

FRED'S INC
Form 10-Q
September 08, 2011

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

FORM 10-Q

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

For the quarterly period ended July 30, 2011.
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 001-14565

FRED'S, INC.
(Exact name of registrant as specified in its charter)

TENNESSEE
(State or Other Jurisdiction of
Incorporation or Organization)

62-0634010
(I.R.S. Employer
Identification Number)

4300 New Getwell Road
Memphis, Tennessee 38118
(Address of Principal Executive Offices)

(901) 365-8880
(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 has submitted electronically and posted on its corporate web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or such shorter period that the registrant was required to submit and post such files). Yes ☒ No ☐.

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

Large accelerated filer ☐

Accelerated filer ☒

Non-accelerated filer ☐

Smaller reporting company ☐

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

The registrant had 38,543,422 shares of Class A voting, no par value common stock outstanding as of September 1, 2011.

FRED'S, INC.

INDEX

Page No.

Part I - Financial Information	
Item 1 - Financial Statements:	
Condensed Consolidated Balance Sheets as of July 30, 2011 (unaudited) and January 29, 2011	3
Condensed Consolidated Statements of Income for the Thirteen Weeks and Twenty-Six Weeks Ended July 30, 2011 (unaudited) and July 31, 2010 (unaudited)	4
Condensed Consolidated Statements of Cash Flows for the Twenty-Six Weeks Ended July 30, 2011 (unaudited) and July 31, 2010 (unaudited)	5
Notes to Condensed Consolidated Financial Statements (unaudited)	6-11
Item 2 - Management's Discussion and Analysis of Financial Condition and Results of Operations	12-17
Item 3 – Quantitative and Qualitative Disclosure about Market Risk	18
Item 4 – Controls and Procedures	18
Part II - Other Information	18-19
Item 1. Legal Proceedings	
Item 1A. Risk Factors	
Item 2. Unregistered Sales of Equity Securities and Use of Proceeds	
Item 6. Exhibits	
Signatures	19
Ex-31.1 Section 302 Certification of the CEO	
Ex-31.2 Section 302 Certification of the CFO	
Ex-32. Section 906 Certification of the CEO and CFO	

Part I – FINANCIAL INFORMATION

Item 1. Financial Statements

FRED'S, INC.
 CONDENSED CONSOLIDATED BALANCE SHEETS
 (in thousands, except for number of shares)

	July 30, 2011 (unaudited)	January 29, 2011
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 46,799	\$49,182
Receivables, less allowance for doubtful accounts of \$1,253 and \$1,218, respectively	28,727	28,146
Inventories	325,438	313,384
Other non-trade receivables	25,457	26,378
Prepaid expenses and other current assets	10,595	12,723
Total current assets	437,016	429,813
Property and equipment, at depreciated cost	157,657	139,931
Equipment under capital leases, less accumulated amortization of \$5,025 and \$4,967, respectively	117	-
Intangibles	21,716	22,193
Other noncurrent assets, net	3,221	3,591
Total assets	\$ 619,727	\$595,528
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	\$ 97,512	\$81,002
Current portion of indebtedness	360	201
Accrued expenses and other	43,728	45,371
Capital lease obligation	131	-
Deferred income taxes	22,245	21,142
Total current liabilities	163,976	147,716
Long-term portion of indebtedness	7,107	3,969
Deferred income taxes	1,702	2,069
Other noncurrent liabilities	17,149	17,886
Total liabilities	189,934	171,640
Commitments and Contingencies		
Shareholders' equity:		
Preferred stock, nonvoting, no par value, 10,000,000 shares authorized, none outstanding	-	-
Preferred stock, Series A junior participating nonvoting, no par value, 224,594 shares authorized, none outstanding	-	-
Common stock, Class A voting, no par value, 60,000,000 shares authorized, 39,309,107 and 39,363,462 shares issued and outstanding, respectively	126,608	131,367
Common stock, Class B nonvoting, no par value, 11,500,000 shares authorized, none outstanding	-	-
Retained earnings	302,313	291,649

Accumulated other comprehensive income	872	872
Total shareholders' equity	429,793	423,888
Total liabilities and shareholders' equity	\$ 619,727	\$595,528

See accompanying notes to condensed consolidated financial statements.

FRED'S, INC.
CONDENSED CONSOLIDATED STATEMENTS OF INCOME
(unaudited)
(in thousands, except per share amounts)

	Thirteen Weeks Ended		Twenty-Six Weeks Ended	
	July 30, 2011	July 31, 2010	July 30, 2011	July 31, 2010
Net sales	\$452,690	\$449,467	\$937,089	\$921,114
Cost of goods sold	325,759	323,531	672,216	658,229
Gross profit	126,931	125,936	264,873	262,885
Depreciation and amortization	8,076	7,227	15,849	14,190
Selling, general and administrative expenses	110,587	110,473	225,633	227,277
Operating income	8,268	8,236	23,391	21,418
Interest income	(58)	(60)	(115)	(120)
Interest expense	151	117	278	227
Income before income taxes	8,175	8,179	23,228	21,311
Provision for income taxes	3,089	3,221	8,628	8,162
Net income	\$5,086	\$4,958	\$14,600	\$13,149
Net income per share				
Basic	\$0.13	\$0.13	\$0.37	\$0.34
Diluted	\$0.13	\$0.13	\$0.37	\$0.34
Weighted average shares outstanding				
Basic	39,134	39,179	39,118	39,164
Effect of dilutive stock options	113	61	104	53
Diluted	39,247	39,240	39,222	39,217
Dividends per common share	\$0.05	\$0.04	\$0.10	\$0.08
Comprehensive income:				
Net income	\$5,086	\$4,958	\$14,600	\$13,149
Other comprehensive income (expense), net of tax postretirement plan adjustment	-	-	-	-
Comprehensive income	\$5,086	\$4,958	\$14,600	\$13,149

See accompanying notes to condensed consolidated financial statements.

FRED'S, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(in thousands)

	Twenty-Six Weeks Ended	
	July 30, 2011	July 31, 2010
Cash flows from operating activities:		
Net income	\$ 14,600	\$ 13,149
Adjustments to reconcile net income to net cash flows from operating activities:		
Depreciation and amortization	15,903	14,190
Net loss on asset disposition	253	258
Provision for store closures and asset impairment	185	-
Stock-based compensation	897	896
Provision for uncollectible receivables	35	212
LIFO reserve increase	1,092	944
Deferred income tax expense (benefit)	627	(833)
Income tax benefit upon exercise of stock options	15	6
(Increase) decrease in operating assets:		
Trade and non-trade receivables	(266)	(3,913)
Insurance receivables	26	13
Inventories	(13,331)	(21,722)
Other assets	2,388	545
Increase (decrease) in operating liabilities:		
Accounts payable and accrued expenses	15,011	6,833
Income taxes payable	708	5,507
Other noncurrent liabilities	(806)	(13)
Net cash provided by operating activities	37,337	16,072
Cash flows from investing activities:		
Capital expenditures	(27,372)	(13,245)
Proceeds from asset dispositions	17	140
Insurance recoveries for replacement assets	-	47
Asset acquisition, net (primarily intangibles)	(2,559)	(4,405)
Net cash used in investing activities	(29,914)	(17,463)
Cash flows from financing activities:		
Payments of indebtedness and capital lease obligations	(213)	(609)
Excess tax charges from stock-based compensation	(15)	(6)
Proceeds from exercise of stock options and employee stock purchase plan	211	257
Repurchase of shares	(5,852)	(2,977)
Cash dividends paid	(3,936)	(3,144)
Net cash used in financing activities	(9,805)	(6,479)
Increase in cash and cash equivalents	(2,382)	(7,870)
Cash and cash equivalents:		
Beginning of year	49,181	54,742
End of year	\$ 46,799	\$ 46,872
Supplemental disclosures of cash flow information:		

Edgar Filing: FREDs INC - Form 10-Q

Interest paid	\$163	\$ 57
Income taxes paid	\$7,210	\$ 2,419
Non-cash investing and financial activities:		
Assets acquired through term loan	\$3,497	\$ -
Assets acquired through capital lease	\$135	\$ -

See accompanying notes to consolidated financial statements.

FRED'S, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(unaudited)

NOTE 1: BASIS OF PRESENTATION

Fred's, Inc. and subsidiaries ("We", "Our", "Us" or "Company") operates, as of July 30, 2011, 674 discount general merchandise stores, including 22 franchised Fred's stores, in 15 states in the southeastern United States. 310 of the stores have full service pharmacies.

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles ("GAAP") for interim financial information and are presented in accordance with the requirements of Form 10-Q and therefore do not include all information and notes necessary for a fair presentation of financial position, results of operations and cash flows in conformity with GAAP. The statements reflect all adjustments (consisting of only normal recurring accruals) which are, in the opinion of management, necessary for a fair presentation of financial position in conformity with GAAP. The statements should be read in conjunction with the Notes to the Consolidated Financial Statements for the fiscal year ended January 29, 2011 incorporated into Our Annual Report on Form 10-K.

The results of operations for the thirteen week and twenty-six week periods ended July 30, 2011 are not necessarily indicative of the results to be expected for the full fiscal year.

NOTE 2: INVENTORIES

Merchandise inventories are valued at the lower of cost or market using the retail first-in, first-out (FIFO) method for goods in our stores and the cost first-in, first-out (FIFO) method for goods in our distribution centers. The retail inventory method is a reverse mark-up, averaging method which has been widely used in the retail industry for many years. This method calculates a cost-to-retail ratio that is applied to the retail value of inventory to determine the cost value of inventory and the resulting cost of goods sold and gross margin. The assumption that the retail inventory method provides for valuation at lower of cost or market and the inherent uncertainties therein are discussed in the following paragraphs. In order to assure valuation at the lower of cost or market, the retail value of our inventory is adjusted on a consistent basis to reflect current market conditions. These adjustments include increases to the retail value of inventory for initial markups to set the selling price of goods or additional markups to adjust pricing for inflation and decreases to the retail value of inventory for markdowns associated with promotional, seasonal or other declines in the market value. Because these adjustments are made on a consistent basis and are based on current prevailing market conditions, they approximate the carrying value of the inventory at net realizable value (market value). Therefore, after applying the cost to retail ratio, the cost value of our inventory is stated at the lower of cost or market as is prescribed by U.S. GAAP.

Because the approximation of net realizable value (market value) under the retail inventory method is based on estimates such as markups, markdowns and inventory losses (shrink), there exists an inherent uncertainty in the final determination of inventory cost and gross margin. In order to mitigate that uncertainty, the Company has a formal review by product class which considers such variables as current market trends, seasonality, weather patterns and age of merchandise to ensure that markdowns are taken currently, or a markdown reserve is established to cover future anticipated markdowns. This review also considers current pricing trends and inflation to ensure that markups are taken if necessary. The estimation of inventory losses (shrink) is a significant element in approximating the carrying value of inventory at net realizable value, and as such the following paragraph describes our estimation method as well as the steps we take to mitigate the risk of this estimate in the determination of the cost value of inventory.

The Company calculates inventory losses (shrink) based on actual inventory losses occurring as a result of physical inventory counts during each fiscal period and estimated inventory losses occurring between yearly physical inventory counts. The estimate for shrink occurring in the interim period between physical counts is calculated on a store-specific basis and is based on history, as well as performance on the most recent physical count. It is calculated by multiplying each store's shrink rate, which is based on the previously mentioned factors, by the interim period's sales for each store. Additionally, the overall estimate for shrink is adjusted at the corporate level to a three-year historical average to ensure that the overall shrink estimate is the most accurate approximation of shrink based on the Company's overall history of shrink. The three-year historical estimate is calculated by dividing the "book to physical" inventory adjustments for the trailing 36 months by the related sales for the same period. In order to reduce the uncertainty inherent in the shrink calculation, the Company first performs the calculation at the lowest practical level (by store) using the most current performance indicators. This ensures a more reliable number, as opposed to using a higher level aggregation or percentage method. The second portion of the calculation ensures that the extreme negative or positive performance of any particular store or group of stores does not skew the overall estimation of shrink. This portion of the calculation removes additional uncertainty by eliminating short-term peaks and valleys that could otherwise cause the underlying carrying cost of inventory to fluctuate unnecessarily. Management believes that the Company's retail inventory method provides an inventory valuation which reasonably approximates cost and results in carrying inventory at the lower of cost or market.

For pharmacy inventories, which were approximately \$34.2 million and \$32.5 million at July 30, 2011 and January 29, 2011, respectively, cost was determined using the retail LIFO (last-in, first-out) method in which inventory cost is maintained using the retail inventory method, then adjusted by application of the Producer Price Index published by the U.S. Department of Labor for the cumulative annual periods. The current cost of inventories exceeded the LIFO cost by approximately \$25.1 million at July 30, 2011 and \$24.0 million at January 29, 2011.

The Company has historically included an estimate of inbound freight and certain general and administrative costs in merchandise inventory as prescribed by GAAP. These costs include activities surrounding the procurement and storage of merchandise inventory such as merchandise planning and buying, warehousing, accounting, information technology and human resources, as well as inbound freight. The total amount of procurement and storage costs and inbound freight included in merchandise inventory at July 30, 2011 is \$20.8 million, with the corresponding amount of \$19.5 million at January 29, 2011.

NOTE 3: STOCK-BASED COMPENSATION

The Company accounts for its stock-based compensation plans in accordance with FASB ASC 718 “Compensation – Stock Compensation”. Under FASB ASC 718, stock-based compensation expense is based on awards ultimately expected to vest, and therefore has been reduced for estimated forfeitures. Forfeitures are estimated at the time of grant based on the Company’s historical forfeiture experience and will be revised in subsequent periods if actual forfeitures differ from those estimates.

FASB ASC 718 also requires the benefits of income tax deductions in excess of recognized compensation cost to be reported as a financing cash flow, rather than as an operating cash flow as required prior to FASB ASC 718. A summary of the Company’s stock-based compensation (a component of selling and general and administrative expenses) and related income tax benefit is as follows (in thousands):

	Thirteen Weeks Ended		Twenty-Six Weeks Ended	
	July 30, 2011	July 31, 2010	July 30, 2011	July 31, 2010
Stock option expense	\$ 82	\$ 152	\$ 251	\$ 323
Restricted stock expense	330	333	559	503
ESPP expense	43	35	87	70
Total stock-based compensation	\$ 455	\$ 520	\$ 897	\$ 896
Income tax benefit on stock-based compensation	\$ 134	\$ 139	\$ 231	\$ 235

The fair value of each option granted during the thirteen and twenty-six week periods ended July 30, 2011 and July 31, 2010, respectively, are estimated on the date of grant using the Black-Scholes option-pricing model with the following weighted average assumptions:

	Thirteen Weeks Ended				Twenty-Six Weeks Ended			
	July 30, 2011		July 31, 2010		July 30, 2011		July 31, 2010	
Stock Options								
Expected volatility	40.5	%	41.7	%	41.7	%	42.0	%
Risk-free interest rate	2.5	%	3.1	%	2.1	%	3.1	%
Expected option life (in years)	5.84		5.84		4.67		5.84	
Expected dividend yield	0.86	%	0.61	%	0.93	%	0.63	%
Weighted average fair value at grant date	\$	5.29	\$	4.84	\$	4.60	\$	4.86
Employee Stock Purchase Plan								
Expected volatility	21.8	%	31.5	%	21.5	%	31.9	%
Risk-free interest rate	0.3	%	0.6	%	0.3	%	0.6	%
Expected option life (in years)	0.50		0.50		0.38		0.38	
Expected dividend yield	0.68	%	0.46	%	0.51	%	0.35	%
Weighted average fair value at grant date	\$	2.94	\$	2.43	\$	2.81	\$	2.31

The following is a summary of the methodology applied to develop each assumption:

Expected Volatility - This is a measure of the amount by which a price has fluctuated or is expected to fluctuate. The Company uses actual historical changes in the market value of our stock to calculate expected price volatility because management believes that this is the best indicator of future volatility. The Company calculates weekly market value changes from the date of grant over a past period representative of the expected life of the options to determine volatility. An increase in the expected volatility will increase compensation expense.

Risk-free Interest Rate - This is the yield of a U.S. Treasury zero-coupon bond issue effective at the grant date with a remaining term equal to the expected life of the option. An increase in the risk-free interest rate will increase compensation expense.

Expected Lives - This is the period of time over which the options granted are expected to remain outstanding and is based on historical experience. Options granted have a maximum term of seven and one-half years. An increase in the expected life will increase compensation expense.

Dividend Yield - This is based on the historical yield for a period equivalent to the expected life of the option. An increase in the dividend yield will decrease compensation expense.

Forfeiture Rate - This is the estimated percentage of options granted that are expected to be forfeited or cancelled before becoming fully vested. This estimate is based on historical experience. An increase in the forfeiture rate will decrease compensation expense.

Employee Stock Purchase Plan

The 2004 Employee Stock Purchase Plan (the "2004 Plan"), which was approved by Fred's stockholders, permits eligible employees to purchase shares of our common stock through payroll deductions at the lower of 85% of the fair market value of the stock at the time of grant or 85% of the fair market value at the time of exercise. There were 24,026 shares issued during the twenty-six weeks ended July 30, 2011. There are 1,410,928 shares approved to be issued under the 2004 Plan and as of July 30, 2011, there were 1,002,807 shares available.

Stock Options

The following table summarizes stock option activity during the twenty-six weeks ended July 30, 2011:

	Options	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life (Years)	Aggregate Intrinsic Value (Thousands)
Outstanding at January 29, 2011	918,462	\$ 12.15	3.2	\$ 1,524
Granted	58,817	\$ 13.21		
Forfeited / Cancelled	(61,983)	\$ 14.34		
Exercised	(10,217)	\$ 10.33		
Outstanding at July 30, 2011	905,079	\$ 12.08	2.9	\$ 1,463
Exercisable at July 30, 2011	597,905	\$ 12.51	2.1	\$ 780

The aggregate intrinsic value in the table above represents the total pre-tax intrinsic value (the difference between Fred's closing stock price on the last trading day of the period ended July 30, 2011 and the exercise price of the option multiplied by the number of in-the-money options) that would have been received by the option holders had all option holders exercised their options on that date. As of July 30, 2011, total unrecognized stock-based compensation expense net of estimated forfeitures related to non-vested stock options was approximately \$543.4 thousand, which is expected to be recognized over a weighted average period of approximately 3.05 years. The total fair value of options vested during the twenty-six weeks ended July 30, 2011 was \$373.1 thousand.

Restricted Stock

The following table summarizes restricted stock activity during the twenty-six weeks ended July 30, 2011:

	Number of Shares	Weighted Average Grant Date Fair Value
Non-vested Restricted Stock at January 29, 2011	472,927	\$ 12.55
Granted	155,676	\$ 13.69
Forfeited / Cancelled	(44,782)	\$ 12.99
Vested	(40,051)	\$ 14.16
Non-vested Restricted Stock at July 30, 2011	543,770	\$ 12.72

The aggregate pre-tax intrinsic value of restricted stock outstanding as of July 30, 2011 is \$7.3 million with a weighted average remaining contractual life of 4.3 years. The unrecognized compensation expense net of estimated forfeitures, related to the outstanding stock is approximately \$3.94 million, which is expected to be recognized over a weighted average period of approximately 7.0 years. The total fair value of restricted stock awards that vested during the twenty-six weeks ended July 30, 2011 was \$575.4 thousand.

NOTE 4: PROPERTY AND EQUIPMENT

Property and Equipment are carried at cost. Depreciation is recorded using the straight-line method over the estimated useful lives of the assets. Improvements to leased premises are amortized using the straight-line method over the shorter of the initial term of the lease or the useful life of the improvement. Leasehold improvements added late in the lease term are amortized over the shorter of the remaining term of the lease (including the upcoming renewal option, if the renewal is reasonably assured) or the useful life of the improvement. Assets under capital leases are amortized in accordance with the Company's normal depreciation policy for owned assets or over the lease term (regardless of renewal options), if shorter, and the charge to earnings is included in depreciation expense in the consolidated financial statements. Gains or losses on the sale of assets are recorded as a component of operating income.

The following illustrates the breakdown of the major categories within Property and Equipment (in thousands):

	July 30, 2011	January 29, 2011
Property and equipment, at cost:		
Buildings and building improvements	\$ 110,616	\$ 96,923
Leasehold improvements	66,302	62,504
Automobiles and vehicles	5,312	5,198
Airplane	4,697	4,697
Furniture, fixtures and equipment	241,551	234,710
	428,478	404,032
Less: Accumulated depreciation and amortization	(279,429)	(271,129)
	149,049	132,903
Construction in progress	751	198
Land	7,857	6,830
Total Property and equipment, at depreciated cost	\$ 157,657	\$ 139,931

NOTE 5: EXIT AND DISPOSAL ACTIVITIES

Lease Termination

A lease obligation still exists for some store closures that occurred in 2008. We record the estimated future liability associated with the rental obligation on the cease use date (when the stores were closed). The lease obligations are established at the cease use date for the present value of any remaining operating lease obligations, net of estimated sublease income, and at the communication date for severance and other exit costs, as prescribed by FASB ASC 420, "Exit or Disposal Cost Obligations". Key assumptions in calculating the liability include the timeframe expected to terminate lease agreements, estimates related to the sublease potential of closed locations, and estimates of other related exit costs. If actual timing and potential termination costs or realization of sublease income differ from our estimates, the resulting liabilities could vary from recorded amounts. These liabilities are reviewed periodically and adjusted when necessary.

During the first half of fiscal 2011, we utilized \$0.3 million of the remaining lease liability for 2008 store closures, leaving \$0.4 million in the reserve at July 30, 2011.

The following table illustrates the exit and disposal activity related to the store closures discussed in the previous paragraph (in millions):

	Balance at January 29, 2011	Additions	Utilization	Ending Balance July 30, 2011
Lease contract termination liability	\$ 0.7	\$ -	\$ 0.3	\$ 0.4

NOTE 6: ACCUMULATED OTHER COMPREHENSIVE INCOME

Comprehensive income consists of two components, net income and other comprehensive income (loss). Other comprehensive income (loss) refers to gains and losses that under GAAP are recorded as an element of shareholders' equity but are excluded from net income. The Company's accumulated other comprehensive income includes the unrecognized prior service costs, transition obligations and actuarial gains/losses associated with our postretirement benefit plan.

The following table illustrates the activity in accumulated other comprehensive income:

(in thousands)	Twenty-Six Weeks Ended		Year Ended
	July 30, 2011	July 31, 2010	January 29, 2011
Accumulated other comprehensive income	\$ 872	\$ 904	\$ 872
Amortization of postretirement benefit	-	-	-
Ending balance	\$ 872	\$ 904	\$ 872

NOTE 7: RELATED PARTY TRANSACTIONS

Atlantic Retail Investors, LLC, which is partially owned by Michael J. Hayes, a director of the Company, owned the land and buildings occupied by twelve Fred's stores, until March 2011 when, as described below, a portion of these properties were purchased by the Company. The terms and conditions regarding the leases on these locations were consistent in all material respects with other stores leases of the Company with unrelated landlords.

In February 2011, Atlantic Retail Investors, LLC, purchased the land and building occupied by one of Fred's stores, bringing the total related party leases to thirteen. The store was purchased by Atlantic Retail Investors, LLC, from an independent landlord/developer. On March 30, 2011, Fred's purchased ten of the thirteen properties leased from Atlantic Retail Investors, LLC, one of which has an additional parcel that is leased to an unrelated party, for \$7.5 million in cash and assumed mortgage debt of \$3.5 million. The Board of Directors approved these transactions based on an evaluation by an independent real estate broker, who concluded that all were acquired at comparable, and favorable, purchase prices to market value and were financially beneficial to Fred's as the depreciation expense for the newly acquired assets will be less than the future value of the lease payments that would have been due.

In May 2011, Atlantic Retail Investors, LLC, purchased land and buildings occupied by four Fred's stores, bringing the number of locations leased from Atlantic Retail Investors, LLC to seven. These stores were purchased by Atlantic Retail Investors, LLC, from a lender who had foreclosed on the independent landlord/developer. The terms and conditions regarding the leases on these locations are consistent in all material respects with the Company's other store leases.

In June 2011, Fred's purchased four of the seven leased properties from Atlantic Retail Investors, LLC together with an additional parcel at an existing owned location, for a total consideration of \$2.4 million in cash. No mortgage debt was assumed in this transaction. The Board of Directors approved these transactions based on the financial terms that were more favorable to market value and financially beneficial to Fred's as a result of the depreciation expense on the newly acquired assets being less than the future value of lease payments that would have been due.

As of July 30, 2011, Fred's is leasing three properties from Atlantic Retail Investors, LLC. The total rental payments related to related party leases were \$276.3 thousand and \$639.7 thousand for the twenty-six weeks ended July 30, 2011 and July 31, 2010, respectively.

Item 2:

Management's Discussion and Analysis of Financial
Condition and Results of Operations

GENERAL

Executive Overview

During the second quarter of 2011, we continued the implementation of our key initiatives to differentiate our stores from other small-box discount retailers. The Core 5 Program is our long-term strategy designed to highlight key categories within our stores that differentiate us from our competition. The Core 5 categories - Home, Celebration, Pet, Pharmacy and Paper and Chemical – are strong trip driving departments in which FRED'S has a clear and marketable advantage versus small box competitors. Additionally, these categories have high household penetration and resonate with customers across multiple demographics. This initiative is also intended to shift our product mix toward the more discretionary, higher margin categories and away from the lower margin consumable categories, thus driving higher margin and leading to increased operating profit.

The implementation of the Core 5 Program requires a moderate refresh of the store to address space allocation, product placement and adjacencies and signage in the Core 5 categories. The implementation is also accompanied by an extensive direct mail marketing campaign timed to coincide with the refresh of the store and then continuing for six months thereafter. During the second quarter of 2011, we implemented the Core 5 Program in 68 remodeled and upgraded stores, bringing the total completed stores to 332 during 2010 and 2011 to date. We plan to implement the program in approximately 200 stores during fiscal 2011, bringing the total number of stores during the two year period to over 400 stores.

As mentioned, our Pharmacy department is one of our Core 5 categories and is a key differentiating factor from other small-box discount retailers. As such, we have accelerated our growth strategy in this area and are aggressively pursuing opportunities to acquire independent pharmacies within our targeted markets. Our emphasis will continue to be on acquiring prescription files, but cold starts will be employed where it makes sense to do so. During the second quarter, we opened one new pharmacy location in our chain. During the first half of 2011, we opened four pharmacy express locations and one new pharmacy and closed eight pharmacy locations.

Another key focus in the second quarter of 2011 has been improvement of our store in-stock position. Recognizing in-stock position as one of the fundamental drivers of our business, we have dedicated significant resources to improving the tools we use to monitor and measure in-stock position in our stores. As an extension of this initiative, we have made significant improvements to our freight flow processes to ensure that product is in the store and available for our customers. Improvement in store in-stock position will continue to be a key initiative in FY 2011, and additional enhancements that are currently in development, both in terms of freight flow processes and in-stock measurement, will be deployed later in the year.

Our Own Brand initiative continues to be a key strategy for the Company in terms of building customer loyalty and increasing gross margin. As of July 30, 2011, we exceeded an Own Brand penetration rate of 18.4% of consumable product sales, and expect that number will continue to grow throughout the year as new Own Brand products are introduced. Our commitment to quality in our Own Brand products is resonating with our customers and they continue to make the switch to our "Fred's Brand". We are continuing to add new products to our Own Brand line on an ongoing basis, with new items in food and health and beauty aids introduced in the second quarter of 2011.

While our private label, or FRED'S Brand products, continues to be a focus in 2011, we also carry several national brands in our stores, such as Coke, Purina, Energizer, Prestone, and Sunbeam. Our customers identify with these

national brands, which provide them with a more complete shopping trip. Throughout the year, we will be evaluating additional name brands that are the most popular with our customers and will be adding those that complement our current product mix.

Gross margin improvement continues to be a key focus of the Company, as highlighted above with our Core 5 and Own Brand strategies. We are aggressively pursuing product sourcing improvements and cost reductions across all product lines in order to drive overall product costs down and in turn raise our gross margin. Additionally, we have implemented new processes intended to control both promotional and clearance markdowns. We also continue to make improvements in our loss prevention processes and procedures to control shrinkage in our stores and consequently increase gross margin.

Over the remainder of 2011, we intend to continue with capital improvements in infrastructure, including new stores as well as existing store expansion and remodels, including the 200 Core 5 Program upgrades, distribution center upgrades and further development of our information technology capabilities. Technology upgrades will be made in the areas of IT software and hardware, RF gun replacements and pharmacy server upgrades.

As previously reported in the second quarter press release filed August 25, 2011, the Company expects total sales to increase 2% to 4% during the third quarter. Comparable store sales are expected to increase 1% to 3% versus an increase of 1.5% in the third quarter last year. Earnings per diluted share are forecasted to increase 5% to 15% to a range of \$0.21 to \$0.23 in the third quarter compared with \$0.20 per diluted share in the same period last year. Based on this outlook, the Company expects total earnings per diluted share for 2011 to be in the range of \$0.83 to \$0.88, representing an increase of 11% to 17% over last year's \$0.75.

Key factors that will be critical to the Company's future success include the successful roll-out of our Core 5 program, as well as managing the strategy for opening new stores and pharmacies, including the ability to open and operate efficiently, maintaining high standards of customer service, maximizing efficiencies in the supply chain, controlling working capital needs through improved inventory turnover, controlling the effects of inflation or deflation, controlling product mix, increasing operating margin through improved gross margin and leveraging operating costs, and generating adequate cash flow to fund the Company's future needs.

Other factors that will affect Company performance in 2011 include the continuing management of the impacts of the changing regulatory environment in which our pharmacy department operates. Additionally, we believe that the protracted elevation in commodity and fuel prices, as well as the unemployment rate continues to place tremendous economic pressure on the consumer. However, we also continue to believe that our affordable pricing and value proposition make us an attractive destination to the price conscious consumer.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

The Company's discussion and analysis of its financial condition and results of operations are based upon the Company's condensed financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States. The critical accounting matters that are particularly important to the portrayal of the Company's financial condition and results of operations, and require some of management's most difficult, subjective and complex judgments, are described in detail in the Company's Annual Report on Form 10-K for the fiscal year ended January 29, 2011. The preparation of condensed financial statements requires the Company to make estimates and judgments that affect the reported amounts of assets, liabilities, revenue and expenses, and related disclosure of contingent assets and liabilities. On an ongoing basis, the Company evaluates its estimates, including those related to inventories, income taxes, insurance reserves, contingencies and litigation. The Company bases its estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions.

RESULTS OF OPERATIONS

Thirteen Weeks Ended July 30, 2011 and July 31, 2010

Sales

Net sales for the second quarter of 2011 increased to \$452.7 million from \$449.5 million in 2010, a year-over-year increase of \$3.2 million or 0.7%. The net sales increase during the quarter was primarily driven by higher pharmacy department sales. General merchandise (non-pharmacy) sales decreased 0.7% from 2010. We experienced sales decreases in categories such as electronics, health and beauty, small appliances and home furnishings, which were partially offset by sales increases in direct-to-store food and pet. On a comparable store basis, sales decreased 0.4% (\$2.1 million) compared with a 2.5% (\$10.5 million) increase in the same period last year.

The Company's pharmacy department sales were 34.7% of total sales (\$156.9 million) in 2011 compared to 33.6% of total sales (\$151.2 million) in the prior year and continue to rank as the largest department within the Company. The total sales in this department increased 3.8% over 2010 with third party prescription sales representing approximately 91% of total pharmacy sales, the same as in the prior year. The Company's pharmacy department continues to benefit from an ongoing program of purchasing prescription files from independent pharmacies as well as the addition of pharmacy departments in existing store locations.

During the second quarter, one franchised location closed leaving 22 franchised locations as of July 30, 2011. Sales to these 22 franchised locations during 2011 decreased to \$8.6 million (1.9% of sales) from \$9.0 million (2.0% of sales) in 2010. The Company does not intend to expand its franchise network.

The following table illustrates the sales mix unadjusted for deferred layaway sales:

	Thirteen Weeks Ended			
	July 30, 2011		July 31, 2010	
Pharmaceuticals	34.7	%	33.6	%
Household Goods	23.4	%	23.9	%
Food and Tobacco	17.0	%	17.0	%
Paper and Cleaning Supplies	8.9	%	8.6	%
Apparel and Linens	6.7	%	7.2	%
Health and Beauty Aids	7.4	%	7.7	%
Franchise	1.9	%	2.0	%
	100.0	%	100.0	%

For the quarter, comparable store customer traffic increased 0.1% over last year while the average customer ticket decreased .5% to \$19.31.

Gross Profit

Gross profit for the quarter increased to \$126.9 million in 2011 from \$125.9 million in 2010, a year-over-year increase of \$1.0 million or 0.8%. Gross margin, measured as a percentage of sales was 28.0% in 2011, unchanged from the same quarter last year. In the quarter, the pressures of the product mix shift and the pharmacy department reimbursement rates were offset by improved markdown and shrink performance.

Selling, General and Administrative Expenses

Selling, general and administrative expenses, including depreciation and amortization, increased to \$118.7 million in 2011 (26.2% of sales) from \$117.7 million in 2010 (26.2% of sales). While selling, general and administrative expenses were controlled as a percent of sales, there were increases in labor (\$1.1 million), depreciation and amortization expenses (\$.9 million), fuel (\$.4 million), insurance expense (\$.3 million) and utilities (\$.3 million) that were partially offset by decreases in advertising expense (\$1.5 million) and store occupancy costs (\$.7 million).

Operating Income

Operating income increased to \$8.3 million in 2011 (1.8% of sales) from \$8.2 million in 2010 (1.8% of sales). The year-over-year variance is approximately flat and is attributable to the \$1.0 million increase in gross profit as described in the Gross Profit section above offset by the \$1.0 million increase in selling, general and administrative expenses as detailed in the Selling, General and Administrative Expenses section above.

Interest Expense, Net

Net interest expense for 2011 totaled \$.09 million or less than .1% of sales compared to \$.06 million which was also less than .1% of sales in 2010.

Income Taxes

The effective income tax rate was 37.8% in 2011 compared to 39.4% in 2010. The decrease in the effective tax rate was primarily attributable to one year employment tax credits resulting from the New Hire Act. The year over year benefit was partially offset by reduced federal benefit from Work Opportunity Tax Credits.

Net Income

Net income increased to \$5.1 million (\$.13 per diluted share) in 2011 from \$5.0 million (\$.13 per diluted share) in 2010. The increase in net income is primarily attributable to an increase in gross profit of \$1.0 million which was offset by an increase in selling, general and administrative expenses of \$1.0 million. The increase in selling, general

and administrative expenses was primarily attributable to increases in labor (\$1.1 million), depreciation and amortization expenses (\$.9 million), fuel (\$.4 million), insurance expense (\$.3 million) and utilities (\$.3 million) that were partially offset by decreases in advertising expense (\$1.5 million) and store occupancy costs (\$.7 million).

Twenty-Six Weeks Ended July 30, 2011 and July 31, 2010

Sales

Net sales for the first half of 2011 increased to \$937.1 million from \$921.1 million in 2010, a year-over-year increase of \$16.0 million or 1.7%. The sales increase resulted primarily from categories such as pharmacy, food, pet, tobacco and lawn and garden, which were partially offset by sales decreases in electronics and home furnishings. On a comparable store basis, sales increased 0.4% (\$3.7 million) compared with a 2.3% (\$20.3 million) increase in the same period last year.

The Company's pharmacy department sales were 34.2% of total sales (\$320.3 million) in 2011 compared to 33.8% of total sales (\$310.5 million) in the prior year and continue to rank as the largest department within the Company. The total sales in this department increased 3.2% over 2010 with third party prescription sales representing approximately 91% of total pharmacy sales, the same as in the prior year. The Company's pharmacy department continues to benefit from an ongoing program of purchasing prescription files from independent pharmacies as well as the addition of pharmacy departments in existing store locations.

During the first half of 2011, two franchised locations closed leaving 22 franchised locations as of July 30, 2011. Sales to these 22 franchised locations during 2011 decreased to \$18.0 million (1.9% of sales) from \$18.8 million (2.0% of sales) in 2010. The Company does not intend to expand its franchise network.

The following table illustrates the sales mix unadjusted for deferred layaway sales:

	Twenty-Six Weeks Ended			
	July 30, 2011		July 31, 2010	
Pharmaceuticals	34.2	%	33.8	%
Household Goods	24.0	%	24.0	%
Food and Tobacco	16.7	%	16.7	%
Paper and Cleaning Supplies	8.7	%	8.6	%
Apparel and Linens	7.1	%	7.5	%
Health and Beauty Aids	7.4	%	7.4	%
Franchise	1.9	%	2.0	%
	100.0	%	100.0	%

For the first half, comparable store customer traffic increased 0.3% over last year while the average customer ticket was flat to last year at \$19.88.

Gross Profit

Gross profit for the first half of 2011 increased to \$264.9 million in 2011 from \$262.9 million in 2010, a year-over-year increase of \$2.0 million or 0.8%. Gross margin, measured as a percentage of sales was 28.3% in 2011 as compared to 28.5% from last year. In the first half, the pressures of the product mix shift, the lower pharmacy department reimbursement rates and the fuel price increases on inbound freight were partially mitigated by improved markdown and shrink performance.

Selling, General and Administrative Expenses

Selling, general and administrative expenses, including depreciation and amortization was \$241.5 million in 2011 (25.8% of sales) equal to \$241.5 million in 2010 (26.2% of sales). The 40 basis points leveraging as a percent of sales during the quarter was derived by positive expense management of advertising costs (\$2.2 million), professional fees

(\$1.1 million), store occupancy costs (\$0.7 million) and insurance expense (\$0.9 million) as well as increased labor controls (\$0.8 million), which were partially offset by deleveraging in depreciation and amortization expenses (\$1.7 million) and fuel (\$.9 million).

Operating Income

Operating income increased to \$23.4 million in 2011 (2.5% of sales) from \$21.4 million in 2010 (2.3% of sales). The year-over-year variance of \$2.0 million is attributable to the \$2.0 million increase in gross profit as described in the Gross Profit section above.

Interest Expense, Net

Net interest expense for 2011 totaled \$0.2 million or less than .1% of sales compared to \$.1 million which was also less than .1% of sales in 2010.

Income Taxes

The effective income tax rate was 37.1% in 2011 compared to 38.3% in 2010. The decrease in the effective tax rate was primarily attributable to one year employment tax credits resulting from the New Hire Act. The year over year benefit was partially offset by reduced federal benefit from Work Opportunity Tax Credits.

Net Income

Net income increased to \$14.6 million (\$.37 per diluted share) in 2011 from \$13.1 million (\$.34 per diluted share) in 2010. The increase in net income is primarily attributable to an increase in gross profit of \$2.0 million as described in the Gross Profit section above and a reduction in income tax expense of \$.5 million related to the decrease in the effective tax rate as described in the Income Taxes section above.

LIQUIDITY AND CAPITAL RESOURCES

Due to the seasonality of our business and the continued increase in the number of stores and pharmacies, inventories are generally lower at year-end than at each quarter-end of the following year.

Cash provided by operating activities totaled \$37.3 million during the twenty-six week period ended July 30, 2011 compared to \$16.1 million in the same period of the prior year. We generated operating cash flow primarily through \$1.5 million more in quarterly income and \$8.2 million from our ongoing initiative to better manage our Accounts Payable processes. We also used \$8.4 million less to purchase inventory in the first half of 2011 versus the same time last year and had \$3.6 million less in trade and non-trade receivables.

Cash used in investing activities totaled \$29.9 million, and consisted primarily of expenditures related to existing stores (\$21.0 million) of which \$10.0 million was related to the acquisition of land and building as described in Note 7: Related Party Transactions, pharmacy acquisitions and new store openings (\$2.4 million) and technology and other corporate expenditures (\$4.0 million). During the first half of 2011, we opened three new stores and four pharmacy express locations and one new pharmacy. We also closed seven underperforming stores, eight pharmacy locations and two franchises. We also refreshed 68 stores with the new Core 5 elements, bringing the total refreshed over 2010 and 2011 to 332 locations. In 2011, the Company is planning capital expenditures totaling approximately \$46.5 million. Expenditures are planned totaling \$37.3 million for new and existing stores and pharmacies. Planned expenditures also include approximately \$5.6 million for technology upgrades and approximately \$3.6 million for distribution center equipment and other capital maintenance. Technology upgrades in 2011 will be made in the areas of IT software and hardware, RF gun replacements and pharmacy server upgrades. To date, the Company has spent \$30.9 million towards these transactions. In addition, the Company planned expenditures of approximately \$13.7 million in 2011 for the acquisition of prescription lists and other pharmacy related items of which \$2.6 million has been spent to date.

Cash used by financing activities totaled \$9.8 million and included \$3.9 million for the payment of cash dividends, \$5.9 million for the repurchase of shares and \$.2 million for the repayment of debt. There were \$7.5 million in borrowings outstanding at July 30, 2011 related to real estate mortgages compared to \$4.2 million at January 29, 2011. The increase is attributable to \$3.4 million of mortgage debt assumed in the related party acquisition completed on March 30, 2011 as described in the Note 8: Related Party Transactions.

We believe that sufficient capital resources are available in both the short-term and long-term through currently available cash and cash generated from future operations and, if necessary, the ability to obtain additional financing.

FORWARD-LOOKING STATEMENTS

Other than statements based on historical facts, many of the matters discussed in this Form 10-Q relate to events which we expect or anticipate may occur in the future. Such statements are defined as “forward-looking statements” under the Private Securities Litigation Reform Act of 1995 (the “Reform Act”), 15 U.S.C. Sections 77z-2 and 78u-5. The Reform Act created a safe harbor to protect companies from securities law liability in connection with forward-looking statements. We intend to qualify both our written and oral forward-looking statements for protection

under the Reform Act and any other similar safe harbor provisions.

The words “believe”, “anticipate”, “project”, “plan”, “expect”, “estimate”, “objective”, “forecast”, “goal”, “intend”, “will likely continue” and similar expressions generally identify forward-looking statements. All forward-looking statements are inherently uncertain, and concern matters that involve risks and other factors that may cause the actual performance of the Company to differ materially from the performance expressed or implied by these statements. Therefore, forward-looking statements should be evaluated in the context of these uncertainties and risks, including but not limited to:

- Economic and weather conditions which affect buying patterns of our customers and supply chain efficiency.
- Changes in consumer spending and our ability to anticipate buying patterns and implement appropriate inventory strategies.
 - Continued availability of capital and financing.
 - Competitive factors.
 - Unemployment.
 - Changes in reimbursement practices for pharmaceuticals.

- Governmental regulation.
- Increases in fuel and utility rates.
- Potential adverse results in the litigation described under Legal Proceedings on page 18.
- Other factors affecting business beyond our control, including (but not limited to) those discussed under Part 1, ITEM 1A “Risk Factors” of the Company’s Annual Report on Form 10-K for the fiscal year ended January 29, 2011.

Consequently, all forward-looking statements are qualified by this cautionary statement. Readers should not place undue reliance on any forward-looking statements. We undertake no obligation to update any forward-looking statement to reflect events or circumstances arising after the date on which it was made.

Item 3.

QUANTITATIVE AND QUALITATIVE DISCLOSURE ABOUT MARKET RISK

We have no holdings of derivative financial or commodity instruments as of July 30, 2011. We are exposed to financial market risks, including changes in interest rates. We had no borrowings under our Revolving Credit Agreement, which bears interest at LIBOR plus 112.5 basis points. An increase in interest rates of 100 basis points would not significantly affect our income. All of our business is transacted in U.S. dollars and, accordingly, foreign exchange rate fluctuations have not had a significant impact on us, and they are not expected to in the foreseeable future.

Item 4.

CONTROLS AND PROCEDURES

(a) Conclusion Regarding the Effectiveness of Disclosure Controls and Procedures. As of the end of the period covered by this report, the Company carried out an evaluation, under the supervision and with the participation of our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the Company's disclosure controls and procedures (as defined in Rules 13a-15(e) under the Securities and Exchange Act of 1934, as amended (the "Exchange Act")). Based on that evaluation, the Chief Executive Officer and the Chief Financial Officer concluded that the Company's disclosure controls and procedures are effective to ensure that information required to be disclosed by the issuer in the reports that it files or submits under the Act (15 U.S.C. 78 et seq.) is recorded, processed, summarized and reported, within the time periods specified in the Commission's rules and forms. Additionally, they concluded that our disclosure controls and procedures are designed to ensure that information required to be disclosed by the Company in the reports that the Company is required to file or submit under the Exchange Act is accumulated and communicated to management, including the Chief Executive Officer and the Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosures.

(b) Changes in Internal Control over Financial Reporting. There have been no changes during the quarter ended July 30, 2011 in the Company's internal control over financial reporting (as defined in Exchange Act Rule 13a-15(f)) that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

In December 2008, a lawsuit entitled Whiteaker, et al v. FRED'S Stores of Tennessee, Inc., et al, was filed in the United States District Court in the Northern District of Mississippi, in which the plaintiffs allege past and future damages as a result of a 2006 trip and fall accident at a Fred's store. The Company denied liability and vigorously defended the case on its merits. In accordance with FASB ASC 450, "Contingencies", the Company did not feel that a loss in this matter was probable or could be reasonably estimated. However, on November 17, 2010, a jury rendered a \$1.1 million verdict and apportioned the Company with 81% fault. The judge then vacated the \$1.1 million verdict and ordered a new trial on damages. Prior to the new trial commencing, the Company's insurance carrier settled the matter for \$700,000. This case is covered by the Company's General Liability insurance, which has a \$250 thousand deductible that has been reserved for as of July 30, 2011.

In July 2008, a lawsuit styled Jessica Chapman, on behalf of herself and others similarly situated, v. FRED'S Stores of Tennessee, Inc. was filed in the United States District Court for the Northern District of Alabama, Southern Division,

in which the plaintiff alleges that she and other female assistant store managers are paid less than comparable males and seeks compensable damages, liquidated damages, attorney fees and court costs. The plaintiff filed a motion seeking collective action. Briefs have been filed, but the court has not ruled. The Company believes that all assistant managers have been properly paid and that the matter is not appropriate for collective action treatment. Discovery has not yet begun. The Company is and will continue to vigorously defend this matter. In accordance with FASB ASC 450, "Contingencies", the Company does not feel that a loss in this matter is probable or can be reasonably estimated. Therefore, we have not recorded a liability for this case.

In addition to the matters disclosed above, the Company is party to several pending legal proceedings and claims arising in the normal course of business. Although the outcome of the proceedings and claims cannot be determined with certainty, management of the Company is of the opinion that it is unlikely that these proceedings and claims will have a material adverse effect on the financial statements as a whole. However, litigation involves an element of uncertainty. There can be no assurance that pending lawsuits will not consume the time and energy of our management or that future developments will not cause these actions or claims, individually or in aggregate, to have a material adverse effect on the financial statements as a whole. We intend to vigorously defend or prosecute each pending lawsuit.

Item 1A. Risk Factors

The risk factors listed in Part I, “Item 1A. Risk Factors” in the Annual Report on Form 10-K for the fiscal year ended January 29, 2011, should be considered with the information provided elsewhere in this Quarterly Report on Form 10-Q, which could materially adversely affect the business, financial condition or results of operations. There have been no material changes to the risk factors as previously disclosed in such Annual Report on Form 10-K.

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

On August 27, 2007, the Board of Directors approved a plan that authorized stock repurchases of up to 4.0 million shares of the Company’s common stock. Under the plan, the Company may repurchase its common stock in the open market or through privately negotiated transactions at such times and at such prices as determined to be in the Company’s best interest. These repurchases may be commenced or suspended without prior notice depending on then-existing business or market conditions and other factors. The following table sets forth the amounts of our common stock purchased by the Company through July 30, 2011 (amounts in thousands, except price data). The repurchased shares have been cancelled and returned to authorized but unissued shares.

	Total Number Of Shares Purchased	Average Price Paid Per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Program	Maximum Number of Shares That May Yet Be Purchased Under the Plans or Program
Balance at January 29, 2011				2,537.8
January 30 - February 26, 2011	-	\$ -	-	2,537.8
February 27 - April 2, 2011	2.0	\$ 12.50	2.0	2,535.8
April 3, - April 30, 2011	-	\$ -	-	2,535.8
May 1, - May 28, 2011	-	\$ -	-	2,535.8
May 29, - July 2, 2011	256.5	\$ 13.99	256.5	2,279.3
July 3, - July 30, 2011	161.5	\$ 13.86	161.5	2,117.8

Item 6. Exhibits

Exhibits

31.1 Certification of Chief Executive Officer.

31.2 Certification of Chief Financial Officer.

32 Certification of Chief Executive Officer and Chief Financial Officer pursuant to rule 13a-14(b) under the Securities Exchange Act of 1934 and 18 U.S.C. Section 1350.

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.

FRED'S, INC.

Date: September 8, 2011

/s/ Bruce A. Efird
Bruce A. Efird

Chief Executive Officer and
President

Date: September 8, 2011

/s/ Jerry A. Shore
Jerry A. Shore
Executive Vice President and
Chief Financial Officer