclosed in the reports that we file or submit under the Securities Exchange Act of 1934, as amended (the "Exchange Act"), is recorded, processed, summarized and reported within the time periods specified in the Commission's rules and forms. Further, we concluded that our disclosure controls and procedures were effective to ensure that information is accumulated and communicated to management, including our principal executive officer and our principal financial officer, as appropriate to allow timely decisions regarding required disclosure.

There has been no change in our internal control over financial reporting that occurred during the quarter ended June 28, 2014 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II – OTHER INFORMATION

Item 1. Legal Proceedings

We are involved in various lawsuits, claims, investigations and proceedings, including commercial, environmental and employment matters, which arise in the ordinary course of business. We do not expect that the ultimate costs to resolve these matters will have a material adverse effect on our financial position, results of operations or cash flows.

Item 1A. Risk Factors

During the quarter ended June 28, 2014, there were no material changes from the risk factors set forth under Part I, Item 1A., "Risk Factors" in our Annual Report on Form 10-K for the fiscal year ended September 28, 2013. You should carefully consider these factors in addition to the other information set forth in this report which could materially affect our business, financial condition or future results. The risks and uncertainties described in this report and in our Annual Report on Form 10-K for the year ended September 28, 2013, as well as other reports and statements that we file with the SEC, are not the only risks and uncertainties facing us. Additional risks and uncertainties not currently known to us or that we currently deem to be immaterial may also have a material adverse effect on our financial position, results of operations or cash flows.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

On November 18, 2008, our Board of Directors approved a share repurchase authorization to buy back up to \$25.0 million of our outstanding common stock (the "Authorization"). Under the Authorization, repurchases may be made from time to time in the open market or in privately negotiated transactions subject to market conditions, applicable legal requirements and other factors. We are not obligated to acquire any particular amount of common stock and the program may be commenced or suspended at any time at our discretion without prior notice. The Authorization continues in effect until terminated by the Board of Directors. As of June 28, 2014, there was \$24.8 million remaining available for future share repurchases under this authorization. No repurchases of common stock were made during the three- and nine-month periods ended June 28, 2014 and June 29, 2013.

Item 6. Exhibits

- 31.1 Certification of the Chief Executive Officer pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 31.2 Certification of the Chief Financial Officer pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
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- 101 The following financial information from the Quarterly Report on Form 10-Q of Insteel Industries, Inc. for the quarter ended June 28, 2014, formatted in XBRL (eXtensible Business Reporting Language): (i) the Consolidated Statements of Operations and Comprehensive Income for the three and nine months ended June 28, 2014 and June 29, 2013, (ii) the Consolidated Balance Sheets as of June 28, 2014 and September 28, 2013, (iii) the Consolidated Statements of Cash Flows for the nine months ended June 28, 2014 and June 29, 2013, (iv) the Consolidated Statements of Shareholders' Equity as of June 28, 2014 and September 28, 2013, and (v) the Notes to Consolidated Financial Statements.

SIGNATURES

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

INSTEEL INDUSTRIES, INC.

Registrant

Date: July 17, 2014 By: /s/ Michael C. Gazmarian
Michael C. Gazmarian
Vice President, Chief Financial Officer and Treasurer
(Duly Authorized Officer and Principal Financial Officer)

EXHIBIT INDEX

Exhibit

Number Description

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