PGT, Inc.
Form 10-Q
November 14, 2006

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UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q

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

For the quarterly period ended September 30, 2006

OR

o **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 000-52059

PGT, Inc.
1070 Technology Drive
North Venice, FL 34275
Registrant s telephone number**: 941-480-1600**

Delaware	**20-0634715**
State of Incorporation	IRS Employer Identification No.

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 þ No o

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

Large accelerated filer o Accelerated filer o Non-accelerated filer þ

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

Yes o No þ

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

Common Stock, $0.01 par value 27,051,525 shares, as of November 10, 2006.

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PART I FINANCIAL INFORMATION

Item 1. Condensed Consolidated Financial Statements

PGT, INC.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(in thousands, except share and per share amounts)

Three months ended	September 30, 2006	October 1, 2005
	(unaudited)	
Net sales	$ 98,324	$ 87,089
Cost of sales	59,089	54,691
Gross margin	39,235	32,398
Stock compensation expense related to dividends paid (includes expenses related to cost of sales and selling, general and administrative expense of $1,290, and $5,315, respectively, in 2005)		6,605
Selling, general and administrative expenses	22,691	21,544
Income from operations	16,544	4,249
Other expense (income), net	439	(86)
Interest expense	7,791	4,022
Income before income tax expense	8,314	313
Income tax expense	3,240	104
Net income	$ 5,074	$ 209
Basic net income per common share	$ 0.20	$ 0.01
Diluted net income per common and common equivalent share	$ 0.18	$ 0.01
Weighted average common shares outstanding:		
Basic	25,920,001	15,720,351
Diluted	27,747,707	17,221,477

The accompanying notes are an integral part of these condensed consolidated financial statements.

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PGT, INC.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(in thousands, except share and per share amounts)

Nine months ended	September 30, 2006	October 1, 2005
	(unaudited)	
Net sales	$ 303,369	$ 244,669
Cost of sales	181,301	155,127
Gross margin	122,068	89,542
Stock compensation expense related to dividends paid (includes expenses related to cost of sales and selling, general and administrative expense of $5,069, and $21,829, respectively in 2006, and $1,290 and $5,315, respectively in 2005)	26,898	6,605
Selling, general and administrative expenses	68,355	59,517
Income from operations	26,815	23,420
Other income, net	(325)	(9)
Interest expense	25,432	10,368
Income before income taxes	1,708	13,061
Income tax expense	686	4,338
Net income	$ 1,022	$ 8,723
Basic net income per common share	$ 0.05	$ 0.55
Diluted net income per common and common equivalent share	$ 0.05	$ 0.51
Weighted average common shares outstanding:		
Basic	19,273,420	15,720,351
Diluted	21,207,499	17,221,477

The accompanying notes are an integral part of these condensed consolidated financial statements.

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PGT, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS
(in thousands, except share amounts)

	September 30, 2006 *(unaudited)*	December 31, 2005
ASSETS		
Current assets:		
Cash and cash equivalents	$ 28,488	$ 3,270
Accounts receivable, net	37,294	45,193
Inventories	13,649	13,981
Deferred income taxes	10,039	3,133
Other current assets	7,249	11,360
Total current assets	96,719	76,937
Property, plant and equipment, net	82,551	65,508
Goodwill	169,648	169,648
Other intangible assets, net	103,311	107,760
Other assets, net	3,083	5,700
Total assets	$ 455,312	$ 425,553
LIABILITIES AND SHAREHOLDERS EQUITY		
Current liabilities:		
Accounts payable and accrued expenses	$ 28,246	$ 31,137
Total current liabilities	28,246	31,137
Long-term debt less current portion	165,488	183,525
Deferred income taxes	54,319	54,320
Total liabilities	248,053	268,982
Shareholders equity:		
Preferred stock, $.01 par value, 10,000,000 shares authorized; zero shares issued and outstanding at September 30, 2006 and zero shares authorized, issued and outstanding at December 31, 2005		
Common stock, $.01 par value, 200,000,000 shares authorized; 27,048,613 shares issued and 26,986,487 shares outstanding at September 30, 2006 and 15,749,483 shares issued and outstanding at December 31, 2005	269	157
Additional paid-in-capital	205,462	152,647
Retained earnings	1,022	
Accumulated other comprehensive income	506	3,767
Total shareholders equity	207,259	156,571

Total liabilities and shareholders equity	$	455,312	$	425,553

The accompanying notes are an integral part of these condensed consolidated financial statements.

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PGT, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(in thousands)

Nine months ended	September 30, 2006	October 1, 2005
	(unaudited)	
Cash flows from operating activities:		
Net income	$ 1,022	$ 8,723
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	7,131	5,361
Stock-based compensation	269	
Excess tax benefits from stock-based compensation plans	(5,341)	
Amortization	4,349	6,015
Deferred Financing	7,107	927
Derivative financial instruments	(325)	(9)
Deferred income taxes	5,911	
Loss on disposal of assets	55	325
Change in operating assets and liabilities:		
Accounts receivable	5,061	(19,904)
Inventories	332	(989)
Other current assets	(3,524)	3,053
Accounts payable and accrued expenses	(2,860)	8,894
Net cash provided by operating activities	**19,187**	**12,396**
Cash flows from investing activities:		
Purchases of property, plant and equipment	(24,234)	(11,322)
Proceeds from sales of equipment and intagibles	105	31
Net cash used in investing activities	**(24,129)**	**(11,291)**
Cash flows from financing activities:		
Net change in revolving line of credit		(2,000)
Net proceeds from initial public offering	129,574	
Exercise of stock options	1,226	
Excess tax benefits from stock-based compensation plans	5,341	
Proceeds from issuance of long-term debt	320,000	190,000
Payment of dividends	(83,484)	(20,000)
Payment of financing costs	(4,459)	(904)
Payment of long-term debt	(338,038)	(166,375)
Net cash provided by financing activities	30,160	721

Net increase in cash and cash equivalents	**25,218**	**1,826**
Cash and cash equivalents at beginning of period	**3,270**	**2,525**
Cash and cash equivalents at end of period	**$ 28,488**	**$ 4,351**
Supplemental cash flow information:		
Interest paid	$ 19,681	$ 10,187
Income taxes paid	$ 1,242	$ 7,949

The accompanying notes are an integral part of these condensed consolidated financial statements.

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PGT, INC.
CONDENSED CONSOLIDATED STATEMENT OF SHAREHOLDERS EQUITY
(in thousands except share amounts)

	Common stock Shares	Common stock Amount	Additional paid-in capital	Retained earnings	Accumulated other comprehensive income (loss)	Total
Balance at December 31, 2005	15,749,483	$ 157	$ 152,647	$	$ 3,767	$ 156,571
Dividends paid			(83,484)			(83,484)
Initial public offering, net of offering costs	10,147,058	101	129,473			129,574
Stock-based compensation			269			269
Exercise of stock options, including tax benefit of $5,342 associated with the exercise of stock options	1,089,946	11	6,557			6,568
Amortization of ineffective interest rate swap					(235)	(235)
Change in fair value of interest rate swap, net of tax benefit of $70					(110)	(110)
Change in fair value of aluminum forward contracts, net of tax benefit of $1,865					(2,916)	(2,916)
Net income				1,022		1,022
Balance at September 30, 2006	26,986,487	$ 269	$ 205,462	$ 1,022	$ 506	$ 207,259

The accompanying notes are an integral part of these condensed consolidated financial statements.

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PGT, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(unaudited)

1. BASIS OF PRESENTATION

The accompanying unaudited consolidated financial statements include the accounts of PGT, Inc. and its wholly-owned subsidiary (the Company) after elimination of intercompany accounts and transactions. These statements have been prepared in accordance with the instructions to Form 10-Q and do not include all of the information and footnotes required by U.S. generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments (consisting only of normal recurring accruals) considered necessary for a fair presentation have been included. All significant intercompany accounts and transactions have been eliminated in consolidation. Operating results for the interim periods are not necessarily indicative of the results that may be expected for the remainder of the current year or for any future periods.

The condensed consolidated balance sheet at December 31, 2005 has been derived from the audited consolidated financial statements at that date but does not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements.

For further information, refer to the consolidated financial statements and footnotes thereto included in the Company s registration statement on Form S-1 (File No. 333-132365) declared effective by the SEC on June 27, 2006.

Stock Split

On June 5, 2006, our board of directors and our stockholders approved a 662.07889-for-1 stock split of our common stock and approved increasing the number of shares of common stock that the Company is authorized to issue to 200.0 million.

After the stock split, effective June 6, 2006, each holder of record held 662.07889 shares of common stock for every 1 share held immediately prior to the effective date. As a result of the stock split, the board of directors also exercised its discretion under the anti-dilution provisions of our 2004 Stock Incentive Plan to adjust the number of shares underlying stock options and the related exercise prices to reflect the change in the per share value and outstanding shares on the date of the stock split. The effect of fractional shares is not material.

Following the effective date of the stock split, the par value of the common stock remained at $0.01 per share. As a result, we have increased the common stock in our consolidated balance sheets and statements of shareholders equity included herein on a retroactive basis for all of our Company s periods presented, with a corresponding decrease to additional paid-in capital. All share and per share amounts and related disclosures have also been retroactively adjusted for all of our Company s periods presented to reflect the 662.07889-for-1 stock split.

New Accounting Pronouncements

In July 2006, the Financial Accounting Standards Board (FASB) issued FASB Interpretation No. 48 (FIN 48), Accounting for Uncertainty in Income Taxes, an interpretation of FASB Statement No. 109, Accounting for Income Taxes. FIN 48 clarifies the accounting for income taxes by prescribing the minimum recognition threshold a tax position is required to meet before being recognized in the financial statements. FIN 48 also provides guidance on de-recognition, measurement, classification, interest and penalties, accounting in interim periods, disclosure and transition. In addition, FIN 48 clearly excludes income taxes from Financial Accounting Standards Board Statement No. 5, *Accounting for Contingencies*. FIN 48 applies to all tax positions related to income taxes subject to Financial Accounting Standards Board Statement No. 109, *Accounting for Income Taxes,* (FAS 109). FIN 48 is effective for fiscal years beginning after December 15, 2006. Differences between the amounts recognized in the statements of financial position prior to the adoption of FIN 48 and the amounts reported after adoption are accounted for as a cumulative-effect adjustment recorded to the beginning balance of retained earnings. The cumulative effect adjustment would not apply to those items that would not have been recognized in earnings. We believe that the adoption of FIN 48 will not have a material impact on our Company s financial position or results of operations.

In September 2006, the Securities and Exchange Commission staff issued Staff Accounting Bulletin No. 108, *Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements* (SAB 108). SAB 108 was issued in order to eliminate the diversity of practice surrounding how public companies quantify financial statement misstatements.

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SAB 108 requires quantification of financial statement misstatements based on the effects of the misstatements on each of a company s financial statements and the related financial statement disclosures. The Company will initially apply the provisions of SAB 108 in connection with the preparation of its annual financial statements for the year ending December 30, 2006. The Company has considered the provisions of SAB 108 and does not expect the initial application of SAB 108 to affect its annual financial statements for the year ending December 30, 2006.

In September 2006, the FASB issued SFAS 157, *Fair Value Measurements* (SFAS 157), which defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements. The provisions of SFAS 157 are effective as of the beginning of the Company s 2008 fiscal year. The Company has considered the provisions of SFAS 157 and does not expect the application of SFAS 157 to have a material effect on its financial statements.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Fiscal Period

Each of our Company s fiscal quarters consist of 13 weeks.

Segment Information

Our Company operates in one operating segment: manufacturer and supplier of windows and doors.

Use of Estimates

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Critical accounting estimates involved in applying our Company s accounting policies are those that require management to make assumptions about matters that are uncertain at the time the accounting estimate was made and those for which different estimates reasonably could have been used for the current period, or changes in the accounting estimate are reasonably likely to occur from period to period, and would have a material impact on the presentation of our Company s financial condition, changes in financial condition or results of operations. Actual results could materially differ from those estimates.

Revenue recognition

We recognize sales when all of the following criteria have been met: a valid customer order with a fixed price has been received; the product has been delivered and accepted by the customer; and collectibility is reasonably assured. All sales recognized are net of allowances for cash discounts and estimated returns, which are estimated using historical experience.

Warranty Expense

Our Company has warranty obligations with respect to most of our manufactured products. Warranty periods, which vary by product component, range from 1 to 10 years. However, the majority of the products sold have warranties on components which range from 1 to 3 years. The reserve for warranties is based on management s assessment of the cost per service call and the number of service calls expected to be incurred to satisfy warranty obligations on recorded net sales. The reserve is determined after assessing our Company s warranty history and specific identification of our estimated future warranty obligations. The following provides information with respect to our Company s warranty accrual:

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Allowance for Warranty	Balance at Beginning of Period	Accruals for Warranties Issued During Period	Adjustments Made	Settlements Made	Balance at End of Period
			(In thousands)		
Three months ended Sept 30, 2006	$4,732	1477	(223)	(1255)	$4,731
Three months ended October 1, 2005	$3,063	2094	266	(1050)	$4,373
Nine months ended Sept 30, 2006	$4,501	4552	(460)	(3862)	$4,731
Nine months ended October 1, 2005	$2,863	3670	638	(2798)	$4,373

Inventories

Inventories consist principally of raw materials purchased for manufacturing of our products. Our Company has limited finished goods inventory since all products are custom, made-to-order products. Finished goods inventory costs include direct materials, direct labor, and overhead. All inventories are stated at the lower of cost (first-in, first-out method) or market value. The reserve for obsolescence is based on management s assessment of the amount of inventory that may become obsolete in the future and is determined based on our Company s history, specific identification method, and consideration of prevailing economic and industry conditions.

Inventories consist of the following:

	September 30, 2006	December 31, 2005
	(in thousands)	
Finished goods	$ 2,116	$ 1,867
Work in progress	919	467
Raw materials	11,642	12,460
Less reserve for obsolescence	(1,028)	(813)
	$ 13,649	$ 13,981

3. Shareholders Equity

Initial Public Offering

On June 27, 2006, the SEC declared our Company s registration statement on Form S-1 effective, and our Company completed an initial public offering (IPO) of 8,823,529 shares of its common stock at a price of $14.00 per share. Our Company s common stock began trading on The Nasdaq National Market under the symbol PGTI on June 28, 2006. After underwriting discounts of approximately $8.6 million and estimated transaction costs of approximately $2.5 million, net proceeds received by the Company on July 3, 2006, were $112.3 million. Our Company used net IPO proceeds, together with cash on hand, to repay $137.0 of borrowings under our senior secured credit facilities. (See Note 7.)

Our Company granted the underwriters an option to purchase up to an additional 1,323,529 shares of common stock at the IPO price, which the underwriters exercised in full on July 27, 2006. After underwriting discounts of approximately $1.3 million, aggregate net proceeds received by the Company on August 1, 2006 were $17.2 million of which $17.0 million was used to repay a portion of our outstanding debt.

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In conjunction with the IPO, our Company s stockholders approved an amendment and restatement of the Company s certificate of incorporation. The amended and restated certificate of incorporation provides that the Company is authorized to issue 200.0 million shares of common stock, par value $0.01 per share, and 10.0 million shares of preferred stock, par value $0.01 per share.

Special Cash Dividends

In February 2006, our Company paid a special cash dividend to our stockholders of $83.5 million. In connection with the payment of this dividend, our Company also made a compensatory cash payment of $26.9 million to stock option holders (including applicable payroll taxes of $0.5 million) in-lieu of adjusting exercise prices, that was recorded as stock compensation expense in the accompanying condensed consolidated statement of operations for the nine months ended September 30, 2006.

In September 2005, our Company paid a special cash dividend to our stockholders of $20.0 million. In connection with the payment of this dividend, our Company also made a compensatory cash payment of $6.6 million to stock option holders (including applicable payroll taxes of $0.2 million) in-lieu of adjusting exercise prices, that was recorded as stock compensation expense in the accompanying condensed consolidated statement of operations for the nine months ended October 1, 2005.

4. NET INCOME PER COMMON SHARE

Net income per common share (EPS) is calculated in accordance with SFAS No. 128, Earnings per Share, which requires the presentation of basic and diluted EPS. Basic EPS is computed using the weighted average number of common shares outstanding during the period. Diluted EPS is computed using the weighted average number of common shares outstanding during the period, plus the dilutive effect of common stock equivalents.

The table below presents a reconciliation of weighted average common shares used in the calculation of basic and diluted EPS for our Company:

	For the Three Months Ended		**For the Nine Months Ended**	
	September 30, 2006	**October 1, 2005**	**September 30, 2006**	**October 1, 2005**
Weighted average common shares for basic EPS	25,920,001	15,720,351	19,273,420	15,720,351
Effect of dilutive stock options	1,827,706	1,501,126	1,934,079	1,501,126
Weighted average common and common equivalent shares for diluted EPS	27,747,707	17,221,477	21,207,499	17,221,477

5. STOCK COMPENSATION

On January 29, 2004, our Company adopted the JLL Window Holdings, Inc. 2004 Stock Incentive Plan (the 2004 Plan), whereby stock-based awards may be granted by the Board of Directors (the Board) to officers, key employees, consultants and advisers of our Company.

In conjunction with the acquisition of PGT Holding Company, our Company rolled over 2.9 million option shares belonging to option holders of the acquired entity. These options have a ten year term and are fully vested. Of these options, 1.1 million have an exercise price of $0.38 per share, and 1.8 million have an exercise price of $1.51 per share.

Also in conjunction with the acquisition, our Company granted 1.6 million option shares to key employees. These options have a ten-year life, fully vest after five years and have an accelerated vesting based on achievement of certain financial targets over three years, with an exercise price of $8.64 per share. On July 5, 2005, and November 30, 2005, our Company granted 0.5 million and 0.2 million option shares, respectively. These options have a ten-year life, fully vest after five years, and have accelerated vesting based on certain financial targets over three years, with an exercise price of $8.64 and $12.84 per share, respectively. There were 36,413 shares of restricted stock granted under the 2004 Plan during the first nine months of 2006. There are 137,094 shares available for grant under the 2004 Plan at September 30, 2006.

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On June 5, 2006, our Company adopted the 2006 Equity Incentive Plan (the 2006 Plan) whereby equity-based awards may be granted by the Board to eligible non-employee directors, selected officers and other employees, advisors and consultants of our Company. There were 172,138 options and 25,713 shares of restricted stock granted under the 2006 Plan during the first nine months of 2006. There are 2,802,149 shares available for grant under the 2006 Plan at September 30, 2006.

We adopted Statement of Financial Accounting Standards No. 123R, Share-Based Payment (SFAS 123R), on January 1, 2006. This statement is a fair-value approach for measuring stock-based compensation and requires us to recognize the cost of employee and non-employee directors services received in exchange for our Company s equity instruments. Under SFAS 123R, we are required to record compensation expense over an award s vesting period based on the award s fair value at the date of grant. We have adopted SFAS 123R on a prospective basis; accordingly, our financial statements for periods prior to January 1, 2006, do not include compensation cost calculated under the fair value method.

Prior to January 1, 2006, our Company applied Accounting Principles Board Opinion 25, Accounting for Stock issued to Employees (APB 25), and therefore recorded the intrinsic value of stock-based compensation as expense. Under APB 25, compensation cost was recorded only to the extent that the exercise price was less than the fair value of our Company s stock on the date of grant. No compensation expense was recognized in previous financial statements under APB 25. Additionally, our Company reported the pro forma impact of using a fair value based approach to valuing stock options under the Statement of Financial Accounting Standards No. 123, Accounting for Stock Based Compensation (SFAS 123).

Stock options granted prior to our Company s initial public offering were valued using the minimum value method in the pro-forma disclosures required by SFAS 123. The minimum value method excludes volatility in the calculation of fair value of stock based compensation. In accordance with SFAS No. 123R, options that were valued using the minimum value method, for purposes of pro forma disclosure under SFAS 123, must be transitioned to SFAS 123R using the prospective method. As a result, these options will continue to be accounted for under the same accounting principles (recognition and measurement) originally applied to those awards in the income statement, which for our Company was APB 25. Accordingly, the adoption of SFAS 123R did not result in any compensation cost being recognized for these options. Additionally, pro forma information previously required under SFAS 123 and SFAS 148 will no longer be presented for these options.

The compensation cost that was charged against income for stock compensation plans was approximately $269,000 for the first nine months of 2006. The total income tax benefit recognized in the condensed consolidated statement of operations for share-based compensation arrangements was approximately $108,000 for the first nine months of 2006.

The fair value of each stock option grant was estimated on the date of grant using a Black-Scholes option-pricing model with the following weighted-average assumptions used for grants under the 2006 Plan in the first nine months of 2006: dividend yield of 0%, expected volatility of 34.5%, risk-free interest rate of 5.2%, and expected life of 7 years.

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Stock Options
A summary of the status of our Company s stock options as of September 30, 2006, and the change during 2006 is presented below:

	Number of Shares Underlying Options *(in thousands)*		Weighted Average Exercise Price
Outstanding at December 31, 2005	4,982	$	4.43
Granted		$	
Exercised		$	
Cancelled	(44)	$	8.64
Outstanding at April 1, 2006	**4,938**	**$**	**4.39**
Granted	172	$	14.00
Exercised		$	
Cancelled		$	
Outstanding at July 1, 2006	**5,110**	**$**	**4.72**
Granted		$	
Exercised	(1,090)	$	1.13
Cancelled		$	
Outstanding at September 30, 2006	**4,020**	**$**	**5.69**

The following table summarizes information about employee stock options outstanding at September 30, 2006 (options are in thousands):

	Options Outstanding			Options Exercisable		
		Weighted Average			Weighted Average	
Exercise Prices	**Outstanding at September 30, 2006**	**Exercise Price**	**Remaining Contractual Life**	**Exercisable at September 30, 2006**	**Exercise Price**	**Remaining Contractual**