

ADVO INC
Form 10-Q
May 04, 2006
Table of Contents

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

Quarterly Report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the quarterly period ended March 25, 2006

or

Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the transition period from _____ to _____

Commission file number 1-11720

ADVO, Inc.

(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of

incorporation or organization)

One Targeting Centre, Windsor, CT
(Address of principal executive offices)

Registrant's telephone number including area code: (860) 285-6100

06-0885252
(I.R.S. Employer

Identification No.)

06095
(Zip Code)

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Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

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

Large accelerated filer

Accelerated filer

Non-accelerated filer

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

As of April 22, 2006 there were 31,741,019 shares of common stock outstanding.

Table of Contents

ADVO, Inc.

Index to Quarterly Report

on Form 10-Q

Quarter Ended March 25, 2006

	Page
<u>Part I - Financial Information</u>	
Item 1. Financial Statements (Unaudited).	
<u>Consolidated Balance Sheets - March 25, 2006 and September 24, 2005.</u>	2
<u>Consolidated Statements of Operations - Six months and three months ended March 25, 2006 and March 26, 2005.</u>	3
<u>Consolidated Statements of Cash Flows - Six months ended March 25, 2006 and March 26, 2005.</u>	4
<u>Notes to Consolidated Financial Statements.</u>	5
Item 2. <u>Management's Discussion and Analysis of Financial Condition and Results of Operations.</u>	12
Item 3. <u>Quantitative and Qualitative Disclosures About Market Risk.</u>	19
Item 4. <u>Controls and Procedures.</u>	19
<u>Part II - Other Information</u>	
Item 2. <u>Changes in Securities, Use of Proceeds and Issuer Purchases of Equity Securities.</u>	20
Item 6. <u>Exhibits.</u>	21
<u>Signatures</u>	22

Table of Contents**ADVO, Inc.****CONSOLIDATED BALANCE SHEETS***(In thousands, except share data)*

	<i>March 25, 2006 Unaudited</i>	<i>September 24, 2005</i>
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 37,864	\$ 46,238
Accounts receivable, net	185,010	162,542
Inventories	2,447	2,500
Prepaid postage	211	10,747
Prepaid expenses and other current assets	5,513	6,360
Federal income taxes receivable		2,884
Deferred income taxes	12,873	10,996
Total current assets	243,918	242,267
Property, plant and equipment	440,295	420,738
Less accumulated depreciation and amortization	(244,499)	(226,735)
Net property, plant and equipment	195,796	194,003
Investment in deferred compensation plan	16,248	15,134
Goodwill	22,829	22,824
Other assets	3,935	4,502
TOTAL ASSETS	\$ 482,726	\$ 478,730
LIABILITIES		
Current liabilities:		
Accounts payable	\$ 31,869	\$ 55,276
Accrued compensation and benefits	25,964	27,919
Customer advances	15,505	7,302
Federal and state income taxes payable	1,823	325
Other current liabilities	23,829	25,468
Total current liabilities	98,990	116,290
Long-term debt	123,905	124,867
Deferred income taxes	28,775	29,641
Deferred compensation plan	17,350	16,172
Other liabilities	11,758	6,475
STOCKHOLDERS EQUITY		
Preferred stock, \$.01 par value (Authorized 5,000,000 shares, none issued)		
Common stock, \$.01 par value (Authorized 80,000,000 shares, issued 32,025,736 and 31,719,419 shares, respectively)	320	317
Additional paid-in capital	183,273	180,510
Unamortized deferred compensation		(3,846)
Accumulated earnings	27,724	17,182
Less shares of common stock held in treasury, at cost	(8,847)	(8,124)
Less shares of common stock held in deferred compensation trust	(1,101)	(1,038)

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Accumulated other comprehensive income	579	284
Total stockholders' equity	201,948	185,285
TOTAL LIABILITIES & STOCKHOLDERS' EQUITY	\$ 482,726	\$ 478,730

See Accompanying Notes.

-2-

Table of Contents**ADVO, Inc.****CONSOLIDATED STATEMENTS OF OPERATIONS (Unaudited)***(In thousands, except per share data)*

	<i>Six months ended</i>		<i>Three months ended</i>	
	<i>March 25, 2006</i>	<i>March 26, 2005</i>	<i>March 25, 2006</i>	<i>March 26, 2005</i>
Revenues	\$ 713,006	\$ 688,816	\$ 354,781	\$ 338,763
Costs and expenses:				
Cost of sales	556,181	529,398	279,833	260,673
Selling, general and administrative	122,636	123,177	63,073	57,839
Provision for bad debts	3,278	3,633	1,612	1,789
Operating income	30,911	32,608	10,263	18,462
Interest expense	(4,066)	(3,240)	(2,080)	(1,694)
Equity earnings in joint ventures	1,565	1,073	738	417
Other income (expense), net	88	(280)	49	(125)
Income before income taxes	28,498	30,161	8,970	17,060
Provision for income taxes	11,029	11,621	3,472	6,610
Net income	\$ 17,469	\$ 18,540	\$ 5,498	\$ 10,450
Basic earnings per share	\$ 0.56	\$ 0.60	\$ 0.18	\$ 0.34
Diluted earnings per share	\$ 0.55	\$ 0.59	\$ 0.17	\$ 0.33
Dividends declared per share	\$ 0.22	\$ 0.22	\$ 0.11	\$ 0.11
Weighted average basic shares	31,305	30,857	31,361	30,985
Weighted average diluted shares	31,505	31,291	31,587	31,448

See Accompanying Notes.

Table of Contents**ADVO, Inc.****CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)***(In thousands)*

	<i>Six months ended</i>	
	<i>March 25, 2006</i>	<i>March 26, 2005</i>
Cash flows from operating activities:		
Net income	\$ 17,469	\$ 18,540
Adjustments to reconcile net income to net cash flows provided by operating activities:		
Depreciation	20,382	19,039
Stock-based compensation	3,837	1,313
Amortization of debt issue costs	277	277
Deferred income taxes	(2,928)	1,225
Provision for bad debts	3,278	3,633
Equity earnings from joint ventures	(1,565)	(1,073)
Other	18	149
Change in operating assets and liabilities, net of effects of acquisitions:		
Accounts receivable	(25,739)	(12,811)
Inventories	54	(371)
Prepaid postage	10,536	(830)
Prepaid expenses and other current assets	847	518
Investment in deferred compensation plan	181	(306)
Other assets	345	2,641
Accounts payable	(23,410)	(6,015)
Accrued compensation and benefits	(1,957)	(2,399)
Deferred compensation plan	(181)	306
Customer advances	8,203	187
Federal and state income taxes payable	4,252	(136)
Other liabilities	3,172	(446)
Distributions from equity joint ventures	1,510	1,157
Net cash provided by operating activities	18,581	24,598
Cash flows from investing activities:		
Expenditures for property, plant and equipment	(22,567)	(20,293)
Proceeds from disposals of property, plant and equipment	375	81
Net cash used by investing activities	(22,192)	(20,212)
Cash flows from financing activities:		
Proceeds from exercise of stock options	2,426	9,272
Tax benefit from stock transactions	479	
Treasury stock transactions related to stock awards	(722)	(1,382)
Cash dividends paid	(6,950)	(6,802)
Net cash (used) provided by financing activities	(4,767)	1,088
Effect of exchange rate changes on cash and cash equivalents	4	55
Change in cash and cash equivalents	(8,374)	5,529
Cash and cash equivalents at beginning of period	46,238	30,284

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Cash and cash equivalents at end of period	\$ 37,864	\$ 35,813
Noncash activities:		
(Increase) in the fair market value of interest rate swaps	(494)	(229)
Deferred compensation plan investment gains	1,359	1,103
	See Accompanying Notes.	

-4-

Table of Contents

ADVO, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

1. Basis of presentation

The accompanying unaudited consolidated financial statements have been prepared in accordance with generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments considered necessary for a fair presentation have been included.

Operating results for the six-month period ended March 25, 2006 are not necessarily indicative of the results that may be expected for the fiscal year ending September 30, 2006. For further information, refer to the consolidated financial statements and footnotes thereto included in ADVO's Annual Report on Form 10-K for the fiscal year ended September 24, 2005.

Certain reclassifications have been made in the fiscal 2005 financial statements to conform with the 2006 presentation.

The Company's fiscal year 2006 contains an additional week compared to the prior fiscal year as a result of the Company's 52-53 week accounting cycle. The extra week will be reflected within the third quarter of fiscal year 2006.

2. Significant Accounting Policies

A comprehensive discussion of the Company's significant accounting policies is included in the notes to the consolidated financial statements in the Company's Annual Report on Form 10-K for the fiscal year ended September 24, 2005. The Company's stock-based compensation accounting policy has changed to reflect the adoption of Statement of Financial Accounting Standards No. 123r, (Statement 123r), Share Based Payments.

Stock-Based Compensation In the first quarter of fiscal 2006, the Company adopted Statement 123r. Prior to fiscal year 2006, the Company accounted for stock awards under the recognition and measurement principles of Accounting Principles Board Opinion No. 25, Accounting for Stock Issued to Employees (APB 25) and related interpretations. Accordingly, compensation cost was recognized only for those arrangements, such as restricted stock, where the quoted market price of the stock at the grant date, was in excess of the amount the employee was required to pay to acquire the stock. Prior to fiscal year 2006, no compensation expense was recognized for stock options granted to employees because all stock options granted had exercise prices equal to the market price of the underlying common stock on the date of the grant.

Effective September 25, 2005, the first day of the Company's fiscal year, the Company adopted Statement 123r which requires all share based payments, including grants of stock options, to be recognized in the consolidated statement of operations as an operating expense, based on their fair values on the grant date, over the requisite service period. The Company elected to adopt Statement 123r under the modified-prospective transition method. Prior period stock option financial information was valued using the Black-Scholes option-pricing model. The Company is not required to restate prior periods. Under this transition method, stock-based compensation expense for three and six months ended March 25, 2006 includes:

- (a) Compensation expense for all stock option awards granted prior to, but not vested as of September 25, 2005, based on the fair value estimated at grant date in accordance with the original provisions of Statement No. 123, Accounting for Stock-Based Compensation;

Table of Contents

ADVO, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

(b) Compensation expense for all stock option awards granted subsequent to September 25, 2005, based on the fair value estimated at grant date in accordance with Statement 123r; and

(c) Compensation expense for all restricted stock awards in accordance with the provisions of Statement 123r.

Compensation expense for stock-based awards is recognized in the consolidated statement of operations in cost of sales and general and administrative expenses. For the quarters ended March 25, 2006 and March 26, 2005, the Company's total stock-based compensation expense was \$2.3 million (\$1.4 million, net of tax) and \$0.6 million (\$0.4 million, net of tax), respectively. The Company's total stock-based compensation for the six-month periods ended March 25, 2006 and March 26, 2005 was \$3.8 million (\$2.4 million, net of tax) and \$1.3