

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

FORM 10-Q

(Mark One)

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

For the quarterly period ended DECEMBER 31, 2002

or

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number: 1-11692

ETHAN ALLEN INTERIORS INC.

(Exact name of registrant as specified in its charter)

DELAWARE

06-1275288

(State or other jurisdiction of incorporation or organization) (I.R.S. Employer ID No.)

ETHAN ALLEN DRIVE, DANBURY, CONNECTICUT 06811

(Address of principal executive offices)

(203) 743-8000

(Registrant's telephone number, including area code)

N/A

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

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

Yes  No

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act).

Yes  No

APPLICABLE ONLY TO ISSUERS INVOLVED IN BANKRUPTCY  
PROCEEDINGS DURING THE PRECEDING FIVE YEARS:

Indicate by check mark whether the registrant has filed all documents and reports required to be filed by Sections 12, 13 or 15(d) of the Securities Exchange Act of 1934 subsequent to the distribution of securities under a plan confirmed by a court.

Yes  No

APPLICABLE ONLY TO CORPORATE ISSUERS:

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

As of December 31, 2002, there were 37,773,539 shares  
of Common Stock, par value \$.01 outstanding.

ETHAN ALLEN INTERIORS INC. AND SUBSIDIARY

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PART I - FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS  
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ETHAN ALLEN INTERIORS INC. AND SUBSIDIARY  
CONSOLIDATED BALANCE SHEETS  
(In thousands, except share data)

<CAPTION>

	December 31, 2002	June 2002
	(unaudited)	(unaudited)
	-----	-----
30,---		
<S>	<C>	<C>
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 69,557	\$
75,688		
Accounts receivable, less allowance for doubtful accounts of \$1,535 at December 31, 2002 and \$2,019 at June 30, 2002	21,859	
32,845		
Inventories, net (note 3)	179,842	
174,147		
Prepaid expenses and other current assets	22,259	
18,731		
Deferred income taxes	18,304	
17,345	-----	-----

---			
	Total current assets	311,821	
318,756			
	Property, plant and equipment, net	302,925	
293,626			
	Intangible assets, net (note 5)	78,354	
69,708			
	Other assets	5,788	
6,665			
		-----	-----
---			
	Total assets	\$ 698,888	\$
688,755			
		=====	
=====			
	LIABILITIES AND SHAREHOLDERS' EQUITY		
	Current liabilities:		
	Current maturities of long-term debt and capital		
	lease obligations	\$ 193	\$
107			
	Customer deposits	47,372	
42,966			
	Accounts payable	27,476	
38,027			
	Accrued compensation and benefits	28,479	
30,190			
	Accrued expenses (note 4)	16,020	
17,838			
		-----	-----
---			
	Total current liabilities	119,540	
129,128			
	Long-term debt	10,126	
9,214			
	Other long-term liabilities	2,442	
2,066			
	Deferred income taxes	38,783	
37,158			
		-----	-----
---			
	Total liabilities	170,891	
177,566			
	Shareholders' equity:		
	Class A common stock, par value \$.01, 150,000,000 shares		
	authorized; 45,289,349 shares issued at December 31,		
	2002 and 45,252,880 shares issued at June 30, 2002	453	
453			
	Class B common stock, par value \$.01, 600,000 shares		
	authorized; no shares issued and outstanding at		
	December 31, 2002 and June 30, 2002	--	
--			
	Preferred stock, par value \$.01, 1,055,000 shares		
	authorized; no shares issued and outstanding at		
	December 31, 2002 and June 30, 2002	--	
--			
	Additional paid-in capital	277,924	
277,694			
		-----	-----
---			
		278,377	
278,147			
	Less: Treasury stock (at cost), 7,515,810 shares at		
	December 31, 2002 and 6,794,510 shares at June 30, 2002	(183,809)	
(161,428)			
	Retained earnings	433,091	
394,470			
	Accumulated other comprehensive income (note 8)	338	-
-			
		-----	-----
---			
	Total shareholders' equity	527,997	
511,189			
		-----	-----
---			
	Total liabilities and shareholders' equity	\$ 698,888	\$
688,755			
		=====	

=====  
</TABLE>

See accompanying notes to consolidated financial statements.

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<TABLE>

ETHAN ALLEN INTERIORS INC. AND SUBSIDIARY  
CONSOLIDATED STATEMENTS OF OPERATIONS  
(UNAUDITED)  
(In thousands, except per share data)

<CAPTION>

Ended December 31, 2001	Three Months Ended		Six Months
	December 31,		
	2002	2001	2002
	-----	-----	-----
<S>	<C>	<C>	<C>
<C>			
Net sales \$429,582	\$229,713	\$222,857	\$446,242
Cost of sales 232,233	113,909	119,477	223,723
	-----	-----	-----
Gross profit 197,349	115,804	103,380	222,519
Operating expenses:			
Selling 78,724	43,875	39,886	86,765
General and administrative 58,884	34,734	30,288	66,716
	-----	-----	-----
Total operating expenses 137,608	78,609	70,174	153,481
	-----	-----	-----
Operating income 59,741	37,195	33,206	69,038
Interest and other miscellaneous income, net 1,558	125	1,046	741
Interest and other related financing costs 325	204	176	377
	-----	-----	-----
Income before income taxes 60,974	37,116	34,076	69,402
Income tax expense 23,048	14,030	12,881	26,234
	-----	-----	-----
Net income \$ 37,926	\$ 23,086	\$ 21,195	\$ 43,168
	=====	=====	=====

PER SHARE DATA (NOTE 7):

Basic earnings per common share:

Net income per basic share \$ 0.97	\$ 0.61	\$ 0.55	\$ 1.14
	=====	=====	=====

Basic weighted average common shares  
38,952

37,767                      38,691                      37,876

Diluted earnings per common share:

Net income per diluted share	\$ 0.60	\$ 0.53	\$ 1.11
\$ 0.95	=====	=====	=====
=====			
Diluted weighted average common shares 40,026	38,793	39,781	38,854

</TABLE>

See accompanying notes to consolidated financial statements.

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<TABLE>

ETHAN ALLEN INTERIORS INC. AND SUBSIDIARY  
CONSOLIDATED STATEMENTS OF CASH FLOWS  
(UNAUDITED)  
(In thousands)

<CAPTION>

	Six Months Ended December 31,	
	2002	2001
	-----	-----
<S>	<C>	<C>
Operating activities:		
Net income	\$ 43,168	\$ 37,926
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	10,367	9,455
Compensation expense related to restricted stock award	(398)	(223)
Provision for deferred income taxes	666	(1,432)
Other non-cash expense (income)	(112)	(542)
Change in assets and liabilities, net of the effects of acquired and divested businesses:		
Accounts receivable	10,467	8,495
Inventories	3,987	23,838
Prepaid and other current assets	(2,448)	1,120
Other assets	(404)	438
Customer deposits	(277)	(527)
Accounts payable	(7,213)	(14,853)
Income taxes payable	1,919	3,423
Accrued expenses	(3,539)	(2,197)
Other liabilities	(150)	(619)
	-----	-----
Net cash provided by operating activities	56,033	64,302
-	-----	-----
Investing activities:		
Proceeds from the disposal of property, plant and equipment	2,435	2,307
Capital expenditures	(16,925)	(17,709)
Acquisitions	(10,742)	(10,484)
Other	178	81
	-----	-----
Net cash used in investing activities	(25,054)	(25,805)
	-----	-----
Financing activities:		
Borrowings on revolving credit facility	--	--
Payments on revolving credit facility	--	--
Other payments on long-term debt and capital leases	(3,435)	(68)
Net proceeds from issuance of common stock	490	1,171
Dividends paid	(4,587)	(3,113)
Payments to acquire treasury stock	(29,578)	(20,781)
	-----	-----
Net cash used in financing activities	(37,110)	(22,791)
	-----	-----
Net (decrease) increase in cash and cash equivalents	(6,131)	15,706
Cash and cash equivalents - beginning of period	75,688	48,112

Cash and cash equivalents - end of period	\$ 69,557	\$ 63,818
	=====	=====

</TABLE>

See accompanying notes to consolidated financial statements.

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<TABLE>

ETHAN ALLEN INTERIORS INC. AND SUBSIDIARY  
CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY  
SIX MONTHS ENDED DECEMBER 31, 2002  
(Unaudited)  
(In thousands, except share data)

<CAPTION>

	Common Stock	Additional Paid-in Capital	Treasury Stock	Accumulated Other Comprehensive Income	Retained Earnings	
Total	-----	-----	-----	-----	-----	---
<S>	<C>	<C>	<C>	<C>	<C>	<C>
Balance at June 30, 2002 \$511,189	\$ 453	\$277,694	\$ (161,428)	\$ --	\$394,470	
Issuance of 36,469 shares of common stock upon the exercise of stock options	--	92	--	--	--	
92						
Purchase of 721,300 shares of treasury stock (22,381)	--	--	(22,381)	--	--	
Tax benefit associated with exercise of employee stock options 138	--	138	--	--	--	
Dividends declared on common stock (4,547)	--	--	--	--	(4,547)	
Other comprehensive income (note 8) 338	--	--	--	338	--	
Net income 43,168	--	--	--	--	43,168	
-----						---
Total comprehensive income 43,506	-----	-----	-----	-----	-----	---
-----						
Balance at December 31, 2002 \$527,997	\$ 453	\$277,924	\$ (183,809)	\$ 338	\$433,091	
=====	=====	=====	=====	=====	=====	

</TABLE>

See accompanying notes to consolidated financial statements.

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ETHAN ALLEN INTERIORS INC. AND SUBSIDIARY  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
(unaudited)

(1) BASIS OF PRESENTATION

Ethan Allen Interiors Inc. (the "Company") is a Delaware corporation

incorporated on May 25, 1989. The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiary Ethan Allen Inc. ("Ethan Allen") and Ethan Allen's subsidiaries. All of Ethan Allen's capital stock is owned by the Company. The Company has no other assets or operating results other than those associated with its investment in Ethan Allen.

(2) INTERIM FINANCIAL PRESENTATION

All intercompany accounts and transactions have been eliminated in the consolidated financial statements. In the opinion of the Company, all adjustments, consisting only of normal recurring accruals necessary for fair presentation, have been included in the financial statements. The results of operations for the three and six months ended December 31, 2002 are not necessarily indicative of results for the fiscal year. It is suggested that the interim consolidated financial statements be read in conjunction with the consolidated financial statements and accompanying notes included in the Company's Annual Report on Form 10-K for the year ended June 30, 2002.

Certain reclassifications have been made to prior year financial information in order to conform to the current year's presentation. These changes were made for disclosure purposes only and did not have an impact on previously reported results of operations or shareholders' equity.

(3) INVENTORIES

Inventories at December 31, 2002 and June 30, 2002 are summarized as follows (in thousands):

	December 31, 2002 -----	June 30, 2002 -----
Finished goods	\$130,061	\$123,906
Work in process	14,981	15,418
Raw materials	34,800	34,823
	-----	-----
	\$179,842	\$174,147
	=====	=====

(4) RESTRUCTURING AND IMPAIRMENT CHARGE

During each of the last two fiscal years, the Company developed and executed plans to consolidate its manufacturing operations as part of an overall strategy to maximize production efficiencies and maintain its competitive advantage. In the fourth quarter of fiscal 2002, the Company initiated a plan which involved the closure of one of its manufacturing facilities as well as the rough mill operation of a separate facility. Closure of these facilities resulted in the elimination of approximately 220 employees; 150 employees effective June 29, 2002, and 70 employees terminated during the first quarter of fiscal 2003. A pre-tax restructuring and impairment charge of \$5.1 million was recorded for costs associated with these plant closings, of which \$2.0 million principally relates to employee severance and benefits costs and plant exit costs, and \$3.1 million relates to a fixed asset impairment charge, primarily for properties and machinery and equipment of the closed facilities.

In the fourth quarter of fiscal 2001, the Company announced the closure of three of its manufacturing facilities and the elimination of approximately 350 employees effective August 6, 2001. A pre-tax restructuring and impairment charge of \$6.9 million was recorded for costs associated with the plant closings, of which \$3.3 million principally relates to employee severance and benefits costs and plant exit costs, and \$3.6 million relates to a fixed asset impairment charge, primarily for properties and machinery and equipment of the closed facilities.

As of December 31, 2002, remaining restructuring reserves totaling \$0.3 million were included in the Consolidated Balance Sheet as an accrued expense within current liabilities. In addition, total impairment charges of \$6.7 million (\$3.1 million and \$3.6 million in 2002 and 2001,

respectively) were recorded to reduce certain property, plant and equipment to their net realizable value.

Activity in the Company's restructuring reserves is summarized as follows (in thousands):

<TABLE>  
<CAPTION>

FISCAL 2002 RESTRUCTURING

	Original Charges	Cash Payments	Non-cash Utilized	Total
<S>	<C>	<C>	<C>	<C>
Employee severance and other related payroll and benefit costs	\$ 1,847	\$(1,757)	\$ --	\$ 90
Plant exit costs and other	171	(24)	--	147
Write-down of long-lived assets	3,105	--	(3,105)	--
Balance as of December 31, 2002	\$ 5,123	\$(1,781)	\$ (3,105)	\$ 237

</TABLE>  
<TABLE>  
<CAPTION>

FISCAL 2001 RESTRUCTURING

	Original Charges	Cash Payments	Non-cash Utilized	Total
<S>	<C>	<C>	<C>	<C>
Employee severance and other related payroll and benefit costs	\$ 2,974	\$(2,916)	\$ (58)	\$ --
Plant exit costs and other	332	(258)	(34)	40
Write-down of long-lived assets	3,600	--	(3,600)	--
Balance as of December 31, 2002	\$ 6,906	\$(3,174)	\$ (3,692)	\$ 40

</TABLE>

(5) BUSINESS ACQUISITIONS

During the quarter, the Company acquired two Ethan Allen retail stores for total consideration of approximately \$0.8 million. As a result of these acquisitions, the Company (i) recorded additional inventory of \$0.9 million and other assets of \$0.2 million, and (ii) assumed customer deposits of \$0.8 million and other liabilities of \$0.1 million. Goodwill associated with these acquisitions totaled \$0.6 million and represents the effects of ordinary fair value adjustments to the assets acquired and liabilities assumed, as well as the premium paid to the sellers for (i) the ability to further develop the Company's presence in a particular geographic market and (ii) the acquired customer base, including related order backlog of approximately \$1.5 million.

As of December 31, 2002, the Company had goodwill, including product technology, (net of accumulated amortization) of \$58.6 million and other identifiable intangible assets (net of accumulated amortization) of \$19.7 million. Comparable balances as of June 30, 2002 were \$50.0 million and \$19.7 million, respectively.

Goodwill in the wholesale and retail segments was \$27.5 million and \$31.1 million, respectively, at December 31, 2002 and \$27.5 million and \$22.5 million, respectively, at June 30, 2002. The wholesale segment, at both dates, includes additional intangible assets of \$19.7 million. These assets consist of Ethan Allen trade names which, prior to the Company's adoption of Statement of Financial Accounting Standards ("SFAS") No. 142, GOODWILL AND OTHER INTANGIBLE ASSETS, on July 1, 2001, were being amortized over 40 years. In connection with the adoption of SFAS No. 142, the Company re-assessed the useful lives of goodwill and other intangible assets and both were determined to have indefinite useful lives. As such, amortization ceased on that date. No impairment losses were recorded on these intangible assets as a result of the adoption of SFAS No. 142.



(6) LITIGATION

The Company has been named as a potentially responsible party ("PRP") for the cleanup of three active sites currently listed or proposed for inclusion on the National Priorities List ("NPL") under the Comprehensive Environmental Response, Compensation and Liability Act of 1980 ("CERCLA"). The Company has resolved its liability at one of the sites by completing remedial action activities. With regard to the other two sites, the Company does not anticipate incurring significant cost as it believes that it is not a major contributor based on the very small volume of waste generated by the Company in relation to total volume at the sites. However, liability under CERCLA may be joint and several. Additionally, the Company has been notified by the State of New York that it may be a PRP in a separate, unrelated matter. As a result, the extent of any adverse effect on the Company's financial condition, results of operations, or cash flows with respect to this matter cannot be reasonably estimated at this time.

(7) EARNINGS PER SHARE

Basic and diluted earnings per share are calculated using the following weighted average share data (in thousands):

<TABLE>

<CAPTION>

	Three Months Ended December 31,		Six Months Ended December 31,	
	2002	2001	2002	2001
	-----	-----	-----	-----
<S>	<C>	<C>	<C>	<C>
Weighted average common shares outstanding for basic calculation	37,767	38,691	37,876	38,952
Add: Dilutive effect of stock options and warrants	1,026	1,090	978	1,074
	-----	-----	-----	-----
Weighted average common shares outstanding, adjusted for diluted calculation	38,793	39,781	38,854	40,026
	=====	=====	=====	=====

</TABLE>

As of December 31, 2002 and 2001, stock options to purchase 88,819 shares and 26,500 shares of common stock, respectively, had exercise prices which exceeded the average market price for the corresponding period. These options have been excluded from the respective diluted earnings per share calculation as their impact is anti-dilutive.

ETHAN ALLEN INTERIORS INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(unaudited)

(8) COMPREHENSIVE INCOME

Total comprehensive income represents the sum of net income and items of "other comprehensive income or loss" that are reported directly in equity. Such items may include foreign currency translation adjustments, minimum pension liability adjustments, fair value adjustments on certain derivative instruments, and unrealized gains and losses on certain investments in debt and equity securities. The Company has reported its total comprehensive income in the Consolidated Statement of Shareholders' Equity.

The Company's other comprehensive income, which is attributable solely to foreign currency translation adjustments, was \$0.3 million for the six-month period ended December 31, 2002. This amount, as well as the Company's accumulated other comprehensive income included in equity, are the result of changes in foreign currency exchange rates related to the operations of 7 Ethan Allen-owned retail stores located in Canada. Foreign currency translation adjustments exclude income tax expense (benefit) given that the earnings of non-U.S. subsidiaries are deemed to be reinvested for an indefinite period of time.

(9) SEGMENT INFORMATION

The Company's reportable segments are strategic business areas that are

managed separately and offer different products and services. The Company's operations are classified into two main segments: wholesale and retail.

The wholesale segment is principally involved in the manufacture, sale and distribution of home furnishing products to a network of independently-owned and Ethan Allen-owned stores. Wholesale profitability includes the wholesale gross margin, which is earned on wholesale sales to all retail stores, including Ethan Allen-owned stores.

The retail segment sells home furnishing products through a network of Ethan Allen-owned stores. Retail profitability includes the retail gross margin, which represents the difference between retail sales price and the cost of goods purchased from the wholesale segment.

The Company evaluates performance of the respective segments based upon revenues and operating income. Inter-segment eliminations primarily consist of the wholesale sales and profit on the transfer of inventory between segments. Inter-segment eliminations also include items not allocated to reportable segments.

The following table presents segment information for the three and six months ended December 31, 2002 and 2001 (in thousands):

<TABLE>  
<CAPTION>

	Three Months Ended December 31,		Six Months Ended December 31,	
	2002	2001	2002	2001
<S>	<C>	<C>	<C>	<C>
NET SALES:				
Wholesale segment	\$158,362	\$158,206	\$ 316,208	\$313,090
Retail segment	139,294	116,915	259,773	215,755
Elimination of inter-company sales	(67,943)	(52,264)	(129,739)	(99,263)
Consolidated Total	\$229,713	\$222,857	\$ 446,242	\$429,582
OPERATING INCOME:				
Wholesale segment	\$ 28,012	\$ 24,473	\$ 56,889	\$ 47,737
Retail segment	8,056	7,727	11,103	10,729
Elimination (1)	1,127	1,006	1,046	1,275
Consolidated Total	\$ 37,195	\$ 33,206	\$ 69,038	\$ 59,741

</TABLE>

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ETHAN ALLEN INTERIORS INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(unaudited)

<TABLE>  
<CAPTION>

	Three Months Ended December 31,		Six Months Ended December 31,	
	2002	2001	2002	2001
<S>	<C>	<C>	<C>	<C>
CAPITAL EXPENDITURES:				
Wholesale segment	\$ 3,744	\$ 2,493	\$ 7,707	\$ 6,747
Retail segment	3,872	7,085	9,218	10,962
Acquisitions (2)	812	118	10,742	10,484
Consolidated Total	\$ 8,428	\$ 9,696	\$ 27,667	\$ 28,193

</TABLE>

	December 31, 2002	June 30, 2002
TOTAL ASSETS:		
Wholesale segment	\$445,761	\$459,311
Retail segment	283,865	259,770
Inventory profit elimination (3)	(30,738)	(30,326)
Consolidated Total	\$698,888	\$688,755

(1) Adjustment reflects the change in the elimination entry for profit in ending inventory.

- (2) Acquisitions include the purchase of 2 retail stores during the three months ended December 31, 2002 and none during the three months ended December 31, 2001. For the six month period ended December 31, 2002, acquisitions include the purchase of 15 retail stores, while for the six month period ended December 31, 2001, acquisitions include the purchase of 10 retail stores.
- (3) Inventory profit elimination reflects the embedded wholesale profit in the Ethan Allen-owned store inventory that has not been realized. These profits will be recorded when shipped to the retail customer.

At December 31, 2002, there are 30 Ethan Allen retail stores located outside the United States, of which 23 are independently-owned. Approximately 2% of the Company's net sales for the three and six month periods ended December 31, 2002 and 2001 were derived from sales to non-domestic, independently-owned retail stores.

(10) RECENT ACCOUNTING PRONOUNCEMENTS

In October 2002, the Emerging Issues Task Force ("EITF") of the Financial Accounting Standards Board ("FASB") reached a consensus on EITF Issue No. 02-17, "Recognition of Customer Relationship Intangible Assets Acquired in a Business Combination". EITF 02-17 addresses the application of the separate recognition criteria specified in SFAS No. 141, BUSINESS COMBINATIONS, in establishing intangible assets, apart from goodwill, that meet the contractual-legal or separability provisions of that Statement. Specifically, EITF 02-17 addresses the recognition of customer-related intangible assets acquired in a purchase business combination, including (i) order or production backlog, (ii) customer contracts and related customer relationships, and (iii) non-contractual customer relationships. The provisions of this EITF consensus are to be applied to business combinations consummated, and goodwill impairment tests performed, after October 25, 2002. The Company is currently evaluating the impact of adopting EITF 02-17 and, at this time, does not expect that application of the provisions of this authoritative guidance will have a material effect on the consolidated financial statements.

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ETHAN ALLEN INTERIORS INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(unaudited)

In November 2002, the FASB approved FASB Interpretation No. ("FIN") 45, GUARANTOR'S ACCOUNTING AND DISCLOSURE REQUIREMENTS FOR GUARANTEES, INCLUDING INDIRECT GUARANTEES OF INDEBTEDNESS OF OTHERS, AN INTERPRETATION OF FASB STATEMENTS NO. 5, 57 AND 107 AND RESCISSION OF FASB INTERPRETATION NO. 34. FIN 45 clarifies the requirements of SFAS No. 5, ACCOUNTING FOR CONTINGENCIES, relating to a guarantor's accounting for, and disclosure of, the issuance of certain types of guarantees. Specifically, FIN 45 requires a guarantor to recognize a liability for the non-contingent component of certain guarantees, representing the obligation to stand ready to perform in the event that specified triggering events or conditions occur. The initial measurement of the liability is the fair value of the guarantee at inception and recognition is required even if it is not probable that payment will be required under the guarantee. The provisions for initial recognition and measurement are effective on a prospective basis for guarantees that are issued or modified after December 31, 2002, irrespective of a guarantor's fiscal year-end. However, the disclosure provisions of FIN 45 are effective for financial statements of interim or annual periods ending after December 15, 2002. The Company is currently evaluating the impact of adopting FIN 45 and, at this time, does not expect that application of the provisions of this interpretation will have a material effect on the consolidated financial statements.

In December 2002, the FASB issued SFAS No. 148, ACCOUNTING FOR STOCK-BASED COMPENSATION -- TRANSITION AND DISCLOSURE -- AN AMENDMENT OF FASB STATEMENT NO. 123. SFAS No. 148 amends SFAS No. 123, ACCOUNTING FOR STOCK-BASED COMPENSATION, to provide alternative methods of transition for a voluntary change to the fair value method of accounting for stock-based compensation. In addition, Statement No. 148 amends the disclosure requirements of Statement No. 123 to require more prominent disclosures in both annual and interim financial statements about the method of accounting employed for stock-based compensation and the effect of the method used on reported results. The Company is required to follow the prescribed format, and provide the additional disclosures set forth in Statement No. 148 in its annual financial statements for the year ended June 30, 2003. In addition, the Company must also provide the required

disclosures in quarterly reports containing its consolidated financial statements for interim periods beginning with the quarterly period ended March 31, 2003.

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ETHAN ALLEN INTERIORS INC. AND SUBSIDIARY

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

The discussions set forth in this form 10-Q should be read in conjunction with the financial information included herein and the Company's Annual Report on Form 10-K for the year ended June 30, 2002. Management's discussion and analysis of financial condition and results of operations and other sections of this quarterly report contain forward-looking statements relating to future results of the Company. Such forward-looking statements are identified by use of forward-looking words such as "anticipates", "believes", "plans", "estimates", "expects", and "intends" or words or phrases of similar expression. These forward-looking statements are subject to various assumptions, risk and uncertainties, including but not limited to, changes in political and economic conditions, demand for the Company's products, acceptance of new products, conditions in the various geographical markets where the Company does business, technology developments affecting the Company's products and to those matters discussed in the Company's filings with the Securities and Exchange Commission. Accordingly, actual results could differ materially from those contemplated by the forward-looking statements.

CRITICAL ACCOUNTING POLICIES

The Company's consolidated financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America which require that certain estimates and assumptions be made that affect the amounts and disclosures reported in the those financial statements and the related accompanying notes. Actual results could differ from these estimates and assumptions. Management uses its best judgment in valuing these estimates and may, as warranted, solicit external advice. Estimates are based on current facts and circumstances, prior experience and other assumptions believed to be reasonable. The following critical accounting policies, some of which are impacted significantly by judgments, assumptions and estimates, affect the Company's consolidated financial statements.

RETAIL STORE ACQUISITIONS - The Company accounts for the acquisition of retail stores and related assets in accordance with Statement of Financial Accounting Standards ("SFAS") No. 141, BUSINESS COMBINATIONS, which requires application of the purchase method for all business combinations initiated after June 30, 2001. Accounting for these transactions as purchase business combinations requires the allocation of purchase price paid to the assets acquired and liabilities assumed based on their fair values as of the date of the acquisition. The amount paid in excess of the fair value of net assets acquired is accounted for as goodwill.

IMPAIRMENT OF LONG-LIVED ASSETS AND GOODWILL - The Company periodically evaluates whether events or circumstances have occurred that indicate that long-lived assets may not be recoverable or that the remaining useful life may warrant revision. When such events or circumstances are present, the Company assesses the recoverability of long-lived assets by determining whether the carrying value will be recovered through the expected undiscounted future cash flows resulting from the use of the asset. In the event the sum of the expected undiscounted future cash flows is less than the carrying value of the asset, an impairment loss equal to the excess of the asset's carrying value over its fair value is recorded. The long-term nature of these assets requires the estimation of its cash inflows and outflows several years into the future and only takes into consideration technological advances known at the time of the impairment test.

In accordance with SFAS No. 142, GOODWILL AND OTHER INTANGIBLE ASSETS, which was adopted by the Company on July 1, 2001, goodwill and other intangible assets are to be evaluated for impairment at the reporting unit level on an annual basis and between annual tests whenever events or circumstances indicate that the carrying value of a reporting unit may exceed its fair value. A discounted cash flow model is used to estimate the fair value of a reporting unit. This model requires the use of long-term planning forecasts and assumptions regarding industry-specific economic conditions that are outside the control of the Company.

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ALLOWANCE FOR DOUBTFUL ACCOUNTS - The Company maintains an allowance for doubtful accounts for estimated losses resulting from the inability of its customers to make required payments. The allowance for doubtful accounts is based on a review of specifically identified accounts in addition to an overall aging analysis. Judgments are made with respect to the collectibility of accounts receivable based on historical experience and current economic trends. Actual losses could differ from those estimates.

INVENTORIES - Inventories (finished goods, work in process and raw materials) are stated at the lower of cost, determined on a first-in, first-out basis, or market. The Company estimates an inventory reserve for excess quantities and obsolete items based on specific identification and historical write-offs, taking into account future demand and market conditions. If actual demand or market conditions in the future are less favorable than those estimated, additional inventory write-downs may be required.

REVENUE RECOGNITION - Revenue is recognized when the risks and rewards of ownership and title to the product have transferred to the buyer. This generally occurs upon the shipment of goods to independent dealers or, in the case of Ethan Allen-owned retail stores, upon delivery to the customer. Recorded sales provide for estimated returns and allowances. The Company permits retail customers to return defective products and incorrect shipments for credit against other purchases. Terms offered by the Company are standard for the industry.

BUSINESS INSURANCE RESERVES - The Company has insurance programs in place to cover workers' compensation and property/casualty claims. The insurance programs, which are funded through self-insured retention, are subject to various stop-loss limitations. The Company accrues estimated losses using actuarial models and assumptions based on historical loss experience. Although management believes that the insurance reserves are adequate, the reserve estimates are based on historical experience, which may not be indicative of current and future losses. In addition, the actuarial calculations used to estimate insurance reserves are based on numerous assumptions, some of which are subjective. The Company adjusts insurance reserves, as needed, in the event that future loss experience differs from historical loss patterns.

OTHER LOSS RESERVES - The Company has a number of other potential loss exposures incurred in the ordinary course of business such as environmental claims, product liability, litigation, restructuring charges, and the recoverability of deferred income tax benefits. Establishing loss reserves for these matters requires management's estimate and judgment with regard to maximum risk exposure and ultimate liability or realization. As a result, these estimates are often developed with the Company's counsel, or other appropriate advisors, and are based on management's current understanding of the underlying facts and circumstances. Because of uncertainties related to the ultimate outcome of these issues or the possibilities of changes in the underlying facts and circumstances, additional charges related to these issues could be required in the future.

RESULTS OF OPERATIONS

The Company's revenues are comprised of wholesale sales to dealer-owned and Ethan Allen-owned retail stores and retail sales of Ethan Allen-owned stores. See Note 9 to the Company's Consolidated Financial Statements for the three and six months ended December 31, 2002 and 2001. The components of consolidated revenues and operating income are as follows (in millions):

<TABLE>  
<CAPTION>

	Three Months Ended		Six Months Ended	
	December 31,		December 31,	
	2002	2001	2002	2001
	-----	-----	-----	-----
<S>	<C>	<C>	<C>	<C>
REVENUE:				
Wholesale segment	\$158.4	\$158.2	\$316.2	\$313.1
Retail segment	139.3	116.9	259.8	215.8
Elimination of inter-segment sales	(68.0)	(52.2)	(129.8)	(99.3)
	-----	-----	-----	-----
Consolidated Revenue	\$229.7	\$222.9	\$446.2	\$429.6
	=====	=====	=====	=====

</TABLE>

<TABLE>  
<CAPTION>

	Three Months Ended		Six Months Ended	
	December 31,		December 31,	
	2002	2001	2002	2001
	-----	-----	-----	-----
<S>	<C>	<C>	<C>	<C>
OPERATING INCOME:				
Wholesale segment	\$28.0	\$ 24.5	\$ 56.9	\$ 47.7
Retail segment	8.1	7.7	11.1	10.7
Elimination	1.1	1.0	1.0	1.3
	-----	-----	-----	-----
Consolidated Operating Income	\$37.2	\$ 33.2	\$ 69.0	\$ 59.7
	=====	=====	=====	=====

</TABLE>

THREE MONTHS ENDED DECEMBER 31, 2002 COMPARED TO THREE MONTHS ENDED DECEMBER 31, 2001

Consolidated revenue for the three months ended December 31, 2002 increased by \$6.8 million, or 3.1%, to \$229.7 million from \$222.9 million for the three months ended December 31, 2001. Net sales increased due to the continued expansion of the Company's retail segment, partially offset by the effects of a relative softness in consumer spending caused by a sluggish economy. The Company's first quarter results were negatively impacted by an inability to service orders of certain off-shore sourced product lines due to delays caused by shutdowns at selected West Coast ports. With that work stoppage resolved, those orders were delivered during the current quarter. Also during the quarter, the Company initiated selected price reductions within four collections: British Classics; Country French; Horizons by Ethan Allen; and Country Crossings. The objective of these price reductions was to increase sales volume within some of the more popular collections while continuing to expand the Company's consumer reach. Although it is difficult to quantify, management does not believe that the price reductions had a material effect on the Company's consolidated operations for the period.

Total wholesale revenue for the second quarter of fiscal year 2003 increased by \$0.2 million, or 0.1%, to \$158.4 million from \$158.2 million in the second quarter of fiscal year 2002. The wholesale segment continues to be challenged by the state of the U.S. economy and its effects on consumer confidence and the incoming order rate.

Total retail revenue from Ethan Allen-owned stores for the three months ended December 31, 2002 increased by \$22.4 million, or 19.1%, to \$139.3 million from \$116.9 million for the three months ended December 31, 2001. The increase in retail sales by Ethan Allen-owned stores was attributable to an increase in sales generated by newly-opened or acquired stores of \$30.5 million, partially offset by a decrease in comparable store delivered sales of \$3.5 million, or 3.2%, and a decrease resulting from sold and closed stores, which generated \$4.6 million fewer sales in fiscal year 2003 as compared to fiscal year 2002. The number of Ethan Allen-owned stores increased to 118 as of December 31, 2002 as compared to 93 as of December 31, 2001. During that twelve month period, the Company acquired 25 stores from independent dealers, sold 1 to an independent dealer, relocated 2 stores, opened 2 new stores, and closed 1 store.

Comparable stores are those newly-opened stores which have been operating for at least 15 months. Minimal net sales, derived from the delivery of customer ordered product, are generated during the first three months of operations of newly-opened stores. Stores acquired from dealers by Ethan Allen are included in comparable store sales in their 13th full month of Ethan Allen-owned operations.

Total booked orders, which include wholesale orders and written business of Ethan Allen-owned retail stores, increased from the prior year quarter by 6.7%, reflecting the continued expansion of the Company's retail segment, partially offset by the effects of a relative softness in consumer spending. Comparing the current quarter to the prior year quarter, wholesale orders increased 3.4% while Ethan Allen-owned store orders increased 19.1%. Comparable store written business decreased 3.4% over that same period.

Gross profit increased during the second quarter to \$115.8 million from \$103.4 million in the second quarter of the prior year. The \$12.4 million, or 12.0%, increase

in gross profit was primarily attributable to (i) a higher proportionate share of retail sales to total sales (61% in the current year quarter compared to 52% in the prior year quarter), and (ii) lower costs associated with wholesale sales returns and allowances and certain raw materials. Gross profit for the quarter was also positively impacted, to a lesser extent, by higher margins attributable to the off-shore sourcing of certain recent product introductions and increased production efficiencies resulting from the Company's continued focus on quality.

These favorable variances were partially offset by increased costs associated with excess capacity at our manufacturing facilities. Consolidated gross margin increased to 50.4% in the second quarter of fiscal year 2003 from 46.4% in the prior year second quarter. The gross margin was positively impacted as a result of the factors identified previously.

Operating expenses increased \$8.4 million, or 12.0%, to \$78.6 million, or 34.2% of net sales, in the current quarter from \$70.2 million, or 31.5% of net sales, in the prior year comparable quarter. This increase is primarily attributable to further expansion of the retail segment and the higher proportionate share of retail sales to total sales in the current quarter as compared to the prior year quarter. The addition of 25 net new Ethan Allen-owned stores since December 2001 has resulted in higher costs associated with warehousing and delivery, occupancy, advertising, healthcare, district management and design consultant salaries. These increases were partially offset by lower selling costs within the wholesale segment as a result of a decline in wholesale sales volume.

Operating income for the three months ended December 31, 2002 was \$37.2 million, or 16.2% of net sales, compared to \$33.2 million, or 14.9% of net sales, for the three months ended December 31, 2001. This represents an increase of \$4.0 million, or 12.0%, which is primarily attributable to a higher gross margin and lower costs at the wholesale level, both of which were noted above, partially offset by increased operating expenses resulting from the continued expansion of the retail segment.

Total wholesale operating income for the second quarter of fiscal year 2003 was \$28.0 million, or 17.7% of net sales, compared to \$24.5 million, or 15.5% of net sales, in the second quarter of fiscal year 2002. The increase of \$3.5 million, or 14.3%, is primarily attributable to (i) lower costs associated with sales returns and allowances and certain raw materials, and (ii) a decrease in selling expenses. These favorable variances were partially offset by increased costs associated with excess capacity at our manufacturing facilities.

During the current quarter, operating income for the retail segment increased \$0.3 million, or 4.3%, to \$8.0 million, or 5.8% of net sales, from \$7.7 million, or 6.6% of net sales, in the prior year quarter. The increase in retail operating income generated by Ethan Allen-owned stores is primarily attributable to increased sales volume associated with new stores, partially offset by a 3.2% decline in comparable store delivered sales, reduced sales volume resulting from closed and sold stores, and higher operating expenses related to the addition of 25 net new stores since December 2001.

Interest and other miscellaneous income for the current quarter was \$0.1 million, a decrease of \$0.9 million from the prior year quarter. The decrease is the result of a \$0.8 million gain recognized in the prior year quarter in connection with the sale of real estate.

Income tax expense was \$14.0 million for the quarter ended December 31, 2002 as compared to \$12.9 million for the comparable quarter in the prior year. The Company's effective tax rate was 37.8% in both periods.

For the three months ended December 31, 2002, the Company recorded net income of \$23.1 million, an increase of \$1.9 million, or 8.9%, from \$21.2 million recorded for the three months ended December 31, 2001. Earnings per diluted share were \$0.60 for the current quarter representing an increase of \$0.07, or 13.2%, from \$0.53 per diluted share in the prior year quarter.

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SIX MONTHS ENDED DECEMBER 31, 2002 COMPARED TO SIX MONTHS ENDED  
DECEMBER 31, 2001

Consolidated revenue for the six months ended December 31, 2002 increased by \$16.6 million, or 3.9%, to \$446.2 million from \$429.6 million for the six months ended December 31, 2001. Net sales increased due to the continued expansion of the Company's retail segment, partially offset by the effects of a relative softness in consumer spending caused by a sluggish economy during the past six months.

Total wholesale revenue for the first half of fiscal year 2003 increased by \$3.1 million, or 1.0%, to \$316.2 million from \$313.1 million in the first half of fiscal year 2002. The wholesale segment continues to be challenged by the state of the U.S. economy and its effects on consumer confidence and the incoming order rate.

Total retail revenue from Ethan Allen-owned stores for the six months ended December 31, 2002 increased by \$44.0 million, or 20.4%, to \$259.8 million from \$215.8 million for the six months ended December 31, 2001. The increase in retail sales by Ethan Allen-owned stores was attributable to an increase in sales generated by newly-opened or acquired stores of \$58.3 million, partially offset by a decrease in comparable store delivered sales of \$7.2 million, or 3.5%, and a decrease resulting from sold and closed stores, which generated \$7.1

million fewer sales in fiscal year 2003 as compared to fiscal year 2002.

Total booked orders, which include wholesale orders and written business of Ethan Allen-owned retail stores, increased from the prior year six month period by 8.3%, reflecting the continued expansion of the Company's retail segment, partially offset by the effects of a relative softness in consumer spending. Comparing the current six month period to the prior year six month period, wholesale orders increased 3.5% while Ethan Allen-owned store orders increased 25.6%. Comparable store written business increased 0.7% over that same period.

Gross profit increased during the first half of the current year to \$222.5 million from \$197.3 million in the first half of the prior year. The \$25.2 million, or 12.8%, increase in gross profit was primarily attributable to (i) a higher proportionate share of retail sales to total sales (58% in the current six month period compared to 50% in the prior year six month period), (ii) lower costs associated with wholesale sales returns and allowances and certain raw materials, and (iii) higher margins attributable to the off-shore sourcing of certain recent product introductions and increased production efficiencies resulting from the Company's continued focus on quality. These favorable variances were partially offset by increased costs associated with excess capacity at our manufacturing facilities. Consolidated gross margin increased to 49.9% for the first half of fiscal year 2003 from 45.9% in the first half of the prior fiscal year. The gross margin was positively impacted as a result of the factors identified previously.

Operating expenses increased \$15.9 million, or 11.5%, to \$153.5 million, or 34.4% of net sales, in the current year six month period from \$137.6 million, or 32.0% of net sales, in the prior year six month period. This increase is primarily attributable to further expansion of the retail segment and the higher proportionate share of retail sales to total sales in the current period as compared to the prior year period. The addition of 25 net new Ethan Allen-owned stores since December 2001 has resulted in higher costs associated with warehousing and delivery, occupancy, advertising, healthcare, district management and design consultant salaries. These increases were partially offset by lower selling costs within the wholesale segment as a result of a decline in wholesale sales volume.

Operating income for the six months ended December 31, 2002 was \$69.0 million, or 15.5% of net sales, compared to \$59.7 million, or 13.9% of net sales, for the six months ended December 31, 2001. This represents an increase of \$9.3 million, or 15.6%, which is primarily attributable to a higher gross margin and lower costs at the wholesale level, both of which were noted above, partially offset by increased operating expenses resulting from the continued expansion of the retail segment.

ETHAN ALLEN INTERIORS INC. AND SUBSIDIARY

Total wholesale operating income for the first half of fiscal year 2003 was \$56.9 million, or 18.0% of net sales, compared to \$47.7 million, or 15.2% of net sales, in the first half of fiscal year 2002. The increase of \$9.2 million, or 19.2%, is primarily attributable to (i) lower costs associated with sales returns and allowances and certain raw materials, (ii) a decrease in selling expenses, and (iii) higher margins attributable to the off-shore sourcing of certain recent product introductions and increased production efficiencies resulting from the Company's continued focus on quality. These favorable variances were partially offset by increased costs associated with excess capacity at our manufacturing facilities.

Operating income for the retail segment during the current six month period increased \$0.4 million, or 3.5%, to \$11.1 million, or 4.3% of net sales, from \$10.7 million, or 5.0% of net sales, in the prior year six month period. The increase in retail operating income generated by Ethan Allen-owned stores is primarily attributable to increased sales volume associated with new stores, partially offset by a 3.5% decline in comparable store delivered sales, reduced sales volume resulting from closed and sold stores, and higher operating expenses related to the addition of 25 net new stores since December 2001.

Interest and other miscellaneous income for the current year six month period was \$0.7 million, a decrease of \$0.8 million from the prior year six month period. The decrease is due, primarily, to (i) slightly higher gains recognized in the prior year in connection with the sale of real estate, (ii) a decrease in interest income associated with the Company's investment portfolio as a result of a decline in interest rates during the period, and (iii) the Company's share of current year losses incurred in connection with the start-up of its United Kingdom joint venture with MFI Furniture Group Plc.

Income tax expense was \$26.2 million for the six months ended December 31, 2002 as compared to \$23.0 million for the comparable six month period in the prior year. The Company's effective tax rate was 37.8% in both periods.



For the six months ended December 31, 2002, the Company recorded net income of \$43.1 million, an increase of \$5.2 million, or 13.8%, from \$37.9 million recorded for the six months ended December 31, 2001. Earnings per diluted share were \$1.11 for the current period representing an increase of \$0.16, or 16.8%, from \$0.95 per diluted share in the prior year period.

#### FINANCIAL CONDITION AND LIQUIDITY

The Company's principal sources of liquidity are cash flow from operations and borrowing capacity under a revolving credit facility. Net cash provided by operating activities totaled \$56.0 million for the six months ended December 31, 2002, compared to \$64.3 million for the six months ended December 31, 2001. The year-over-year decrease of \$8.3 million in net cash provided by operating activities was principally the result of a decline in inventory levels (net of inventories acquired in the purchase of retail stores) at a rate substantially lower than that noted in the prior year (\$19.9 million), partially offset by (i) a decrease in cash required to satisfy outstanding accounts payable (\$7.6 million), and (ii) an increase in net income (\$5.2 million). The decline in the year-over-year rate of inventory reduction is the result of the Company's decision to close three of its manufacturing facilities during the summer of 2001 and other inventory management efforts.

During the current six month period, net cash used in investing activities decreased to \$25.1 million from \$25.8 million in the prior year six month period. Of those amounts, \$10.7 million was used to finance acquisitions during the current year as compared to \$10.5 million in the prior year. During the six months ended December 31, 2002, capital spending, exclusive of acquisitions, totaled \$16.9 million as compared to \$17.7 million for the six months ended December 31, 2001. The current level of capital spending is principally attributable to (i) new store development and renovation and (ii) technology improvements. Capital expenditures for fiscal year

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2003, exclusive of acquisitions, are anticipated to be approximately \$35.0 million. The Company anticipates that cash from operations will be sufficient to fund such capital expenditures.

Net cash used in financing activities totaled \$37.1 million in the current six month period as compared to \$22.8 million in the prior year six month period, an increase of \$14.3 million. The increase in net cash used in financing activities is primarily the result of an increase in payments related to the acquisition of treasury stock, an increase in dividends paid, and the repayment of debt. Total debt outstanding at December 31, 2002 was \$10.3 million. At December 31, 2002, there were no revolving loans outstanding and \$19.6 million of trade and standby letters of credit outstanding under the Company's credit facility. The Company had \$105.4 million available under its revolving credit facility at December 31, 2002.

The Company has been authorized by its Board of Directors to repurchase its common stock, from time to time, either directly or through agents, in the open market at prices and on terms satisfactory to the Company. The Company also retires shares of unvested restricted stock and, prior to June 30, 2002, repurchased shares of common stock from terminated or retiring employee's accounts in the Ethan Allen Retirement Savings Plan. All of the Company's common stock repurchases and retirements are recorded as treasury stock and result in a reduction of shareholders' equity. During the first six months of fiscal year 2003 and 2002, the Company repurchased the following shares of its common stock:

	Six Months Ended December 31,	
	2002	2001
	-----	-----
Common shares repurchased	721,300	727,680
Cost to repurchase common shares	\$22,381,598	\$20,556,471
Average price per share	\$31.03	\$28.25

The Company funded its common stock repurchases through available cash and cash from operations. As of December 31, 2002, the Company had a remaining Board authorization to purchase 2.0 million shares.

As of December 31, 2002, the aggregate scheduled maturities of the Company's long-term debt for each of the next five fiscal years are as follows: \$0.8 million in fiscal 2004, \$4.7 million in fiscal 2005, \$0.2 million in fiscal 2006, \$0.1 million in fiscal 2007, \$0.1 million in fiscal 2008, and \$4.2 million thereafter. Management believes that its cash flow from operations, together with its other available sources of liquidity, will be adequate to make all required payments of principal and interest on its debt, to permit anticipated capital expenditures and to fund working capital and other cash requirements over the next twelve months. As of December 31, 2002, the Company had working capital of \$192.3 million and a current ratio of 2.61 to 1.

#### OTHER COMMITMENTS, CONTINGENCIES AND CONTRACTUAL OBLIGATIONS

From time to time, in the ordinary course of business, the Company, or its wholly-owned subsidiaries, may provide guarantees on behalf of selected affiliated entities or become contractually obligated to perform in accordance with the terms and conditions of certain business agreements. The nature and extent of these guarantees and obligations varies based on the underlying relationship of the benefiting party to the Company and the business purpose for which the guarantee or obligation is being provided. Details of those arrangements for which the Company, or any of its wholly-owned subsidiaries, act as guarantor or obligor are provided below.

#### DEALER-RELATED GUARANTEES

As part of the Company's expansion strategy for the Ethan Allen retail store network, selected independent dealers are provided, on rare occasion, with financial

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guarantees relating to leases in connection with certain store locations. As of December 31, 2002, two such guarantees exist; one has been provided by Ethan Allen Inc. on behalf of an independent dealer while the other has been provided by Ethan Allen Interiors Inc. on behalf of an independent dealer currently operating as assignee under a lease agreement previously entered into by Ethan Allen Inc. The remaining terms of these guarantees range from three months to two years, and generally represent the remaining contractual terms of the underlying lease agreements (subject to certain term limitations). The Company is obligated to act under such guarantees in the event of default by the respective dealers (lessees). The guarantee terms may be extended, in the event that applicable lease renewal options are exercised, for a period of up to ten years.

The maximum potential amount of future payments (undiscounted) that the Company could be required to make under these guarantees is limited to the amount of the remaining contractual lease payments (subject to certain term limitations) and, as such, is not an estimate of future cash flows. As of December 31, 2002, the amount of remaining contractual lease payments guaranteed by the Company was approximately \$0.6 million. The Company maintains specific recourse rights related to these dealer arrangements that would enable recovery of up to \$0.5 million of any amount paid under these guarantees. Management expects, based on the underlying creditworthiness of the guaranteed parties, these guarantees will expire without requiring funding by the Company. Accordingly, as of December 31, 2002, the carrying amount of the liability related to such guarantees is zero.

In addition, Ethan Allen Inc. has obligated itself, on behalf of one of its independent dealers, with respect to a \$1.3 million credit facility (the "Credit Facility"). This obligation requires the Company, in the event of the dealer's default under the Credit Facility, to repurchase the dealer's inventory, applying such purchase price to the dealer's outstanding indebtedness under the Credit Facility. The Company's obligation remains in effect for as long as the Credit Facility is in existence. The maximum potential amount of future payments (undiscounted) that the Company could be required to make under this obligation is limited to the amount outstanding under the Credit Facility at the time of default (subject to pre-determined lending limits based on the value of the underlying inventory) and, as such, is not an estimate of future cash flows. No specific recourse or collateral provisions exist that would enable recovery of any portion of amounts paid under this obligation, except to the extent that the Company maintains the right to take title to the repurchased inventory. Management anticipates that the repurchased inventory could subsequently be sold through the Company's retail store network. As of December 31, 2002, the amount outstanding under the Credit Facility totaled approximately \$1.0 million, of which \$0.7 million was in the form of a revolving credit line. Management expects, based on the underlying creditworthiness of the respective dealer, this obligation will expire without requiring funding by the Company. Accordingly, as of December 31, 2002, the carrying amount of the liability related to such obligation is zero.

#### INDEMNIFICATION AGREEMENT

In connection with the Company's joint venture arrangement with United Kingdom-based MFI Industries Plc., Ethan Allen Inc. has entered into a tax cross-indemnification agreement with the joint venture partner. The indemnification agreement stipulates that both parties agree to pay fifty percent of the amount of any tax liability arising as a result of (i) an adverse tax judgment or (ii) the imposition of additional taxes against either partner, and attributable to the operations of the joint venture. The indemnification agreement is effective until such time that the joint venture is terminated. At the present time, management anticipates that the joint venture will continue to operate for the foreseeable future.

The maximum potential amount of future payments (undiscounted) that the Company could be required to make under this indemnification agreement is indeterminable as no such tax liability currently exists. Further, the nature,

extent and magnitude of any such tax liability arising in the future as a result of an adverse tax judgment or

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change in applicable tax law cannot be estimated with any reasonable certainty. It should be further noted that no recourse or collateral provisions exist that would enable recovery of any portion of amounts paid under this indemnification agreement. Management expects, based on its current understanding of the applicable tax laws and the existing legal structure of the joint venture, subject to future changes in applicable laws and regulations, this cross-indemnity agreement will expire without requiring funding by the Company. Accordingly, as of December 31, 2002, the carrying amount of the liability related to this indemnification agreement is zero.

RESIDUAL VALUE GUARANTEES

In connection with its distribution activities, the Company has entered into operating lease agreements for certain trucks and trailers within its fleet. For a portion of these vehicles, the Company has guaranteed the related residual values upon completion of the contractual lease terms. The remaining terms of such guarantees range from one to two years, and generally represent the remaining contractual terms of the underlying lease agreements. The Company is obligated to act under such guarantees in the event that the fair value of the vehicles at the end of the lease term is less than the guaranteed residual value. The maximum potential amount of future payments (undiscounted) that the Company could be required to make under these guarantees is limited to the guaranteed residual value for each respective vehicle subject to such guarantee and, as such, is not an estimate of future cash flows. As of December 31, 2002, the Company's maximum potential exposure related to residual value guarantees was approximately \$0.5 million. While no specific recourse or collateral provisions exist that would enable recovery of any portion of amounts paid under these guarantees, all payments made by the Company related to such guarantees are computed net of the proceeds received by the lessor upon sale of the underlying assets. Management expects, based on historical experience and the present condition of its fleet, these guarantees will expire without requiring funding by the Company. Accordingly, as of December 31, 2002, the carrying amount of the liability related to such guarantees is zero.

PRODUCT WARRANTIES

The Company's products, including its case goods, upholstery and home accents, generally carry explicit product warranties that extend from three to five years and are provided based on terms that are generally accepted in the industry. All of the Company's independent dealers are required to enter into, and perform in accordance with the terms and conditions of, a warranty service agreement. The Company records provisions for estimated warranty and other related costs at time of sale based on historical warranty loss experience and makes periodic adjustments to those provisions to reflect actual experience. On rare occasion, certain warranty and other related claims involve matters of dispute that ultimately are resolved by negotiation, arbitration or litigation. In certain cases, a material warranty issue may arise which is beyond the scope of the Company's historical experience. The Company provides for such warranty issues as they become known and estimable. It is reasonably possible that, from time to time, additional warranty and other related claims could arise from disputes or other matters beyond the scope of the Company's historical experience. As of December 31, 2002, the Company's product warranty liability totaled \$0.7 million and, for the six month period then ended, no settlements (in cash or in-kind) were made.

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ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURE ABOUT MARKET RISK

As of December 31, 2002, the Company was essentially debt-free. Cash and short-term investments totaled \$69.6 million and there were no revolving loans outstanding under the Company's credit facility. The current portion of the Company's outstanding long-term debt and capital lease obligations totaled \$0.2 million as of December 31, 2002, while the long-term portion totaled \$10.1 million.

The Company is exposed to interest rate risk primarily through its borrowing activities. The Company's policy has been to utilize United States dollar denominated borrowings to fund its working capital and investment needs. Short term debt, if required, is used to meet working capital requirements and long-term debt is generally used to finance long-term investments. There is

inherent roll-over risk for borrowings as they mature and are renewed at current market rates. The extent of this risk is not quantifiable or predictable because of the variability of future interest rates and the Company's future financing requirements.

The Company has one long-term debt instrument outstanding with a variable interest rate. This debt instrument has a principal balance of \$4.6 million, which matures in 2004. Based on the principal balance outstanding, a one percentage point increase in the variable interest rate would not have had a significant impact on the Company's interest expense.

Currently, the Company does not enter into financial instrument transactions for trading or other speculative purposes or to manage foreign currency exchange, commodity price or interest rate exposure.

#### ITEM 4. CONTROLS AND PROCEDURES

Ethan Allen management, including the Chairman of the Board and Chief Executive Officer ("CEO") and the Chief Financial Officer ("CFO"), conducted an evaluation of the effectiveness of disclosure controls and procedures (as such term is defined in Rules 13a-14 and 15d-14 under the Securities Exchange Act of 1934, as amended (the "Exchange Act")) as of a date within 90 days prior to the filing of this quarterly report (the "Evaluation Date"). Based on such evaluation, the CEO and CFO have concluded that, as of the Evaluation Date, the Company's disclosure controls and procedures are effective in ensuring that material information relating to the Company (including its consolidated subsidiaries), which is required to be included in the Company's periodic filings under the Exchange Act, has been made known to them in a timely fashion.

There have been no significant changes in internal controls, or in factors that could significantly affect internal controls, nor were any corrective actions required with regard to significant deficiencies and material weaknesses, subsequent to the Evaluation Date.

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### ETHAN ALLEN INTERIORS INC. AND SUBSIDIARY

#### PART II - OTHER INFORMATION

##### ITEM 1. LEGAL PROCEEDINGS

There has been no change to matters discussed in Part I, Item 3 - Legal Proceedings in the Company's Annual Report on Form 10-K as filed with the Securities and Exchange Commission on September 30, 2002.

##### ITEM 2. CHANGES IN SECURITIES AND USE OF PROCEEDS

None.

##### ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

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

None.

##### ITEM 5. OTHER INFORMATION

None.

##### ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

(a) Exhibits

None.

(b) Reports on Form 8-K

On November 12, 2002, the Company filed its quarterly report on Form 10-Q for the three month period ended September 30, 2002 with the Securities and Exchange Commission. Accompanying such report was a certification, filed on Form 8-K, of the

ETHAN ALLEN INTERIORS INC. AND SUBSIDIARY

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.

ETHAN ALLEN INTERIORS INC.  
(Registrant)

DATE: February 12, 2003

BY: /S/ M. FAROOQ KATHWARI

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M. Farooq Kathwari  
Chairman of the Board,  
President and Chief Executive Officer  
(Principal Executive Officer)

DATE: February 12, 2003

BY: /S/ EDWARD D. TEPLITZ

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Edward D. Teplitz  
Vice President and Chief Financial Officer  
(Principal Financial Officer)

ETHAN ALLEN INTERIORS INC. AND SUBSIDIARY

CERTIFICATION OF PRINCIPAL EXECUTIVE OFFICER AS REQUIRED BY SECTION 302  
OF THE SARBANES-OXLEY ACT OF 2002

I, M. Farooq Kathwari, do hereby certify that:

- (1) I have reviewed the December 31, 2002 quarterly report on Form 10-Q filed by Ethan Allen Interiors Inc. (the "Company");
- (2) Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;
- (3) Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the Company as of, and for, the periods presented in this quarterly report;
- (4) I and the other certifying officers are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the Company and have:
  - (i) Designed such disclosure controls and procedures to ensure that material information relating to the Company, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;
  - (ii) Evaluated the effectiveness of the Company's disclosure controls and procedures as of a date within 90 days prior to the filing date of this quarterly report (the "Evaluation Date"); and
  - (iii) Presented in this quarterly report our conclusions about the effectiveness of the disclosure controls

and procedures based on our evaluation as of the Evaluation Date;

- (5) I and the other certifying officers have disclosed, based on our most recent evaluation, to the Company's auditors and the Audit Committee of the Board of Directors (or persons fulfilling the equivalent function):
- (i) All significant deficiencies in the design or operation of internal controls which could adversely affect the Company's ability to record, process, summarize and report financial data and have identified for the Company's auditors any material weaknesses in internal controls; and
  - (ii) Any fraud, whether or not material, that involves management or other employees who have a significant role in the Company's internal controls; and
- (6) I and the other certifying officers have indicated in this quarterly report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

/S/ M. FAROOQ KATHWARI

Chairman, Chief Executive  
Officer and Director

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(M. Farooq Kathwari)

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CERTIFICATION OF PRINCIPAL FINANCIAL OFFICER AS REQUIRED BY SECTION 302  
OF THE SARBANES-OXLEY ACT OF 2002

I, Edward D. Teplitz, do hereby certify that:

- (1) I have reviewed the December 31, 2002 quarterly report on Form 10-Q filed by Ethan Allen Interiors Inc. (the "Company");
- (2) Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;
- (3) Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the Company as of, and for, the periods presented in this quarterly report;
- (4) I and the other certifying officers are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the Company and have:
- (i) Designed such disclosure controls and procedures to ensure that material information relating to the Company, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;
  - (ii) Evaluated the effectiveness of the Company's disclosure controls and procedures as of a date within 90 days prior to the filing date of this quarterly report (the "Evaluation Date"); and
  - (iii) Presented in this quarterly report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;
- (5) I and the other certifying officers have disclosed, based on our most recent evaluation, to the Company's auditors and the Audit Committee of the Board of Directors (or persons fulfilling the equivalent function):
- (i) All significant deficiencies in the design or

operation of internal controls which could adversely affect the Company's ability to record, process, summarize and report financial data and have identified for the Company's auditors any material weaknesses in internal controls; and

(ii) Any fraud, whether or not material, that involves management or other employees who have a significant role in the Company's internal controls; and

(6) I and the other certifying officers have indicated in this quarterly report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

/S/ EDWARD D. TEPLITZ

Chief Financial Officer

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(Edward D. Teplitz)