

POOL CORP
Form 10-Q
August 09, 2006

**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 June 30, 2006

or

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

For the transition period from _____ to _____

Commission File Number: 0-26640

POOL CORPORATION

(Exact name of Registrant as specified in its charter)

Delaware

0-26640

36-3943363

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(State or other jurisdiction of
incorporation)

(Commission File Number)

(IRS Employer
Identification No.)

109 Northpark Boulevard, Covington, Louisiana
(Address of Principal Executive Offices)

70433-5001
(Zip Code)

Registrant's telephone number, including area code **(985) 892-5521**

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 x NO "

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

Large accelerated filer x

Accelerated Filer "

Non-accelerated filer "

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act) YES " NO x

At August 2, 2006, there were 51,825,352 outstanding shares of the registrant's common stock, \$.001 par value per share.

POOL CORPORATION Form 10-Q For the Quarter Ended June 30, 2006

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

POOL CORPORATION
Consolidated Statements of Income
(Unaudited)
(In thousands, except per share data)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2006	2005	2006	2005
		(As Adjusted - See Note 5)		(As Adjusted - See Note 5)
Net sales	\$ 705,703	\$ 563,978	\$ 1,054,259	\$ 829,139
Cost of sales	496,703	401,297	747,211	594,507
Gross profit	209,000	162,681	307,048	234,632
Selling and administrative expenses	105,662	81,292	188,688	142,987
Operating income	103,338	81,389	118,360	91,645
Interest expense, net	3,856	1,905	6,707	2,985
Income before income taxes and equity earnings (loss)	99,482	79,484	111,653	88,660
Provision for income taxes	38,410	30,717	43,109	34,309

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	Three Months Ended		Six Months Ended	
	1,038	1,942	(12)	460
Equity earnings (loss) in unconsolidated investments				
Net income	\$ 62,110	\$ 50,709	\$ 68,532	\$ 54,811
Earnings per share:				
Basic	\$ 1.18	\$ 0.97	\$ 1.30	\$ 1.05
Diluted	\$ 1.12	\$ 0.91	\$ 1.23	\$ 0.99
Weighted average shares outstanding:				
Basic	52,608	52,491	52,602	52,383
Diluted	55,544	55,782	55,499	55,633
Cash dividends declared per common share	\$ 0.105	\$ 0.090	\$ 0.195	\$ 0.160

The accompanying Notes are an integral part of the Consolidated Financial Statements

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POOL CORPORATION
Consolidated Balance Sheets
(Unaudited)
(In thousands, except share data)

	June 30, 2006	June 30, 2005	December 31, 2005
		(As Adjusted - See Note 5)	(As Adjusted - See Note 5)
Assets			
Current assets:			
Cash and cash equivalents	\$ 32,507	\$ 36,652	\$ 26,866
Receivables, net	76,407	59,540	42,809
Receivables pledged under receivables facility	219,315	172,196	98,976
Product inventories, net	367,096	247,350	330,575
Prepaid expenses	8,493	4,466	5,190
Deferred income taxes	4,004	4,395	7,977
Total current assets	\$ 707,822	\$ 524,599	\$ 512,393
Property and equipment, net	30,289	21,761	25,598
Goodwill	142,177	104,602	139,546
Other intangible assets, net	17,933	10,826	22,838
Equity interest investments	29,882	20,197	29,907

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	June 30, 12,561	June 30, 10,833	December 31, 15,098
Other assets, net			
Total assets	\$ 940,664	\$ 692,818	\$ 745,380
Liabilities and stockholders' equity			
Current liabilities:			
Accounts payable	\$ 207,727	\$ 165,872	\$ 174,170
Accrued and other current liabilities	101,300	57,997	76,645
Short-term financing	150,000	100,000	65,657
Current portion of other long-term liabilities	2,850	1,350	1,350
Total current liabilities	\$ 461,877	\$ 325,219	\$ 317,822
Deferred income taxes	14,048	13,123	14,600
Long-term debt	151,500	70,191	129,100
Other long-term liabilities	2,268	3,202	2,134
Total liabilities	\$ 629,693	\$ 411,735	\$ 463,656
Stockholders' equity:			
Common stock, \$.001 par value; 100,000,000 shares authorized; 51,964,383, 52,604,237 and 52,414,883 shares issued and outstanding at June 30, 2006, June 30, 2005 and December 31, 2005, respectively	51	52	52
Additional paid-in capital	137,654	106,046	119,770
Retained earnings	169,589	172,695	160,684
Treasury stock	--	(93)	(921)
Accumulated other comprehensive income	3,677	2,383	2,139
Total stockholders' equity	\$ 310,971	\$ 281,083	\$ 281,724
Total liabilities and stockholders' equity	\$ 940,664	\$ 692,818	\$ 745,380

The accompanying Notes are an integral part of the Consolidated Financial Statements.

POOL CORPORATION
Condensed Consolidated Statements of Cash Flows
(Unaudited)
(In thousands)

	Six Months Ended June 30,	
	2006	2005
		(As Adjusted -

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Six Months Ended
See Note 5)

Operating activities		
Net income	\$ 68,532	\$ 54,811
Adjustments to reconcile net income to net cash used in operating activities:		
Depreciation	3,833	2,444
Amortization	2,398	1,868
Share-based compensation	4,007	3,007
Excess tax benefits from share-based compensation	(9,363)	(5,554)
Equity losses (earnings) in unconsolidated investments	25	(460)
Other	99	(865)
Changes in operating assets and liabilities, net of effects of acquisitions:		
Receivables	(153,883)	(134,018)
Product inventories	(37,531)	(52,530)
Accounts payable	33,541	52,758
Other current assets and liabilities	39,137	27,531
Net cash used in operating activities	(49,205)	(51,008)
Investing activities		
Acquisition of businesses, net of cash acquired	(1,446)	(3)
Equity interest investment	--	(1,121)
Purchase of property and equipment, net of sale proceeds	(7,723)	(5,575)
Net cash used in investing activities	(9,169)	(6,699)
Financing activities		
Proceeds from revolving line of credit	177,038	147,238
Payments on revolving line of credit	(153,138)	(127,467)
Proceeds from asset-backed financing	93,347	62,170
Payments on asset-backed financing	(9,004)	(4,765)
Payments on other long-term debt	(47)	(47)
Payments of deferred financing costs	(18)	(11)
Payments of capital lease obligations	(257)	--
Excess tax benefits from share-based compensation	9,363	5,554
Issuance of common stock under stock option plans	4,513	1,885
Payment of cash dividends	(10,290)	(8,401)
Purchase of treasury stock	(48,423)	(3,072)
Net cash provided by financing activities	63,084	73,084
Effect of exchange rate changes on cash	931	(487)
Change in cash and cash equivalents	5,641	14,890
Cash and cash equivalents at beginning of period	26,866	21,762
Cash and cash equivalents at end of period	\$ 32,507	\$ 36,652

The accompanying Notes are an integral part of the Consolidated Financial Statements

POOL CORPORATION
Notes to Consolidated Financial Statements
(Unaudited)

Note 1 Summary of Significant Accounting Policies

Pool Corporation (the *Company*, which may be referred to as *POOL*, *we*, *us* or *our*) prepared the unaudited interim consolidated financial statements following accounting principles generally accepted in the United States (GAAP) and the requirements of the Securities and Exchange Commission (SEC) for interim financial information. As permitted under those rules, certain footnotes or other financial information required by GAAP for complete financial statements have been condensed or omitted. In management's opinion, the financial statements include all normal and recurring adjustments that are considered necessary for the fair presentation of our financial position and operating results including the elimination of all significant intercompany accounts and transactions among our wholly owned subsidiaries.

A description of our significant accounting policies is included in our 2005 Annual Report on Form 10-K. The consolidated financial statements should be read in conjunction with the consolidated financial statements and accompanying notes in our Annual Report. The results for the three and six month periods ended June 30, 2006 are not necessarily indicative of the results to be expected for the twelve months ending December 31, 2006.

On January 1, 2006, we adopted Statement of Financial Accounting Standards (SFAS) 123(R), *Share-Based Payments*. We have selected a Black-Scholes-Merton option valuation model for estimating the grant date fair value of share-based payments under SFAS 123(R) and we have elected to use the modified-retrospective transition method. We have adjusted all prior period financial statements to reflect compensation cost for the amounts previously reported in our pro-forma footnote disclosures required by SFAS 123, *Accounting for Stock-Based Compensation* as corrected for immaterial amounts of compensation cost associated with our employee stock purchase plan. Please see Note 5 for additional information.

Reclassifications

We have reclassified the payment of deferred financing costs and the related non-cash amortization of these amounts in our 2005 Condensed Consolidated Statements of Cash Flows to conform to the 2006 presentation. The non-cash amortization was reclassified within the operating activities section to the amortization line item. Additionally, deferred financing costs have been reclassified as a use of cash from financing activities. Previously, we classified these amounts as a change in prepaid and other assets. These reclassifications had no effect on net income or earnings per share as previously reported.

Recent Accounting Pronouncements

In July 2006, the Financial Accounting Standards Board (FASB) issued FASB Interpretation (FIN) No. 48, *Accounting for Uncertainty in Income Taxes - an interpretation of FASB Statement No. 109*, which clarifies the accounting and disclosure for uncertainty in tax positions. FIN 48 seeks to reduce the diversity in practice associated with certain aspects of the measurement and recognition in accounting for income taxes. FIN 48 is effective for fiscal years beginning after December 15, 2006. We are currently evaluating the impact that FIN 48 will have on our financial position and results of operations.

Note 2 Earnings Per Share

We calculate basic earnings per share (EPS) by dividing net income by the weighted average number of common shares outstanding. Diluted EPS includes the dilutive effects of stock and option awards.

POOL CORPORATION
Notes to Consolidated Financial Statements (Continued)
(Unaudited)

The table below presents the reconciliation of basic and diluted weighted average number of shares outstanding and the related EPS calculation (in thousands, except EPS):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2006	2005	2006	2005
Net income	\$ 62,110	\$ 50,709	\$ 68,532	\$ 54,811
Weighted average common shares outstanding:				
Basic	52,608	52,491	52,602	52,383
Effect of dilutive securities:				
Stock options	2,901	3,265	2,860	3,224
Restricted stock awards	32	23	31	21
Employee stock purchase plan	3	3	6	5
Diluted	55,544	55,782	55,499	55,633
Basic earnings per share	\$ 1.18	\$ 0.97	\$ 1.30	\$ 1.05
Diluted earnings per share	\$ 1.12	\$ 0.91	\$ 1.23	\$ 0.99

Note 3 Comprehensive Income

Comprehensive income includes net income, foreign currency translation adjustments and the unrealized gain or loss on interest rate swaps. Comprehensive income was \$63.1 million and \$50.3 million for the three months ended June 30, 2006 and June 30, 2005, respectively and \$70.1 million and \$54.3 million for the six months ended June 30, 2006 and June 30, 2005, respectively.

Note 4 Acquisitions

As discussed in Note 2 of our Annual Report on Form 10-K, in October 2005 we acquired Automatic Rain Company through our newly formed and wholly owned subsidiary Horizon Distributors, Inc. (Horizon). The purchase price for the issued and outstanding stock of Automatic Rain Company was approximately \$87.1 million in cash, which included approximately \$1.4 million in working capital adjustments that were recorded as of December 31, 2005, and paid in the first quarter of 2006.

During the first quarter of 2006, we made a purchase price allocation adjustment that lowered the estimated fair value of non-compete provisions within the employment contracts of certain members of Horizon's management team. We have completed preliminary purchase price allocations for our acquisition of Automatic Rain Company, subject to adjustment should new or additional facts about the business become known. We expect to finalize the allocations by the third quarter of 2006.

POOL CORPORATION
Notes to Consolidated Financial Statements (Continued)
(Unaudited)

Note 5 Share-Based Compensation

As discussed in Note 1, we adopted SFAS 123(R) on January 1, 2006 using a Black-Scholes-Merton option valuation model and the modified retrospective transition method. Prior to January 1, 2006, we accounted for stock option awards under the intrinsic value method prescribed by APB 25, as permitted by SFAS 123. Accordingly, we did not record compensation expense for options issued with an exercise price equal to the stock's market price on the grant date. The impact of the adoption of SFAS 123(R), including adjustments to all prior period financial statements presented, is summarized below.

We award stock options and restricted stock to our employees and non-employee directors under our stock option plans.

Under the 1995 Stock Option Plan (the 1995 Plan) our Board of Directors (the Board) was authorized to grant stock options to employees, agents, consultants or independent contractors. These options generally were exercisable two years after the grant date, and they expire ten years from the grant date. In May 1998, the Board suspended the 1995 Plan. Options granted prior to the suspension were not affected by this action.

In May 1998, our stockholders approved the 1998 Stock Option Plan (the 1998 Plan), which authorized the Board to grant stock options, stock appreciation rights, restricted stock and performance awards to employees, agents, consultants or independent contractors. These options generally were exercisable three or more years after the grant date, and they expire ten years after the grant date. In May 2002, the Board suspended the 1998 Plan. Options granted prior to the suspension were not affected by this action.

In May 2002, our stockholders approved the 2002 Long-Term Incentive Plan (the 2002 Plan), which authorized the Board to grant stock options and restricted stock awards to employees, agents, consultants or independent contractors. In May 2004, our stockholders approved an amendment to increase the number of shares authorized for issuance under the 2002 Plan from 1,575,000 to 2,700,000 shares. Granted options have an exercise price equal to our stock's market price on the grant date. These options generally vest either five years from the grant date or on a three/five year split vest schedule, where half of the options vest three years from the grant date and the remainder vest five years from the grant date. These options expire ten years from the grant date.

The SCP Pool Corporation Non-Employee Directors Equity Incentive Plan permits the Board to grant stock options to each non-employee director. No more than 1,350,000 shares may be issued under this plan. The exercise price of the granted options is equal to our stock's market price on the grant date. The options generally may be exercised one year after the grant date, and they expire ten years after the grant date.

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POOL CORPORATION
Notes to Consolidated Financial Statements (Continued)
(Unaudited)

The following is a summary of the stock option activity under our stock option plans for the six months ended June 30, 2006:

	Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term (years)	Aggregate Intrinsic Value
Balance, December 31, 2005	6,796,687	\$ 10.46		
Granted (at market price)	597,150	38.86		
Exercised	684,674	5.37		
Forfeited	18,435	25.77		
Balance, June 30, 2006	6,690,728	\$ 13.47	5.44	\$ 201,776,865

			Weighted	
Exercisable, June 30, 2006	4,096,331	\$	6.98	4.02 \$ 150,127,616

The following table summarizes the cash proceeds and tax benefits realized from the exercise of stock options:

	Six Months Ended June 30,	
(In thousands, except share data)	2006	2005
Options exercised	684,674	490,886
Cash proceeds	\$ 3,677	\$ 1,335
Intrinsic value of options exercised	\$ 25,600	\$ 14,862
Tax benefits realized	\$ 9,884	\$ 5,828

We estimated the fair value of employee stock option awards at the grant date based on the assumptions summarized in the following table:

	Six Months Ended June 30,	
(Weighted average)	2006	2005
Expected volatility	30.8%	30.3%
Expected term	6.0 years	7.0 years
Risk-free interest rate	4.33%	4.22%
Expected dividend yield	1.0%	1.0%

We calculated expected volatility over the expected term of the awards based on our historical volatility using weekly price observations. We estimated the expected term based on the vesting period of the awards and our historical exercise activity for awards with similar characteristics. The risk-free interest rate is based on the U.S. Treasury zero-coupon issues with a remaining term approximating the expected term of the option. We determined the expected dividend yield based on the anticipated dividends over the expected term.

The weighted average grant date fair value of options granted during the six months ended June 30, 2006 and June 30, 2005 was \$13.26 and \$11.34, respectively. For purposes of recognizing share-based compensation expense, the estimated fair value of employee stock options is ratably expensed over the options' vesting period. We recognize compensation cost for awards with graded vesting using the graded vesting recognition method.

POOL CORPORATION
Notes to Consolidated Financial Statements (Continued)
(Unaudited)

The following is a summary of the restricted stock awards activity under our stock option plans for the six months ended June 30, 2006:

	Shares	Weighted Average Remaining Contractual Term (years)	Aggregate Intrinsic Value
Balance, December 31, 2005	52,400		
Granted (at market price)	--		
Vested	--		
Forfeited	--		

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		Weighted	
Balance, June 30, 2006	52,400	7.32	\$ 2,286,212
Vested, June 30, 2006	2,500	8.12	\$ 109,075

The restricted stock awards generally vest five years from the grant date, and expire ten years from the grant date. At June 30, 2006, the unamortized compensation expense related to the restricted stock awards totaled \$0.6 million, which will be recognized over a weighted average period of 2.4 years.

Prior to the adoption of SFAS 123(R), we recorded restricted stock awards as unearned compensation, a reduction of stockholders' equity, based on the quoted fair market value of our common stock on the date of grant. We adjusted the common stock balances on the date of grant to reflect the issuance of the restricted stock awards. We recorded compensation expense ratably over the vesting period with an offsetting credit to the unearned compensation balance. Under the provisions of SFAS 123(R), restricted stock awards are not deemed to be issued until the end of the vesting period. As such, we eliminated the unearned compensation balance upon adoption and we recognize compensation cost over the requisite service period with an offsetting credit to additional paid-in capital.

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POOL CORPORATION
Notes to Consolidated Financial Statements (Continued)
(Unaudited)

The impact of the adoption of SFAS 123(R) on our Consolidated Statements of Income and Consolidated Statements of Cash Flows is as follows (in thousands, except per share data):

	Six Months Ended June 30,	
	2006	2005
	Increase/ (decrease)	Increase/ (decrease)
Income before income taxes and equity earnings (loss)	\$ (3,862)	\$ (2,451)
Provision for income taxes	(1,379)	(869)
Net income	(2,483)	(1,582)
Basic earnings per share	\$ (0.05)	\$ (0.03)
Diluted earnings per share	\$ (0.04)	\$ (0.02)
Net cash used in operating activities	\$ 520	\$ 632
Net cash provided by financing activities	(520)	(632)

The impact of the adoption of SFAS 123(R) on our Consolidated Balance Sheet at December 31, 2005 is as follows (in thousands):

	Increase/ (decrease)
Deferred income taxes (included in Other assets, net)	\$ 8,744
Additional paid-in capital	23,719
Retained earnings	(15,678)
Unearned compensation	703

In March 1998, the Board adopted the SCP Pool Corporation Employee Stock Purchase Plan. Under this plan, employees who meet minimum age and length of service requirements may purchase stock at 85% of the lower of:

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- a. the closing price of our common stock at the end of a six month period ending either June 30 or December 31; or
- b. the average of the beginning and ending closing prices of our common stock for such six month period.

No more than 956,250 shares of our common stock may be issued under this plan. We awarded 31,131 shares under this plan during the six months ended June 30, 2006 and 22,707 shares under this plan during the six months ended June 30, 2005. Share-based compensation expense related to the Employee Stock Purchase Plan was \$0.3 million for the six months ended June 30, 2006 and \$0.2 million for the six months ended June 30, 2005. The grant date fair value for the purchase period ended June 30, 2006 was \$9.52 per share and \$6.62 per share for the purchase period ended June 30, 2005.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

You should read the following discussion in conjunction with Management's Discussion and Analysis included in our 2005 Annual Report on Form 10-K.

OVERVIEW

Financial Results

Net sales grew 25% to \$705.7 million in the second quarter of 2006 compared to \$564.0 million in 2005. Base business sales growth of 13% contributed \$70.5 million to the increase with the remaining increase attributable to acquired and new sales centers, including the Horizon business acquired in October 2005.

Our base business sales growth continues to reflect the growth in the installed base of swimming pools, our execution of sales, marketing and service programs that we offer to our customers, growth in complementary product sales and passing on inflationary price increases. In the second quarter of 2006, complementary product sales grew 23% compared to the same period in 2005. The impact of weather on sales in the quarter was mixed. Above normal temperatures across much of the country benefited maintenance and impulse sales, while heavy rainfall in certain regions delayed some pool construction.

Our gross profit as a percent of net sales (gross margin) increased 80 basis points to 29.6% in the second quarter of 2006 from 28.8% in the second quarter of 2005. This increase is attributable primarily to the benefits achieved through our supply chain management initiatives, including favorable sales mix from our focus on higher margin products and the benefits of forward inventory purchases since the fourth quarter of 2005.

Our operating income increased 27% to \$103.3 million in the second quarter of 2006 while operating margin expanded 20 basis points to 14.6% of sales despite the inclusion of the lower operating margins of Horizon in 2006. The growth in sales and gross margins were more than enough to offset slightly higher selling and operating expense growth. Net income increased 22% compared to the same period in 2005 and included \$1.0 million of net equity earnings from our investment in Latham Acquisition Corporation (LAC).

Financial Position and Liquidity

Consistent with the increase in net sales, accounts receivable increased \$64.0 million to \$295.7 million at June 30, 2006 from \$231.7 million at June 30, 2005. Days sales outstanding (DSO) increased between periods to 34.0 days at June 30, 2006 compared to 33.3 days at June 30, 2005 as a result of the addition of Horizon's receivables which have slightly longer collection cycles. Excluding Horizon, DSO improved by half a day over 2005.

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Our inventory levels increased 48% to \$367.1 million as of June 30, 2006, compared to June 30, 2005, due to the Horizon acquisition, additional pre-price increase inventory purchases made in the first half of the year, the increased level of base business sales, new sales center inventory and increased stocking levels for certain higher margin products. As a result of this increase, our inventory turns have slowed to 4.0 times as of June 30, 2006 from 4.5 times as of June 30, 2005. However, our inventory quality remains high as measured by the percentage of inventory in our fastest-turning inventory classes. Our slowest moving class of inventory as a percentage of total inventory remained consistent quarter over quarter.

Total debt outstanding increased 76% to \$306.6 million at June 30, 2006 compared to \$174.7 at June 30, 2005. This increase is attributable to increased borrowings to fund the Horizon acquisition, additional working capital and our second quarter share repurchases. We continue to maintain a healthy current ratio, which was down slightly to 1.5 as of June 30, 2006 compared to 1.6 as of June 30, 2005.

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Recent Developments

In August 2006, we acquired Wickham Supply, Inc. and Water Zone, LP (collectively Wickham), a leading regional irrigation products distributor in Texas. Wickham operates 14 distribution sales centers with 13 locations throughout Texas and one location in Georgia. Wickham's net sales are expected to approximate \$50.0 million for fiscal 2006. This transaction, which is expected to be accretive in 2007 and beyond, expands our footprint in the \$3 plus billion irrigation and landscape distribution marketplace by providing a significant presence in the strategically important Texas market. We funded this transaction through utilization of our existing bank facilities.

With the recent focus on public company stock option practices, we elected to conduct an internal review of our annual stock option grants since our initial public offering in 1995. During this review, we identified certain issues with our historical option granting process, including instances in which the grant dates and exercise prices approved by the Compensation Committee of our Board of Directors for the certain annual option grants differed from the grant dates and option exercise prices set forth in the respective employee stock option agreements for such grants. As a result, we will modify these stock option agreements to reflect the proper grant dates and exercise prices.

Based on our review, we concluded that there is no material impact to our prior period financial statements. As such, we are not required to restate our previously filed financial statements.

Outlook

Based on our financial results through the first half of 2006, we expect earnings per share for the year ending December 31, 2006 will be approximately \$1.80 per diluted share, including an expected \$0.08 impact from stock option expensing.

Our business is subject to significant risks, including weather, competition, general economic conditions and other risks detailed in Part II Item 1A. Risk Factors and our Cautionary Statement for Purpose of the Safe Harbor Provisions of the Private Securities Litigation Reform Act of 1995.

RESULTS OF OPERATIONS

As of June 30, 2006, we conducted operations through 256 sales centers in North America and Europe.

The following table presents information derived from the Consolidated Statements of Income expressed as a percentage of net sales.

	Three Months Ended June 30,		Six Months Ended June 30,	
	2006	2005	2006	2005
Net sales	100.0%	100.0%	100.0%	100.0%
Cost of sales	70.4	71.2	70.9	71.7

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	Three Months Ended		Six Months Ended	
Gross profit	29.6	28.8	29.1	28.3
Selling and administrative expenses	15.0	14.4	17.9	17.2
Operating income	14.6	14.4	11.2	11.1
Interest expense	0.5	0.3	0.6	0.4
Income before income taxes and equity earnings (loss)	14.1	14.1	10.6	10.7

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The following discussion of consolidated operating results includes the operating results from acquisitions in 2005 and 2004. We accounted for these acquisitions using the purchase method of accounting, and we have included the results of operations in our consolidated results since the respective acquisition dates.

We exclude the following sales centers from base business for 15 months:

- acquired sales centers;
- sales centers divested or consolidated with acquired sales centers; and
- new sales centers opened in new markets.

Additionally, we generally allocate overhead expenses to acquired sales centers on the basis of acquired sales center net sales as a percentage of total net sales.

Three Months Ended June 30, 2006 Compared to Three Months Ended June 30, 2005

(Unaudited) (In thousands)	Base Business Three Months Ended June 30,		Acquired Three Months Ended June 30,		Total Three Months Ended June 30,	
	2006	2005	2006	2005	2006	2005
Net sales	\$ 634,489	\$ 563,978	\$ 71,214	\$ --	\$ 705,703	\$ 563,978
Gross profit	187,554	162,681	21,446	--	209,000	162,681
Gross margin	29.6%	28.8%	30.1%	--	29.6%	28.8%
Selling and administrative expenses	92,286	81,292	13,376	--	105,662	81,292
Expenses as a % of net sales	14.6%	14.4%	18.8%	--	15.0%	14.4%
Operating income	95,268	81,389	8,070	--	103,338	81,389
Operating income margin	15.0%	14.4%	11.3%	--	14.6%	14.4%

For purposes of comparing operating results for the three months ended June 30, 2006 to the three months ended June 30, 2005, 210 sales centers were included in the base business calculations and 46 sales centers were excluded because they were acquired or opened in new markets within the last 15 months. The effect of sales center acquisitions in the table above includes the operations of the following:

Acquired	Acquisition Date	Period Excluded ⁽¹⁾
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Acquired	Acquisition Date	Period Excluded ⁽¹⁾
B&B s.r.l. (Busatta)	October 2005	April - June 2006
Direct Replacements, Inc.	October 2005	April - June 2006
Horizon Distributors, Inc.	October 2005	April - June 2006

⁽¹⁾ After 15 months of operations, we include acquired sales centers in the base business calculation including the comparative prior year period.

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Net Sales

(in millions)	Three Months Ended June 30,		Change	
	2006	2005		
Net sales	\$ 705.7	\$ 564.0	\$ 141.7	25%

Base business sales growth was 13% in the second quarter of 2006. Net sales increased primarily due to the following:

- a larger installed base of swimming pools resulting in increased sales of non-discretionary products;
- the continued successful execution of our sales, marketing and service programs, resulting in market share gains;
- price increases, which were passed through the supply chain; and
- 23% growth in complementary product sales.

The complementary product sales growth rate slowed to 23% in the second quarter of 2006 due primarily to flat spa sales resulting from supplier capacity issues. We have added additional spa suppliers to meet the market demand and expect our complementary product sales growth rate to improve as the growth rate for spa sales returns to a more normalized level.

The remaining increase in net sales is attributable to acquired and new sales centers. Including Horizon's second quarter 2006 sales, complementary product sales grew 160% over the second quarter of 2005 and accounted for 17% of total net sales.

Gross Profit

(in millions)	Three Months Ended June 30,		Change	
	2006	2005		
Gross profit	\$ 209.0	\$ 162.7	\$ 46.3	29%
Gross margin	29.6%	28.8%	0.8%	

Gross margin increased 80 basis points between periods due primarily to the benefits achieved through our supply chain management initiatives, including favorable sales mix from our focus on higher margin products and the benefits from our forward inventory purchases.

Operating Expenses

(in millions)	Three Months Ended June 30,		Change	
	2006	2005		
Operating expenses	\$ 105.7	\$ 81.3	\$ 24.4	30%

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Three Months Ended June 30,

Operating expenses as a percentage of net sales **15.0%** 14.4% 0.6%

Compared to second quarter of 2005, operating expenses grew 30% and increased 60 basis points as a percentage of net sales. This increase is due primarily to the addition of Horizon's operating expenses, which include amortization expense related to the Horizon acquisition, start-up costs and higher expense ratios for new pool sales centers, higher incentive compensation and increased promotional costs. Base business operating expenses were 14% higher in the second quarter of 2006 compared to the same period in 2005 and relatively consistent as a percentage of sales.

Interest Expense

Interest expense increased \$2.0 million between periods due to a 47% increase in the average debt outstanding compared to the second quarter of 2005 and an increase in the effective interest rate to 5.6% in 2006 from 3.9% in 2005.

Income Taxes

The increase in income taxes is due to the \$20.0 million increase in income before income taxes and equity earnings. Our effective income tax rate was 38.6% at June 30, 2006 and June 30, 2005.

Net Income and Earnings Per Share

Net income increased 23% to \$62.1 million in the second quarter of 2006 from \$50.7 million in the second quarter of 2005. The 2006 amount included \$1.0 million of net equity earnings from our investment in LAC, down from \$1.9 million for the same period last year due to additional taxes now accrued on this income. Diluted earnings per share increased 23% to \$1.12 per share in the second quarter of 2006 compared to \$0.91 per share in the second quarter of 2005.

Six Months Ended June 30, 2006 Compared to Six Months Ended June 30, 2005

(Unaudited) (In thousands)	Base Business Six Months Ended June 30,		Acquired Six Months Ended June 30,		Total Six Months Ended June 30,	
	2006	2005	2006	2005	2006	2005
Net sales	\$ 936,674	\$ 827,345	\$ 117,585	\$ 1,794	\$ 1,054,259	\$ 829,139
Gross profit	272,907	234,137	34,141	495	307,048	234,632
Gross margin	29.1%	28.3%	29.0%	27.6%	29.1%	28.3%
Selling and administrative expenses	162,857	142,430	25,831	557	188,688	142,987
Expenses as a % of net sales	17.4%	17.2%	22.0%	31.0%	17.9%	17.2%
Operating income (loss)	110,050	91,707	8,310	(62)	118,360	91,645
Operating income (loss) margin	11.8%	11.1%	7.1%	(3.5)%	11.2%	11.1%

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For purposes of comparing operating results for the six months ended June 30, 2006 to the six months ended June 30, 2005, 207 sales centers were included in the base business calculations and 49 sales centers were excluded because they were acquired or opened in new markets within the last 15 months. The effect of sales center acquisitions in the table above includes the operations of the following:

Acquired	Acquisition Date	Period Excluded ⁽¹⁾
Pool Tech Distributors, Inc.	December 2004	January - February 2006 and 2005
B&B s.r.l. (Busatta)	October 2005	January - June 2006
Direct Replacements, Inc.	October 2005	January - June 2006
Horizon Distributors, Inc.	October 2005	January - June 2006

⁽¹⁾ After 15 months of operations, we include acquired sales centers in the base business calculation including the comparative prior year period.

Net Sales

(in millions)	Six Months Ended June 30,		Change	
	2006	2005		
Net sales	\$ 1,054.3	\$ 829.1	\$ 225.2	27%

Base business sales growth was 13% in the first six months of 2006. Net sales increased primarily due to the following:

- a larger installed base of swimming pools resulting in increased sales of non-discretionary products;
- price increases, which were passed through the supply chain;
- the continued successful execution of our sales, marketing and service programs resulting in market share gains; and
- 27% growth in complementary product sales.

The remaining increase in net sales is attributable to acquired and new sales centers. Including Horizon's 2006 year to date sales, complementary product sales grew 172% over the first six months of 2005 and accounted for 19% of total net sales.

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Gross Profit

(in millions)	Six Months Ended June 30,		Change	
	2006	2005		
Gross profit	\$ 307.0	\$ 234.6	\$ 72.4	31%
Gross margin	29.1%	28.3%	0.8%	

Gross margin increased 80 basis points between periods due primarily to the benefits achieved through our supply chain management initiatives, including the benefits of our forward inventory purchases in the fourth quarter of 2005 and a shift in product mix to higher margin products compared to the first six months of 2005.

Operating Expenses

Six Months Ended June 30,

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Six Months Ended June 30,

(in millions)	2006	2005	Change
Operating expenses	\$ 188.7	\$ 143.0	\$ 45.7 32%
Operating expenses as a percentage of net sales	17.9%	17.2%	0.7%

Operating expenses grew 32% and as a percentage of net sales increased 70 basis points from the first six months of 2005 due primarily to the addition of Horizon's operating expenses, which include amortization expense related to the Horizon acquisition. Base business operating expenses were 14% higher in the first six months of 2006 compared to the same period in 2005 and only slightly higher as a percentage of sales. The increase in base business operating expenses is due to higher incentive compensation, higher share-based compensation costs due largely to accelerated expense for options issued to retirement eligible employees, expenses for newly opened pool sales centers and increased promotional costs.

We opened twelve sales centers in the first half of 2006 compared to only three sales centers in the first half of 2005. The sales centers opened in 2006 include nine new pool sales centers and three new Horizon sales centers. The increase in operating expenses related to new sales centers also includes start-up costs for two sales centers opened in early July 2006.

Interest Expense

Interest expense increased \$3.7 million between periods as average debt outstanding was 65% higher in the first six months of 2006 compared to the first six months of 2005 and the effective interest rate increased to 5.4% in 2006 from 3.8% in 2005.

Income Taxes

The increase in income taxes is due to the \$23.0 million increase in income before income taxes and equity earnings (loss). Our effective income tax rate was 38.6% at June 30, 2006 and June 30, 2005.

Net Income and Earnings Per Share

Net income increased 25% to \$68.5 million in the first six months of 2006 from \$54.8 million in the first six months of 2005. Our equity interest in LAC produced a small loss in the first six months of 2006. For the year, we expect a positive contribution to our earnings from LAC.

Earnings per share for the first six months of 2006 increased 24% to \$1.23 per diluted share compared to \$0.99 in the first six months of 2005.

Seasonality and Quarterly Fluctuations

Our business is highly seasonal. In general, sales and operating income are highest during the second and third quarters, which represent the peak months of both swimming pool use and installation and landscape installations and maintenance. Sales are substantially lower during the first and fourth quarters when we may incur net losses.

We typically experience a build-up of product inventories and accounts payable during the winter months in anticipation of the peak selling season. Excluding borrowings to finance acquisitions and share repurchases, our peak borrowing usually occurs during the second quarter, primarily because extended payment terms offered by our suppliers typically are payable in April, May and June, while our peak accounts receivable collections typically occur in June, July and August.

The following table presents certain unaudited quarterly data for the first and second quarters of 2006, the four quarters of 2005 and the third and fourth quarters of 2004. We have included income statement and balance sheet data for the most recent eight quarters to allow for a meaningful comparison of the seasonal fluctuations in these amounts. In our opinion, this information reflects all normal and recurring adjustments considered necessary for a fair presentation of this data. Due to the seasonal nature of our industry, the results of any one or more quarters are

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not necessarily an accurate indication of results for an entire fiscal year or of continuing trends.

(Unaudited)

QUARTER

(in thousands)	QUARTER							
	2006		2005 ⁽¹⁾				2004 ⁽¹⁾	
	Second	First	Fourth	Third	Second	First	Fourth	Third
Statement of Income Data								
Net sales	\$ 705,703	\$ 348,556	\$ 299,791	\$ 423,729	\$ 563,978	\$ 265,161	\$ 209,937	\$ 362,091
Gross profit	209,000	98,048	83,211	114,605	162,681	71,951	56,404	104,183
Operating income (loss)	103,338	15,022	2,288	41,431	81,389	10,256	(5,013)	35,908
Net income (loss)	62,110	6,422	(876)	26,521	50,709	4,102	(3,656)	21,360

Balance Sheet Data

Total receivables, net	\$ 295,722	\$ 211,578	\$ 141,785	\$ 152,037	\$ 231,736	\$ 164,507	\$ 97,589	\$ 130,360
Product inventories, net	367,096	406,310	330,575	197,135	247,350	281,267	195,787	167,024
Accounts payable	207,727	267,296	174,170	99,920	165,872	219,290	113,114	76,454
Total debt	306,618	239,712	198,241	86,922	174,743	145,045	97,505	102,197

- (1) As adjusted to reflect the impact of share-based compensation expense related to the adoption of SFAS 123(R) using the modified retrospective transition method. For additional information, see Note 5 of Notes to Consolidated Financial Statements included in Item 1 of this Form 10-Q.

In the fourth quarter of 2005 and first two quarters of 2006, our results of operations include the Horizon business acquired in October 2005. We expect that our quarterly results of operations will continue to fluctuate depending on the timing and amount of revenue contributed by new and acquired sales centers. We attempt to open new sales centers at the end of the fourth quarter or the first quarter of the subsequent year to take advantage of preseason sales programs and the following peak selling season.

Weather is the principal external factor affecting our business. The table below presents some of the possible effects resulting from various weather conditions.

Weather	Possible Effects
Hot and dry	Increased purchases of chemicals and supplies for existing swimming pools Increased purchases of above-ground pools and irrigation products
Unseasonably cool weather or extraordinary amounts of rain	Fewer pool and landscape installations Decreased purchases of chemicals and supplies Decreased purchases of impulse items such as above-ground pools and accessories

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Unseasonably early warming trends in spring /
late cooling trends in fall

A longer pool and landscape season, thus
increasing our sales

(primarily in the northern half of the US)

Unseasonably late warming trends in spring /
early cooling trends in fall

A shorter pool and landscape season, thus
decreasing our sales

(primarily in the northern half of the US)

In the second quarter of 2006, our sales benefited from record high temperatures across most of North America but rain hindered sales in western and northern markets.

LIQUIDITY AND CAPITAL RESOURCES

Liquidity is defined as the ability to generate adequate amounts of cash to meet current cash needs. We assess our liquidity in terms of our ability to generate cash to fund our operating activities, taking into consideration the seasonal nature of our business. Significant factors which could affect our liquidity include the following:

- cash flows generated from operating activities;
- the adequacy of available bank lines of credit;
- acquisitions;
- the timing and extent of share repurchases;
- capital expenditures;
- dividend payments; and
- the ability to attract long-term capital with satisfactory terms.

Our primary capital needs are seasonal working capital obligations and other general corporate purposes, including acquisitions, share repurchases and dividend payments. Our primary sources of working capital are cash from operations supplemented by bank borrowings, which combined with seller financing have historically been sufficient to support our growth and finance our acquisitions. The same principle applies for funds used for share repurchases and capital expenditures. Our priorities for the use of cash are as follows:

- maintenance and new sales center capital expenditures estimated at 0.5% to 0.75% of net sales;
- strategic acquisitions executed opportunistically;
- payment of cash dividends as and when declared by the Board of Directors;
- repurchase of common stock at Board-defined parameters; and
- repayment of debt.

Sources and Uses of Cash

The following table summarizes our cash flows (in thousands):

	Six Months Ended June 30,	
	2006	2005
Operating activities	\$ (49,205)	\$ (51,008)
Investing activities	(9,169)	(6,699)
Financing activities	63,084	73,084

Cash flow used in operations decreased \$1.8 million to \$49.2 million in the first six months of 2006 compared to \$51.0 million in the same period in 2005. We used most of the increase in our net income to fund our working capital investment. Through the second quarter of 2006, we continued to benefit from the deferral of our estimated federal tax payments due to the provisions of hurricane tax relief offered by the Internal

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Revenue Service. During the quarter, we repurchased 1.0 million shares of our common stock, using \$43.8 million in borrowing capacity to fund these purchases.

Future Sources and Uses of Cash

Our unsecured syndicated senior credit facility (the Credit Facility), which matures on December 20, 2010, provides for a \$120.0 million five-year revolving credit facility (the Revolver) and a \$60.0 million term loan (the Term Loan). The Credit Facility includes sublimits for the issuance of swingline loans and standby letters of credit. The aggregate maximum principal amount of the commitments under the Credit Facility may be increased from time to time by a total amount up to \$40.0 million.

At June 30, 2006, there was \$93.0 million outstanding and \$25.8 million available for borrowing under the Revolver. The average effective interest rate on the Revolver was approximately 5.6% for the six months ended June 30, 2006.

At June 30, 2006, there was \$60.0 million outstanding under the Term Loan. Since our first scheduled principal payment on the Term Loan of \$750,000 is due on March 31, 2007, this amount is classified as current as of June 30, 2006. The average effective interest rate of the Term Loan was approximately 5.3% for the six months ended June 30, 2006.

Our obligations under the Credit Facility are guaranteed by certain of our existing and future domestic subsidiaries. The Credit Facility contains terms and provisions (including representations, covenants and conditions) and events of default customary for transactions of this type. If an event of default occurs and is continuing under the Credit Facility, the lenders may terminate their obligations thereunder and may require us to repay all amounts thereunder. For additional information regarding the Credit Facility, see Note 5 of Notes to Consolidated Financial Statements, included in our 2005 Annual Report on Form 10-K.

In March 2006, we renewed our accounts receivable securitization facility (the Receivables Facility), which provides a seasonal borrowing capacity of up to \$150.0 million, through March 2007. The Receivables Facility provides for the true sale of certain of our receivables as they are created to a wholly-owned, bankruptcy-remote subsidiary. This subsidiary grants an undivided security interest in the receivables to an unrelated commercial paper conduit. Because of the structure of the bankruptcy-remote subsidiary and our ability to control its activities, we include the transferred receivables and related debt in our Consolidated Balance Sheet. We continue to employ this arrangement because it provides us with a lower cost form of financing. At June 30, 2006, there was \$150.0 million outstanding under the Receivables Facility at an average effective interest rate of 5.4%.

As of June 30, 2006, we were in compliance with all covenants and financial ratio requirements related to our Credit Facility and our Receivables Facility.

In the third quarter of 2006, we repurchased approximately \$6.1 million, or 151,400 shares, of our common stock on the open market at an average share price of \$40.55. This used most of the remaining amount of our existing share repurchase authorization. In August 2006, our Board of Directors (our Board) increased the authorization for the repurchase of shares of our common stock in the open market to \$50.0 million, all of which remained available as of August 7, 2006. We intend to continue to repurchase shares on the open market from time to time, depending on market conditions. We may use cash flows from operations to fund these purchases, or we may incur additional debt.

The third quarter normally generates strong seasonal cash flows from operating activities. This trend will continue in the third quarter of 2006, although our cash flows from operating activities will be negatively impacted by the payment of approximately \$60.0 million for estimated federal tax payments, partially offset by lower inventory purchases as a result of pre-price increase inventory purchases made in the second quarter of 2006. The tax payments include deferred taxes from the second half of 2005 and the first half of 2006 as allowed by the Katrina Emergency Tax Relief Act of 2005.

In the third quarter of 2006, our cash flows will also be impacted by our acquisition of Wickham in August 2006. We funded this transaction through borrowings under our existing bank facilities.

We believe we have adequate availability of capital to fund present operations and anticipated growth, including expansion in existing and targeted market areas. We continually evaluate potential acquisitions and hold discussions with acquisition candidates. If suitable acquisition opportunities or working capital needs arise that would require additional financing, we believe that our financial position and earnings history provide a solid base for obtaining additional financing resources at competitive rates and terms. Additionally, we may issue common or preferred stock to raise funds.

CRITICAL ACCOUNTING ESTIMATES

We prepare our consolidated financial statements in accordance with accounting principles generally accepted in the United States (GAAP), which requires management to make estimates and assumptions that affect reported amounts and related disclosures. Management identifies critical accounting estimates as:

those that require the use of assumptions about matters that are inherently and highly uncertain at the time the estimates are made; and those for which changes in the estimate or assumptions, or the use of different estimates and assumptions, could have a material impact on our consolidated results of operations or financial condition.

Management has discussed the development, selection and disclosure of our critical accounting estimates with the Audit Committee of our Board of Directors. For a description of our critical accounting estimates that require us to make the most difficult, subjective or complex judgments, please see our Annual Report on Form 10-K for the year ended December 31, 2005. We have not changed these policies from those previously disclosed.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Interest Rate Risk

There have been no material changes from what we reported in our Form 10-K for the year ended December 31, 2005.

Foreign Exchange Risk

There have been no material changes from what we reported in our Form 10-K for the year ended December 31, 2005.

Item 4. Controls and Procedures

The term disclosure controls and procedures is defined in Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934 (the Act). The rules refer to the controls and other procedures designed to ensure that information required to be disclosed in reports that we file or submit under the Act is recorded, processed, summarized and reported within the time periods specified. As of June 30, 2006, management, including the CEO and CFO, performed an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures. Based on that evaluation, management, including the CEO and CFO, concluded that as of June 30, 2006, our disclosure controls and procedures were effective at ensuring that material information related to us or our consolidated subsidiaries is made known to them and is disclosed on a timely basis in our reports filed under the Act.

We maintain a system of internal control over financial reporting that is designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with accounting principles generally accepted in the United States. Based on the most recent evaluation, we have concluded that no change in our internal control over financial reporting occurred during the last fiscal quarter that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II. OTHER INFORMATION

Item 1A. Risk Factors

Cautionary Statement for Purposes of the Safe Harbor Provisions of the Private Securities Litigation Reform Act of 1995

Our disclosure and analysis in this report contains forward-looking information that involves risks and uncertainties. Our forward-looking statements express our current expectations or forecasts of possible future results or events, including projections of future performance, statements of management's plans and objectives, future contracts, and forecasts of trends and other matters. You can identify these statements by the fact that they do not relate strictly to historic or current facts and often use words such as "anticipate," "estimate," "expect," "believe," "will likely result," "outlook," "project" and other words and expressions of similar meaning. No assurance can be given that the results in any forward-looking statements will be achieved and actual results could be affected by one or more factors, which could cause them to differ materially. For these statements, we claim the protection of the safe harbor for forward-looking statements contained in the Private Securities Litigation Reform Act.

Risk Factors

Certain factors that may affect our business and could cause actual results to differ materially from those expressed in any forward-looking statements include the following:

We are susceptible to adverse weather conditions.

Weather is the principal external factor affecting our business. For example, unseasonably late warming trends can decrease the length of the pool season and unseasonably cool weather or extraordinary rainfall during the peak season can decrease swimming pool use, installation and maintenance, as well as landscape installations and maintenance. These weather conditions adversely affect sales of our products. For a discussion regarding seasonality and weather, see Part I Item 2, Management's Discussion and Analysis of Financial Condition and Results of Operations—Seasonality and Quarterly Fluctuations.

Our distribution business is highly dependent on our ability to maintain favorable relationships with suppliers and manufacturers.

As a distribution company, maintaining favorable relationships with our suppliers is critical to the success of our business. We believe that we add considerable value to the swimming pool supply chain and landscape supply chain by purchasing products from a large number of manufacturers and distributing the products to a highly fragmented customer base on conditions that are more favorable than these customers could obtain on their own. We believe that we currently enjoy good relationships with our suppliers, who generally offer us competitive pricing, return policies and promotional allowances. However, our inability to maintain favorable relationships with our suppliers could have an adverse effect on our business.

Our largest suppliers are Pentair Corporation, Hayward Pool Products, Inc. and Waterpik Technologies, Inc., which accounted for approximately 20%, 13% and 7%, respectively, of the costs of products we sold in 2005. While we do not believe that the loss of any single supplier would adversely affect our business, a decision by several suppliers, acting in concert, to sell their products directly to retail customers and other end-users of their products, bypassing distribution companies like ours, would have an adverse effect on our business. We dedicate significant resources to promote the benefits and affordability of pool ownership, which we believe greatly benefits our swimming pool customers and suppliers.

We face intense competition both from within our industry and from other leisure product alternatives.

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We face competition from both inside and outside of our industry. Within our industry, we compete against various regional and local distributors and, to a lesser extent, mass market retailers and large pool supply retailers. Outside of our industry, we compete with sellers of other leisure product alternatives, such as boats and motor homes, and with other companies who rely on discretionary homeowner expenditures, such as home remodelers. New competitors may emerge as there are low barriers to entry in our industry. Some geographic markets that we serve, particularly our largest, higher density markets in California, Florida, Texas and Arizona, representing approximately 54% of our net sales in 2005, also tend to be more competitive than others.

More aggressive competition by mass merchants could adversely affect our sales.

Mass market retailers today carry a limited range of, and devote a limited amount of shelf space to, merchandise and products targeted to our industry. Historically, mass market retailers have generally expanded by adding new stores and product breadth, but their product offering of pool and landscape related products has remained relatively constant. Should mass market retailers increase their focus on the pool or professional landscape industries, or increase the breadth of their pool and landscape related product offerings, they may become a more significant competitor for direct and end-use customers which could have an adverse impact on our business.

The demand for our swimming pool and related outdoor lifestyle products may be adversely affected by economic downturns.

In economic downturns, the demand for swimming pool or leisure related products may decline as discretionary consumer spending, the increase in pool eligible households and swimming pool construction decline. Although maintenance products and repair and replacement equipment that must be purchased by pool owners to maintain existing swimming pools account for more than 60% of our gross profits, the growth of our business depends on the expansion of the installed pool base, which may be viewed by most consumers as a discretionary expenditure that may be adversely affected by economic downturns.

We depend on key personnel.

We consider our employees to be the foundation for our growth and success. As such, our future success depends in large part on our ability to attract, retain and motivate qualified personnel, including our executive officers and key management personnel. If we are unable to attract and retain key personnel, our operating results could be adversely affected.

Specifically, our future success depends to an extent upon the continued service of Manuel Perez de la Mesa, our Chief Executive Officer. The loss of Mr. Perez de la Mesa in particular could have a material adverse effect on our business. Mr. Perez de la Mesa is not nearing retirement age, and we have no indication that he intends to retire in the near future. We do not currently maintain key man insurance on Mr. Perez de la Mesa.

We may not be able to sustain our pace of growth.

We have experienced substantial sales growth in recent years through acquisitions and new sales center openings that have increased our size, scope and geographic distribution. Since 2001, we have opened 33 new sales centers and have completed 13 acquisitions including our acquisition of Horizon in October 2005. These acquisitions have added 93 sales centers, net of sales center closings and consolidations, and a centralized shipping location to our distribution networks. While we contemplate continued growth through acquisitions and internal expansion, no assurance can be made as to our ability to:

- penetrate new markets;
- identify appropriate acquisition candidates;
- complete acquisitions on satisfactory terms and successfully integrate acquired businesses;
- obtain financing;
- generate sufficient cash flows to support expansion plans and general operating activities;
- maintain favorable supplier arrangements and relationships; and
- identify and divest assets which do not continue to create value consistent with our objectives.

If we do not manage these potential difficulties successfully, our operating results could be adversely affected.

The growth of our business depends on effective marketing programs.

The growth of our business depends on the expansion of the installed pool base. Thus, an important part of our strategy is to promote the growth of the pool industry through our extensive advertising and promotional programs that attempt to raise consumer awareness regarding the benefits and affordability of pool ownership, the ease of pool maintenance and the many ways in which a pool may be enjoyed beyond swimming. These programs include media advertising, website development such as www.swimmingpool.com and public relations campaigns. We believe these programs benefit the entire supply chain from our suppliers to our customers.

We also promote the growth of our customers' businesses through comprehensive support programs that offer promotional tools and marketing support to help generate increased sales for our customers. Our programs include such things as personalized websites, brochures, marketing campaigns and business development training. We also provide certain retail store customers with assistance in site selection, store layout and design and business management system implementation. Our inability to sufficiently develop effective advertising, marketing and promotional programs to succeed in a weakened economic environment and an increasingly competitive marketplace, in which we (and our entire supply chain) also compete with other luxury product alternatives, could have a material adverse effect on our business.

Our business is highly seasonal.

In 2005, approximately 64% of our net sales and 89% of our operating income were generated in the second and third quarters of the year, which represent the peak months of swimming pool use, installation, remodeling and repair. Our sales are substantially lower during the first and fourth quarters of the year, when we may incur net losses.

The nature of our business subjects us to compliance with Environmental, Health, Transportation and Safety Regulations.

We are subject to regulation under federal, state and local environmental, health, transportation and safety requirements, which govern such things as packaging, labeling, handling, transportation, storage and sale of pool chemicals and landscape chemicals and fertilizers. For example, we sell algaecides and pest control products that are regulated as pesticides under the Federal Insecticide, Fungicide and Rodenticide Act and various state pesticide laws. These laws are primarily related to labeling, annual registration and licensing.

Failure to comply with these laws and regulations may result in the assessment of administrative, civil and criminal penalties or the imposition of injunctive relief. Moreover, compliance with such laws and regulations in the future could prove to be costly, and there can be no assurance that we will not incur such costs in material amounts. These laws and regulations have changed substantially and rapidly over the last 20 years, and we anticipate that there will be continuing changes. The clear trend in environmental, health, transportation and safety regulation is to place more restrictions and limitations on activities that impact the environment, such as the use and handling of chemical substances. Increasingly, strict restrictions and limitations have resulted in increased operating costs for us, and it is possible that the costs of compliance with such laws and regulations will continue to increase. We will attempt to anticipate future regulatory requirements that might be imposed and we will plan accordingly to remain in compliance with changing regulations and to minimize the costs of such compliance.

We store chemicals, fertilizers and other combustible materials that involve fire, safety and casualty risks.

We store chemicals and fertilizers, including certain combustible, oxidizing compounds, at our sales centers. A fire, explosion or flood affecting one of our facilities could give rise to fire, safety and casualty losses and related liability claims. We maintain what we believe is prudent insurance protection. However, we cannot guarantee that our insurance coverage will be adequate to cover future claims that may arise or that we will be able to maintain adequate insurance in the future at rates we consider reasonable. Successful claims for which we are not fully insured may adversely affect our working capital and profitability. In addition, changes in the insurance industry have generally led to higher insurance costs and decreased availability of coverage.

We conduct business internationally, which exposes us to additional risks.

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Our international operations expose us to certain additional risks, including difficulty in staffing and managing foreign subsidiary operations, uncertain political and regulatory conditions, foreign currency fluctuations, adverse tax consequences and dependence on foreign economies.

We source certain products we sell, including our private label products, from Asia and other foreign locations. There is a significant risk that we may not be able to access products in a timely and efficient manner, and we may also be subject to certain trade restrictions that prevent us from obtaining products. Fluctuations in other factors relating to foreign trade, such as tariffs, currency exchange rates, transportation costs and inflation are beyond our control.

A terrorist attack or the threat of a terrorist attack could have a material adverse effect on our business.

The terrorist attacks that took place on September 11, 2001, in the U.S. were unprecedented events that have created many economic and political uncertainties, some of which may materially impact our business. Discretionary spending on leisure products such as ours is generally adversely affected during times of economic uncertainty. The potential for future terrorist attacks, the national and international responses to terrorist attacks, and other acts of war or hostility have created many economic and political uncertainties, which could adversely affect our business for the short or long-term in ways that cannot presently be predicted.

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

The table below summarizes the repurchases of our common stock in the second quarter of 2006:

Period	Total number of shares purchased ⁽¹⁾	Average price paid per share	Total number of shares purchased as part of publicly announced plan ⁽²⁾	Maximum approximate dollar value that may yet be purchased under the plan
April 1-30, 2006	--	\$ --	--	\$ 50,000,000
May 1-31, 2006	380,647	\$ 43.66	370,600	\$ 33,846,645
June 1-30, 2006	664,317	\$ 41.74	662,905	\$ 6,173,845

- (1) These shares include shares of our common stock surrendered to us by employees in order to satisfy tax withholding obligations in connection with certain exercises of employee stock options and/or the exercise price of such options granted under our 1995 and 1998 Stock Option Plans. Shares surrendered totaled 0 shares in April, 10,047 shares in May and 1,412 shares in June.
- (2) In July 2002, our Board authorized \$50.0 million for the repurchase of shares of our common stock in the open market. In August 2004 and November 2005, our Board increased the authorization for the repurchase of shares of our common stock in the open market to a total of \$50.0 million from the amounts remaining at each of those dates. In August 2006, when less than \$50,000 of the existing authorized amount remained available for share repurchases, our Board increased the authorization for the repurchase of shares of our common stock in the open market to \$50.0 million.

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

At the Annual Meeting of Stockholders held on May 9, 2006, the following proposals were adopted by the margins indicated:

1. To elect a Board of Directors to hold office until the next Annual Meeting of Stockholders and until their successors are elected and qualified.

Number of Shares

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	Number of Shares	
	For	Withheld
Andrew W. Code	48,469,304	1,296,516
James J. Gaffney	49,396,750	369,071
George T. Haymaker	49,480,786	285,035
Manuel J. Perez de la Mesa	48,691,521	1,074,299
Harlan F. Seymour	49,395,166	370,655
Wilson B. Sexton	48,624,713	1,141,107
Robert C. Sledd	46,134,099	3,631,721
John E. Stokely	47,878,063	1,887,757

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2. To approve the Strategic Plan Incentive Plan of SCP Pool Corporation.

For	43,174,121
Against	192,229
Abstain	38,185

3. To ratify the appointment of Ernst & Young LLP, certified public accountants, as our independent auditors for the fiscal year ending December 31, 2006.

For	49,663,914
Against	88,951
Abstain	12,955

Item 6. Exhibits

Exhibits filed as part of this report are listed in the Index to Exhibits appearing on page 28.

Items 1, 3 and 5 are not applicable and have been omitted.

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Signature Page

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 on August 9, 2006.

Items 1, 3 and 5 are not applicable and have been omitted.

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POOL CORPORATION

BY: /s/ Mark W. Joslin
Mark W. Joslin

Vice President and Chief Financial Officer,
and

duly authorized signatory on behalf of the
Registrant

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Index to Exhibits

No.	Description	Filed with this Form 10-Q	Incorporated by Reference		
			Form	File No.	Date Filed
3.1	Restated Certificate of Incorporation of the Company.	X			
3.2	Restated Composite Bylaws of the Company.	X			
4.1	Form of certificate representing shares of common stock of the Company.		8-K	000-26640	05/19/2006
10.1	Strategic Incentive Plan of SCP Pool Corporation.	X			
31.1	Certification by Mark W. Joslin pursuant to Rule 13a-14(a) and 15d-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.	X			
31.2	Certification by Manuel J. Perez de la Mesa pursuant to Rule 13a-14(a) and 15d-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.	X			
32.1	Certification by Manuel J. Perez de la Mesa and Mark W. Joslin pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002	X			

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