

FORM 10-Q

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON D.C. 20549

QUARTERLY REPORT UNDER SECTION 13 OR 15 (d)
OF THE SECURITIES AND EXCHANGE ACT OF 1934

For Quarter Ended
June 30, 2004

Commission File Number:
0-21026

ROCKY SHOES & BOOTS, INC.

(Exact name of registrant as specified in its charter)

Ohio
(State of Incorporation)

31-1364046
(IRS Employer Identification Number)

39 E. Canal Street
Nelsonville, Ohio 45764
(Address of principal executive offices)

(740) 753-1951
(Registrant's telephone number, including area code)

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

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding twelve (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 ninety (90) days.

Yes No

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

Yes No

4,597,476 common shares, no par value, outstanding at July 30, 2004

Rocky Shoes & Boots, Inc. and Subsidiaries

Form 10-Q

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PART 1 - FINANCIAL INFORMATION
ITEM 1 - FINANCIAL STATEMENTS

Rocky Shoes & Boots, Inc. and Subsidiaries
Condensed Consolidated Balance Sheets

	June 30, 2004	December 31, 2003	June 30, 2003
	Unaudited	Unaudited	Unaudited
ASSETS:			
CURRENT ASSETS:			
Cash and cash equivalents	\$ 492,408	\$ 2,159,050	\$ 1,450,044
Trade receivables – net	27,422,370	19,532,287	21,356,964
Other receivables	863,709	830,131	1,062,552
Inventories	38,641,868	38,068,187	38,332,365
Deferred income taxes	959,810	959,810	578,951
Prepaid expenses	1,105,070	1,045,238	1,706,029
Total current assets	<u>69,485,235</u>	<u>62,594,703</u>	<u>64,486,905</u>
FIXED ASSETS – net	19,055,324	17,610,238	18,270,014
DEFERRED PENSION ASSET	1,499,524	1,499,524	1,651,222
DEFERRED INCOME TAXES	-	-	153,495
OTHER ASSETS	<u>4,672,682</u>	<u>4,470,371</u>	<u>3,208,827</u>
TOTAL ASSETS	<u><u>\$ 94,712,765</u></u>	<u><u>\$ 86,174,836</u></u>	<u><u>\$ 87,770,463</u></u>
LIABILITIES AND SHAREHOLDERS' EQUITY:			
CURRENT LIABILITIES:			
Accounts payable	\$ 6,829,747	\$ 2,810,161	\$ 7,637,974
Current maturities - long term debt	518,226	503,934	490,218
Accrued expenses:			
Income taxes	45,064	1,929,808	-
Taxes - other	491,828	372,432	471,780
Salaries and wages	988,107	1,885,896	904,834
Plant closing costs	63,228	195,500	210,000
Other	636,805	686,934	753,743
Total current liabilities	<u>9,573,005</u>	<u>8,384,665</u>	<u>10,468,549</u>
LONG TERM DEBT-less current maturities	21,493,872	17,514,994	25,228,589
DEFERRED LIABILITIES	<u>2,225,067</u>	<u>1,890,500</u>	<u>1,842,769</u>
TOTAL LIABILITIES	33,291,944 [¶]	27,790,159 [¶]	37,539,907
SHAREHOLDERS' EQUITY:			
Common stock, no par value;			
10,000,000 shares authorized; issued and outstanding			
June 30, 2004 - 4,587,476; December 31, 2003 - 4,360,400;			
June 30, 2003 - 4,097,930	36,396,070	34,880,199	32,653,420
Accumulated other comprehensive loss	(1,950,400)	(1,950,400)	(2,311,749)
Retained earnings	<u>26,975,151</u>	<u>25,454,878</u>	<u>19,888,885</u>
Total shareholders' equity	<u>61,420,821</u>	<u>58,384,677</u>	<u>50,230,556</u>
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	<u><u>\$ 94,712,765</u></u>	<u><u>\$ 86,174,836</u></u>	<u><u>\$ 87,770,463</u></u>

See notes to the interim unaudited condensed consolidated financial statements.

Rocky Shoes & Boots, Inc. and Subsidiaries
Condensed Consolidated Statements of Operations
(Unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	<u>2004</u>	<u>2003</u>	<u>2004</u>	<u>2003</u>
NET SALES	\$ 27,433,987	\$ 21,863,148	\$ 49,316,076	\$ 35,618,089
COST OF GOODS SOLD	<u>19,657,778</u>	<u>15,128,164</u>	<u>35,921,263</u>	<u>25,417,577</u>
GROSS MARGIN	7,776,209	6,734,984	13,394,813	10,200,512
SELLING, GENERAL AND ADMINISTRATIVE EXPENSES	<u>5,396,376</u>	<u>4,944,319</u>	<u>10,724,067</u>	<u>9,194,925</u>
INCOME FROM OPERATIONS	2,379,833	1,790,665	2,670,746	1,005,587
OTHER INCOME AND (EXPENSES):				
Interest expense	(274,868)	(313,438)	(533,441)	(509,618)
Other – net	<u>24,182</u>	<u>88,230</u>	<u>98,388</u>	<u>180,103</u>
Total other - net	(250,686)	(225,208)	(435,053)	(329,515)
INCOME BEFORE INCOME TAXES	2,129,147	1,565,457	2,235,693	676,072
INCOME TAX EXPENSE	<u>681,325</u>	<u>469,638</u>	<u>715,420</u>	<u>202,822</u>
NET INCOME	<u>\$ 1,447,822</u>	<u>\$ 1,095,819</u>	<u>\$ 1,520,273</u>	<u>\$ 473,250</u>
NET INCOME PER SHARE				
Basic	<u>\$ 0.32</u>	<u>\$ 0.27</u>	<u>\$ 0.34</u>	<u>\$ 0.11</u>
Diluted	<u>\$ 0.29</u>	<u>\$ 0.25</u>	<u>\$ 0.31</u>	<u>\$ 0.11</u>
WEIGHTED AVERAGE NUMBER OF COMMON SHARES OUTSTANDING				
Basic	<u>4,557,954</u>	<u>4,067,353</u>	<u>4,492,989</u>	<u>4,214,417</u>
Diluted	<u>5,003,956</u>	<u>4,361,037</u>	<u>4,949,805</u>	<u>4,424,355</u>

See notes to the interim unaudited condensed consolidated financial statements.

Rocky Shoes & Boots, Inc. and Subsidiaries
Condensed Consolidated Statements of Cash Flows
(Unaudited)

	Six Months Ended	
	June 30,	
	<u>2004</u>	<u>2003</u>
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	\$ 1,520,273	\$ 473,250
Adjustments to reconcile net income to net cash used in operating activities:		
Depreciation and amortization	1,558,687	1,795,013
Deferred income taxes	334,567	327,991
Loss on sale of fixed assets	-	8,684
Stock issued as directors' compensation	50,000	
Change in assets and liabilities:		
Receivables	(7,923,661)	(5,963,184)
Inventories	(573,681)	(13,110,306)
Other current assets	(59,832)	(438,932)
Other assets	(214,951)	46,745
Accounts payable	3,837,559	5,993,277
Accrued and other liabilities	(2,845,538)	453,460
	<hr/>	<hr/>
Net cash used in operating activities	(4,316,577)	(10,414,002)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchase of fixed assets	(2,782,106)	(1,039,201)
Acquisition of business	-	(3,510,070)
Proceeds from sale of fixed assets	-	27,955
	<hr/>	<hr/>
Net cash used in investing activities	(2,782,106)	(4,521,316)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from long-term debt	49,651,822	48,091,811
Payments on long-term debt	(45,685,652)	(33,347,553)
Purchase of treasury stock	-	(3,106,156)
Proceeds from exercise of stock options	1,465,871	470,538
	<hr/>	<hr/>
Net cash provided by financing activities	5,432,041	12,108,640
DECREASE IN CASH AND CASH EQUIVALENTS	(1,666,642)	(2,826,678)
CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD	<hr/>	<hr/>
	2,159,050	4,276,722
CASH AND CASH EQUIVALENTS, END OF PERIOD	<hr/> <hr/>	<hr/> <hr/>
	\$ 492,408	\$ 1,450,044

See notes to the interim unaudited condensed consolidated financial statements.

**Rocky Shoes & Boots, Inc.
and Subsidiaries**

**Notes to the Interim Unaudited Condensed Consolidated Financial Statements
For the Periods Ended June 30, 2004 and 2003**

1. INTERIM FINANCIAL REPORTING

In the opinion of management, the accompanying interim unaudited condensed consolidated financial statements reflect all adjustments which are necessary for a fair presentation of the financial results. All such adjustments reflected in the unaudited interim consolidated financial statements are considered to be of a normal and recurring nature. The results of the operations for the three-month and six-month periods ended June 30, 2004 and 2003 are not necessarily indicative of the results to be expected for the whole year. Accordingly, these consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto contained in the Company's Annual Report to Shareholders on Form 10-K for the year ended December 31, 2003.

Certain reclassifications have been made to the prior year amounts in order to conform to the current year presentation.

The Company accounts for its stock option plans in accordance with APB Opinion No. 25, under which no compensation cost has been recognized. Had compensation cost for all stock option plans been determined consistent with the SFAS No. 123, "Accounting for Stock Based Compensation," the Company's net income and earnings per share would have resulted in the amounts as reported below.

	Three Months Ended June 30,		Six Months Ended June 30,	
	2004	2003	2004	2003
Net income as reported	\$ 1,447,822	\$ 1,095,819	\$ 1,520,273	\$ 473,250
Deduct: Stock based employee compensation expense determined under fair value based method for all awards, net	276,830	250,230.00	429,845	333,640
Pro forma net income	\$ 1,170,992	\$ 845,589	\$ 1,090,428	\$ 139,610
Earnings per share:				
Basic - as reported	\$ 0.32	\$ 0.27	\$ 0.34	\$ 0.11
Basic - pro forma	\$ 0.26	\$ 0.21	\$ 0.24	\$ 0.03
Diluted - as reported	\$ 0.29	\$ 0.25	\$ 0.31	\$ 0.11
Diluted - pro forma	\$ 0.23	\$ 0.19	\$ 0.22	\$ 0.03

The pro forma amounts are not representative of the effects on reported net income for future years.

2. INVENTORIES

Inventories are comprised of the following:

	<u>June 30, 2004</u>	<u>December 31, 2003</u>	<u>June 30, 2003</u>
Raw materials	\$ 6,949,144	\$ 5,087,468	\$ 8,008,009
Work in process	1,469,094	878,091	1,617,562
Finished good	28,878,360	31,168,371	27,602,186
Factory outlet finished goods	1,570,270	1,299,257	1,276,608
Reserve for obsolescence or lower of cost or market	<u>(225,000)</u>	<u>(365,000)</u>	<u>(172,000)</u>
Total	<u>\$ 38,641,868</u>	<u>\$ 38,068,187</u>	<u>\$ 38,332,365</u>

3. SUPPLEMENTAL CASH FLOW INFORMATION

Cash paid for interest and Federal, state and local income taxes was as follows:

	Six Months Ended June 30,	
	<u>2004</u>	<u>2003</u>
Interest	<u>\$503,023</u>	<u>\$506,499</u>
Federal, state and local income taxes	<u>\$2,580,000</u>	<u>\$ 80,000</u>

Accounts payable at June 30, 2004 and June 30, 2003 include a total of \$209,474 and \$5,084 respectively, relating to the purchase of fixed assets.

4. PER SHARE INFORMATION

Basic earnings per share (EPS) is computed by dividing net income applicable to common shareholders by the basic weighted average number of common shares outstanding during each period. The diluted earnings per share computation includes common share equivalents, when dilutive. There are no adjustments to net income necessary in the calculation of basic and diluted earnings per share.

A reconciliation of the shares used in the basic and diluted income per common share computation for the three months and six months ended June 30, 2004 and 2003 is as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
	<u>2004</u>	<u>2003</u>	<u>2004</u>	<u>2003</u>
Basic Weighted average shares outstanding	4,557,954	4,067,353	4,492,989	4,214,417
Diluted securities:				
Stock options	<u>445,982</u>	<u>293,684</u>	<u>456,816</u>	<u>209,938</u>
Diluted Weighted average shares outstanding	<u>5,003,936</u>	<u>4,361,037</u>	<u>4,949,805</u>	<u>4,424,355</u>

5. RECENTLY ADOPTED FINANCIAL ACCOUNTING STANDARDS

In December 2003, the FASB issued Revised SFAS No. 132, “Employers’ Disclosures about Pensions and Other Postretirement Benefits” (“SFAS No. 132”). SFAS No. 132 revises the annual disclosure requirements for pensions and postretirement plans to include additional disclosures about assets, obligations, cash flows, and net periodic benefit costs of defined benefit pension and other defined benefit postretirement plans. SFAS No. 132 also revises the interim disclosure requirements to include disclosures of the net periodic benefit costs for each period in which an income statement is presented and the employer’s contributions paid and expected to be paid during the current fiscal year, if the contributions are significantly different than previously disclosed amounts. The Statement is effective for financial statements with fiscal years ending after December 15, 2003. For interim-period disclosures, the Statement is effective for interim periods beginning after December 15, 2003. We have adopted this Statement for interim-period disclosures in these condensed consolidated financial statements, and we will adopt the annual disclosures with our December 31, 2004 Form 10-K. The adoption of FAS No. 132 does not have an impact on our financial condition or results of operations, as it pertains only to disclosure provisions.

In May 2004, the FASB issued FSP FAS 106-2 to provide guidance on “Accounting and Disclosure Requirements Related to the Medicare Prescription Drug, Improvement and Modernization Act of 2003” (FSP FAS 106-2), which supersedes FSP FAS 106-1, “Accounting and Disclosure Requirements Related to the Medicare Prescription Drug, Improvement and Modernization Act of 2003”. FSP FAS 106-2 is effective for interim and annual periods beginning after June 15, 2004. The effect of FSP 106-2 is not expected to have a material effect on our results of operations, cash flows or financial position.

6. ACQUISITION

On April 15, 2003, the Company completed the purchase of certain assets from Gates-Mills, Inc. (“Gates”). Under the terms of the Purchase Agreement, Rocky acquired all of the intellectual property of Gates, including ownership of the Gates ® trademark, selected raw material and finished goods inventory, and certain records in connection with the Gates business in exchange for a total purchase price of \$4.9 million, of which \$3.5 million had been expended through June 30, 2003.

7. CAPITAL STOCK

The Company was authorized to repurchase up to 500,000 shares of our outstanding common shares. Purchases occurred on the open market and/or in privately negotiated transactions as market conditions warranted. During the three-month period ended March 31, 2003, the Company repurchased 483,533 shares at an average price of \$6.42. As of March 31, 2003, the Company had purchased a total of 499,933 shares at an average price of \$6.38. No additional shares have been repurchased since March 31, 2003.

For the six months ended June 30, 2004, options for 224,400 of the Company's common stock were exercised at an average price of \$6.46. The outside members of the Board of Directors received a total of 2,676 shares in lieu of cash as part of their director compensation.

8. RETIREMENT PLANS

SFAS No. 132 (revised 2003), "Employers' Disclosures about Pensions and Other Postretirement Benefits," generally requires additional disclosures to those in the original Statement 132 about the assets, obligations, cash flows, and net periodic benefit cost of defined benefit pension plans and other defined benefit postretirement plans.

Net pension cost of the Company's plans is as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2004	2003	2004	2003
Service cost	\$ 128,080	\$ 96,923	\$256,159	\$193,846
Interest	90,758	150,870	252,271	301,740
Expected return on assets	(86,391)	(138,247)	(257,465)	(276,494)
Amortization of unrecognized net loss	32,141	44,660	67,552	89,320
Amortization of unrecognized transition obligation	4,076	4,077	8,153	8,154
Amortization of unrecognized prior service cost	33,849	33,848	67,697	67,696
	<u> </u>	<u> </u>	<u> </u>	<u> </u>
Net pension cost	<u>\$ 202,513</u>	<u>\$ 192,131</u>	<u>\$394,367</u>	<u>\$384,262</u>

The Company's unrecognized benefit obligations existing at the date of transition for the non-union plan is being amortized over 21 years. Actuarial assumptions used in the accounting for the plans were as follows:

	June 30,	
	2004	2003
Discount rate	5.75 %	5.75 %
Average rate of increase in compensation levels (non-union only)	3.0 %	3.0 %
Expected long-term rate of return on plan assets	8.0 %	8.0 %

The Company's desired investment result is a long-term rate of return on assets that is at least a 8%. The target rate of return for the plans have been based upon the assumption that returns will approximate the long-term rates of return experienced for each asset class in the Company's investment policy. The Company's investment guidelines are based upon an investment horizon of greater than five years, so that interim fluctuations should be viewed with appropriate perspective. Similarly, the Plan's strategic asset allocation is based on this long-term perspective.

The Company expects to make contributions to the plan in 2004 of approximately \$1.5 million. For the six months ended June 30, 2004, no Company contribution had been made.

In 2001, the Company announced a restructuring plan to consolidate and realign the Company's footwear manufacturing operations. As part of the plan, 67 employees were eliminated and the plan assets were frozen as of September 30, 2001. In April of 2004 the remaining assets of the Union pension plan were used to purchase individual annuities for the terminated employees. No further contributions will be made to the plan.

ITEM 2

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

Results of Operations

The following table sets forth, for the periods indicated, information derived from the Company's Interim Unaudited Condensed Consolidated Financial Statements, expressed as a percentage of net sales. The discussion that follows the table should be read in conjunction with the Interim Unaudited Condensed Consolidated Financial Statements of the Company.

	Percentage of Net Sales			
	Three Months Ended		Six Months Ended	
	June 30,		June 30,	
	2004	2003	2004	2003
Net Sales	100.0%	100.0%	100.0%	100.0%
Cost of Goods Sold	71.7%	69.2%	72.8%	71.4%
Gross Margin	<u>28.3%</u>	<u>30.8%</u>	<u>27.2%</u>	<u>28.6%</u>
Selling, General and Administrative Expenses	19.7%	22.6%	21.7%	25.8%
Income from Operations	<u>8.6%</u>	<u>8.2%</u>	<u>5.5%</u>	<u>2.8%</u>

Three Months Ended June 30, 2004 Compared to Three Months Ended June 30, 2003

Net Sales

Net sales increased in the second quarter 2004 to \$27.4 million compared to \$21.9 million for the same period in 2003. This 25.5% increase was attributable to a 13% increase in branded sales and shipments of boots to the U.S. military. The \$2.8 million increase in branded sales was lead by increased sales of GATES[®] products and ROCKY[®] apparel. Shipments of boots for delivery to the U.S. military were \$2.8 million in second quarter 2004 compared to none for the same period last year.

Gross Margin

Gross profit was \$7.8 million, or 28.3% of net sales for the first quarter 2004 compared to \$6.7 million, or 30.8% of net sales, for the same period in the prior year. The decrease in gross margin percentage was due to shipments of boots for delivery to the U.S. military and related start-up costs for these boots in 2004 compared to none for the same period last year. The Company manufactures military boots at lower gross margin than its branded products.

Selling, General and Administrative Expenses

Selling, general and administrative (“SG&A”) expenses were \$5.4 million, or 19.7% of net sales, for the quarter ended June 30, 2004 compared to \$4.9 million, or 22.6% of net sales, for the same period in the prior year. The decline in SG&A expenses as a percentage of sales was attributable to nominal SG&A expenses related to the sales of boots for delivery to the U.S. military. The increase in SG&A expenses was primarily due to higher advertising expenses that increased \$0.2 million, higher commissions that increased \$0.1 million, distribution costs associated with the growth in branded product sales that increased \$0.1 million and industry trade show expense that increased \$0.1 million when compared to a year ago.

Interest Expense

Interest expense was \$0.3 million in the second quarter 2004 compared to \$0.3 million for the same period the prior year. The Company’s funded debt as of June 30, 2004 was \$3.7 million below funded debt on the same date last year.

Income Taxes

Income tax expense for the quarter ended June 30, 2004 was \$.7 million compared to \$.5 million and for the same period a year ago. The Company’s effective tax rate was 32.0% for the three months ended June 30, 2004 versus 30.0% for the same period in 2003. The increase in the effective tax rate in 2004 over 2003 is due primarily to the increase in sales of sourced products, which are taxed at U.S. effective tax rates.

Six Months Ended June 30, 2004 compared to the Six Months Ended June 30, 2003

Net Sales

Net sales increased in the six months ended June 30, 2004 to \$49.3 million compared to \$35.6 million for the same period in 2003. This represents a 38.5% increase and is attributable to a \$6.0 million increase in branded sales and \$7.7 million increase in sales to the U.S. military when compared to the prior year. The branded sales increase was led by sales of GATES® products, ROCKY® Work footwear and ROCKY® apparel categories.

Gross Margin

Gross profit for the six months ended June 30, 2004 was \$13.3 million, or 27.2% of net sales compared to \$10.2 million, or 28.6% of net sales, the prior year. The decrease in gross margin percentage was due to shipments of boots for delivery to the U.S. military and related start-up costs for these boots in 2004 compared to none for the same period last year. The Company manufactures military boots at lower gross margin than its branded products.

Selling, General and Administrative Expenses

Selling, general and administrative (“SG&A”) expenses were \$10.7 million, or 21.7% of net sales, for the six months ended June 30, 2004 compared to \$9.2 million, or 25.8% of net sales, the prior year. The increase in SG&A expenses was primarily due to commissions that increased \$0.5 million, advertising expenses that increased \$0.2 million, distribution costs associated with the growth in branded product sales that increased \$0.2 million and industry trade show expense that increased \$0.3 million when compared to a year ago.

Interest Expense

Interest expense for the six months ended June 30, 2004 increased to \$0.5 million versus \$0.5 million for the same period a year ago. The increase in interest is the result of more borrowing on the line of credit in 2004.

Income Taxes

Income taxes for the six months ended June 30, 2004 increased to \$.7 million compared to \$.2 million and the same period last year. The Company's effective tax rate of 32.0% for the first half of 2004 compares with an effective tax rate 30% for the same period a year ago.

Liquidity and Capital Resources

The Company principally funds working capital requirements and capital expenditures through income from operations, borrowings under its credit facility and other indebtedness. Working capital is primarily used to support changes in accounts receivable and inventory because of the Company's seasonal business cycle and business expansion. These requirements are generally lowest in the months of January through March of each year and highest during the months of May through October. At June 30, 2004, the Company had working capital of \$59.9 million versus \$54.0 million on the same date last year and \$54.2 million at December 31, 2003.

The Company's line of credit provides for advances based on a percentage of eligible accounts receivable and inventory with maximum borrowings under the line of credit of \$45.0 million. As of June 30, 2004, the Company had borrowed \$16.8 million against its then currently available line of credit of \$37.1 million compared with \$20.4 million and \$26.8 million respectively in the same period of 2003.

The Company's cash flow used in operations was \$4.3 million in the first six months of 2004 compared to \$10.4 million in the same period of 2003. Increases in accounts receivable was partially offset by an increase in accounts payable, both the result of increased sales volume. The reduction in accrued liabilities was due to the payment of income taxes and incentives that resulted from the record operating results of fiscal 2003. Most of the respective balance sheet fluctuations reflect the seasonal nature of the Company's business, and the increased sales and bookings for the current year.

The principal use of cash flows in investing activities for the first six months of 2004 and 2003 has been for the acquisition and investment in property, plant, and equipment. In the first half of 2003 the Company acquired certain assets of Gates-Mills, Inc. In the first six months of 2004, property, plant, and equipment expenditures were \$2.8 million versus \$1.0 million in the same period of 2003. The Gates-Mills, Inc. assets were acquired for \$3.5 million in 2003. The current year expenditures primarily represent investments in expansion of the workspace at the Company's distribution center, retail outlet, as well as sales fixtures and displays.

The Company's net cash provided by financing activities for the six months ended June 30, 2004 was \$5.4 million, comprised of the proceeds from the exercise of stock options of \$1.4 million, as well as a net increase on its revolving credit facility and long-term mortgage facility of \$4.0 million.

Inflation

The Company cannot determine the precise effects of inflation; however, inflation continues to have an influence on the cost of materials, salaries, and employee benefits. The Company attempts to offset the effects of inflation through increased selling prices, productivity improvements, and reduction of costs.

Critical Accounting Policies and Estimates

Management's Discussion and Analysis of Financial Condition and Results of Operations discuss the Company's consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of these consolidated financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period.

Management regularly reviews its accounting policies to make certain they are current and also provide readers of the consolidated financial statements with useful and reliable information about our operating results and financial condition. These include, but are not limited to, matters related to accounts receivable, inventories, pension benefits, and income taxes. Implementation of these accounting policies includes estimates and judgments by management based on historical experience and other factors believed to be reasonable. This may include judgments about the carrying value of assets and liabilities based on considerations that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions.

Management believes the following critical accounting policies are most important to the portrayal of the Company's financial condition and results of operations, and require more significant judgments and estimates in the preparation of its consolidated financial statements.

Revenue Recognition:

Customer sales are recognized when revenue is realized and earned. The Company recognizes revenue when the risk and title passes to the customer, generally at the time of shipment. Customer sales are recorded net of allowances for estimated returns, trade promotions and other discounts, which are recognized as a deduction from sales at the time of sale.

Sales returns and allowances:

Revenue principally consists of sales to customers, and, to a lesser extent, license fees. Revenue is recognized upon shipment of product to customers, while license fees are recognized when earned. The Company records a reduction to gross sales based on estimated customer returns and allowances. These reductions are influenced by historical experience, based on customer returns and allowances. The actual amount of sales returns and allowances realized may differ from the Company's estimates. If the Company determines that sales returns or allowances should be either increased or decreased, then the adjustment would be made to net sales in the period in which such a determination is made.

Accounts receivable allowances:

Management maintains allowances for doubtful accounts for estimated losses resulting from the inability of its customers to make required payments. If the financial condition of the Company's customers were to deteriorate, resulting in an impairment of their ability to make payments, additional allowances may be required. Management also records estimates for customer returns and discounts offered to customers. Should a greater proportion of customers return goods and take advantage of discounts than estimated by the Company, additional allowances may be required.

Inventories:

Management identifies slow moving or obsolete inventories and estimates appropriate loss provisions related to these inventories. Historically, these loss provisions have not been significant as the vast majority of the Company's inventories are considered saleable and the Company has been able to liquidate slow moving or obsolete inventories through the Company's factory outlet stores or through various discounts to customers. Should management encounter difficulties liquidating slow moving or obsolete inventories, additional provisions may be necessary. Management regularly reviews the adequacy of its inventory reserves and makes adjustments to them as required.

Pension benefits:

Accounting for pensions and other postretirement benefits involves estimating the cost of benefits to be provided well into the future and attributing that cost over the time period each employee works. To accomplish this, extensive use is made of assumptions about inflation, investment returns, mortality, turnover, medical costs and discount rates. These assumptions are reviewed annually.

Pension and post-retirement benefit expenses are determined by actuaries using assumptions concerning the discount rate, expected return on plan assets and rate of compensation increase. An actuarial analysis of benefit obligations and plan assets is determined as of September 30 each year. The funded status of the Company's plans and reconciliation of accrued pension cost is determined annually as of December 31. Further discussion of the Company's pension and post-retirement benefit plans and related assumptions is included in Note 9, Retirement Plans, to the consolidated financial statements included in the Annual Report on Form 10-K. Actual results would be different using other assumptions. Management records an accrual for pension costs associated with the Company sponsored noncontributory defined benefit pension plans covering the union and non-union workers of the Company. The union plan was frozen in 2001 and no additional benefits have been earned under this plan since that time; the obligations under this plan were settled in April 2004. Future adverse changes in market conditions or poor operating results of underlying plan assets could result in losses or a higher accrual.

Income taxes:

Currently, management has not recorded a valuation allowance to reduce its deferred tax assets to the amount that it believes is more likely than not to be realized. The Company has considered future taxable income and ongoing prudent and feasible tax planning strategies in assessing the need for a valuation allowance, however in the event the Company were to determine that it would not be able to realize all or part of its net deferred tax assets in the future, an adjustment to the deferred tax assets would be charged to income in the period such determination was made. Finally, if the Company decided to repatriate any of its earnings in its Five Star subsidiary to the United States, the Company's effective tax rate would increase.

Intangible Assets:

The Company had \$4.2 million of intangible assets at June 30, 2004 and \$4.1 million at December 31, 2003. Goodwill and trademarks are tested for impairment at least annually by comparing the fair value of the reporting units to their carrying values. Fair values are estimated using discounted cash flow methodologies that are based on projections of the amounts and timing of future revenues and cash flows. Based on this testing, none of our goodwill nor trademarks were impaired as of December 31, 2003, and no impairment indicators have occurred since that date.

SAFE HARBOR STATEMENT UNDER THE PRIVATE SECURITIES LITIGATION REFORM ACT OF 1995.

This Quarterly Report on Form 10-Q contains forward-looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended, and Section 27A of the Securities Act of 1933, as amended, which are intended to be covered by the safe harbors created thereby. Those statements include, but may not be limited to, all statements regarding intent, beliefs, expectations, projections, forecasts, and plans of the Company and its management. Investors are cautioned that such statements involve risks and uncertainties, including, but not limited to, changes in consumer demand, seasonality, impact of weather, competition, reliance on suppliers, changing retailing trends, reliance on foreign manufacturing, changes in tax rates, limited protection of proprietary technology, and other risks, uncertainties and factors described in the Company's most recent Annual Report on Form 10-K and other filings from time to time with the Securities and Exchange Commission. One or more of these factors have affected, and in the future could affect the Company's business and financial results and cause actual results to differ materially from plans and projections. Although the Company and its management believe that the assumptions underlying the forward-looking statements contained herein are reasonable, any of the assumptions could be inaccurate. Therefore, there can be no assurance that the forward-looking statements included herein will prove to be accurate. In light of the significant uncertainties inherent in the forward-looking statements contained herein, the inclusion of such information should not be regarded as a representation by the Company, its management or any other person that the Company's objectives and plans will be achieved. All forward-looking statements made herein are based on information presently available to the management of the Company. The Company undertakes no obligation to publicly update or revise any forward-looking statements.

PART 1 - FINANCIAL INFORMATION

ITEM 3 - QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

There have been no material changes since December 31, 2003.

ITEM 4 – CONTROLS AND PROCEDURES

As of the end of the period covered by this report, the Company's management carried out an evaluation, with the participation of the Company's principal executive officer and principal financial officer, of the effectiveness of the Company's disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) promulgated under the Securities Exchange Act of 1934). Based upon that evaluation, the Company's principal executive officer and principal financial officer concluded that the Company's disclosure controls and procedures were effective as of the end of the period covered by this report. It should be noted that the design of any system of controls is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions, regardless of how remote.

There were no changes in the Company's internal controls over financial reporting that occurred during the Company's most recent fiscal quarter 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.

None

Item 2. Changes in Securities, Use of Proceeds and Issuer Purchases of Equity Securities.

See Note 7 to the Condensed Consolidated Financial Statements for further discussion.

Item 3. Defaults Upon Senior Securities.

None

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

The 2004 Annual Meeting of Shareholders was held on May 11, 2004, and the following proposals were acted upon:

Proposal: To elect three Class II Directors of the Company, each to serve for a two-year term expiring at the 2006 Annual Meeting of Shareholders

	<u>Number of Shares Voted</u>		
	FOR	WITHHELD AUTHORITY	TOTAL
Michael L. Finn	4,084,727	272,353	4,357,080
G. Courtney Haning	4,100,102	256,978	4,357,080
Curtis A. Loveland	3,066,909	1,290,171	4,357,080

Proposal: To approve and adopt the Company's 2004 Stock Incentive Plan.

<u>Number of Shares Voted</u>	
For Stock Incentive Plan	1,639,183
Against Stock Incentive Plan	1,622,050
Withheld Authority	<u>16,239</u>
Total Shares Voted	3,277,472

Item 5. Other Information.

None

Item 6. Exhibits and Reports on Form 8-K.

(a) Exhibits.

31.1 Certification of CEO under Section 302 of the Sarbanes-Oxley Act of 2002.

31.2 Certification of CFO under Section 302 of the Sarbanes-Oxley Act of 2002.

32.1 Certification of CEO under Section 906 of the Sarbanes-Oxley Act of 2002.

32.2 Certification of CFO under Section 906 of the Sarbanes-Oxley Act of 2002.

(b) Reports on Form 8-K.

1) Form 8-K dated April 29, 2004, filed with the Securities and Exchange Commission on April 29, 2004 pursuant to Item 12, regarding the Company's financial results for the first quarter ended March 31, 2004.

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.

ROCKY SHOES & BOOTS, INC.

Date: August 4, 2004

/s/ James E. McDonald
James E. McDonald, Vice President and
Chief Financial Officer*

* In his capacity as Vice President and Chief Financial Officer, Mr. McDonald is duly authorized to sign this report on behalf of the Registrant.