

ENNIS, INC.  
Form 10-Q  
July 10, 2006

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**UNITED STATES SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549**

**FORM 10-Q**

(Mark One)

**Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934  
For the Quarterly Period Ended May 31, 2006**

**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 1-5807**

**ENNIS, INC.**

(Exact Name of Registrant as Specified in Its Charter)

**Texas**

**75-0256410**

(State or Other Jurisdiction of Incorporation or  
Organization)

(I.R.S. Employer Identification No.)

**2441 Presidential Pkwy., Midlothian, Texas**

**76065**

(Address of Principal Executive Offices)

(Zip code)

**(972) 775-9801**

(Registrant's Telephone Number, Including Area Code)

Indicate by check mark whether the Registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes  No   
Indicate by check mark whether the Registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act.

Large accelerated Filer  Accelerated filer  Non-accelerated filer

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

As of July 7, 2006, there were 25,540,243 shares of the Registrant's common stock outstanding.

**ENNIS, INC. AND SUBSIDIARIES**  
**FORM 10-Q**  
**FOR THE PERIOD ENDED MAY 31, 2006**  
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Certification of Chief Executive Officer

Certification of Chief Financial Officer

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**ENNIS, INC. AND SUBSIDIARIES**  
**CONSOLIDATED BALANCE SHEETS**  
*(Dollars in thousands)*

| <b>Assets</b>   | <b>May 31,<br/>2006<br/>(unaudited)</b> | <b>February<br/>28,<br/>2006</b> |
|---|---|----------------------------------|
| Current assets:   |   |                                  |
| Cash and cash equivalents   | \$ 9,322                                | \$ 13,860                        |
| Accounts receivables, net of allowance for doubtful receivables of \$2,957 at May 31, 2006 and \$3,001 at February 28, 2006 | 46,750                                  | 41,686                           |
| Prepaid expenses  | 6,343                                   | 4,425                            |
| Inventories   | 89,227                                  | 89,155                           |
| Other current assets  | 9,330                                   | 9,329                            |
| <b>Total current assets</b>   | <b>160,972</b>                          | <b>158,455</b>                   |
| Property, plant and equipment, at cost  |   |                                  |
| Plant, machinery and equipment  | 124,682                                 | 120,456                          |
| Land and buildings  | 39,555                                  | 38,038                           |
| Other   | 20,478                                  | 20,292                           |
| <b>Total property, plant and equipment</b>  | <b>184,715</b>                          | <b>178,786</b>                   |
| Less accumulated depreciation   | 118,856                                 | 114,983                          |
| <b>Net property, plant and equipment</b>  | <b>65,859</b>                           | <b>63,803</b>                    |
| Goodwill  | 178,280                                 | 178,280                          |
| Trademarks, net   | 61,904                                  | 61,941                           |
| Purchased customer lists, net   | 21,222                                  | 21,632                           |
| Deferred finance charges, net   | 1,709                                   | 1,390                            |
| Prepaid pension asset   | 7,818                                   | 8,277                            |
| Other assets  | 679                                     | 623                              |
| <b>Total assets</b>   | <b>\$ 498,443</b>                       | <b>\$ 494,401</b>                |

*See accompanying notes to consolidated financial statements.*

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**ENNIS, INC. AND SUBSIDIARIES**  
**CONSOLIDATED BALANCE SHEETS**  
*(Dollars in thousands)*

|   | <b>May 31,<br/>2006</b> | <b>February<br/>28,<br/>2006</b> |
|---|-------------------------|----------------------------------|
|   | <i>(unaudited)</i>      |                                  |
| <b>Liabilities and Shareholders Equity</b>  |                         |                                  |
| Current liabilities:  |                         |                                  |
| Accounts payable  | \$ 24,485               | \$ 26,589                        |
| Accrued expenses  |                         |                                  |
| Employee compensation and benefits  | 15,722                  | 17,250                           |
| Taxes other than income   | 1,538                   | 1,488                            |
| Federal and state income taxes payable  | 7,828                   | 2,490                            |
| Other   | 7,029                   | 4,524                            |
| Current installments of long-term debt  | 11,255                  | 11,620                           |
| <br>Total current liabilities   | <br>67,857              | <br>63,961                       |
| <br>Long-term debt, less current installments   | <br>95,814              | <br>102,916                      |
| Deferred credits, principally income taxes  | 29,971                  | 30,189                           |
| <br>Total liabilities   | <br>193,642             | <br>197,066                      |
| <br>Shareholders equity   |                         |                                  |
| Series A junior participating preferred stock of \$10 par value. Authorized 1,000,000 shares; none issued             |                         |                                  |
| Common stock \$2.50 par value, authorized 40,000,000 shares; issued 30,053,443 shares at May 31 and February 28, 2006 | 75,134                  | 75,134                           |
| Additional paid in capital  | 122,969                 | 122,922                          |
| Retained earnings   | 188,804                 | 181,423                          |
| Accumulated other comprehensive income-Foreign currency translation   | 472                     | 460                              |
|   | 387,379                 | 379,939                          |
| <br>Treasury stock:   |                         |                                  |
| Cost of 4,572,837 shares at May 31, 2006 and 4,574,329 shares at February 28, 2006                                    | (82,578)                | (82,604)                         |
| <br>Total shareholders equity   | <br>304,801             | <br>297,335                      |
| <br>Total liabilities and shareholders equity   | <br>\$ 498,443          | <br>\$ 494,401                   |

*See accompanying notes to consolidated financial statements.*



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**ENNIS, INC. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF EARNINGS**  
*(Dollars in thousands except share and per share amounts)*  
**(Unaudited)**

|  | <b>Three months ended</b> |             |
|--|---------------------------|-------------|
|  | <b>May 31,</b>            |             |
|  | <b>2006</b>               | <b>2005</b> |
| Net sales                                  | \$ 145,113                | \$ 149,113  |
| Cost of goods sold                         | 107,298                   | 111,635     |
| Gross profit                               | 37,815                    | 37,478      |
| Selling, general and administrative        | 18,078                    | 17,837      |
| Earnings from operations                   | 19,737                    | 19,641      |
| Other income (expense)                     |                           |             |
| Interest expense                           | (1,792)                   | (2,243)     |
| Other income, net                          | 38                        | (90)        |
|  | (1,754)                   | (2,333)     |
| Net income before income taxes             | 17,983                    | 17,308      |
| Provision for income taxes                 | 6,653                     | 6,750       |
| Net earnings                               | \$ 11,330                 | \$ 10,558   |
| Weighted average common shares outstanding |                           |             |
| Basic                                      | 25,479,722                | 25,426,595  |
| Diluted                                    | 25,790,687                | 25,692,557  |
| Per share amounts                          |                           |             |
| Net earnings basic                         | \$ 0.44                   | \$ 0.42     |
| Net earnings diluted                       | \$ 0.44                   | \$ 0.41     |
| Cash dividends per share                   | \$ 0.155                  | \$ 0.155    |

*See accompanying notes to consolidated financial statements.*

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**ENNIS, INC. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
*(Dollars in thousands)*  
**(Unaudited)**

|   | <b>Three months ended</b> |             |
|---|---------------------------|-------------|
|   | <b>May 31,</b>            |             |
|   | <b>2006</b>               | <b>2005</b> |
| Cash flows from operating activities:   |                           |             |
| Net earnings  | \$ 11,330                 | \$ 10,558   |
| Adjustments to reconcile net earnings to net cash provided by operating activities: |                           |             |
| Depreciation  | 3,894                     | 3,908       |
| Amortization of deferred financing charges  | 92                        | 242         |
| Amortization of trademarks and customer lists                                       | 497                       | 479         |
| Loss (Gain) on the sale of equipment  | 3                         | (2)         |
| Bad debt expense  |                           | 369         |
| Stock based compensation  | 59                        |             |
| Changes in operating assets and liabilities, net of the effects of acquisitions:    |                           |             |
| Accounts receivables  | (4,150)                   | 976         |
| Prepaid expenses  | (2,011)                   | (448)       |
| Inventories   | 675                       | 4,261       |
| Other current assets  | (1)                       | (19)        |
| Accounts payable and accrued expenses   | 2,352                     | (2,431)     |
| Prepaid pension assets  | 459                       | 501         |
| Other assets  | (1,018)                   | 381         |
| Excess tax benefits from stock-based payment arrangements                           | (3)                       |             |
| Net cash provided by operating activities   | 12,178                    | 18,775      |
| <br>  |                           |             |
| Cash flows from investing activities:   |                           |             |
| Capital expenditures  | (636)                     | (4,521)     |
| Purchase of operating assets, net of cash acquired                                  | (4,627)                   | (366)       |
| Proceeds from disposal of property  | 3                         | 7           |
| Net cash used in investing activities   | (5,260)                   | (4,880)     |
| <br>  |                           |             |
| Cash flows from financing activities:   |                           |             |
| Debt issued   |                           | 5,000       |
| Repayment of debt   | (7,473)                   | (19,035)    |
| Dividends   | (3,949)                   | (3,940)     |
| Purchase of treasury stock  |                           | 301         |
| Proceeds from exercise of stock options   | 14                        |             |
| Excess tax benefits from stock-based payment arrangements                           | 3                         |             |
| Net cash used in financing activities   | (11,405)                  | (17,674)    |
| <br>  |                           |             |
| Effect of exchange rate changes on cash   | (51)                      | (21)        |

|  |          |          |
|--|----------|----------|
| Net change in cash and cash equivalents        | (4,538)  | (3,800)  |
| Cash and cash equivalents at beginning of year | 13,860   | 10,694   |
| <br>   |          |          |
| Cash and cash equivalents at end of year       | \$ 9,322 | \$ 6,894 |

*See accompanying notes to consolidated financial statements.*

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**ENNIS, INC. AND SUBSIDIARIES  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
FOR THE PERIOD ENDED MAY 31, 2006**

**1. Basis of Presentation**

These unaudited consolidated financial statements of Ennis, Inc. and its subsidiaries (collectively the Company or Ennis ), for the quarter ended May 31, 2006 have been prepared in accordance with generally accepted accounting principles for interim financial reporting. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements and should be read in conjunction with the audited consolidated financial statements and notes thereto included in the Company's Form 10-K for the year ended February 28, 2006, from which the accompanying consolidated balance sheet at February 28, 2006 was derived. All significant intercompany balances and transactions have been eliminated in consolidation. In the opinion of management, all adjustments considered necessary for a fair presentation of the interim financial information have been included. In preparing the financial statements, the Company is required to make estimates and assumptions that affect the disclosure and reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. The Company evaluates these estimates and judgments on an ongoing basis, including those related to bad debts, inventory valuations, property, plant and equipment, intangible assets and income taxes. The Company bases estimates and judgments on historical experience and on various other factors that are believed to be reasonable under the circumstances. The results of operations for any interim period are not necessarily indicative of the results of operations for a full year.

**2. Stock Option Plans and Stock Based Compensation**

The Company has stock options granted to key executives and managerial employees and non-employee directors. The Company has two stock option plans: the 1998 Option and Restricted Stock Plan amended and restated as of June 17, 2004 and the 1991 Incentive Stock Option Plan. The Company has 398,208 shares available for grant under the stock option plans for issuance to officers and directors and supervisory employees of the Company and its subsidiaries. The exercise price of each option granted equals the quoted market price of the Company's common stock on the date of grant, and an option's maximum term is ten years. Options may be granted at different times during the year and vest over a period of immediate to a five-year period. For the three-month periods ended May 31, 2006 and 2005, 37,700 and 35,000 of options, respectively, were not included in the diluted earnings per share computation because their exercise price exceeded the average fair market value of the Company's stock for the period. The fair value of the restricted stock awards is based upon the market price of the underlying common stock as of the date of the grant and is amortized over the applicable vesting period using the straight-line method. The Company currently uses treasury stock to satisfy option exercises and restricted stock awards. The Company adopted Statement of Financial Accounting Standards No. 123 (revised 2004), Share-Based Payment ( SFAS 123R ), effective March 1, 2006. SFAS 123R requires the recognition of the fair value of stock-based compensation in net earnings. The Company recognizes stock-based compensation expense net of estimated forfeitures (estimated at 1.1%) over the requisite service period of the individual grants, which generally equals the vesting period. For the three months ended May 31, 2006, in accordance with SFAS 123R, we recorded stock based compensation expense of approximately \$59,000 and related tax benefit of \$3,000 related to stock options and restricted stock units.

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**ENNIS, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
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**2. Stock Option Plans and Stock Based Compensation-continued**

Prior to March 1, 2006, the company applied the disclosure-only provisions of Statement of Financial Accounting Standards No. 123, Accounting for Stock-Based Compensation, (FAS 123). In accordance with the provisions of FAS 123, the Company accounted for stock options granted to its employees and Board of Directors using the recognition and measurement provisions of Accounting Principles Board Opinion No. 25, Accounting for Stock Issued to Employees, and its related interpretations, (APB 25) and accordingly did not recognize compensation expense for stock options issued to employees and board members. For disclosure purposes, the Company used the Black-Scholes option pricing model to calculate the related compensation expense for stock options granted, as if it had applied the fair value recognition provisions of FAS 123. The Company has elected to utilize the modified prospective transition method for adopting SFAS 123R. Under this method, the provisions of SFAS 123R apply to all awards granted or modified after the date of adoption. If the Company had applied the fair value recognition provisions of SFAS 123 stock-based employee compensation for the quarter ended May 31, 2005, net earnings and earnings per share would have been as follows (in thousands except per share amounts):

|  | <b>For the three<br/>months<br/>ended<br/>May 31, 2005</b> |
|--|--|
| Net earnings:  |  |
| As reported  | \$ 10,558  |
| Deduct: Stock-based Employee compensation expense not included in reported earnings, net of related tax effects \$7. | (12)   |
| Pro forma  | \$ 10,546  |

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**ENNIS, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**FOR THE PERIOD ENDED MAY 31, 2006**

**2. Stock Option Plans and Stock Based Compensation-continued**

|                         | <b>For the three<br/>months<br/>ended<br/>May 31, 2005</b> |
|-------------------------|--|
| Net earnings per share: |  |
| Basic as reported       | \$ 0.42  |
| Basic pro forma         | \$ 0.41  |
| Diluted as reported     | \$ 0.41  |
| Diluted pro forma       | \$ 0.41  |

Results for prior periods have not been restated and do not reflect the recognition of stock-based compensation. A summary of the option activity under the plans for the three months ended May 31, 2006 is as follows:

|                                  | <b>Number<br/>of<br/>Shares<br/>(exact<br/>quantity)</b> | <b>Weighted<br/>Average<br/>Exercise<br/>Price</b> | <b>Weighted<br/>Average<br/>Remaining<br/>Contractual<br/>Life<br/>(in years)</b> | <b>Aggregate<br/>Intrinsic<br/>Value<br/>(in<br/>thousands)(a)</b> |
|----------------------------------|--|--|---|--|
| Outstanding at February 28, 2006 | 687,600  | \$ 10.94   |   |  |
| Granted                          |  |  |   |  |
| Terminated                       |  |  |   |  |
| Exercised                        | (1,500)  | 10.25  |   |  |
| Outstanding at May 31, 2006      | 686,100  | \$ 10.63   | 4.4   | \$ 6,100   |
| Exercisable at May 31, 2006      | 581,150  | \$ 9.81  | 3.7   | \$ 5,643   |

(a) Value is calculated on the basis of the difference between the market value of the Company's Common Stock as reported on the New York Stock Exchange on May 31, 2006 (\$19.52) and the weighted average exercise price, multiplied by the number of shares indicated.

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**ENNIS, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**FOR THE PERIOD ENDED MAY 31, 2006**

**2. Stock Option Plans and Stock Based Compensation-continued**

The Company did not grant any stock options during the three months ended May 31, 2006. The following is a summary of the assumptions used and the weighted average grant-date fair value of the stock options granted during the three months ended May 31, 2005:

|  | <b>Three months<br/>ended<br/>May 31, 2005</b> |
|--|--|
| Expected volatility                        | 23.89%   |
| Expected term (years)                      | 5  |
| Risk free interest rate                    | 3.85%  |
| Dividend yield                             | 3.81%  |
| <br>Weighted average grant-date fair value | <br>\$ 2.85                                    |

A summary of the stock options exercised during the three months ended May 31, 2006 and 2005 is presented below (in thousands):

|                             | <b>Three months ended<br/>May 31,</b> |             |
|-----------------------------|---------------------------------------|-------------|
|                             | <b>2006</b>                           | <b>2005</b> |
| Total Cash Received         | \$ 15                                 | \$ 300      |
| Income tax benefits         | \$ 3                                  | \$ 72       |
| Total grant-date fair value | \$ 2                                  | \$ 34       |
| Intrinsic value             | \$ 14                                 | \$ 40       |

A summary of the status of the company's unvested stock options at May 31, 2006, and changes during the three months ended May 31, 2006 is presented below:

|                               | <b>Three months May 31, 2006</b> |   |
|-------------------------------|----------------------------------|---|
|                               | <b>No of<br/>Options</b>         | <b>Weighted<br/>Average<br/>Grant<br/>Date<br/>Fair Value</b> |
| Unvested at February 28, 2006 | 143,700                          | \$ 2.28   |
| New Grants                    |                                  | \$  |
| Vested                        | (38,750)                         | \$ 1.66   |
| Forfeited                     |                                  | \$  |
| Unvested at May 31, 2006      | 104,950                          | \$ 2.51   |

As of May 31, 2006, there was \$198,000 of unrecognized compensation cost related to nonvested share based compensation arrangements granted under the Plan. The cost is expected to be recognized over a weighted-average period of 2 years. The total fair value of shares vested during the three months ended May 31, 2006 was \$756,000.



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**ENNIS, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**FOR THE PERIOD ENDED MAY 31, 2006**

**2. Stock Option Plans and Stock Based Compensation-continued**

A summary of restricted stock award activity under the plans for the three months ended May 31, 2006 is as follows:

|                                  | <b>Number of<br/>Shares</b> | <b>Weighted<br/>Average<br/>Grant<br/>Date<br/>Fair Value</b> |
|----------------------------------|-----------------------------|---|
| Outstanding at February 28, 2006 | 23,919                      | \$ 19.69  |
| Granted                          |                             |   |
| Forfeited                        |                             |   |
| Outstanding at May 31, 2006      | 23,919                      | \$ 19.69  |
| Vested at May 31, 2006           |                             |   |

As of May 31, 2006, the total remaining unrecognized compensation cost related to unvested restricted stock was approximately \$432,000. The weighted average remaining requisite service period of the unvested stock options was 1.8 years.

**3. Employee Benefit Plans**

The Company and certain subsidiaries have a noncontributory defined benefit retirement plan covering approximately 15% of their employees. Benefits are based on years of service and the employee's average compensation for the highest five compensation years preceding retirement or termination. The Company's funding policy is to contribute annually an amount in accordance with the requirements of the Employee Retirement Income Security Act of 1974 (ERISA).

Pension expense is composed of the following components included in our consolidated statement of earnings for the three months ended (in thousands):

|   | <b>Three months ended<br/>May 31,</b> |             |
|---|---------------------------------------|-------------|
|   | <b>2006</b>                           | <b>2005</b> |
| Components of net periodic benefit cost |                                       |             |
| Service cost                            | \$ 360                                | \$ 356      |
| Interest cost                           | 610                                   | 611         |
| Expected return on plan assets          | (712)                                 | (693)       |
| Amortization of:                        |                                       |             |
| Prior service cost                      | (36)                                  | (36)        |
| Unrecognized net loss                   | 239                                   | 264         |
| Net periodic benefit cost               | \$ 461                                | \$ 502      |

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**ENNIS, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**FOR THE PERIOD ENDED MAY 31, 2006**

**3. Employee Benefit Plans (continued)**

The Company is required to make contributions to its defined benefit pension plan. These contributions are required under the minimum funding requirements of the Employee Retirement Pension Plan Income Security Act (ERISA). For the current fiscal year ending February 28, 2007, there is not a minimum contribution requirement and no pension payments have been made; however, the Company expects to contribute from \$2.0 million to \$3.0 million in the fourth quarter of fiscal year 2007. The Company contributed \$2,000,000 to its pension plan during fiscal year 2006.

**4. Due From Factors**

Pursuant to terms of an agreement between the Company and various factors, the Company sells a majority of the trade accounts receivable of the Apparel Segment to the factors on a non-recourse basis. The price at which the accounts are sold is the invoice amount reduced by the factor commission of between 0.25% and 1.50%. Additionally, some trade accounts receivable are sold to the factors on a recourse basis.

Trade accounts receivable not sold to the factor remain in the custody and control of the Company and the Company maintains all credit risk on those accounts as well as accounts which are sold to the factor with recourse. The Company accounts for receivables sold to the factors with recourse as accrued borrowings.

The Company may request payment from the factor in advance of the collection date or maturity. Any such advance payments are assessed in interest charges through the collection date or maturity at the JP Morgan Chase Prime Rate. The Company's obligations with respect to advances from the factor are limited to the interest charges thereon. Advance payments are limited to a maximum of 90% (ninety percent) of eligible accounts receivable.

The following table represents amounts due from factors included in accounts receivable for the periods ended (in thousands):

|                                  | <b>May 31<br/>2006</b> | <b>February<br/>28,<br/>2006</b> |
|----------------------------------|------------------------|----------------------------------|
| Outstanding factored receivables |                        |                                  |
| Without recourse                 | \$ 22,470              | \$ 19,762                        |
| With recourse                    | 1,611                  | 1,099                            |
| Advances from factors            | (19,228)               | (17,772)                         |
| Due from factors                 | \$ 4,853               | \$ 3,089                         |

**5. Accounts Receivable and Allowance for Doubtful Accounts**

Accounts receivable are reduced by an allowance for an estimate of amounts that are uncollectible. Approximately 99% of the Company's receivables are due from customers in North America. The Company extends credit to its customers based upon its evaluation of the following factors: (i) the

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**ENNIS, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**FOR THE PERIOD ENDED MAY 31, 2006**

**5. Accounts Receivable and Allowance for Doubtful Accounts-continued**

customer's financial condition, (ii) the amount of credit the customer requests and (iii) the customer's actual payment history (which includes disputed invoice resolution). The Company does not typically require its customers to post a deposit or supply collateral. The Company's allowance for doubtful accounts reserve is based on an analysis that estimates the amount of its total customer receivable balance that is not collectible. This analysis includes assessing a default probability to customers' receivable balance, which is influenced by several factors including (i) current market conditions, (ii) periodic review of customer credit worthiness, and (iii) review of customer receivable aging and payment trends. The Company writes-off accounts receivable when they become uncollectible, and payments subsequently received on such receivables are credited to bad debt expense in the period the payment is received. Credit losses from continuing operations have consistently been within management's expectations.

The following table represents the activity in the Company's allowance for doubtful accounts for the three months ended (in thousands):

|                                | <b>Three months ended</b> |             |
|--------------------------------|---------------------------|-------------|
|                                | <b>May 31</b>             |             |
|                                | <b>2006</b>               | <b>2005</b> |
| Balance at beginning of period | \$ 3,001                  | \$ 3,567    |
| Bad debt expense               |                           | 369         |
| Recoveries                     | 91                        | 25          |
| Accounts written off           | (135)                     | (444)       |
| Balance at end of period       | \$ 2,957                  | \$ 3,517    |

**6. Inventories**

The Company uses the lower of last-in, first-out (LIFO) cost or market to value certain of its business forms inventory and the lower of first-in, first-out (FIFO) cost or market to value its remaining and apparel inventories. The Company regularly reviews inventory values on hand, using specific aging categories, and writes down the carrying value of its inventory for excess and potentially obsolete inventories based on historical usage and estimated future usage. In assessing the ultimate realization of its inventory, the company is required to make judgments as to future demand requirements. As actual future demand or market conditions may vary from those projected by the Company, adjustments to inventories may be required.

The following table summarizes the components of inventories at the different stages of production as of the dates indicated (in thousands):

|                 | <b>May 31,</b> | <b>February</b>           |
|-----------------|----------------|---------------------------|
|                 | <b>2006</b>    | <b>28,</b><br><b>2006</b> |
| Raw material    | \$ 7,571       | \$ 12,694                 |
| Work-in-process | 18,471         | 16,886                    |
| Finished goods  | 63,185         | 59,575                    |
|                 | \$ 89,227      | \$ 89,155                 |



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**ENNIS, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
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**7. Acquisitions**

The Company purchased all of the outstanding stock of Specialized Printed Forms, Inc., ( SPF ) a privately held company headquartered in Caledonia, New York and the associated land and buildings for \$4.6 million in cash on March 31, 2006. SPF had sales of \$9.2 million for the twelve month period ended July 31, 2005. The acquisition of SPF continues the Ennis strategy of growth through related manufactured products to further service our existing customer base. The acquisition added additional short-run print products, long-run (jumbo rolls) products and solutions as well as integrated labels and form/label combinations sold through the indirect sales (distributorship) marketplace.

The following is a summary of the purchase price allocation (in thousands).

|  |          |
|--|----------|
| Accounts receivable, net                 | \$ 826   |
| Inventories                              | 579      |
| Property, plant & equipment              | 5,444    |
| Accounts payable and accrued liabilities | (2,222)  |
|  | \$ 4,627 |

The Company's results of operations for the three month period ended May 31, 2006 included from SPF sales in the amount of \$1.3 million and net income before income taxes of \$52,000 from its acquisition date of March 31, 2006. Pro-forma information has not been presented as it was not material to the previously reported revenue, net income or earnings per share of the Company.

**8. Goodwill and Other Intangible Assets**

Goodwill represents the excess of the purchase price over the fair value of net assets of acquired businesses and is not amortized. Goodwill and indefinite-lived intangibles are evaluated for impairment on an annual basis, or more frequently if impairment indicators arise, using a fair-value-based test that compares the fair value of the asset to its carrying value. Fair values of reporting units are typically calculated using a factor of expected earnings before interest, taxes, depreciation, and amortization. Based on this evaluation, no impairment was recorded. The Company must make assumptions regarding estimated future cash flows and other factors to determine the fair value of the respective assets in assessing the recoverability of its goodwill and other intangibles. If these estimates or the related assumptions change, the Company may be required to record impairment charges for these assets in the future.

Intangible assets with determinable lives are amortized on a straight-line basis over the estimated useful life. The cost of trademarks is based on fair values at the date of acquisition. Trade names with determinable lives and a net book value of \$904,000 at May 31, 2006 are amortized on a straight-line basis over the estimated useful life (between 1 and 10 years). Trademarks with indefinite-lived lives with a net book value of \$61,000,000 at May 31, 2006 are evaluated for impairment on an annual basis.

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**8. Goodwill and Other Intangible Assets-continued**

The cost of purchased trade names is based on fair values at the date of acquisition and is amortized on a straight-line basis over the estimated useful life (between 10 and 15 years) of such trade names. The Company assesses the recoverability of its definite-lived intangible assets primarily based on its current and anticipated future undiscounted cash flows.

|   | <b>Gross<br/>Carrying<br/>Amount</b> | <b>Accumulated<br/>Amortization</b> | <b>Net</b>       |
|---|--------------------------------------|-------------------------------------|------------------|
| <b>As of May 31, 2006</b>   |                                      |                                     |                  |
| Amortized intangible assets (in thousands)  |                                      |                                     |                  |
| Trademarks  | \$ 1,234                             | \$ 330                              | \$ 904           |
| Purchased customer lists  | 23,760                               | 2,538                               | 21,222           |
|   | <b>\$ 24,994</b>                     | <b>\$ 2,868</b>                     | <b>\$ 22,126</b> |
| <b>As of February 28, 2006</b>  |                                      |                                     |                  |
| Amortized intangible assets (in thousands)  |                                      |                                     |                  |
| Trademarks  | \$ 1,234                             | \$ 293                              | \$ 941           |
| Purchased customer lists  | 23,760                               | 2,128                               | 21,632           |
|   | <b>\$ 24,994</b>                     | <b>\$ 2,421</b>                     | <b>\$ 22,573</b> |
| Unamortized intangible assets (trademarks), as of May 31, 2006 and 2005 (in thousands): |                                      |                                     | \$ 61,000        |

Aggregate amortization expense for three months ended May 31, 2006 and May 31, 2005 was \$497,000 and \$479,000 respectively.

The Company's estimated amortization expense for the next five years is as follows (in thousands):

|      |          |
|------|----------|
| 2007 | \$ 1,944 |
| 2008 | 1,805    |
| 2009 | 1,792    |
| 2010 | 1,776    |
| 2011 | 1,775    |

Changes in the net carrying amount of goodwill are as follows:

|   | <b>May 31,<br/>2006</b> | <b>February<br/>28,<br/>2006</b> |
|---|-------------------------|----------------------------------|
| Balance as of the beginning of the period | \$ 178,280              | \$ 178,472                       |
| Goodwill adjusted during year             |                         | (192)                            |
| Balance as of the end of the period       | \$ 178,280              | \$ 178,280                       |



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**9. Long-Term Debt**

Long-term debt consisted of the following as of the dates indicated (in thousands):

|                                    | <b>May 31,<br/>2006</b> | <b>February<br/>28,<br/>2006</b> |
|------------------------------------|-------------------------|----------------------------------|
| Revolving credit facility          | \$ 95,500               | \$ 62,500                        |
| Term credit facility               |                         | 40,000                           |
| Capital lease obligations          | 583                     | 736                              |
| Notes payable to finance companies | 982                     | 1,300                            |
| Other                              | 10,004                  | 10,000                           |
|                                    | 107,069                 | 114,536                          |
| Less current installments          | 11,255                  | 11,620                           |
| Long-term debt                     | \$ 95,814               | \$ 102,916                       |

On March 31, 2006, The Company entered into an amended and restated credit agreement with a group of lenders led by LaSalle Bank N.A. (the Facility). The Facility provides us access to \$150 million in revolving credit and matures on March 31, 2010. The facility bears interest at the London Interbank Offered Rate (LIBOR) plus a spread ranging from .50% to 1.50% (currently LIBOR + .75% = 5.8425%), depending on our total funded debt to EBITDA ratio, as defined. The Facility is secured by substantially all of our personal and investment property. The Facility contains financial covenants, restrictions on capital expenditures, acquisitions, asset dispositions, and additional debt, as well as other customary covenants.

Notes payable to finance companies bear interest ranging from at 6.86% to 9.46%, and require monthly payments of principal and interest. The notes mature at dates ranging from September 2006 through November 2007 and are collateralized by certain equipment.

Notes payable classified as Other were obligations of Alstyle Apparel. These notes were assumed by the Company in connection with its acquisition of Alstyle Apparel in November 2004. These loans are to individuals (former shareholders of Alstyle) with annual payments bearing interest at rates of 4.0% and matures in November 2007.

Payments on these notes are subject to set-off arbitration procedures relating to subsequently discovered pre-acquisition liabilities that were either undisclosed at the time of closing or inappropriately accrued for in the books and records, and other terms and provisions. The Company made a \$5.0 million principal payment on June 5, 2006 relating to these notes and \$5.0 million remains subject to set-off arbitration procedures.

**10. Shareholders Equity**

Comprehensive income is defined as all changes in equity during a period, except for those resulting from investments by owners and distributions to owners. The components of comprehensive income were as follows (in thousands):

|   | <b>Three months ended<br/>May 31,</b> |             |
|---|---------------------------------------|-------------|
|   | <b>2006</b>                           | <b>2005</b> |
| Net earnings from continuing operations | \$ 11,330                             | \$ 10,558   |
| Interest rate hedge                     |                                       | (2)         |
| Foreign currency translation adjustment | 12                                    | (22)        |

Comprehensive income

\$ 11,342

\$ 10,534

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**10. Shareholders' Equity (continued)**

Changes in our shareholders' equity accounts for the three months ended May 31, 2006 are as follows (in thousands):

|  | Common<br>Stock<br>(\$) | Additional<br>Paid-In<br>Capital | Retained<br>Earnings | Accumulated<br>Other<br>Comprehensive<br>Income | Treasury<br>Stock<br>(\$) | Total     |
|--|-------------------------|----------------------------------|----------------------|---|---------------------------|-----------|
| Balance at February 28, 2006               | \$75,134                | \$122,922                        | \$181,423            | \$460   | \$(82,604)                | \$297,335 |
| Net earnings                               |                         |                                  |                      |   |                           |           |
| 11,330                                     |                         |                                  |                      |   |                           | 11,330    |
| Foreign currency translation               |                         |                                  |                      |   |                           |           |
| 12   |                         |                                  |                      |   |                           | 12        |
| Comprehensive income                       |                         |                                  |                      |   |                           |           |
| 11,342                                     |                         |                                  |                      |   |                           |           |
| Dividends declared (\$.155 per share)      |                         |                                  |                      |   |                           |           |
| (3,949)                                    |                         |                                  |                      |   |                           | (3,949)   |
| Exercise of stock options                  |                         |                                  |                      |   |                           |           |
| (12)                                       |                         |                                  |                      |   |                           | 26        |
| 14   |                         |                                  |                      |   |                           |           |
| Charge related to stock-based compensation |                         |                                  |                      |   |                           |           |
| 59   |                         |                                  |                      |   |                           | 59        |
| Balance at May 31, 2006                    | \$75,134                | \$122,969                        | \$188,804            | \$472   | \$(82,578)                | \$304,801 |

**11. Earnings per share**

Basic earnings per share have been computed by dividing net earnings by the weighted average number of common shares outstanding during the applicable period. Diluted earnings per share reflect the potential dilution that could occur if options or other contracts to issue common shares were exercised or converted into common stock. The following table sets forth the computation for basic and diluted earnings per share for the periods indicated.

|  | Three months ended<br>May 31, |            |
|--|-------------------------------|------------|
|  | 2006                          | 2005       |
| Basic weighted average common shares outstanding   | 25,479,722                    | 25,426,595 |
| Effect of dilutive options                         | 310,965                       | 265,962    |
| Diluted weighted average common shares outstanding | 25,790,687                    | 25,692,557 |
| Per share amounts:                                 |                               |            |
| Net earnings - basic                               | \$ 0.44                       | \$ 0.42    |
| Net earnings - diluted                             | \$ 0.44                       | \$ 0.41    |

|                |    |       |    |       |
|----------------|----|-------|----|-------|
| Cash dividends | \$ | 0.155 | \$ | 0.155 |
|----------------|----|-------|----|-------|

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**ENNIS, INC. AND SUBSIDIARIES  
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**12. Segment Information and Geographic Information**

The Company operates in two segments – the Print Segment and the Apparel Segment.

The Print Segment, which represented 53% of the Company's consolidated sales for the three months ended May 31, 2006, is in the business of manufacturing, design and selling business forms and other printed business products primarily to distributors located in the United States.

The Print Segment operates 33 manufacturing locations throughout the United States in 15 strategically located domestic states. Approximately 98% of the business products manufactured by the Print Segment are custom and semi-custom, constructed in a wide variety of sizes, colors, number of parts and quantities on an individual job basis depending upon the customers' specifications.

The products sold include snap sets, continuous forms, laser cut sheets, tags, labels, integrated products, jumbo rolls and pressure sensitive products in short, medium and long runs under the following labels: Ennis, Royal, TBF/Avant-Garde, 360° Custom Labels, Witt Printing and Calibrated Forms. The Print Segment also sells: the Adams-McClure brand (which provides Point of Purchase advertising for large franchise and fast food chains as well as kitting and fulfillment); the Admore brand (which provides presentation folders and document folders); Ennis Tag & Label (which provides tags and labels, promotional products and advertising concept products), GenForms (which provides short-run and long-run label production) and Northstar and GFS (which provides financial and security documents).

The Print Segment sells predominantly through private printers and independent distributors. Northstar and GFS also sell directly to a small number of direct customers. Northstar has continued its focus with large banking organizations on a direct basis (where a distributor is not acceptable or available to the end-user) and has acquired several of the top 100 banks in the United States as customers and is actively working on other large banks within the top 100 tier of banks in the United States. Adams-McClure sales are generally provided through advertising agencies.

The second segment, the Apparel Segment, which represented 47% of the Company's consolidated sales for the three months ended May 31, 2006, consists of Alstyle Apparel, which is primarily engaged in the production and sale of active-wear including t-shirts, fleece goods and other wearables. Alstyle sales are seasonal, with sales in the first and second quarters generally being the highest. Corporate information is included to reconcile segment data to the consolidated financial statements and includes assets and expenses related to the Company's corporate headquarters and other administrative costs.

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**12. Segment Information and Geographic Information-continued**

Segment data for the three months ended May 31, 2006 and 2005 were as follows (in thousands):

|   | <b>Print<br/>Segment</b> | <b>Apparel<br/>Segment</b> | <b>Corporate</b> | <b>Consolidated<br/>Totals</b> |
|---|--------------------------|----------------------------|------------------|--------------------------------|
| <b><u>Three months ended May 31, 2006</u></b> |                          |                            |                  |                                |
| Net sales                                     | \$ 77,096                | \$ 68,017                  | \$               | \$145,113                      |
| Depreciation                                  | 2,024                    | 1,719                      | 151              | 3,894                          |
| Amortization of trademark                     | 93                       | 404                        |                  | 497                            |
| Segment earnings (loss) before income tax     | 11,271                   | 10,042                     | (3,330)          | 17,983                         |
| Segment assets                                | 159,106                  | 320,754                    | 18,583           | 498,443                        |
| Capital expenditures                          | 371                      | 187                        | 78               | 636                            |
| <b><u>Three months ended May 31, 2005</u></b> |                          |                            |                  |                                |
| Net sales                                     | \$ 80,724                | \$ 68,389                  | \$               | \$149,113                      |
| Depreciation                                  | 1,839                    | 1,909                      | 160              | 3,908                          |
| Amortization of trademark                     | 90                       | 389                        |                  | 479                            |
| Segment earnings (loss) before income tax     | 11,448                   | 8,367                      | (2,507)          | 17,308                         |
| Segment assets                                | 161,259                  | 311,801                    | 13,968           | 487,028                        |
| Capital expenditures                          | 329                      | 3,868                      | 324              | 4,521                          |

Identifiable long-lived assets by country includes property, plant and equipment net of accumulated depreciation. The Company attributes revenues from external customers to individual geographic areas based on the country where the sale originated. Information about the Company's operations in different geographic areas of and for the three months ended is as follow (in thousands):

|                                     | <b>United<br/>States</b> | <b>Canada</b> | <b>Mexico</b> | <b>Total</b> |
|-------------------------------------|--------------------------|---------------|---------------|--------------|
| <b><u>Through May 31, 2006</u></b>  |                          |               |               |              |
| Net sales to unaffiliated customers |                          |               |               |              |
| Print Segment                       | \$ 77,096                | \$            | \$            | \$ 77,096    |
| Apparel Segment                     | 62,265                   | 5,752         |               | 68,017       |
|                                     | \$ 139,361               | \$ 5,752      | \$            | \$ 145,113   |
| Identifiable long-lived assets      |                          |               |               |              |
| Print Segment                       | \$ 44,683                | \$            | \$            | \$ 44,683    |
| Apparel Segment                     | 11,509                   | 97            | 3,376         | 14,982       |
| Corporate                           | 6,194                    |               |               | 6,194        |
|                                     | \$ 62,386                | \$ 97         | \$ 3,376      | \$ 65,859    |

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**12. Segment Information and Geographic Information-continued**

|                                     | United<br>States | Canada   | Mexico   | Total      |
|-------------------------------------|------------------|----------|----------|------------|
| <b><u>Through May 31, 2005</u></b>  |                  |          |          |            |
| Net sales to unaffiliated customers |                  |          |          |            |
| Print Segment                       | \$ 80,724        | \$       | \$       | \$ 80,724  |
| Apparel Segment                     | 66,239           | 2,150    |          | 68,389     |
|                                     | \$ 146,963       | \$ 2,150 | \$       | \$ 149,113 |
| Identifiable long-lived assets      |                  |          |          |            |
| Print Segment                       | \$ 44,231        | \$       | \$       | \$ 44,231  |
| Apparel Segment                     | 16,880           | 131      | 4,313    | 21,324     |
| Corporate                           | 7,072            |          |          | 7,072      |
|                                     | \$ 68,183        | \$ 131   | \$ 4,313 | \$ 72,627  |

**13. Supplemental Cash Flow Information**

Net cash flows from operating activities reflects cash payments for interest and income taxes as follows (in thousands):

|                   | <b>Three months ended<br/>May 31,</b> |             |
|-------------------|---------------------------------------|-------------|
|                   | <b>2006</b>                           | <b>2005</b> |
| Interest paid     | \$1,300                               | \$2,228     |
| Income taxes paid | \$1,264                               | \$ 829      |

**14. Assets Held for Sale**

Included in other assets is land and building with an approximate value of \$2.4 million at May 31, 2006 and February 28, 2006 which is being held for sale. The Company closed on the sale of this property on June 28, 2006 for approximately \$2.5 million.

**15. Subsequent Events**

On June 30, 2006, the Company declared a quarterly cash dividend of 15 1/2 cents a share on its common stock. The dividend is payable August 1, 2006 to shareholders of record on July 14, 2006.

On June 7, 2006, the Company entered into a Letter of Intent to acquire all the stock of Block Graphics, Inc. ( Block ) for approximately \$14.5 million in cash. Block had sales of approximately \$35 million for the year ended December 31, 2005. The acquisition will add additional short-run print products (snaps, continuous forms and cut-sheet forms) as well as the production of envelopes, a new product for the Company.

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

**Overview**

Ennis, Inc. (formerly Ennis Business Forms, Inc.) was organized under the laws of Texas in 1909. Ennis, Inc. and its subsidiaries (collectively known as the Company, Registrant, Ennis, or we, us, or our) prints and constructs a line of business forms and other business products and also manufactures a line of activewear for distribution throughout North America. Distribution of business products and forms throughout the United States and Canada is primarily through independent dealers, and with respect to our activewear products, through sales representatives. This distributor channel encompasses print distributors, stationers, quick printers, computer software developers, activewear wholesalers, screen printers and advertising agencies, among others.

On March 31, 2006, we purchased the outstanding stock of Specialized Printed Forms, Inc., (SPF) a privately held company headquartered in Caledonia, New York and the associated land and buildings. The purchase price of this transaction was \$4.6 million (in cash). SPF had sales of \$9.2 million for the twelve month period ended July 31, 2005. The acquisition of SPF continues the Ennis strategy of growth through related manufactured products to further service our existing customer base. The acquisition added additional short-run print products, long-run (jumbo rolls) products and solutions as well as integrated labels and form/label combinations sold through the indirect sales (distributorship) marketplace.

**Business Segment Overview**

We operate in two business segments, the Print Segment and the Apparel Segment. The following is a description of each segment. Prior to February 28, 2006, the Print Segment operated in three operating groups—the Forms Solutions Group, the Promotional Solutions Group and the Financial Solutions Group. The print market continues to evolve due to technology improvements, consolidations, etc. Plants that once only produced standard form products, or were niche product printers, now produce promotional products, labels, etc. and provide other value-add services. Our plants have seen the same degree of evolution over the past several years, which resulted in them losing, to some degree, their product/group specific identity. For the aforementioned reasons, we now consider it prudent to manage/monitor and report these plants at the Print Segment level and not at the Group level.

**Print Segment**

The Print Segment, which represented 53% of our consolidated sales for the three months ended May 31, 2006, is in the business of manufacturing, design and selling business forms and other printed business products primarily to distributors located in the United States. The Print Segment operates 33 manufacturing locations throughout the United States in 15 strategically located domestic states. Approximately 98% of the business products manufactured by the Printing Segment are custom and semi-custom products, constructed in a wide variety of sizes, colors and quantities on an individual job basis depending upon the customers' specifications.

The products sold include snap sets, continuous forms, laser cut sheets, tags, labels, integrated products, jumbo rolls and pressure sensitive products in short, medium and long runs under the following

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labels: Ennis, Royal, TBF/Avant-Garde, 360° Custom Labels, Witt Printing and Calibrated Forms. The Print Segment also sells: the Adams-McClure brand (which provides Point of Purchase advertising for large franchise and fast food chains as well as kitting and fulfillment); the Admore brand (which provides presentation folders and document folders); Ennis Tag & Label (which provides tags and labels, promotional products and advertising concept products), GenForms (which provides short-run and long-run label production) and Northstar and GFS (which provides financial and security documents).

The Print Segment sells predominantly through private printers and independent distributors. Northstar and GFS also sell directly to a small number of direct customers. Northstar has continued its focus with large banking organizations on a direct basis (where a distributor is not acceptable or available to the end-user) and has acquired several of the top 100 banks in the United States as customers and is actively working on other large banks within the top 100 tier of banks in the United States. Adams-McClure sales are generally provided through advertising agencies.

The printing industry generally sells its products in two ways. One market direction is to sell predominately to end users, and is dominated by a few large manufacturers, such as Moore Wallace (a subsidiary of R.R. Donnelly), Standard Register, and Cenveo. The other market direction, which the Company primarily serves, sells forms and other business products through a variety of independent distributors and distributor groups. While it is not possible, because of the lack of adequate statistical information, to determine Ennis' share of the total business products market, management believes Ennis is one of the largest producers of business forms in the United States distributing primarily through independent dealers, and that its business forms offering is more diversified than that of most companies in the business forms industry. There are a number of competitors that operate in this segment, ranging in size from single employee-owner operations to multi-plant organizations, such as Cenveo and their Quality Park brand. We believe our strategic locations and buying power permit us to compete on a favorable basis within the distributor market on competitive factors, such as service, quality and price.

Distribution of business forms and other business products throughout the United States is primarily done through independent dealers, including business forms distributors, stationers, printers, computer software developers, advertising agencies, etc.

Raw materials of the Printing Segment principally consist of a wide variety of weights, widths, colors, sizes and qualities of paper for business products purchased from a number of major suppliers at prevailing market prices.

Business products usage in the printing industry is generally not seasonal. General economic conditions and contraction of traditional business forms industry are the predominant factor in quarterly volume fluctuations.

**Apparel Segment**

The Apparel Segment represented 47% of our consolidated sales for the three months ended May 31, 2006. This segment operates under the name of Alstyle Apparel ( Alstyle ). Alstyle markets high quality knit basic activewear (t-shirts, tank tops and fleece) across all market segments. Approximately 88% of Alstyle's revenues are derived from t-shirt sales, and 94% of those are domestic sales. Alstyle's branded product lines are AAA, Gaziani, Diamond Star, Murina, A Classic, Tennessee River, D Drive and Hyland Headware.

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Alstyle is headquartered in Anaheim, California, where they knit domestic cotton yarn and some polyester fibers into tubular material. The material is then dyed at that facility and then shipped to its plants in Ensenada or Hermosillo, Mexico, where it is cut and sewn into finished goods. Alstyle also ships a small amount of their dyed and cut product to El Salvador and Costa Rica for sewing. After sewing and packaging is completed, product is shipped to one of Alstyle's seven distribution centers located across the United States and in Canada.

Alstyle utilizes a customer-focused internal sales team comprised of 19 sales representatives assigned to specific geographic territories in the United States and Canada. Sales representatives are allocated performance objectives for their respective territories and are provided financial incentives for achievement of their target objectives. Sales representatives are responsible for developing business with large accounts and spend approximately half their time in the field.

Alstyle employs a staff of customer service representatives that handle call-in orders from smaller customers. Sales personnel sell directly to Alstyle's customer base, which consists primarily of screen printers, embellishers, retailers, and mass marketers.

A majority of Alstyle's sales are related to direct customer, branded products and the remainder relate to private label and re-label programs. Generally, sales to screen printers and mass marketers are driven by the availability of competitive products and price considerations, while sales in the private label business are characterized by slightly higher customer loyalty.

Alstyle's most popular styles are produced based on forecasts to permit quick shipment and to level production schedules. Alstyle offers same-day shipping and uses third party carriers to ship products to its customers.

Alstyle's sales are seasonal, with sales in the first and second quarters generally being the highest. The general apparel industry is characterized by rapid shifts in fashion, consumer demand and competitive pressures, resulting in both price and demand volatility. However, the imprinted activewear market that Alstyle sells to is event driven. Blank t-shirts can be thought of as walking billboards promoting movies, concerts, sports teams, and image brands. Still, the demand for any particular product varies from time to time based largely upon changes in consumer preferences and general economic conditions affecting the apparel industry.

The products of the Apparel Segment are standardized shirts manufactured in a variety of sizes and colors. The Apparel Segment operates six manufacturing facilities, one in California and five in Mexico.

The Apparel industry is comprised of numerous companies who manufacture and sell a wide range of products. Alstyle is primarily involved in the activewear and produces t-shirts, fleece items, and outsources such products as hats, shorts, pants and other such activewear apparel from China, Thailand, Pakistan, India, Indonesia, Russia, and other foreign sources to sell to its customers through its sales representatives. Its primary competitors are Delta Apparel (Delta), Russell, Hanes and Gildan Activewear (Gildan). While it is not possible to calculate precisely, based on public information available, management believes that Alstyle is one of the top three providers of blank t-shirts in North America. Alstyle competes with many branded and private label manufacturers of knit apparel in the United States and Canada, some of which are larger in size and have greater financial resources than Alstyle. Alstyle competes on the basis of price, quality, service and delivery. Alstyle's strategy is to

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provide the best value to its customers by delivering a consistent, high-quality product at a competitive price. Alstyle's competitive disadvantage is that its brand name, Alstyle Apparel, is not as well known as the brand names of its largest competitors, such as Gildan, Delta, Hanes and Russell.

No single customer accounts for as much as ten percent of consolidated net sales. Distribution of the Apparel Segment's products is through Alstyle's own staff of sales representatives selling to distributors who resell to retailers, or directly to screen printers, embellishers, retailers and mass marketers.

Raw materials of the Apparel Segment principally consist of cotton and polyester yarn purchased from a number of major suppliers at prevailing market prices, although we purchase more than 50% of our cotton and yarn from one supplier. Reference is made to Risk Factors of this Report.

**Risk Factors**

You should carefully consider the risks described below, as well as the other information included or incorporated by reference in this Annual Report on Form 10-K, before making an investment in our common stock. The risks described below are not the only ones we face in our business. Additional risks and uncertainties not presently known to us or that we currently believe to be immaterial may also impair our business operations. If any of the following risks occur, our business, financial condition or operating results could be materially harmed. In such an event, our common stock could decline in price and you may lose all or part of your investment.

***We may be required to write down goodwill and other intangible assets in the future, which could cause our financial condition and results of operations to be negatively affected in the future.***

When we acquire a business, a portion of the purchase price of the acquisition may be allocated to goodwill and other identifiable intangible assets. The amount of the purchase price which is allocated to goodwill and other intangible assets is determined by the excess of the purchase price over the net identifiable assets acquired. At May 31, 2006, our goodwill and other intangible assets were approximately \$178.3 million and \$83.2 million, respectively. Under current accounting standards, if we determine goodwill or intangible assets are impaired, we would be required to write down the value of these assets. Annually, we have conducted a review of our goodwill and other identifiable intangible assets to determine whether there has been impairment. Such a review was completed for our fiscal year ended February 28, 2006, and we concluded that no impairment charge was necessary. We cannot provide assurance that we will not be required to take an impairment charge in the future. Any impairment charge would have a negative effect on our shareholders' equity and financial results and may cause a decline in our stock price.

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***Printed business forms may be superceded over time by paperless business forms or otherwise affected by technological obsolescence and changing customer preferences, which could reduce our sales and profits.***

Printed business forms and checks may eventually be superceded by paperless business forms, which could have a material adverse effect on our business over time. The price and performance capabilities of personal computers and related printers now provide a cost-competitive means to print low-quality versions of many of our business forms on plain paper. In addition, electronic transaction systems and off-the-shelf business software applications have been designed to automate several of the functions performed by our business form and check products. In response to the gradual obsolescence of our standardized forms business, we continue to develop our capability to provide custom and full-color products. We are also seeking to introduce new products and services that may be less susceptible to technological obsolescence. If new printing capabilities and new product introductions do not continue to offset the obsolescence of our standardized business forms products, there is a risk that the number of new customers we attract and existing customers we retain may diminish, which could reduce our sales and profits. Decreases in sales of our standardized business forms and products due to obsolescence could also reduce our gross margins. This reduction could in turn adversely impact our profits, unless we are able to offset the reduction through the introduction of new high margin products and services or realize cost savings in other areas.

***Our distributors face increased competition from various sources, such as office supply superstores. Increased competition may require us to reduce prices or to offer other incentives in order to enable our distributors to attract new customers and retain existing customers.***

Low price, high value office supply chain stores offer standardized business forms, checks and related products. Because of their size, these superstores have the buying power to offer many of these products at competitive prices. These superstores also offer the convenience of one-stop shopping for a broad array of office supplies that our distributors do not offer. In addition, superstores have the financial strength to reduce prices or increase promotional discounts to expand market share. This could result in us reducing our prices or offering incentives in order to enable our distributors to attract new customers and retain existing customers.

***Technological improvements may reduce our competitive advantage over some of our competitors, which could reduce our profits.***

Improvements in the cost and quality of printing technology are enabling some of our competitors to gain access to products of complex design and functionality at competitive costs. Increased competition from these competitors could force us to reduce our prices in order to attract and retain customers, which could reduce our profits.

***We could experience labor disputes that could disrupt our business in the future.***

As of May 31, 2006, approximately 14% of our domestic employees are represented by labor unions under collective bargaining agreements, which are subject to periodic renegotiations. Two unions represent all of our hourly employees in Mexico. Although we have not experienced any labor stoppages in the last 10 years, there can be no assurance that any future labor negotiations would continue to be successful or would not experience a labor-stoppage, either of these events could have a materially adverse impact on our cost of labor or our ability to produce our products.

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***We obtain our raw materials from a limited number of suppliers and any disruption in our relationships with these suppliers, or any substantial increase in the price of raw materials, could have a material adverse effect on us.***

Cotton yarn is the primary raw material used in Alstyle's manufacturing processes. Cotton accounts for approximately 40% of the manufactured product cost. Alstyle acquires its yarn from five major sources that meet stringent quality and on-time delivery requirements. The largest supplier provides over 50% of Alstyle's yarn requirements and has an entire yarn mill dedicated to Alstyle's production. The other major raw material components used in Alstyle's manufacturing processes are chemicals used to treat the fabric during the dyeing process, which currently Alstyle sole-sources the supply of these chemicals from one supplier. If Alstyle's relations with its suppliers are disrupted, Alstyle may not be able to enter into arrangements with substitute suppliers on terms as favorable as its current terms and our results of operations could be materially adversely affected.

Alstyle generally acquires its cotton yarn under short-term purchase orders with its suppliers, and has exposure to swings in cotton market prices. Alstyle does not use derivative instruments, including cotton option contracts, to manage its exposure to movements in cotton market prices. Alstyle may use such derivative instruments in the future. We believe we are competitive with other companies in the United States apparel industry in negotiating the price of cotton. However, any significant increase in the price of cotton could have a material adverse effect on our results of operations.

We also purchase our paper products from a limited number of sources, which meet stringent quality and on-time delivery standards under long-term contracts. However, fluctuations in the quality of our paper, unexpected price increases, etc. could have a material adverse effect on our operating results.

***Alstyle faces intense competition to gain market share, which may lead some competitors to sell substantial amounts of goods at prices against which we cannot profitably compete.***

Demand for Alstyle's products is dependent on the general demand for T-shirts and the availability of alternative sources of supply. Alstyle's strategy in this market environment is to be a low cost producer and to differentiate itself by providing quality service to its customers. Even if this strategy is successful, its results may be offset by reductions in demand or price declines.

***Apparel business is subject to cyclical trends.***

The United States apparel industry is sensitive to the business cycle of the national economy. Moreover, the popularity, supply and demand for particular apparel products can change significantly from year to year. Alstyle may be unable to compete successfully in any industry downturn due to excess capacity.

***Our apparel foreign operations could be subject to unexpected changes in regulatory requirements, tariffs and other market barriers and political and economic instability in the countries where it operates, which could negatively impact our operating results.***

Alstyle operates cutting and sewing facilities in Mexico, and sources certain product manufacturing and purchases in El Salvador, Pakistan, China and Southeast Asia. Alstyle's foreign operations could be subject to unexpected changes in regulatory requirements, tariffs and other market barriers and political and economic instability in the countries where it operates. The impact of any such events that may occur in the future could subject Alstyle to additional costs or loss of sales, which could adversely affect our operating results. In particular, Alstyle operates its facilities in Mexico pursuant to

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the maquiladora duty-free program established by the Mexican and United States governments. This program enables Alstyle to take advantage of generally lower costs in Mexico, without paying duty on inventory shipped into or out of Mexico. There can be no assurance that the governments of Mexico and the United States will continue the program currently in place or that Alstyle will continue to be able to benefit from this program. The loss of these benefits could have an adverse effect on our business.

***Our apparel products are subject to foreign competition, which in the past has been faced with significant U.S. government import restrictions.***

Foreign producers of apparel often have significant labor cost advantages. Given the number of these foreign producers, the substantial elimination of import protections that protect domestic apparel producers could materially adversely affect Alstyle's business. The extent of import protection afforded to domestic apparel producers has been, and is likely to remain, subject to considerable political considerations.

The North American Free Trade Agreement (NAFTA) became effective on January 1, 1994 and has created a free-trade zone among Canada, Mexico and the United States. NAFTA contains a rule of origin requirement that products be produced in one of the three countries in order to benefit from the agreement. NAFTA has phased out all trade restrictions and tariffs among the three countries on apparel products competitive with those of Alstyle. Alstyle performs substantially all of its cutting and sewing in five plants located in Mexico in order to take advantage of the NAFTA benefits. Subsequent repeal or alteration of NAFTA could adversely affect our business.

The Central American Free Trade Agreement (CAFTA) became effective May 28, 2004 and retroactive to January 1, 2004 for textiles and apparel. It creates a free trade zone similar to NAFTA by and between the United States and Central American countries (El Salvador, Honduras, Costa Rica, Nicaragua and Dominican Republic). Textiles and apparel will be duty-free and quota-free immediately if they meet the agreement's rule of origin, promoting new opportunities for U.S. and Central American fiber, yarn, fabric and apparel manufacturing. The agreement will also give duty-free benefits to some apparel made in Central America that contains certain fabrics from NAFTA partners Mexico and Canada. Alstyle sources approximately 5% of its sewing to a contract manufacturer in El Salvador, and we do not anticipate that this will have a material effect on our operations.

The World Trade Organization (WTO), a multilateral trade organization, was formed in January 1995 and is the successor to the General Agreement on Tariffs and Trade (GATT). This multilateral trade organization has set forth mechanisms by which world trade in clothing is being progressively liberalized by phasing-out quotas and reducing duties over a period of time that began in January of 1995. As it implements the WTO mechanisms, the U.S. government is negotiating bilateral trade agreements with developing countries, which are generally exporters of textile and apparel products, that are members of the WTO to get them to reduce their tariffs on imports of textiles and apparel in exchange for reductions by the United States in tariffs on imports of textiles and apparel.

In January 2005, United States import quotas have been removed on knitted shirts from China. The elimination of quotas and the reduction of tariffs under the WTO may result in increased imports of certain apparel products into North America. In May 2005, quotas on three categories of clothing imports, including knitted shirts, from China were re-imposed. These factors could make Alstyle's products less competitive against low cost imports from developing countries.

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***Environmental regulations may impact our future operating results.***

We are subject to extensive and changing federal, state and foreign laws and regulations establishing health and environmental quality standards, and may be subject to liability or penalties for violations of those standards. We are also subject to laws and regulations governing remediation of contamination at facilities currently or formerly owned or operated by us or to which we have sent hazardous substances or wastes for treatment, recycling or disposal. We may be subject to future liabilities or obligations as a result of new or more stringent interpretations of existing laws and regulations. In addition, we may have liabilities or obligations in the future if we discover any environmental contamination or liability at any of our facilities, or at facilities we may acquire.

***We depend upon the talents and contributions of a limited number of individuals, many of whom would be difficult to replace.***

The loss or interruption of the services of our Chief Executive Officer, Executive Vice President, Chief Financial Officer and Vice President Apparel Division, could have a material adverse effect on our business, financial condition and results of operations. Although we maintain employment agreements with these individuals, it cannot be assured that the services of such individuals will continue.

**Cautionary Statements**

Certain statements in this report, and in particular, statements found in Management's Discussion and Analysis of Financial Condition and Results of Operations, constitute forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. We believe these forward-looking statements are based upon reasonable assumptions within the bounds of our knowledge of Ennis. All such statements involve risks and uncertainties, and as a result, actual results could differ materially from those projected, anticipated or implied by these statements. Such forward-looking statements involve known and unknown risks, including but not limited to, general economic, business and labor conditions; the ability to implement our strategic initiatives; the ability to be profitable on a consistent basis; dependence on sales that are not subject to long-term contracts; dependence on suppliers; the ability to recover the rising cost of key raw materials in markets that are highly price competitive; the ability to meet customer demand for additional value-added products and services; the ability to timely or adequately respond to technological changes in the industry; the impact of the Internet and other electronic media on the demand for forms and printed materials; postage rates; the ability to manage operating expenses; the ability to manage financing costs and interest rate risk; a decline in business volume and profitability could result in an impairment of goodwill; the ability to retain key management personnel; the ability to identify, manage or integrate future acquisitions; the costs associated with and the outcome of outstanding and future litigation; and changes in government regulations.

In view of such uncertainties, investors should not place undue reliance on our forward-looking statements since such statements speak only as of the date when made. We undertake no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.

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Liquidity and Capital Resources

| <i>(Dollars in thousands)</i> | <b>May 31,<br/>2006</b> | <b>February<br/>28,<br/>2006</b> | <b>Change</b> |
|-------------------------------|-------------------------|----------------------------------|---------------|
| Working Capital               | \$93,115                | \$94,494                         | -1.5%         |
| Cash and cash equivalents     | \$ 9,322                | \$13,860                         | -32.7%        |

**Working Capital.** Our working capital decreased by approximately \$1.4 million, or 1.5% from \$94.5 million at February 28, 2006 to \$93.1 million at May 31, 2006. The decrease in our working capital during the period related primarily to our decision to pay-down our long-term debt by approximately \$7 million during the period and the acquisition of SPF for \$4.6 million in cash. As a result, our current ratio, calculated by dividing our current assets by our current liabilities decreased from 2.5-to-1.0 at February 28, 2006 to 2.4-to-1.0 at May 31, 2006.

**Cash and cash equivalents.** Cash and cash equivalents consists of highly liquid investments, such as time deposits held at major banks, commercial paper, United States government agency discounts notes, money market mutual funds and other money market securities with original maturities of 90 days or less.

| <i>(Dollars in thousands)</i>         | <b>Three months ended May 31,</b> |             |               |
|---------------------------------------|-----------------------------------|-------------|---------------|
|                                       | <b>2006</b>                       | <b>2005</b> | <b>Change</b> |
| Cash provided by operating activities | \$ 12,178                         | \$ 18,775   | -35.1%        |
| Cash used for investing activities    | \$ (5,260)                        | \$ (4,880)  | 7.8%          |
| Cash used for financing activities    | \$(11,405)                        | \$(17,674)  | -35.5%        |

**Cash flows from operating activities.** Cash flows from our operating activities decreased in the three months ending May 31, 2006 primarily as a result of our decision to bring in-house more customer receivables that were previously factored. This reduction was partially offset by an increase in our accrued liabilities.

**Cash flows from investing activities.** The changes in cash flows from investing activities primarily relates to our acquisition of Specialized Printed Forms for \$4.6 million on March 31, 2006 and in March 2005 we acquired ownership of certain assets of approximately \$3 million, which were held by Alstyle under operating lease.

**Cash flows from financing activities.** The changes in cash flows from financing activities primarily relate to payments under our debt obligations as well as payment of dividends.

**Credit Facility** On March 31, 2006, we entered into an amended and restated credit agreement with a group of lenders led by LaSalle Bank N.A. (the Facility). The Facility provides us access to \$150 million in revolving credit and matures on March 31, 2010. The facility bears interest at the London Interbank Offered Rate (LIBOR) plus a spread ranging from .50% to 1.50% (currently LIBOR + .75%), depending on our total funded debt to EBITDA ratio, as defined. The Facility is secured by substantially all of our personal and investment property. The Facility contains financial covenants, restrictions on capital expenditures, acquisitions, asset dispositions, and additional debt, as well as other customary covenants. As of May 31, 2006, we had \$95.5 million of borrowings under the revolver and \$13.2 million

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outstanding under letter of credit arrangements, leaving us availability of approximately \$41.3 million. The Facility was secured by substantially all of our personal and investment property and bore interest at a floating rate of LIBOR plus a spread dependent upon our total funded debt level to cash flows as defined. The rate in effect at May 31, 2006 was 5.8425%. The Original Facility contained financial covenants, restrictions on capital expenditures, acquisitions, asset dispositions, and additional debt, as well as other customary covenants.

During the three months ended in May 31, 2006, we repaid \$7,000,000 on the revolver and \$473,000 on other debt. It is anticipated that the available line of credit is sufficient to cover, should it be required, working capital requirements for the foreseeable future.

As previously reported, Alstyle continues to sell a substantial portion of its accounts receivable to factors based upon agreements with various financial institutions. We continue with plans to fund these receivables through the existing bank line or from working capital generated by Alstyle over the next twelve to fifteen months.

***Pension*** We are required to make contributions to our defined benefit pension plan. These contributions are required under the minimum funding requirements of the Employee Retirement Pension Plan Income Security Act (ERISA). We anticipate that we will contribute from \$2.0 million to \$3.0 million during our current fiscal year. We made contributions of \$2,000,000 to our pension plan during fiscal year 2006.

***Inventories*** We believe our current inventory levels are sufficient to satisfy our customer demands and we anticipate having adequate sources of raw materials to meet future business requirements. The previously reported long-term contracts (that govern prices, but do not require minimum volume) with paper and yarn suppliers continue to be in effect.

***Capital Expenditures*** We expect our capital requirements for the fiscal year to be in-line with our historical levels of between \$5.0 million and \$7.0 million and would expect to fund these expenditures through existing cash flows. We would expect to generate sufficient cash flows from our operating activities in order to cover our operating and other capital requirements for our foreseeable future.

***Contractual Obligations & Off-Balance Sheet Arrangements*** There have been no significant changes in our contractual obligations since February 28, 2006 that have, or are reasonably likely to have, a material impact on our results of operations or financial condition. We had no off-balance sheet arrangements in place as of May 31, 2006.

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**Results of Operations Consolidated**

*Net Sales.* Net sales for the three months ended May 31, 2006 were \$145.1 million compared to \$149.1 million for the three months ended May 31, 2005. This represented a decrease of 2.7% over the same quarter last year. The decrease in the quarter sales related primarily to the decrease in our Print Segment sales which decreased by approximately \$3.6 million. See Results of Operation Segments of this Report for further discussion.

*Gross profit.* Our gross profit for the three months ended May 31, 2006 was \$37.8 million, or 26.1% of sales, compared to \$37.5 million, or 25.1% of sales for the three months ended May 31, 2005. The increase in our gross margin during the period related primarily from the continued benefits associated with our cost reduction programs implemented last year in the Apparel Segment. See Results of Operations Segments of this Report for further discussion.

*Selling, general and administrative expenses.* For the three months ended May 31, 2006, our selling, general and administrative expenses were \$18.1 million, or 12.5% of sales, compared to \$17.8 million, or 12.0% of sales, for the three months ended May 31, 2005. The increase in our selling, general and administrative expenses during the period related primarily to an increase in our selling expenses, which were offset for the most part by decreases in our administrative expenses.

*Earnings from operations.* As a result of the above factors, our earnings from operations have increased from \$19.6 million, or 13.2% of sales for the three months ended May 31, 2005 to earnings of \$19.7 million, or 13.6% of sales for the comparable period this year.

*Other income and expense.* For the three months ended May 31, 2006, our other expense decreased by approximately \$.5 million from \$2.3 million for the three months ended May 31, 2005, to approximately \$1.8 million for the three months ended May 31, 2006. The decrease during the current period related primarily to our decreased interest expense which decreased from approximately \$2.2 million to approximately \$1.8 million for the three months ended May 31, 2005 and 2006, respectively.

*Provision for income taxes.* Our effective tax rates for the periods were 37.0% and 39.0% for the three months ended May 31, 2006 and 2005, respectively. The decrease in our effective tax rate during the current period over the comparable period last year related primarily to an increase in our foreign income tax credit and the American Jobs Creation Act credit.

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*Net earnings.* As a result of the above factors, our net earnings increased from earnings of approximately \$10.6 million, or 7.1% of sales for the three months ended May 31, 2005 to approximately \$11.3 million, or 7.8% of sales for the three months ended May 31, 2006. Basic earnings per share increased from earnings of \$.42 per share for the three months ended May 31, 2005, to \$.44 per share for the three months ended May 31, 2006. Diluted earnings per share increased from earnings of \$.41 per share for the three months ended May 31, 2005, to \$.44 per share for the three months ended May 31, 2006.

**Results of Operations Segments**

| <b>Revenue by Segment (in thousands)</b> | <b>May 31,</b> |             |
|--|----------------|-------------|
|  | <b>2006</b>    | <b>2005</b> |
| Print                                    | \$ 77,096      | \$ 80,724   |
| Apparel                                  | 68,017         | 68,389      |
| Total                                    | \$ 145,113     | \$ 149,113  |

*Print Segment.* Our net sales for our Print Segment, which represented 57% of our consolidated sales during the current period, were approximately \$77.1 million for the three months ended May 31, 2006 compared to approximately \$80.7 million for the three months ended May 31, 2005, or a decrease of \$3.6 million, or 4.5%. The decline in the Print Segment's revenues during the quarter is primarily due to the impact of lost revenues associated with a large promotional customer which we ceased doing business with during the fourth quarter of fiscal year 2006, approximately \$4.0 million, and the impact of the two print plants closings, which were in 2005, approximately \$2.0 million. Without these items, the Print segment's revenues for the quarter actually increased by approximately 3% over same quarter last year.

*Apparel Segment.* Our net sales for the Apparel Segment, which represented 47% of our consolidated sales for the current period, were approximately \$68.0 million for the three months ended May 31, 2006 compared to approximately \$68.4 million for the three months ended May 31, 2005. We believe the start of the summer retail season started out slow this year which impacted our first quarter sales. While our apparel sales during the quarter started off soft, we started to see the trend shift in April when our sales were up 6% over prior years' numbers. This trend continued into May where our apparel sales finished up 14% over the previous years' numbers.

| <b>Gross Profit by Segment (in thousands)</b> | <b>May 31,</b> |             |
|---|----------------|-------------|
|   | <b>2006</b>    | <b>2005</b> |
| Print   | \$ 19,366      | \$ 20,803   |
| Apparel                                       | 18,449         | 16,675      |
| Total   | \$ 37,815      | \$ 37,478   |

*Print Segment.* Our Print Segment's gross profit decreased approximately \$1.4 million, or 6.7% from \$20.8 million to \$19.4 million for the three months ended May 31, 2005 and 2006, respectively. As a percentage of sales, our gross profit was 25.1% and 25.8% for the three months ended May 31, 2006 and 2005, respectively. Our gross profit during the current quarter was impacted by the decrease in the earnings at our Adams McClure facility due to the decreased sales from a large promotional customer as

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previously discussed. Management is in the process of evaluating and implementing changes in both personnel and processes to bring costs in line with expected sales volume at this plant. Without the impact of our Adams McClure facility, our print margins would have been effectively the same for both periods, approximately 26.8%.

**Apparel Segment.** Our Apparel Segment's gross profit margin increased approximately \$1.7 million, from \$16.7 million for the three months ended May 31, 2005 to \$18.4 million for the three months ended May 31, 2006. As a percent of sales, this Segment's gross profit increased from 24.4% for the three months ended May 31, 2005 to 27.1% for the three months ended May 31, 2006. The Segment's performance, for the current quarter continues to be positively impacted by: 1) favorable product mix, and 2) improved manufacturing processes, which have resulted in manufacturing efficiencies, and reduced production costs.

| <b>Profit by Segment (in thousands)</b> | <b>May 31,</b>   |                  |
|---|------------------|------------------|
|   | <b>2006</b>      | <b>2005</b>      |
| Print                                   | \$ 11,271        | \$ 11,448        |
| Apparel                                 | 10,042           | 8,367            |
| Total                                   | 21,313           | 19,815           |
| Less corporate expenses                 | 3,330            | 2,507            |
| <b>Earnings before income taxes</b>     | <b>\$ 17,983</b> | <b>\$ 17,308</b> |

**Print Segment.** Our Print Segment's segment profit for the three months ended May 31, 2006 remained relatively stable at \$11.3 million for the three months ended May 31, 2006 compared to \$11.1 million for the three months ended May 31, 2005. As a percent of sales, our Print Segment's profits increased from 14.2% to 14.6% for the three months ended May 31, 2005 and 2006, respectively. The increase in the Print Segment's profit performance, as a percent of sales, during the current quarter related primarily to the positive impact associated with the closing of the Edison and Medfield plants.

**Apparel Segment.** Our Apparel Segment's profit increased approximately \$1.6 million, from \$8.4 million for the three months ended May 31, 2005 to \$10.0 million for the three months ended May 31, 2006. As a percent of sales, this Segment's profit increased from 12.2% for the three months ended May 31, 2005 to 14.8% for the three months ended May 31, 2006. The increase in this Segment's performance during the quarter is directly related to its improved margins (see discussion above - Gross Profit - Apparel Segment) as our operating expenses remained relatively stable during both periods.

**Critical Accounting Policies and Judgments**

In preparing our consolidated financial statements, we are required to make estimates and assumptions that affect the disclosures and reported amounts of assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. We evaluate our estimates and judgments on an ongoing basis, including those related to allowance for doubtful accounts, inventory valuations, property, plant and equipment, intangible assets, accrued liabilities and income taxes. We base our estimates and judgments on historical experience and on various other factors that we believe to be reasonable under the circumstances. Actual results may differ materially from these estimates under different assumptions or conditions. We believe the following accounting policies are the most critical due to their affect on our more significant estimates and judgments used in preparation of its consolidated financial statements.

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We maintain a defined-benefit pension plan for employees. Included in our financial results are pension costs that are measured using actuarial valuations. The actuarial assumptions used may differ from actual results.

Intangibles generated through acquisitions are based upon independent appraisals of their values and are either amortized over their useful life, or evaluated periodically (at least once a year) to determine whether the value has been impaired by events occurring during the fiscal year.

We exercise judgment in evaluating our long-lived assets for impairment. We assess the impairment of long-lived assets that include other intangible assets, goodwill, and property, plant and equipment annually or whenever events or changes in circumstances indicate that the carrying value may not be recoverable. In performing tests of impairment, we must make assumptions regarding the estimated future cash flows and other factors to determine the fair value of the respective assets in assessing the recoverability of its goodwill and other intangibles. If these estimates or the related assumptions change, we may be required to record impairment charges for these assets in the future. Actual results could differ from assumptions made by management. We believe our businesses will generate sufficient undiscounted cash flow to more than recover the investments we have made in property, plant and equipment, as well as the goodwill and other intangibles recorded as a result of our acquisitions. We cannot predict the occurrence of future impairment triggering events nor the impact such events might have on its reported asset values.

Revenue is generally recognized upon shipment of products. Net sales consist of gross sales invoiced to customers, less certain related charges, including discounts, returns and other allowances. Returns, discounts and other allowances have historically been insignificant. In some cases and upon customer request, Ennis prints and stores custom print product for customer specified future delivery, generally within six months. In this case, risk of loss from obsolescence passes to the customer, the customer is invoiced under normal credit terms and revenue is recognized when manufacturing is complete. Approximately \$5.6 million and \$3.3 million of revenue was recognized under these agreements during the quarter ended May 31, 2006 and May 31, 2005 respectively. Sales in foreign countries were not significant for the three months ended May 31, 2006 or May 31, 2005.

We maintain an allowance for doubtful accounts to reflect estimated losses resulting from the inability of customers to make required payments. On an on-going basis, we evaluate the collectability of accounts receivable based upon historical collection trends, current economic factors, and the assessment of the collectability of specific accounts. We evaluate the collectability of specific accounts using a combination of factors, including the age of the outstanding balances, evaluation of customers' current and past financial condition and credit scores, recent payment history, current economic environment, discussions with our project managers, and discussions with the customers directly.

Our inventories are valued at the lower of cost or market. We regularly review inventory values on hand, using specific aging categories, and write down inventory deemed obsolete and/or slow-moving based on historical usage and estimated future usage to its estimated market value. As actual future demand or market conditions may vary from those projected by management, adjustments to inventory valuations may be required.

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As part of the process of preparing our consolidated financial statements, we are required to estimate our income taxes in each jurisdiction in which we operate. This process involves estimating our actual current tax exposure together with assessing temporary differences resulting from different treatment of items for tax and accounting purposes. These differences result in deferred tax assets and liabilities, which are included in our consolidated balance sheet. We must then assess the likelihood that our deferred tax assets will be recovered from future taxable income or through our ability to carry this deferred tax asset back. To the extent we believe that recovery is not likely, we must establish a valuation allowance. To the extent we establish a valuation allowance, we must include an expense within the tax provision in the consolidated statements of income. In the event that actual results differ from these estimates, our provision for income taxes could be materially impacted.

In addition to the above, we also have to make assessments as to the adequacy of our accrued liabilities, more specifically our liabilities recorded in connection with our workers compensation and health insurance, as these plans are self funded. To help us in this evaluation process we routinely get outside third party appraisals of our potential liabilities under each plan.

In view of such uncertainties, investors should not place undue reliance on our forward-looking statements since such statements speak only as of the date when made. We undertake no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.

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

**Market Risk**

We are exposed to market risk from changes in interest rates on debt. A discussion of our accounting policies for derivative instruments is included in the Summary of Significant Accounting Policies in the Notes to the Consolidated Financial Statements.

We may from time to time utilize interest rate swaps to manage overall borrowing costs and reduce exposure to adverse fluctuations in interest rates. We do not use derivative instruments for trading purposes. We are exposed to interest rate risk on short-term and long-term financial instruments carrying variable interest rates. Our variable rate financial instruments, including the outstanding credit facilities, totaled \$95.5 million at May 31, 2006. The impact on our results of operations of a one-point interest rate change on the outstanding balance of the variable rate financial instruments as of May 31, 2006 would be approximately \$1,000,000.

This market risk discussion contains forward-looking statements. Actual results may differ materially from this discussion based upon general market conditions and changes in domestic and global financial markets.

**Item 4. CONTROLS AND PROCEDURES**

**Evaluation of Disclosure Controls and Procedures.** An evaluation was carried out under the supervision and with the participation of our management, including our Chief Executive Officer and our Chief Financial Officer, of the effectiveness of the design of our disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act) as of the end of the period covered by this quarterly report, pursuant to Exchange Act Rule 13a-15. Based upon that evaluation, the Chief Executive Officer and the Chief Financial Officer have concluded that our disclosure controls and procedures as of May 31, 2006 are effective to ensure that information required to be disclosed by us in the reports filed or submitted by us under the Exchange Act is recorded, processed, summarized, and reported within the time periods specified in the SEC's rules and forms and include controls and procedures designed to ensure that information required to be disclosed by us in such reports is accumulated and communicated to our management, including our principal executive and financial officers as appropriate to allow timely decisions regarding required disclosure. Due to the inherent limitations of control systems, not all misstatements may be detected. Those inherent limitations include the realities that judgments in decision-making can be faulty and that breakdowns can occur because of simple errors or mistakes. Additionally, controls could be circumvented by the individual acts of some persons or by collusion of two or more people. Our controls and procedures can only provide reasonable, not absolute, assurance that the above objectives have been met.

There were no changes in our internal control over financial reporting identified in connection with the evaluation required by paragraph (d) of Exchange Act Rules 13a-15 or 15d-15 that occurred during our last fiscal quarter that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

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PART II. OTHER INFORMATION**

**Item 1. Legal Proceedings**

From time to time we are involved in various litigation matters arising in the ordinary course of our business. We do not believe the disposition of any current matter will have a material adverse effect on our consolidated financial position or our results of operations.

**Item 1A. Risk Factors**

Reference is made to page 24 of this Report on Form 10-Q. There have been no material changes in our Risk Factors as previously discussed in our Annual Report on Form 10-K for the year ended February 28, 2006.

**Items 2, 3 and 5 are not applicable and have been omitted**

**Item 4. Submission of Matters to a Vote of Security Holders**

There were no matters submitted to security holders for a vote during the quarter.

**Item 6. Exhibits**

The following exhibits are filed as part of this report.

- Exhibit 3.1 Restated Articles of Incorporation as amended through June 23, 1983 with attached amendments dated June 20, 1985, July 31, 1985 and June 16, 1988 incorporated herein by reference to Exhibit 5 to the Registrant's Form 10-K Annual Report for the fiscal year ended February 28, 1993.
- Exhibit 3.2 Bylaws of the Registrant as amended through October 15, 1997 incorporated herein by reference to Exhibit 3(ii) to the registrant's Form 10-Q Quarterly Report for the quarter ended November 30, 1997.
- Exhibit 3.3 Articles of Amendment to the Articles of Incorporation of Ennis Business Forms, Inc. filed on June 17, 2004 incorporated herein by reference to Exhibit 3.3 to the registrant's Form 10-Q Quarterly Report for the quarter ended November 30, 2004.
- Exhibit 31.1 Certification Pursuant to Rule 13a-14(a)/15d-14(a) of Chief Executive Officer.\*
- Exhibit 31.2 Certification Pursuant to Rule 13a-14(a)/15d-14(a) of Chief Financial Officer.\*
- Exhibit 32.1 Section 1350 Certification of Chief Executive Officer.\*\*
- Exhibit 32.2 Section 1350 Certification of Chief Financial Officer.\*\*

\* Filed herewith

\*\* Furnished  
herewith

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**ENNIS, INC. AND SUBSIDIARIES  
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**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.

ENNIS, INC.

Date: July 10, 2006

/s/ Keith S. Walters  
Keith S. Walters  
Chairman, Chief Executive Officer and  
President

Date: July 10, 2006

/s/ Richard L. Travis, Jr.  
Richard L. Travis, Jr.  
V.P. Finance and CFO, Secretary and  
Principal Financial and Accounting Officer  
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INDEX TO EXHIBITS**

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herewith