POOL CORP
Form 10-Q
November 01, 2006

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

x **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

¨ **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**

(State or other jurisdiction of incorporation)	(Commission File Number)	(IRS Employer Identification No.)

109 Northpark Boulevard, Covington, Louisiana **70433-5001**
(Address of Principal Executive Offices) (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 October 25, 2006, there were 50,713,677 outstanding shares of the registrant s common stock, $.001 par value per share.

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

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PART I. FINANCIAL INFORMATION

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

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

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2006	**2005**	**2006**	**2005**
		(As Adjusted - See Note 5)		(As Adjusted - See Note 5)
Net sales	**$ 537,017**	$ 423,729	**$ 1,591,276**	$ 1,252,868
Cost of sales	**387,022**	309,124	**1,134,233**	903,631
Gross profit	**149,995**	114,605	**457,043**	349,237
Selling and administrative expenses	**96,903**	73,174	**285,591**	216,161
Operating income	**53,092**	41,431	**171,452**	133,076
Interest expense, net	**4,276**	1,331	**10,983**	4,316
Income before income taxes and equity earnings	**48,816**	40,100	**160,469**	128,760
Provision for income taxes	**18,848**	15,491	**61,957**	49,800
Equity earnings in unconsolidated investments	**1,525**	1,912	**1,513**	2,372

	Three Months Ended		Nine Months Ended	
Net income	**$ 31,493**	$ 26,521	**$ 100,025**	$ 81,332
Earnings per share:				
Basic	**$ 0.61**	$ 0.50	**$ 1.91**	$ 1.55
Diluted	**$ 0.58**	$ 0.47	**$ 1.82**	$ 1.46
Weighted average shares outstanding:				
Basic	**51,532**	52,699	**52,243**	52,489
Diluted	**54,277**	55,945	**55,092**	55,741
Cash dividends declared per common share	**$ 0.105**	$ 0.09	**$ 0.30**	$ 0.25

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)

	September 30, 2006	September 30, 2005 (As Adjusted - See Note 5)	December 31, 2005 (As Adjusted - See Note 5)
Assets			
Current assets:			
Cash and cash equivalents	**$ 40,874**	$ 44,644	$ 26,866
Receivables, net	**64,540**	41,924	42,809
Receivables pledged under receivables facility	**147,049**	110,113	98,976
Product inventories, net	**283,930**	197,135	330,575
Prepaid expenses	**7,785**	3,248	5,190
Deferred income taxes	**4,024**	4,171	7,977
Total current assets	**$ 548,202**	$ 401,235	$ 512,393
Property and equipment, net	**32,201**	21,413	25,598
Goodwill	**156,123**	102,163	139,546
Other intangible assets, net	**19,964**	9,161	22,838
Equity interest investments	**32,383**	29,547	29,907
Other assets, net	**13,862**	10,816	15,098

	September 30,	September 30,	December 31,
Total assets	**$ 802,735**	$ 574,335	$ 745,380
Liabilities and stockholders' equity			
Current liabilities:			
Accounts payable	**$ 111,349**	$ 99,920	$ 174,170
Accrued and other current liabilities	**118,892**	69,148	76,645
Short-term financing	**110,974**	83,170	65,657
Current portion of other long-term liabilities	**3,731**	1,350	1,350
Total current liabilities	**$ 344,946**	$ 253,588	$ 317,822
Deferred income taxes	**12,760**	13,116	14,600
Long-term debt	**144,750**	--	129,100
Other long-term liabilities	**1,625**	2,402	2,134
Total liabilities	**$ 504,081**	$ 269,106	$ 463,656
Stockholders' equity:			
Common stock, $.001 par value; 100,000,000 shares authorized; 50,911,356, 52,769,769 and 52,414,883 shares issued and outstanding at September 30, 2006, September 30, 2005 and December 31, 2005, respectively	**$ 51**	$ 52	$ 52
Additional paid-in capital	**142,242**	111,713	119,770
Retained earnings	**164,744**	191,092	160,684
Treasury stock	**(14,177)**	--	(921)
Accumulated other comprehensive income	**5,794**	2,372	2,139
Total stockholders' equity	**$ 298,654**	$ 305,229	$ 281,724
Total liabilities and stockholders' equity	**$ 802,735**	$ 574,335	$ 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)

	Nine Months Ended September 30,	
	2006	**2005**
		(As Adjusted - See Note 5)

	Nine Months Ended	
Operating activities		
Net income	**$ 100,025**	$ 81,332
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	**5,980**	3,693
Amortization	**3,472**	3,001
Share-based compensation	**5,517**	4,367
Excess tax benefits from share-based compensation	**(10,619)**	(8,433)
Equity earnings in unconsolidated investments	**(2,476)**	(2,373)
Other	**1,645**	(816)
Changes in operating assets and liabilities, net of effects of acquisitions:		
Receivables	**(61,121)**	(54,410)
Product inventories	**53,889**	(2,647)
Accounts payable	**(71,359)**	(15,017)
Other current assets and liabilities	**56,525**	43,576
Net cash provided by operating activities	**81,478**	52,273
Investing activities		
Acquisition of businesses, net of cash acquired	**(26,662)**	(3)
Equity interest investment	**--**	(3,589)
Purchase of property and equipment, net of sale proceeds	**(11,146)**	(6,556)
Net cash used in investing activities	**(37,808)**	(10,148)
Financing activities		
Proceeds from revolving line of credit	**311,838**	189,013
Payments on revolving line of credit	**(293,938)**	(239,433)
Proceeds from asset-backed financing	**93,347**	62,170
Payments on asset-backed financing	**(48,030)**	(21,595)
Payments on other long-term liabilities	**(1,497)**	(964)
Payments of deferred financing costs	**(128)**	(11)
Payments of capital lease obligations	**(257)**	--
Excess tax benefits from share-based compensation	**10,619**	8,433
Issuance of common stock under stock option plans	**6,335**	3,146
Payment of cash dividends	**(15,734)**	(13,152)
Purchase of treasury stock	**(93,495)**	(6,353)
Net cash used in financing activities	**(30,940)**	(18,746)
Effect of exchange rate changes on cash	**1,278**	(497)
Change in cash and cash equivalents	**14,008**	22,882
Cash and cash equivalents at beginning of period	**26,866**	21,762
Cash and cash equivalents at end of period	**$ 40,874**	$ 44,644

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 nine month periods ended September 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 Financial Accounting Standards Board (FASB) 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 reclassed 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 FASB issued FASB Interpretation (FIN) 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.

In September 2006, the FASB issued SFAS 157, *Fair Value Measurements,* which defines fair value, establishes a framework for reporting fair value and expands disclosures about fair value measurements. SFAS 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007. We are currently evaluating the impact that SFAS 157 will have on our financial position and results of operations.

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

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.

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 September 30,		Nine Months Ended September 30,	
	2006	**2005**	**2006**	**2005**
Net income	**$ 31,493**	$ 26,521	**$ 100,025**	$ 81,332
Weighted average common shares outstanding:				
Basic	**51,532**	52,699	**52,243**	52,489
Effect of dilutive securities:				
Stock options	**2,715**	3,219	**2,812**	3,223
Restricted stock awards	**29**	26	**30**	23
Employee stock purchase plan	**1**	1	**7**	6
Diluted	**54,277**	55,945	**55,092**	55,741
Basic earnings per share	**$ 0.61**	$ 0.50	**$ 1.91**	$ 1.55
Diluted earnings per share	**$ 0.58**	$ 0.47	**$ 1.82**	$ 1.46

Note 3 Comprehensive Income

Comprehensive income includes net income, foreign currency translation adjustments and the unrealized gain or loss on interest rate swaps, net of income taxes on the unrealized gain or loss. Comprehensive income was $33.6 million and $26.5 million for the three months ended September 30, 2006 and September 30, 2005, respectively and $103.7 million and $80.8 million for the nine months ended September 30, 2006 and September 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. During the third quarter of 2006, we made a $0.7 million purchase price allocation adjustment that reduced the allowance for doubtful accounts. Based on better collections, the realized value of the accounts receivable was higher than originally estimated. With this adjustment, we have now finalized the purchase price allocations for our acquisition of Automatic Rain Company.

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

In August 2006, we acquired Wickham Supply, Inc. and Water Zone, LP (collectively Wickham), a leading regional irrigation products distributor. Wickham operates 14 distribution sales centers with 13 locations throughout Texas and one location in Georgia. We have included the results of operations for Wickham in our Consolidated Financial Statements since the acquisition date.

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.

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 nine months ended September 30, 2006:

	Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term (years)	Aggregate Intrinsic Value
Balance at December 31, 2005	6,796,687	$ 10.46		
Granted (at market price)	598,800	38.87		
Exercised	790,328	5.58		

			Weighted	
Forfeited	43,025	21.30		
Balance at September 30, 2006	6,562,134	$ 13.81	5.20	$ 162,264,989
Exercisable at September 30, 2006	3,985,852	$ 7.30	3.76	$ 124,372,425

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

	Nine Months Ended September 30,	
(In thousands, except share data)	**2006**	**2005**
Options exercised	**790,328**	727,240
Cash proceeds	**$ 4,399**	$ 1,977
Intrinsic value of options exercised	**$ 29,133**	$ 22,642
Tax benefits realized	**$ 11,248**	$ 8,779

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

	Nine Months Ended September 30,	
(Weighted average)	**2006**	**2005**
Expected volatility	**30.8%**	30.3%
Expected term	**6.0years**	7.0years
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. In prior years, we used monthly price observations for our historical volatility calculation. In 2006, we began using weekly price observations for our historical volatility calculation because we believe that they provide a more appropriate measurement of volatility given the trading patterns or our common stock. 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 nine months ended September 30, 2006 and September 30, 2005 was $13.27 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.

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

	Shares	Weighted Average Remaining Contractual Term (years)	Aggregate Intrinsic Value

		Weighted	
Balance unvested at December 31, 2005	52,400		
Granted (at market price)	--		
Vested	2,500		
Forfeited	--		
Balance unvested at September 30, 2006	49,900	7.39	$ 1,921,150
Vested at September 30, 2006	5,000	7.86	$ 192,500

The restricted stock awards generally vest five years from the grant date, and expire ten years from the grant date. At September 30, 2006, the unamortized compensation expense related to the restricted stock awards totaled $0.5 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.

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 date):

	Nine Months Ended September 30,	
	2006	**2005**
	Increase/ (decrease)	Increase/ (decrease)
Income before income taxes and equity earnings	**$ (5,312)**	$ (3,413)
Provision for income taxes	**(2,051)**	(1,232)
Net income	**(3,261)**	(2,181)
Basic earnings per share	**$ (0.06)**	$ (0.04)
Diluted earnings per share	**$ (0.06)**	$ (0.04)
Net cash provided by operating activities	**$ 629**	$ 997
Net cash used in financing activities	**(629)**	(997)

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:

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 nine months ended September 30, 2006 and 22,707 shares under this plan during the nine months ended September 30, 2005. Share-based compensation expense related to the Employee Stock Purchase Plan was $0.3 million for the nine months ended September 30, 2006 and $0.2 million for the nine months ended September 30, 2005. The grant date fair value for the most recent 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 27% to $537.0 million in the third quarter of 2006 compared to $423.7 million in 2005. Base business sales growth of 9% contributed $37.0 million to the increase with the remaining increase attributable primarily to acquired sales centers, including the Horizon business acquired in October 2005 and the Wickham business acquired in August 2006.

Our base business sales growth continues to reflect the growth in the installed base of swimming pools, market share gains through 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 third quarter of 2006, complementary product sales grew 35% compared to the same period in 2005. We believe the impact of weather on sales in the quarter was neutral overall.

Our gross profit as a percentage of net sales (gross margin) increased 90 basis points to 27.9% in the third quarter of 2006 compared to the same period in 2005. This increase is attributable primarily to the benefits of our second quarter pre-price increase inventory purchases, the success of our sales and marketing initiatives and the contribution from acquired businesses, which had a higher third quarter gross margin than the company as a whole.

Our operating income increased 28% to $53.1 million in the third quarter of 2006 while our operating margin increased slightly to 9.9% of sales from 9.8% in 2005. The growth in sales and gross margins was largely offset by higher selling and operating expense growth, which was negatively impacted by the number of new sales center openings in 2006. Interest expense increased to $4.3 million in the third quarter of 2006, compared to $1.3 million in the third quarter of 2005. This is attributable to higher debt levels due to borrowings to fund acquisitions, higher working capital levels and share repurchases, together with higher effective interest rates. Net income increased 19% compared to the same period in 2005 and included $1.5 million of net equity earnings from our investment in Latham Acquisition Corporation (LAC).

Financial Position and Liquidity

Our accounts receivable balance increased $59.6 million to $211.6 million at September 30, 2006, compared to $152.0 million at September 30, 2005. Excluding $42.5 million in receivables from Horizon and Wickham, our accounts receivable balance increased 11% from September 30, 2005 consistent with our 12% year to date base business sales growth rate. Days sales outstanding (DSO) increased between periods to 34.5 days at September 30, 2006 compared to 33.1 days at September 30, 2005 as a result of the addition of Horizon s receivables, which have slightly longer collection cycles. Excluding Horizon, DSO improved slightly to 32.8 days.

Our inventory levels increased 44% to $283.9 million as of September 30, 2006, compared to $197.1 million at September 30, 2005. The increased balance reflects $47.6 million of acquisition related inventory (including $46.0 million for Horizon and Wickham), $9.2 million of inventory for new sales centers, and approximately $18.0 million of inventory related to product line expansion for construction and plumbing products and replacement parts. Excluding these items, inventory increased 6% compared to September 30, 2005, which is less than the 12% year to date base business sales growth rate. Our inventory balance, which was at a higher than normal seasonal level at June 30, 2006 due to our second quarter pre-price increase inventory purchases, is down to a more normal seasonal level at September 30, 2006.

Due to inventory buy-ins ahead of price increases over the last year our inventory turns have slowed to 3.9 times as of September 30, 2006 from 4.5 times as of September 30, 2005, as calculated on a trailing twelve month basis. However, our inventory quality remains high as measured by the percentage of inventory in our fastest-turning inventory classes.

Total debt outstanding increased to $261.1 million at September 30, 2006 compared to $86.9 million at September 30, 2005. This increase is attributable to increased borrowings to fund the Horizon and Wickham acquisitions, share repurchases of $111.4 million in the fourth quarter of 2005 and first nine months of 2006 and higher working capital levels. We continue to maintain a healthy current ratio of 1.6 as of September 30, 2006, which was consistent between periods.

Recent Developments

Recent economic trends include a slowdown in the domestic housing market, increases in short-term interest rates and some weakening of consumer confidence. While these trends have caused a sharp decrease in new home construction, our sales have not been materially impacted due largely to the following:

- the majority of our business is driven by recurring sales related to the ongoing maintenance and repair of existing pools and landscaped areas, with less than 40% of our sales tied to new pool or irrigation construction;
- we estimate that only 10% to 20% of new pools are constructed along with new home construction; and
- we have a low market share with the largest pool builders who we believe are more heavily tied to new home construction.

Based on the continued favorable demographic and socioeconomic trends in our industry, our competitive industry position, and the factors discussed above, we believe that the recent economic trends should not have a significant impact on our future sales.

Outlook

For our seasonally slower fourth quarter, we anticipate mid-single digit base business sales growth given our 20% base business sales growth in the fourth quarter of 2005. Consistent with our prior guidance, we expect roughly breakeven earnings per share for the fourth quarter. For the full year, we expect to generate about $100.0 million in cash from operations.

Looking ahead, we expect to open 16 new sales centers over the next year including 10 new pool sales centers and 6 new Horizon sales centers.

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 September 30, 2006, we conducted operations through 273 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 September 30,		Nine Months Ended September 30,	
	2006	**2005**	**2006**	**2005**
Net sales	**100.0%**	100.0%	**100.0%**	100.0%
Cost of sales	**72.1**	73.0	**71.3**	72.1
Gross profit	**27.9**	27.0	**28.7**	27.9
Selling and administrative expenses	**18.0**	17.3	**17.9**	17.3
Operating income	**9.9**	9.8	**10.8**	10.6
Interest expense	**0.8**	0.3	**0.7**	0.3
Income before income taxes and equity earnings	**9.1**	9.5	**10.1**	10.3

Note: Due to rounding, percentages may not add to operating income or income before income taxes and equity earnings.

For the purposes of the following base business discussion, the consolidated operating results include the operating results from acquisitions in 2006, 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 September 30, 2006 Compared to Three Months Ended September 30, 2005

(Unaudited) (In thousands)	**Base Business Three Months Ended September 30,**		**Acquired Three Months Ended September 30,**		**Total Three Months Ended September 30,**	
	2006	**2005**	**2006**	**2005**	**2006**	**2005**
Net sales	**$ 460,775**	$ 423,729	**$ 76,242**	$ --	**$ 537,017**	$ 423,729
Gross profit	**127,761**	114,605	**22,234**	--	**149,995**	114,605
Gross margin	**27.7%**	27.0%	**29.2%**		**27.9%**	27.0%

Selling and operating expenses	**81,982**	73,174	**14,921**	--	**96,903**	73,174
Expenses as a % of net sales	**17.8%**	17.3%	**19.6%**		**18.0%**	17.3%
Operating income	**45,778**	41,431	**7,314**	--	**53,092**	41,431
Operating income margin	**9.9%**	9.8%	**9.6%**		**9.9%**	9.8%

For purposes of comparing operating results for the three months ended September 30, 2006 to the three months ended September 30, 2005, 210 sales centers were included in the base business calculations and 63 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**
B&B s.r.l. (Busatta)	October 2005	July - September 2006
Direct Replacements, Inc.	October 2005	July - September 2006
Horizon Distributors, Inc.	October 2005	July - September 2006
Wickham Supply, Inc. and Water Zone, LP	August 2006	August - September 2006

Net Sales

	Three Months Ended September 30,			
(in millions)	**2006**	**2005**	**Change**	
Net sales	**$ 537.0**	$ 423.7	$ 113.3	27%

The increase in net sales is a result of the Horizon and Wickham acquisitions and the growth in base business.

Base business sales growth was 9% in the third quarter of 2006 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
- 35% growth in complementary product sales.

Gross Profit

	Three Months Ended September 30,			
(in millions)	**2006**	**2005**	**Change**	
Gross profit	**$ 150.0**	$ 114.6	$ 35.4	31%
Gross margin	**27.9%**	27.0%	0.9%	

Gross margin increased 90 basis points between periods, including a 70 basis point improvement in base business gross margin, due primarily to the benefits achieved through our pre-price increase inventory purchases in the second quarter, a shift in our product sales mix toward higher margin products and the contributions to margin by our acquired businesses. These increases were partially offset by the impact of a third quarter revision for the estimated amount of vendor incentives earned through the nine months ended September 30, 2006 based on our current expected annual product purchases.

Operating Expenses

(in millions)	Three Months Ended September 30, 2006	2005	Change	
Operating expenses	**$ 96.9**	$ 73.2	$ 23.7	32%
Operating expenses as a percentage of net sales	**18.0%**	17.3%	0.7%	

Compared to the third quarter of 2005, operating expenses grew 32% and increased 70 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, and higher share-based compensation costs. Base business operating expenses were 12% higher in the third quarter of 2006 compared to the same period in 2005 and increased 50 basis points as a percentage of sales.

Interest Expense

Interest expense increased $3.0 million between periods due to a 133% increase in the average debt outstanding compared to the third quarter of 2005 and an increase in the effective interest rate to 6.0% in 2006 from 4.4% in 2005. Our debt levels increased to fund acquisitions and share repurchases.

Income Taxes

The increase in income taxes is due to the $8.7 million increase in income before income taxes and equity earnings. Our effective income tax rate was 38.6% at September 30, 2006 and September 30, 2005.

Net Income and Earnings Per Share

Net income increased 19% to $31.5 million in the third quarter of 2006 from $26.5 million in the third quarter of 2005. The 2006 amount included $1.5 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 $0.58 per share in the third quarter of 2006 compared to $0.47 per share in the third quarter of 2005.

Nine Months Ended September 30, 2006 Compared to Nine Months Ended September 30, 2005

(Unaudited) (In thousands)	Base Business Nine Months Ended September 30,	Acquired Nine Months Ended September 30,	Total Nine Months Ended September 30,

(Unaudited)	Base Business		Acquired		Total	
	2006	**2005**	**2006**	**2005**	**2006**	**2005**
Net sales	**$ 1,400,492**	$ 1,250,499	**$ 190,784**	$ 2,369	**$ 1,591,276**	$ 1,252,868
Gross profit	**401,696**	348,733	**55,347**	504	**457,043**	349,237
Gross margin	**28.7%**	27.9%	**29.0%**	21.3%	**28.7%**	27.9%
Selling and operating expenses	**245,250**	215,581	**40,341**	580	**285,591**	216,161
Expenses as a % of net sales	**17.5%**	17.2%	**21.1%**	24.5%	**17.9%**	17.3%
Operating income (loss)	**156,446**	133,151	**15,006**	(75)	**171,452**	133,076
Operating income (loss) margin	**11.2%**	10.6%	**7.9%**	(3.2)%	**10.8%**	10.6%

For purposes of comparing operating results for the nine months ended September 30, 2006 to the nine months ended September 30, 2005, 207 sales centers were included in the base business calculations and 66 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 - September 2006
Direct Replacements, Inc.	October 2005	January - September 2006
Horizon Distributors, Inc.	October 2005	January - September 2006
Wickham Supply, Inc. and Water Zone, LP	August 2006	August - September 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)	Nine Months Ended September 30, 2006	Nine Months Ended September 30, 2005	Change	
Net sales	**$ 1,591.3**	$ 1,252.9	$ 338.4	27%

The increase in net sales is a result of the Horizon and Wickham acquisitions and the growth in base business.

Base business sales growth was 12% in the first nine months of 2006 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
- 30% 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 189% over the first nine months of 2005 and accounted for 23% of total net sales.

Gross Profit

(in millions)	Nine Months Ended September 30, 2006		Nine Months Ended September 30, 2005		Change	
Gross profit	$	**457.0**	$	349.2	$ 107.8	31%
Gross margin		**28.7%**		27.9%	0.8%	

Gross margin increased 80 basis points between periods due primarily to the benefits achieved through our supply chain management initiatives, including our pre-price increase inventory purchases in the fourth quarter of 2005 and second quarter of 2006, and a shift in product mix to higher margin products compared to the first nine months of 2005. Our gross margin improvements related to favorable product mix are a result of successful sales initiatives including our expansion of parts product and complementary product offerings.

Operating Expenses

(in millions)	Nine Months Ended September 30, 2006		Nine Months Ended September 30, 2005		Change	
Operating expenses	$	**285.6**	$	216.2	$ 69.4	32%
Operating expenses as a percentage of net sales		**17.9%**		17.3%	0.6%	

Operating expenses grew 32% and as a percentage of net sales increased 60 basis points from the first nine 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 nine months of 2006 compared to the same period in 2005 and relatively consistent as a percentage of sales. The increase in base business operating expenses is due to expenses for newly opened pool sales centers, increased promotional costs and higher share-based compensation costs due largely to accelerated expense for options issued to retirement eligible employees.

We opened fifteen sales centers in the first nine months of 2006 compared to only three sales centers in the first nine months of 2005. Since the second half of 2005, we have opened eleven new pool sales centers and five new Horizon sales centers.

Interest Expense

Interest expense increased $6.7 million between periods as average debt outstanding was 85% higher in the first nine months of 2006 compared to the first nine months of 2005 due to increased borrowings to fund acquisitions and share repurchases. The effective interest rate also increased to 5.7% in 2006 from 4.0% in 2005.

Income Taxes

The increase in income taxes is due to the $31.7 million increase in income before income taxes and equity earnings. Our effective income tax rate was 38.6% at September 30, 2006 and September 30, 2005.

Net Income and Earnings Per Share

Net income increased 23% to $100.0 million in the first nine months of 2006 from $81.3 million in the first nine months of 2005. The 2006 amount included $1.5 million of net equity earnings from our investment in LAC, down from $2.3 million for the same period last year due to additional taxes now accrued on this income. For the year, we expect a positive contribution to our earnings from LAC. Earnings per share for the first nine months of 2006 increased 25% to $1.82 per diluted share compared to $1.46 in the first nine months of 2005.

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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, second and third quarters of 2006, the four quarters of 2005 and the fourth quarter 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 not necessarily an accurate indication of results for an entire fiscal year or of continuing trends.

(Unaudited)	**QUARTER**							
(in thousands)	**2006**			**2005(1)**				**2004(1)**
	Third	**Second**	**First**	**Fourth**	**Third**	**Second**	**First**	**Fourth**
Statement of Income Data								
Net sales	**$ 537,017**	$ 705,703	$348,556	$299,791	$ 423,729	$ 563,978	$ 265,161	$ 209,937
Gross profit	**149,995**	209,000	98,048	83,211	114,605	162,681	71,951	56,404
Operating income (loss)	**53,092**	103,338	15,022	2,288	41,431	81,389	10,256	(5,013)
Net income (loss)	**31,493**	62,110	6,422	(876)	26,521	50,709	4,102	(3,656)
Balance Sheet Data								
Total receivables, net	**$ 211,589**	$ 295,722	$211,578	$141,785	$ 152,037	$ 231,736	$ 164,507	$ 97,589
Product inventories, net	**283,930**	367,096	406,310	330,575	197,135	247,350	281,267	195,787
Accounts payable	**111,349**	207,727	267,296	174,170	99,920	165,872	219,290	113,114
Total debt	**261,080**	306,618	239,712	198,241	86,922	174,743	145,045	97,505

(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 three 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.

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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
Unseasonably early warming trends in spring / late cooling trends in fall (primarily in the northern half of the US)	A longer pool and landscape season, thus increasing our sales
Unseasonably late warming trends in spring / early cooling trends in fall (primarily in the northern half of the US)	A shorter pool and landscape season, thus decreasing our sales

In the third quarter of 2006, our sales were not significantly impacted by the mixed weather conditions across North America. While maintenance and impulse sales benefited from near record high temperatures in July and August, sales tied to pool construction and pool usage were hindered by cool and wet weather in the southwest, above average rainfall in the midwest and northeast and much cooler September temperatures.

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):

	Nine Months Ended September 30,	
	2006	**2005**
Operating activities	**$ 81,478**	$ 52,273
Investing activities	**(37,808)**	(10,148)
Financing activities	**(30,940)**	(18,746)

Cash flow provided by operations increased $29.2 million to $81.5 million in the first nine months of 2006 compared to $52.3 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 third 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 Revenue Service, as the payment deadline was extended to October 16, 2006. Year to date open market share repurchases totaled 2.2 million shares as of September 30, 2006 and used $88.1 million in borrowing capacity.

Future Sources and Uses of Cash

Our unsecured syndicated senior credit facility (the Credit Facility), which matures on December 20, 2010, now provides for $220.0 million in borrowing capacity including a $160.0 million five-year revolving credit facility (the Revolver) and a $60.0 million term loan (the Term Loan). During the third quarter of 2006, we exercised the $40.0 million accordion feature under the Revolver, which increased our borrowing capacity from $180.0 million to $220.0 million. The Credit Facility includes sublimits for the issuance of swingline loans and standby letters of credit.

At September 30, 2006, there was $87.0 million outstanding and $72.6 million available for borrowing under the Revolver. The average effective interest rate on the Revolver was approximately 5.9% for the nine months ended September 30, 2006.

At September 30, 2006, there was $60.0 million outstanding under the Term Loan of which $2.3 million is classified as current. The average effective interest rate of the Term Loan was approximately 5.4% for the nine months ended September 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 December 2005, we entered into an interest rate swap agreement to reduce our exposure to fluctuations in interest rates. Effective on June 30, 2006, the swap agreement converts our variable rate Term Loan to a fixed-rate basis until its termination on December 31, 2008. Any difference paid or received on the interest rate swap will be recognized as an adjustment to interest expense over the life of the swap. We record the changes in the fair value of the swap to accumulated other comprehensive income. We have designated this swap as a cash flow hedge. During the quarter ended September 30, 2006, no gains or losses were recognized on this swap.

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 September 30, 2006, there was $111.0 million outstanding under the Receivables Facility at an average effective interest rate of 5.6%.

As of September 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 $44.3 million, or 1.2 million shares, of our common stock on the open market at an average share price of $37.85. Early in the third quarter, we used up most of the remaining amount of the $50.0 million share repurchase authorized by our Board of Directors (our Board) in November 2005. In August 2006, our Board increased the authorization for the repurchase of shares of our common stock in the open market to $50.0 million. Subsequent to the end of the third quarter of 2006, we repurchased an additional $7.8 million, or 204,000 shares, of our common stock on the open market, bringing our year to date share repurchases to a total of $95.9 million and leaving $4.1 million authorized for repurchases at October 19, 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.

In the fourth quarter of 2006, our cash flows from operating activities will be negatively impacted by the payment of approximately $61.0 million for estimated federal tax payments deferred from the second half of 2005 and the first half of 2006 as allowed by the Katrina Emergency Tax Relief Act of 2005. For the full year, we expect to generate about $100.0 million in cash from operations.

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 September 30, 2006, management, including the CEO and CFO, performed an evaluation of the effectiveness of our disclosure controls and procedures. Based on that evaluation, management, including the CEO and CFO, concluded that as of September 30, 2006, our disclosure controls and procedures were effective.

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 likel 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.

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.

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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 37 new sales centers and have completed 14 acquisitions including our acquisitions of Horizon in October 2005 and Wickham in August 2006. These acquisitions have added 107 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.

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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.

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.

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

The table below summarizes the repurchases of our common stock in the third 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
July 1-31, 2006	118,928	$ 40.99	118,928	$ 1,298,896
August 1-31, 2006	463,301	$ 37.18	463,301	$ 34,072,452

September 1-30, 2006	607,583	$	37.81	587,577	$	11,901,517

(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 zero shares in July and August and 20,006 shares in September.

(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. As of October 19, 2006, $4.1 million of the authorized amount remained available.

Item 6. Exhibits

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

Items 1, 3, 4 and 5 are not applicable and have been omitted.

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 November 1, 2006.

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

Index to Exhibits

			Incorporated by Reference		
No.	**Description**	**Filed with this Form 10-Q**	**Form**	**File No.**	**Date Filed**
3.1	Restated Certificate of Incorporation of the Company.		10-Q	000-26640	08/09/2006
3.2	Restated Composite Bylaws of the Company.		10-Q	000-26640	08/09/2006
4.1	Form of certificate representing shares of common stock of the Company.		8-K	000-26640	05/19/2006
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			