

POOL CORP
Form 10-Q
November 01, 2012

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 September 30, 2012

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
(State or other jurisdiction of
incorporation or organization)

36-3943363
(I.R.S. Employer
Identification No.)

109 Northpark Boulevard,
Covington, Louisiana
(Address of principal executive offices)

70433-5001
(Zip Code)

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

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 has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulations S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). YES NO

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

Large accelerated filer

Accelerated filer

Non-accelerated filer (Do not check if a smaller reporting company)

Smaller reporting company

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 October 22, 2012, there were 46,704,043 shares of common stock outstanding.

POOL CORPORATION
Form 10-Q
For the Quarter Ended September 30, 2012

TABLE OF CONTENTS

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements (Unaudited)

| | |
|--|----------|
| <u>Consolidated Statements of Income</u> | <u>1</u> |
| <u>Consolidated Statements of Comprehensive Income</u> | <u>2</u> |
| <u>Consolidated Balance Sheets</u> | <u>3</u> |
| <u>Condensed Consolidated Statements of Cash Flows</u> | <u>4</u> |
| <u>Notes to Consolidated Financial Statements</u> | <u>5</u> |

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations 8

Item 3. Quantitative and Qualitative Disclosures about Market Risk 20

Item 4. Controls and Procedures 20

PART II. OTHER INFORMATION

Item 1. Legal Proceedings 21

Item 1A. Risk Factors 21

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds 21

Item 6. Exhibits 21

SIGNATURE 22

INDEX TO EXHIBITS 23

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

POOL CORPORATION

Consolidated Statements of Income

(Unaudited)

(In thousands, except per share data)

| | Three Months Ended | | Nine Months Ended | |
|--|--------------------|-----------|-------------------|-------------|
| | September 30, | | September 30, | |
| | 2012 | 2011 | 2012 | 2011 |
| Net sales | \$528,027 | \$503,584 | \$1,647,156 | \$1,522,896 |
| Cost of sales | 376,526 | 355,678 | 1,168,687 | 1,072,141 |
| Gross profit | 151,501 | 147,906 | 478,469 | 450,755 |
| Selling and administrative expenses | 103,544 | 106,993 | 316,357 | 311,345 |
| Goodwill impairment | 6,946 | — | 6,946 | — |
| Operating income | 41,011 | 40,913 | 155,166 | 139,410 |
| Interest expense, net | 1,687 | 1,641 | 5,364 | 5,110 |
| Income before income taxes and equity earnings | 39,324 | 39,272 | 149,802 | 134,300 |
| Provision for income taxes | 17,965 | 15,126 | 60,020 | 52,377 |
| Equity earnings in unconsolidated investments | 16 | 23 | 187 | 185 |
| Net income | \$21,375 | \$24,169 | \$89,969 | \$82,108 |
| Earnings per share: | | | | |
| Basic | \$0.46 | \$0.50 | \$1.91 | \$1.70 |
| Diluted | \$0.45 | \$0.50 | \$1.87 | \$1.67 |
| Weighted average shares outstanding: | | | | |
| Basic | 46,574 | 47,987 | 47,076 | 48,357 |
| Diluted | 47,787 | 48,772 | 48,205 | 49,157 |
| Cash dividends declared per common share | \$0.16 | \$0.14 | \$0.46 | \$0.41 |

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

POOL CORPORATION
 Consolidated Statements of Comprehensive Income
 (Unaudited)
 (In thousands)

| | Three Months Ended | | Nine Months Ended | |
|--|--------------------|----------|-------------------|----------|
| | September 30, | | September 30, | |
| | 2012 | 2011 | 2012 | 2011 |
| Net income | \$21,375 | \$24,169 | \$89,969 | \$82,108 |
| Other comprehensive income (loss): | | | | |
| Foreign currency translation adjustments | (135) | (1,233) | (466) | 608 |
| Change in unrealized gains and losses on interest rate swaps, net of tax of \$407, \$(325), \$1,260 and \$(882) | (635) | 502 | (1,970) | 1,363 |
| Total other comprehensive income (loss) | (770) | (731) | (2,436) | 1,971 |
| Comprehensive income | \$20,605 | \$23,438 | \$87,533 | \$84,079 |

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

POOL CORPORATION

Consolidated Balance Sheets

(In thousands, except share data)

| | September 30, 2012 (Unaudited) | September 30, 2011 (Unaudited) | December 31, 2011 ⁽¹⁾ |
|---|--------------------------------------|--------------------------------------|-------------------------------------|
| Assets | | | |
| Current assets: | | | |
| Cash and cash equivalents | \$28,818 | \$20,656 | \$17,487 |
| Receivables, net | 175,459 | 160,647 | 110,555 |
| Product inventories, net | 349,325 | 337,698 | 386,924 |
| Prepaid expenses and other current assets | 8,078 | 7,354 | 11,298 |
| Deferred income taxes | 11,561 | 10,145 | 11,737 |
| Total current assets | 573,241 | 536,500 | 538,001 |
| Property and equipment, net | 46,643 | 40,774 | 41,394 |
| Goodwill | 169,983 | 178,516 | 177,103 |
| Other intangible assets, net | 11,270 | 11,953 | 11,738 |
| Equity interest investments | 1,066 | 976 | 980 |
| Other assets, net | 29,180 | 29,493 | 29,406 |
| Total assets | \$831,383 | \$798,212 | \$798,622 |
| Liabilities and stockholders' equity | | | |
| Current liabilities: | | | |
| Accounts payable | \$163,543 | \$120,221 | \$177,437 |
| Accrued expenses and other current liabilities | 102,805 | 70,718 | 53,398 |
| Current portion of long-term debt and other long-term liabilities | 23 | 22 | 22 |
| Total current liabilities | 266,371 | 190,961 | 230,857 |
| Deferred income taxes | 31,833 | 26,549 | 32,993 |
| Long-term debt | 214,328 | 268,700 | 247,300 |
| Other long-term liabilities | 6,381 | 7,503 | 7,726 |
| Total liabilities | 518,913 | 493,713 | 518,876 |
| Stockholders' equity: | | | |
| Common stock, \$0.001 par value; 100,000,000 shares authorized; 46,596,813, 47,594,628 and 47,366,997 shares issued and outstanding at September 30, 2012, September 30, 2011 and December 31, 2011, respectively | 47 | 48 | 47 |
| Additional paid-in capital | 265,129 | 236,623 | 243,180 |
| Retained earnings | 47,510 | 64,805 | 34,299 |
| Accumulated other comprehensive income (loss) | (216) |) 3,023 | 2,220 |
| Total stockholders' equity | 312,470 | 304,499 | 279,746 |
| Total liabilities and stockholders' equity | \$831,383 | \$798,212 | \$798,622 |

⁽¹⁾ Derived from audited financial statements.

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

3

POOL CORPORATION

Condensed Consolidated Statements of Cash Flows

(Unaudited)

(In thousands)

| | Nine Months Ended September 30, | |
|---|------------------------------------|-----------|
| | 2012 | 2011 |
| Operating activities | | |
| Net income | \$89,969 | \$82,108 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Depreciation | 8,481 | 7,071 |
| Amortization | 962 | 1,243 |
| Share-based compensation | 6,236 | 6,143 |
| Excess tax benefits from share-based compensation | (2,534) | (2,229) |
| Equity earnings in unconsolidated investments | (187) | (185) |
| Goodwill impairment | 6,946 | — |
| Other | 278 | (3,892) |
| Changes in operating assets and liabilities, net of effects of acquisitions: | | |
| Receivables | (63,015) | (55,941) |
| Product inventories | 39,644 | 10,999 |
| Prepaid expenses and other assets | 2,607 | 677 |
| Accounts payable | (15,500) | (49,542) |
| Accrued expenses and other current liabilities | 50,643 | 35,522 |
| Net cash provided by operating activities | 124,530 | 31,974 |
| Investing activities | | |
| Acquisition of businesses, net of cash acquired | (4,580) | (2,961) |
| Purchase of property and equipment, net of sale proceeds | (13,717) | (16,959) |
| Other investments, net | (249) | (177) |
| Net cash used in investing activities | (18,546) | (20,097) |
| Financing activities | | |
| Proceeds from revolving line of credit | 482,669 | 446,649 |
| Payments on revolving line of credit | (415,641) | (376,649) |
| Payments on long-term debt and other long-term liabilities | (100,017) | (145) |
| Payments of deferred acquisition consideration | — | (500) |
| Excess tax benefits from share-based compensation | 2,534 | 2,229 |
| Proceeds from stock issued under share-based compensation plans | 13,180 | 9,506 |
| Payments of cash dividends | (21,669) | (19,798) |
| Purchases of treasury stock | (55,088) | (62,842) |
| Net cash used in financing activities | (94,032) | (1,550) |
| Effect of exchange rate changes on cash and cash equivalents | (621) | 608 |
| Change in cash and cash equivalents | 11,331 | 10,935 |
| Cash and cash equivalents at beginning of period | 17,487 | 9,721 |
| Cash and cash equivalents at end of period | \$28,818 | \$20,656 |

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 we, us or our) prepared the unaudited interim Consolidated Financial Statements following U.S. generally accepted accounting principles (GAAP) and the requirements of the Securities and Exchange Commission (SEC) for interim financial information. As permitted under those rules, we have condensed or omitted certain footnotes and other financial information required for complete financial statements. The Consolidated Financial Statements include all normal and recurring adjustments that are necessary for a 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 2011 Annual Report on Form 10-K. You should read the interim Consolidated Financial Statements in conjunction with the Consolidated Financial Statements and accompanying notes in our Annual Report. The results for our three and nine month periods ended September 30, 2012 are not necessarily indicative of the expected results for our fiscal year ending December 31, 2012.

Note 2 – Goodwill Impairment

As discussed in Note 1 to the Consolidated Financial Statements in our 2011 Annual Report on Form 10-K, goodwill represents the excess of the amount we paid to acquire a company over the estimated fair value of tangible assets and identifiable intangible assets acquired, less liabilities assumed. We test goodwill and other indefinite lived intangible assets for impairment annually as of October 1st and at any other time when impairment indicators exist.

For our annual goodwill impairment test, we estimate the fair value of our reporting units by utilizing a present value model that incorporates our assumptions for projected future cash flows, discount rates and multiples. These assumptions are considered unobservable inputs (Level 3 inputs as defined in the accounting guidance). If the estimated fair value of any of our reporting units has fallen below their carrying value, we compare the estimated fair value of the reporting unit's goodwill to its carrying value. If the carrying value of a reporting unit's goodwill exceeds its estimated fair value, we recognize the difference as an impairment loss in operating income. Since we define an operating segment as an individual sales center and we do not have operations below the sales center level, our reporting unit is an individual sales center.

We performed an interim goodwill impairment analysis for our United Kingdom reporting unit during the third quarter of 2012 based on our identification of impairment indicators related to our results through the end of the 2012 pool season and the current and expected continued depressed economic conditions in the United Kingdom. Our results for the nine months ended September 30, 2012 were significantly lower than our 2012 sales, gross profit and operating profit estimates for the United Kingdom reporting unit that we used in our 2011 annual goodwill impairment test. We updated our 2011 impairment analysis for both our actual 2012 year to date results and our updated growth estimates for future years based on expectations for a more prolonged economic recovery period in the United Kingdom. These updates had a significant impact on our projected future cash flow calculation and resulted in a much lower estimated fair value for our United Kingdom reporting unit.

As a result of our interim impairment analysis, we recorded a \$6.9 million non-cash goodwill impairment charge equal to the total September 30, 2012 goodwill carrying amount of our United Kingdom reporting unit of \$6.9 million. Since the goodwill impairment charge is non deductible for tax purposes, our effective tax rate for both the quarterly and year to date periods ended September 30, 2012 was much higher than normal.

Note 3 – Earnings Per Share

We calculate basic earnings per share (EPS) by dividing net income by the weighted average number of common shares outstanding. We include outstanding unvested restricted stock awards of our common stock in the basic weighted average share calculation. Diluted EPS includes the dilutive effects of other share-based awards. Stock options with exercise prices that are higher than the average market prices of our common stock are excluded from the diluted EPS calculation because their effect is anti-dilutive.

5

The table below presents the computation of earnings per share, including the reconciliation of basic and diluted weighted average shares outstanding (in thousands, except EPS):

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|-------------------------------------|----------|------------------------------------|----------|
| | 2012 | 2011 | 2012 | 2011 |
| Net income | \$21,375 | \$24,169 | \$89,969 | \$82,108 |
| Weighted average shares outstanding: | | | | |
| Basic | 46,574 | 47,987 | 47,076 | 48,357 |
| Effect of dilutive securities: | | | | |
| Stock options and employee stock purchase plan | 1,213 | 785 | 1,129 | 800 |
| Diluted | 47,787 | 48,772 | 48,205 | 49,157 |
| Earnings per share: | | | | |
| Basic | \$0.46 | \$0.50 | \$1.91 | \$1.70 |
| Diluted | \$0.45 | \$0.50 | \$1.87 | \$1.67 |
| Anti-dilutive stock options excluded from diluted earnings per share computations | 4 | 1,418 | 964 | 1,418 |

Note 4 – Acquisitions

In February 2012, we acquired the distribution assets of Ideal Distributors Ltd., a regional swimming pool products distributor with four sales center locations in British Columbia, Canada. In March 2012, we acquired the distribution assets of CCR Distribution, a swimming pool products distributor with one sales center in Ontario, Canada.

We completed our preliminary acquisition accounting for each of these acquisitions, subject to adjustments in accordance with the terms of the purchase agreements during the one year measurement period. These acquisitions did not have a material impact on our financial position or results of operations.

Note 5 – Fair Value Measurements and Interest Rate Swaps

Our assets and liabilities that are measured at fair value on a recurring basis include the unrealized gains or losses on our interest rate swap contracts. We use significant other observable market data or assumptions (Level 2 inputs as defined in the accounting guidance) that we believe market participants would use in pricing similar assets or liabilities, including assumptions about counterparty risk. Our fair value estimates reflect an income approach based on the terms of the interest rate contracts and inputs corroborated by observable market data including interest rate curves.

We have five interest rate swap contracts in place to reduce our exposure to fluctuations in interest rates on our unsecured syndicated senior credit facility (the Credit Facility). These swaps convert the variable interest rate to a fixed interest rate on borrowings under the Credit Facility. Each of these swap contracts terminates on October 19, 2016. The following table provides additional details related to each of these swap contracts:

| Derivative | Effective Date | Notional Amount (in millions) | Fixed Interest Rate |
|----------------------|-------------------|-------------------------------------|---------------------------|
| Interest rate swap 1 | November 21, 2011 | \$25.0 | 1.185% |
| Interest rate swap 2 | November 21, 2011 | \$25.0 | 1.185% |

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| | | | |
|----------------------|-------------------|--------|--------|
| Interest rate swap 3 | December 21, 2011 | \$50.0 | 1.100% |
| Interest rate swap 4 | January 17, 2012 | \$25.0 | 1.050% |
| Interest rate swap 5 | January 19, 2012 | \$25.0 | 0.990% |

6

We recognize any differences between the variable interest rate payments and the fixed interest rate settlements from our swap counterparties as an adjustment to interest expense over the life of the swaps. We have designated these swaps as cash flow hedges and we record the changes in the estimated fair value of the swaps to Accumulated other comprehensive income (loss). If our interest rate swaps became ineffective, we would immediately recognize the changes in the estimated fair value of our swaps in earnings. Since inception, we have not recognized any gains or losses on these swaps through income and there has been no effect on income from hedge ineffectiveness.

In 2011, we had two previous interest rate swap contracts related to our previous debt arrangements. We terminated both of these swap contracts in 2011. For additional information regarding our previous debt arrangements and interest rate swaps, see Note 5 of “Notes to Consolidated Financial Statements,” included in Item 8 of our 2011 Annual Report on Form 10-K.

The table below presents the estimated fair value of our interest rate swap contracts (in thousands):

| Balance Sheet Line Item | Unrealized Losses at | |
|--|----------------------|------------|
| | September 30, | |
| | 2012 | 2011 |
| Accrued expenses and other current liabilities | \$(3,650 |) \$(1,104 |
| | |) |

Failure of our swap counterparties would result in the loss of any potential benefit to us under our swap contracts. In this case, we would still be obligated to pay the variable interest payments underlying the Credit Facility. Additionally, failure of our swap counterparties would not eliminate our obligation to continue to make payments under our existing swap contracts if we continue to be in a net pay position.

The carrying values of cash, receivables, accounts payable and accrued liabilities approximate fair value due to the short maturity of those instruments and the carrying value of long-term debt approximates fair value. Our determination of the estimated fair value of long-term debt reflects a discounted cash flow model using our estimates, primarily those related to assumptions for borrowing rates (Level 3 inputs as defined in the accounting guidance).

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 2011 Annual Report on Form 10-K.

For a discussion of our base business calculations, see the RESULTS OF OPERATIONS section below.

In our discussion of results of operations below, adjusted operating income, adjusted net income and adjusted diluted EPS for all periods exclude the Goodwill impairment line item on the Consolidated Statements of Income. We have provided these adjusted amounts because we believe it helps investors assess our year-over-year operating performance.

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. Forward-looking statements speak only as of the date of this filing, and we undertake no obligation to update or revise such statements to reflect new circumstances or unanticipated events as they occur. 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 may differ materially due to one or more factors, including the sensitivity of our business to weather conditions, changes in the economy and the housing market, our ability to maintain favorable relationships with suppliers and manufacturers, competition from other leisure product alternatives and mass merchants and other risks detailed in our 2011 Annual Report on Form 10-K. For these statements, we claim the protection of the safe harbor for forward-looking statements contained in the Private Securities Litigation Reform Act.

OVERVIEW

Financial Results

We realized strong third quarter results despite the challenging external environment and one less selling day than the third quarter of 2011. Solid execution across the company drove market share gains and record year to date sales and earnings per share.

Net sales increased 5% quarter over quarter, with base business sales up 3% (over 4% on a same selling day basis). This growth is primarily attributable to market share gains, modest growth in consumer discretionary expenditures and some price inflation, offset by a 1% decline from the impact of unfavorable currency fluctuations.

Gross profit for the third quarter of 2012 improved 2% from the comparable 2011 period, while gross profit as a percentage of net sales (gross margin) declined 70 basis points to 28.7%. The decrease in gross margin reflects a difficult comparison given the 60 basis point improvement in the third quarter last year, which included the benefit of 2011 mid-year vendor price increases. Unfavorable product and customer mix changes and continued competitive pricing pressures also contributed to the gross margin decline in the quarter.

Selling and administrative expenses (operating expenses) decreased 3% in the third quarter of 2012 compared to the same period in 2011. Base business operating expenses were down 6% as lower employee incentive costs, the impact of currency fluctuations on expenses, the impact of one less selling day and lower bad debt expense more than offset higher professional fees and inflationary increases in other costs.

We performed an interim goodwill impairment analysis for our United Kingdom reporting unit during the third quarter of 2012 based on our identification of impairment indicators related to our results through the end of the 2012 pool season (sales and profits significantly lower than our forecast for 2012) and the current and expected continued depressed economic conditions in the United Kingdom. As a result of our impairment analysis, we recorded a \$6.9 million non-cash goodwill impairment charge equal to the total September 30, 2012 goodwill carrying amount of our United Kingdom reporting unit of \$6.9 million. This impairment charge had a \$0.14 negative impact on diluted EPS for the three and nine months ended September 30, 2012. Since the goodwill impairment charge is not deductible for tax purposes, our effective tax rate for both the quarterly and year to date periods ended September 30, 2012 was much higher than normal.

Operating income for the quarter was essentially flat at \$41.0 million compared to 2011, while operating income as a percentage of net sales (operating margin) decreased 30 basis points to 7.8% compared to the same period in 2011. Excluding goodwill impairment, adjusted operating income for the quarter increased 17% to \$48.0 million and adjusted operating margin increased 100 basis points to 9.1% for the third quarter of 2012 compared to the same period in 2011.

Net income decreased 12% to \$21.4 million in the third quarter of 2012, with earnings per share down 10% to \$0.45 per diluted share versus \$0.50 per diluted share for the third quarter of 2011. Adjusted net income for the third quarter increased 17% to \$28.3 million, while adjusted EPS increased 18% to \$0.59 per diluted share.

Financial Position and Liquidity

Total net receivables increased 9% due primarily to the increase in net sales and higher vendor receivables. Our allowance for doubtful accounts balance was \$4.8 million at September 30, 2012, a \$0.4 million decrease compared to September 30, 2011 that reflects continued improvements in our receivable aging trends. Days sales outstanding (DSO) improved between periods to 29.0 days at September 30, 2012 compared to 30.3 days at September 30, 2011.

Inventory levels were up 3% to \$349.3 million at September 30, 2012, including a 2% increase from recent acquisitions. The inventory reserve increased to \$9.6 million at September 30, 2012 compared to \$7.4 million at September 30, 2011. Our inventory turns, as calculated on a trailing twelve month basis, increased to 3.3 times at September 30, 2012 compared to 3.2 times at September 30, 2011.

Total debt outstanding was \$214.3 million at September 30, 2012, down \$54.4 million compared to September 30, 2011.

Current Trends and Outlook

For a detailed discussion of trends, see the Current Trends and Outlook section of Management's Discussion and Analysis included in Item 7 of our 2011 Annual Report on Form 10-K. While there have not been any significant changes in those trends, we believe the economic environment remains uncertain given consumer confidence and employment levels in the United States and the lingering debt and economic issues in Europe.

Based on our results through September as well as expectations for the remainder of the year, we revised our 2012 earnings guidance from our previous range of \$1.75 to \$1.82 per diluted share to a projected range of \$1.80 to \$1.83 per diluted share excluding the \$0.14 goodwill impairment charge or \$1.66 to \$1.69 per diluted share including the impact of the goodwill impairment charge.

For the fourth quarter of 2012, we expect mid-single digit base business sales growth including the benefit of one more selling day compared to the fourth quarter of 2011. We believe fourth quarter gross margin will continue to track lower than 2011. While the unfavorable comparative impact related to 2011 mid-season vendor price increases will diminish in the fourth quarter, we believe that unfavorable product and customer mix changes and competitive pricing pressures will continue.

We expect operating expenses will be up 3% to 4% in the fourth quarter compared to the same period in 2011, with the benefit of a projected \$2.0 million decline in employee incentive costs more than offset by expected cost increases in other areas, expenses from our recent acquisitions and the impact of one more selling day. For the full year, we expect modest expense growth overall with employee incentive costs down approximately \$6.0 million to a more normalized expense level after the extraordinary year we had in 2011.

For the full year, we expect our effective income tax rate will be approximately 40%. Excluding the impact of the non-deductible goodwill impairment charge, our full year effective income tax rate should be just over 38%. This is slightly below our more normalized rate of approximately 39% due to the benefit from the expiration of the statute of limitations for both our 2007 and 2008 income tax returns.

Consistent with our results for the first nine months of 2012, we anticipate base business results will generate operating profit growth as a percentage of base business sales growth (contribution margin) of 20% for the full year excluding the impact of goodwill impairment. While favorable timing differences related to inventory and tax payments will reverse in the fourth quarter, we still expect cash provided by operations will exceed net income for the full year as a result of operational improvements.

RESULTS OF OPERATIONS

As of September 30, 2012, we conducted operations through 312 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, | | |
|--|-------------------------------------|---------|------------------------------------|---------|---|
| | 2012 | 2011 | 2012 | 2011 | |
| Net sales | 100.0 | % 100.0 | % 100.0 | % 100.0 | % |
| Cost of sales | 71.3 | 70.6 | 71.0 | 70.4 | |
| Gross profit | 28.7 | 29.4 | 29.0 | 29.6 | |
| Operating expenses | 19.6 | 21.2 | 19.2 | 20.4 | |
| Goodwill impairment | 1.3 | — | 0.4 | — | |
| Operating income | 7.8 | 8.1 | 9.4 | 9.2 | |
| Interest expense, net | 0.3 | 0.3 | 0.3 | 0.3 | |
| Income before income taxes and equity earnings | 7.4 | % 7.8 | % 9.1 | % 8.8 | % |

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

Our discussion of consolidated operating results includes the operating results from acquisitions in 2012 and 2011. We have included the results of operations in our consolidated results since the respective acquisition dates.

Three Months Ended September 30, 2012 Compared to Three Months Ended September 30, 2011

The following table breaks out our consolidated results into the base business component and the excluded components (sales centers excluded from base business):

| (Unaudited) (in thousands) | Base Business | | Excluded | | Total | | |
|-------------------------------|-------------------------------------|-----------|-------------------------------------|---------|-------------------------------------|-----------|---|
| | Three Months Ended September 30, | | Three Months Ended September 30, | | Three Months Ended September 30, | | |
| | 2012 | 2011 | 2012 | 2011 | 2012 | 2011 | |
| Net sales | \$518,504 | \$502,301 | \$9,523 | \$1,283 | \$528,027 | \$503,584 | |
| Gross profit | 148,738 | 147,541 | 2,763 | 365 | 151,501 | 147,906 | |
| Gross margin | 28.7 | % 29.4 | % 29.0 | % 28.4 | % 28.7 | % 29.4 | % |
| Operating expenses | 100,315 | 106,619 | 3,229 | 374 | 103,544 | 106,993 | |
| Expenses as a % of net sales | 19.3 | % 21.2 | % 33.9 | % 29.2 | % 19.6 | % 21.2 | % |
| Goodwill impairment | 6,946 | — | — | — | 6,946 | — | |
| Operating income (loss) | 41,477 | 40,922 | (466) |) (9 |) 41,011 | 40,913 | |
| Operating margin | 8.0 | % 8.1 | % (4.9 |)% (0.7 |)% 7.8 | % 8.1 | % |

In our calculation of base business results, we have excluded the following acquisitions for the periods identified:

| Acquired ⁽¹⁾ | Acquisition Date | Net Sales Centers Acquired | Periods Excluded |
|--------------------------------|------------------|----------------------------|-------------------------|
| CCR Distribution | March 2012 | 1 | July–September 2012 |
| Ideal Distributors Ltd. | February 2012 | 4 | July–September 2012 |
| G.L. Cornell Company | December 2011 | 1 | July–September 2012 |
| Poolway Schwimmbadtechnik GmbH | November 2011 | 1 | July–September 2012 |
| The Kilpatrick Company, Inc. | May 2011 | 4 | July 2012 and July 2011 |

⁽¹⁾ We acquired certain distribution assets of each of these companies.

We exclude the following sales centers from base business results for a period of 15 months (parenthetical numbers for each category indicate the number of sales centers excluded as of September 30, 2012):

- acquired sales centers (see table above);
- existing sales centers consolidated with acquired sales centers (0);
- closed sales centers (0);
- consolidated sales centers in cases where we do not expect to maintain the majority of the existing business (0); and
- sales centers opened in new markets (4).

We generally allocate corporate overhead expenses to excluded sales centers on the basis of their net sales as a percentage of total net sales. After 15 months of operations, we include acquired, consolidated and new market sales centers in the base business calculation including the comparative prior year period.

The table below summarizes the changes in our sales centers in the first nine months of 2012:

| | |
|--------------------|-----|
| December 31, 2011 | 298 |
| Acquired | 5 |
| New locations | 9 |
| September 30, 2012 | 312 |

Net Sales

| (in millions) | Three Months Ended | | |
|---------------|--------------------|---------|-----------|
| | September 30, | | Change |
| | 2012 | 2011 | |
| Net sales | \$528.0 | \$503.6 | \$24.4 5% |

Net sales for the third quarter of 2012 increased 5%, including a 3% increase in base business sales despite a 1% impact from one less selling day and a 1% decrease attributed to the impact of unfavorable currency fluctuations. Our base business sales growth included a 3% increase on the swimming pool side of the business and an 8% increase on the irrigation side of the business. While comparative sales results in July reflected the early peak of the 2012 season, sales growth rates improved throughout the remainder of the third quarter when compared on a same selling day basis.

The overall base business sales increase reflects the impact of the following (listed in order of estimated magnitude):

- market share gains evidenced by sales growth rates for expanded product offerings such as building materials (11% growth) and higher base business sales growth for the irrigation side of the business including the benefit realized from a regional competitor going out of business;
- improvement in consumer discretionary expenditures, including some market recovery in remodeling activity;

the impact of inflationary product cost increases (estimated at approximately 1% to 2%); and higher sales of non-discretionary products due to the increased installed base of pools, which we estimate grew 1% over the past year.

Gross Profit

| (in millions) | Three Months Ended | | | Change | |
|---------------|--------------------|----------|--------|--------|----|
| | September 30, | | | | |
| | 2012 | 2011 | | | |
| Gross profit | \$ 151.5 | \$ 147.9 | \$ 3.6 | | 2% |
| Gross margin | 28.7 | % 29.4 | % | | |

Gross margin declined approximately 70 basis points in the third quarter of 2012. This decrease reflects a difficult comparison to the third quarter of 2011 given the 60 basis point gross margin improvement in that period, which included the benefit from inventory purchases we made in advance of 2011 mid-year vendor price increases. The comparative decline in the third quarter of 2012 also reflected unfavorable changes in product and customer mix and continued competitive pricing pressures. Partially offsetting favorable impacts included lower debit card fees as a percentage of sales and continued improvements in purchasing and pricing discipline.

Operating Expenses

| (in millions) | Three Months Ended | | | Change | |
|--|--------------------|----------|---------|--------|------|
| | September 30, | | | | |
| | 2012 | 2011 | | | |
| Operating expenses | \$ 103.5 | \$ 107.0 | \$(3.5) | | (3)% |
| Operating expenses as a % of net sales | 19.6 | % 21.2 | % | | |

Operating expenses were down 3% compared to the third quarter of 2011, with a 6% drop in base business operating expenses partially offset by the impact of expenses related to recent acquisitions and new market sales center openings. Base business operating expenses declined mainly due to a \$3.8 million decrease in employee incentive costs, a \$0.9 million impact from currency fluctuations, the impact of one less selling day, a \$0.8 million reduction in bad debt expense and small decreases in other expense categories. These expense decreases were partially offset by a \$1.1 million increase in professional fees and inflationary increases in other costs.

Interest Expense, net

Interest expense, net was up 3% between periods due primarily to a year over year increase in interest expense related to borrowings. This increase was attributable to a higher weighted average effective interest rate, which increased to 2.6% for the third quarter of 2012 from 2.4% for the third quarter of 2011.

Income Taxes

Our effective income tax rate was 45.7% for the three months ended September 30, 2012 compared to 38.5% for the three months ended September 30, 2011. Excluding the impact of the \$6.9 million non-deductible goodwill impairment charge, our effective income tax rate was 38.8% for the three months ended September 30, 2012. For a more detailed discussion of the changes to our effective tax rate, please refer to page 15 under the heading "Nine Months Ended September 30, 2012 Compared to Nine Months Ended September 30, 2011".

Net Income and Earnings Per Share

Net income decreased 12% to \$21.4 million compared to the third quarter of 2011, while earnings per share decreased 10% quarter over quarter to \$0.45 per diluted share. Excluding the goodwill impairment charge, adjusted net income for the third quarter increased 17% to \$28.3 million and adjusted earnings per share increased 18% to \$0.59 per diluted share.

Earnings per share for the third quarter of 2012 also included an accretive impact of approximately \$0.01 per diluted share from the reduction in our weighted average shares outstanding due to our share repurchase activities during the year.

Nine Months Ended September 30, 2012 Compared to Nine Months Ended September 30, 2011

The following table breaks out our consolidated results into the base business component and the excluded components (sales centers excluded from base business):

| (Unaudited) (in thousands) | Base Business Nine Months Ended September 30, | | Excluded Nine Months Ended September 30, | | Total Nine Months Ended September 30, | |
|-------------------------------|---|-------------|--|----------|---|-------------|
| | 2012 | 2011 | 2012 | 2011 | 2012 | 2011 |
| Net sales | \$1,608,947 | \$1,517,691 | \$38,209 | \$5,205 | \$1,647,156 | \$1,522,896 |
| Gross profit | 467,582 | 449,285 | 10,887 | 1,470 | 478,469 | 450,755 |
| Gross margin | 29.1 | % 29.6 | % 28.5 | % 28.2 | % 29.0 | % 29.6 |
| Operating expenses | 305,354 | 309,438 | 11,003 | 1,907 | 316,357 | 311,345 |
| Expenses as a % of net sales | 19.0 | % 20.4 | % 28.8 | % 36.6 | % 19.2 | % 20.4 |
| Goodwill impairment | 6,946 | — | — | — | 6,946 | — |
| Operating income (loss) | 155,282 | 139,847 | (116) | (437) | 155,166 | 139,410 |
| Operating margin | 9.7 | % 9.2 | % (0.3) | % (8.4) | % 9.4 | % 9.2 |

In our calculation of base business results, we have excluded the following acquisitions for the periods identified:

| Acquired ⁽¹⁾ | Acquisition Date | Net Sales Centers Acquired | Periods Excluded |
|--------------------------------|---------------------|----------------------------------|--|
| CCR Distribution | March 2012 | 1 | March–September 2012 |
| Ideal Distributors Ltd. | February 2012 | 4 | February–September 2012 |
| G.L. Cornell Company | December 2011 | 1 | January–September 2012 |
| Poolway Schwimmbadtechnik GmbH | November 2011 | 1 | January–September 2012 |
| The Kilpatrick Company, Inc. | May 2011 | 4 | January–July 2012 and May–July 2011 |
| Turf Equipment Supply Co. | December 2010 | 3 | January–February 2012 and January–February 2011 |
| Pool Boat and Leisure, S.A. | December 2010 | 1 | January–February 2012 and January–February 2011 |

⁽¹⁾ We acquired certain distribution assets of each of these companies.

For a more detailed explanation of how we calculated base business results and a summary of the changes in our sales centers since December 31, 2011, please refer to page 11 under the heading “Three Months Ended September 30, 2012 Compared to Three Months Ended September 30, 2011”.

Net Sales

| (in millions) | Nine Months Ended | | | Change | |
|---------------|-------------------|-----------|---------|--------|----|
| | September 30, | | | | |
| | 2012 | 2011 | | | |
| Net sales | \$1,647.2 | \$1,522.9 | \$124.3 | | 8% |

Net sales for the first nine months of 2012 increased 8% on one less selling day, with an increase of 6% in base business sales and a 2% increase related to recent acquisitions and new market sales center openings. Our base business sales growth included a 6% increase on the swimming pool side of the business and more than a 7% increase on the irrigation side of the business, partially offset by a 1% decline from unfavorable currency fluctuations. In local currencies, net sales in Europe declined less than 1% compared to the first nine months of 2011 with sales growth in France, our largest European market, offsetting double digit sales declines in the United Kingdom.

The overall base business sales increase reflects the impact of the following (listed in order of estimated magnitude):

- market share gains evidenced by above market sales growth rates for certain product offerings such as building materials and chemicals (see discussion below) and certain customer segments such as retail (5% growth);
- the gradual improvement in consumer discretionary expenditures, including some market recovery in remodeling activity and increased sales of above ground pools (12% growth);
- the impact of inflationary product cost increases (estimated at approximately 1% to 2%); and
- higher sales of non-discretionary products due to the increased installed base of pools, which we estimate grew 1% over the past year.

Sales of building materials, tile and packaged pool products grew by 15% compared to the first nine months of 2011, although collectively these products only accounted for approximately 12% of our total sales in the first nine months of 2012. Chemical sales grew by over 4%, with a small benefit overall from price inflation despite some lingering price deflation for certain chemical products. Sales for parts products increased only 1% compared to the first nine months of 2011, reflecting a shift by some consumers from repairing to replacing swimming pool equipment.

Sales in 2012 also benefited from favorable weather conditions through May, with an unusually mild winter and record warm spring temperatures driving a higher first quarter base business sales growth rate and the early peak to the 2012 season. However, June sales were negatively impacted by unfavorable weather conditions compared to the same period in 2011. See discussion of significant weather impacts under the subheading Seasonality and Quarterly Fluctuations beginning on page 16.

Gross Profit

| (in millions) | Nine Months Ended | | | Change | |
|---------------|-------------------|---------|--------|--------|----|
| | September 30, | | | | |
| | 2012 | 2011 | | | |
| Gross profit | \$478.5 | \$450.8 | \$27.7 | | 6% |
| Gross margin | 29.0 | % 29.6 | % | | |

Gross margin declined 60 basis points between periods due primarily to difficult comparisons to 2011 (when our gross margin was up 60 basis points from the first nine months of 2010). Going into the 2011 season, we made greater early buy inventory purchases in advance of year-end vendor price increases and we made additional bulk inventory purchases in advance of mid year 2011 vendor price increases. These strategic purchases benefited our gross margin

throughout 2011. We made more modest early buy inventory purchases going into the 2012 season as vendor price increases were more modest.

Unfavorable impacts on comparative gross margin also included the following (listed in order of estimated magnitude):

- unfavorable changes in customer and product mix, including a greater mix of higher priced and more energy efficient products that have higher gross profits per unit but lower gross margins;
- continued competitive pricing pressures, which intensified in the latter part of the second quarter of 2012; and
- a decline of approximately 10 basis points related to higher inventory obsolescence adjustments.

Favorable impacts on comparative gross margin also included the following (listed in order of estimated magnitude):

- continued improvements in purchasing and pricing discipline; and
- a 10 basis point increase attributed to lower debit card fees as a percentage of net sales as a result of the Dodd Frank Wall Street Reform and Consumer Protection Act.

Operating Expenses

| (in millions) | Nine Months Ended | | | Change | |
|--|-------------------|---------|-------|--------|----|
| | September 30, | | | | |
| | 2012 | 2011 | | | |
| Operating expenses | \$316.4 | \$311.3 | \$5.1 | | 2% |
| Operating expenses as a % of net sales | 19.2 | % 20.4 | % | | |

Operating expenses were up 2% compared to the first nine months of 2011 due to recent acquisitions and new market sales center openings. Base business operating expenses declined 1% due to the impact of the following:

- a \$4.0 million decrease in employee incentive costs;
- a \$2.4 million impact from currency fluctuations on expenses; and
- a \$1.7 million reduction in bad debt expense (driven by significant improvements in our past due receivable aging trends).

These decreases were partially offset by higher salary costs due to a 3% increase in average headcount excluding acquisitions, a \$1.7 million increase in professional fees and inflationary increases in other costs.

Interest Expense, net

Interest expense, net increased 5% between periods due to higher interest expense related to borrowings as average debt levels were up 5% compared to the first nine months of 2011. The weighted average effective interest rate was also up slightly between periods to 2.5% for the first nine months of 2012 compared to 2.4% for the first nine months of 2011.

Income Taxes

Our effective income tax rate was 40.1% for the nine months ended September 30, 2012 compared to 39.0% for the nine months ended September 30, 2011. Excluding the impact of the non-deductible \$6.9 million goodwill impairment charge, our year to date effective income tax rate was 38.3%. This lower effective rate includes the impact of a reduction in our estimated annual provision for income taxes recorded in the first quarter of 2012. While this was a routine accounting entry related to previously uncertain tax positions recorded upon the expiration of statutes of limitations for our 2007 income tax returns, the timing was non-routine because we postponed the filing of these returns from September 2008 to January 2009 in accordance with the extended deadline set by the Internal Revenue Service due to Hurricane Gustav. This lower rate also reflects the net impact of adjustments in the third quarter of 2012 due to a reduction in our estimated annual provision for income taxes due to the expiration of the statutes of limitations for our 2008 income tax returns that was partially offset by an increase related to the true up of permanent tax differences in 2012.

Net Income and Earnings Per Share

Net income improved 10% to \$90.0 million compared to the first nine months of 2011, while earnings per share increased 12% to \$1.87 per diluted share. Excluding the \$0.14 per diluted share impact from the goodwill impairment charge, adjusted net income for the first nine months increased 18% to \$96.9 million and adjusted earnings per share increased 20% to \$2.01 per diluted share.

Earnings per share for the first nine months of 2012 also included the following impacts:

- a benefit of \$0.02 per diluted share related to the reduction in our estimated annual provision for income taxes recorded in the first quarter of 2012;
- an accretive impact of approximately \$0.02 per diluted share from the reduction in our weighted average shares outstanding due to our share repurchase activities during the year; and
- an unfavorable impact of \$0.01 per diluted share due to foreign currency fluctuations.

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 maintenance and installation. Sales are substantially lower during the first and fourth quarters, when we may incur net losses. In 2011, approximately 67% of our net sales and over 100% of our operating income were generated in the second and third quarters of the year.

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 2012, the four quarters of 2011 and the fourth quarter of 2010. 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 a good indication of results for an entire fiscal year or of continuing trends.

| (Unaudited) (in thousands) | QUARTER | | | | | | | |
|-------------------------------|-----------|----------------|-----------|-----------|---------------|-----------|-----------|----------------|
| | Third | 2012 Second | First | Fourth | 2011 Third | Second | First | 2010 Fourth |
| Statement of Income | | | | | | | | |
| (Loss) Data | | | | | | | | |
| Net sales | \$528,027 | \$757,175 | \$361,954 | \$270,422 | \$503,584 | \$706,423 | \$312,889 | \$241,426 |
| Gross profit | 151,501 | 222,405 | 104,563 | 80,835 | 147,906 | 211,439 | 91,410 | 73,567 |
| Operating income (loss) | 41,011 | 108,134 | 6,021 | (14,343) | 40,913 | 97,921 | 576 | (16,783) |
| Net income (loss) | 21,375 | 64,943 | 3,651 | (10,115) | 24,169 | 58,577 | (638) | (11,805) |
| Balance Sheet Data | | | | | | | | |
| Receivables, net | \$175,459 | \$270,089 | \$201,792 | \$110,555 | \$160,647 | \$266,032 | \$173,787 | \$101,543 |
| Product inventories, net | 349,325 | 402,266 | 462,810 | 386,924 | 337,698 | 389,763 | 438,791 | 347,439 |
| Accounts payable | 163,543 | 267,990 | 319,462 | 177,437 | 120,221 | 247,904 | 303,395 | 169,700 |
| Total debt | 214,328 | 309,813 | 299,011 | 247,300 | 268,700 | 306,049 | 280,157 | 198,700 |

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. Based on our peak summer selling season, we generally open new sales centers and close or consolidate sales centers, when warranted, either in the first quarter before the peak selling season begins or in the fourth quarter after the peak selling season ends.

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

| Weather | Possible Effects |
|--|--|
| Hot and dry | <ul style="list-style-type: none"> • 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 | <ul style="list-style-type: none"> • 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 U.S. and Canada) | <ul style="list-style-type: none"> • A longer pool and landscape season, thus positively impacting our sales |
| Unseasonably late warming trends in spring/early cooling trends in fall (primarily in the northern half of the U.S. and Canada) | <ul style="list-style-type: none"> • A shorter pool and landscape season, thus negatively impacting our sales |

Our first quarter sales benefited from the unusually mild winter in 2012. Record warm temperatures across the Northeast and Midwest spurred an early start to remodeling projects and new pool construction, resulting in a shift of some sales into March from the second quarter. Temperatures were also much higher than normal across the Southeast and Southwest, resulting in incremental sales of certain maintenance products as many swimming pool owners opened their pools earlier than normal and swimming pool use increased in year-round markets. In our North Texas and Oklahoma markets, this favorable impact was largely offset by a tough comparison to the first quarter of 2011 when we realized higher sales from repair and replacement activity for freeze damaged pool equipment. Weather did not have a significant impact on our first quarter sales along the West Coast, where temperatures were close to historical averages and similar to the same period last year. These weather impacts were apparent when comparing our base business sales for the swimming pool side of the business as California, Texas and Arizona were up 7% in aggregate in the first quarter, while Florida and all other markets were up 18%.

Favorable weather trends continued in April and May with much higher than normal temperatures across the United States, excluding the Pacific Northwest. The three month period between March and May 2012 was the warmest on record both nationally and for 31 of the 37 states east of the Rocky Mountains. The unusually mild winter and record warm spring accounted for the shift of sales into the first and early second quarter and resulted in the earlier than normal peak of the 2012 season. In addition to some sales being pulled forward, June sales were also negatively impacted by weather due to below normal temperatures across the Southeast and cooler temperatures compared to 2011 in most other states excluding California and the Southwest.

In the third quarter of 2012, we estimate that the weather impact on sales was neutral overall compared to the same period in 2011. While average temperatures nationally were the warmest on record in July 2012 and one of warmest on record for the third quarter period, these temperatures were fairly consistent with the same periods in 2011 and did not have a meaningful impact on our comparative sales results. Temperatures did compare favorably to the third quarter of 2011 along the West Coast, but temperatures were less favorable in the third quarter of 2012 across the South and in September 2012 across the Northeast.

LIQUIDITY AND CAPITAL RESOURCES

Liquidity is defined as the ability to generate adequate amounts of cash to meet short-term and long-term 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;
- scheduled debt payments;
- dividend payments;
- capital expenditures;

- the timing and extent of share repurchases; and
- the ability to attract long-term capital with satisfactory terms.

Our primary capital needs are seasonal working capital requirements and other general corporate purposes, including acquisitions, dividend payments and share repurchases. Our primary sources of working capital are cash from operations supplemented by borrowings, which have historically been sufficient to support our growth and finance acquisitions. The same principle applies to funds used for capital expenditures and share repurchases.

We prioritize our use of cash based on investing in our business, maintaining a prudent debt structure and returning money to our shareholders. Our specific priorities for the use of cash are as follows:

- maintenance and new sales center capital expenditures;
- strategic acquisitions executed opportunistically;
- payment of cash dividends as and when declared by our Board of Directors (Board);
- repurchase of common stock at Board-defined parameters; and
- repayment of debt.

Capital expenditures, which historically have averaged 0.5% to 0.75% of net sales, were below and at the bottom of this range between 2008 and 2010 due to lower capacity expansion. In 2011, capital expenditures increased to 1.1% of net sales since we began purchasing rather than leasing new vehicles and forklifts. Going forward, we project annual capital expenditures will be relatively consistent with 2011 and average approximately 1.0% of net sales.

Sources and Uses of Cash

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

| | Nine Months Ended September 30, | |
|----------------------|------------------------------------|-----------|
| | 2012 | 2011 |
| Operating activities | \$ 124,530 | \$ 31,974 |
| Investing activities | (18,546 |) (20,097 |
| Financing activities | (94,032 |) (1,550 |

The improvement in cash provided by operations compared to the first nine months of 2011 included the 10% increase in net income, the impact of favorable timing differences related to the inventory purchase and payment cycle and a \$27.0 million benefit related to the deferral of our third quarter 2012 estimated federal income tax payments until the fourth quarter. We expect the increases attributed to timing differences will reverse in the fourth quarter.

Cash used in investing activities declined slightly between periods as a decrease in purchases of property and equipment offset an increase in cash paid for acquisitions. Cash used in financing activities increased during the first nine months of 2012 due primarily to the change in net proceeds and payments on our debt arrangements. Based on the year over year improvement in cash provided by operations, we had \$33.0 million of net payments on our debt arrangements for the first nine months of 2012 compared to \$70.0 million of net borrowings for the first nine months of 2011. The activity for proceeds and payments on our debt arrangements included the payoff of our \$100.0 million Floating Rate Senior Notes at maturity on February 12, 2012. Higher cash dividend payments reflected the \$0.02 per share increase in our quarterly dividend in the second quarter of 2012. Shares repurchased on the open market were \$53.3 million in the first nine months of 2012, down \$5.7 million compared to the same period in 2011.

Future Sources and Uses of Cash

Our unsecured syndicated senior credit facility (the Credit Facility) provides for \$430.0 million in borrowing capacity under a five-year revolving credit facility and includes sublimits for the issuance of swingline loans and standby letters of credit. Pursuant to an accordion feature, the aggregate maximum principal amount of the commitments under the Credit Facility may be increased at our request and with agreement by the lenders by up to \$75.0 million, to a total of \$505.0 million. The Credit Facility matures on October 19, 2016.

At September 30, 2012, there was \$214.3 million outstanding and \$212.5 million available for borrowing under the Credit Facility. We currently have five interest rate swap contracts in place that reduce our exposure to fluctuations in interest rates on the Credit Facility. These swap contracts convert the Credit Facility's variable interest rate to fixed rates of 1.185% on notional amounts totaling \$50.0 million, 1.100% on a notional amount of \$50.0 million, 1.050% on a notional amount of \$25.0 million and 0.990% on a notional amount of \$25.0 million. Interest expense related to the notional amounts under these swaps is based on the fixed rates plus the applicable margin on the Credit Facility. All five swap contracts will terminate on October 19, 2016. The weighted average effective interest rate for the Credit Facility as of September 30, 2012 was approximately 2.2%, excluding commitment fees.

Financial covenants on the Credit Facility include maintenance of a maximum average total leverage ratio and a minimum fixed charge coverage ratio, which are our most restrictive financial covenants. As of September 30, 2012, the calculations of these two covenants are detailed below:

Maximum Average Total Leverage Ratio. On the last day of each fiscal quarter, our average total leverage ratio must be less than 3.25 to 1.00. Average Total Leverage Ratio is the ratio of the trailing twelve months (TTM) Average Total Funded Indebtedness plus the TTM Average Accounts Securitization Proceeds divided by the TTM EBITDA (as those terms are defined in the Credit Facility). As of September 30, 2012, our average total leverage ratio equaled 1.58 (compared to 1.66 as of June 30, 2012) and the TTM average total debt amount used in this calculation was \$267.9 million.

Minimum Fixed Charge Coverage Ratio. On the last day of each fiscal quarter, our fixed charge ratio must be greater than or equal to 2.25 to 1.00. Fixed Charge Ratio is the ratio of the TTM EBITDAR divided by TTM Interest Expense paid or payable in cash plus TTM Rental Expense (as those terms are defined in the Credit Facility). As of September 30, 2012, our fixed charge ratio equaled 3.74 (compared to 3.59 as of June 30, 2012) and TTM Rental Expense was \$51.9 million.

The Credit Facility also limits the declaration and payment of dividends on our common stock to no more than 50% of the preceding year's Net Income (as defined in the Credit Facility), provided no default or event of default has occurred and is continuing, or would result from the payment of dividends. Further, dividends must be declared and paid in a manner consistent with our past practice. Under the Credit Facility, we may repurchase shares of our common stock provided no default or event of default has occurred and is continuing, or would result from the repurchase of shares, and our maximum average total leverage ratio (determined on a pro forma basis) is less than 2.50 to 1.00. Other covenants include restrictions on our ability to grant liens, incur indebtedness, make investments, merge or consolidate, and sell or transfer assets. Failure to comply with any of our financial covenants or any other terms of the Credit Facility could result in penalty payments, higher interest rates on our borrowings or the acceleration of the maturities of our outstanding debt.

As of September 30, 2012, we were in compliance with all covenants and financial ratio requirements. We believe we will remain in compliance with all covenants and financial ratio requirements throughout the rest of the year. For additional information regarding our debt arrangements, see Note 5 of "Notes to Consolidated Financial Statements," included in Item 8 of our 2011 Annual Report on Form 10-K.

We believe we have adequate availability of capital to fund present operations and the current capacity to finance any working capital needs that may arise. We continually evaluate potential acquisitions and hold discussions with acquisition candidates. If suitable acquisition opportunities arise that would require financing, we believe that we have the ability to finance any such transactions.

As of October 22, 2012, \$114.9 million of the current Board authorized amounts under our share repurchase programs remained available. We expect to repurchase additional shares on the open market from time to time depending on

market conditions. We plan to fund these repurchases with cash provided by operations and borrowings under the Credit Facility.

CRITICAL ACCOUNTING ESTIMATES

We prepare our Consolidated Financial Statements in accordance with U.S. generally accepted accounting principles (GAAP), which require 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, 2011. 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, 2011 that affect fiscal 2012.

Foreign Exchange Risk

There have been no material changes from what we reported in our Form 10-K for the year ended December 31, 2011.

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 (1) recorded, processed, summarized and reported within the time periods specified in the Commission’s rules and forms and (2) accumulated and communicated to our management, including our principal executive officer and principal financial officer, as appropriate to allow timely decisions regarding required disclosure. As of September 30, 2012, 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, 2012, 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 U.S. generally accepted accounting principles. 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 1. Legal Proceedings

There have been no material developments in our previously reported legal proceedings.

Item 1A. Risk Factors

There have been no material changes from the risk factors disclosed in Part I, Item 1A “Risk Factors” in our Annual Report on Form 10-K for the year ended December 31, 2011.

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 2012:

| 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 of Shares That May Yet be Purchased Under the Plan ⁽³⁾ |
|----------------------------------|---|------------------------------|--|--|
| July 1 – July 31, 2012 | 99,212 | \$36.68 | 99,212 | \$22,480,402 |
| August 1 – August 31, 2012 | 206,549 | \$36.72 | 206,549 | \$114,896,445 |
| September 1 – September 30, 2012 | — | \$— | — | \$114,896,445 |
| Total | 305,761 | \$36.71 | 305,761 | |

These shares may 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 or lapses upon vesting of (1) restrictions on previously restricted share awards, and/or to cover the exercise price of such options granted under our share-based compensation plans. There were no shares surrendered for this purpose in the third quarter of 2012.

In May 2011, our Board authorized a new \$100.0 million share repurchase program that replaced our previous (2) share repurchase program. In August 2012, our Board authorized an additional \$100.0 million share repurchase program. Both of these programs are for the repurchase of shares of our common stock in the open market at prevailing market prices or in privately negotiated transactions.

(3) As of October 22, 2012, \$114.9 million of the authorized amounts remained available under our current share repurchase programs.

Item 6. Exhibits

Exhibits filed as part of this report are listed in the Index to Exhibits appearing on page 23.

SIGNATURE

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, 2012.

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

| 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. | | 10-Q | 000-26640 | 8/9/2006 |
| 3.2 | Restated Composite Bylaws of the Company. | | 10-Q | 000-26640 | 8/9/2006 |
| 4.1 | Form of certificate representing shares of common stock of the Company. | | 8-K | 000-26640 | 5/19/2006 |
| <u>31.1</u> | 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 | | | |
| <u>31.2</u> | 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 | | | |
| <u>32.1</u> | 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 | | | |
| 101.INS + | XBRL Instance Document | X | | | |
| 101.SCH + | XBRL Taxonomy Extension Schema Document | X | | | |
| 101.CAL + | XBRL Taxonomy Extension Calculation Linkbase Document | X | | | |
| 101.DEF + | XBRL Taxonomy Extension Definition Linkbase Document | X | | | |
| 101.LAB + | XBRL Taxonomy Extension Label Linkbase Document | X | | | |
| 101.PRE + | XBRL Taxonomy Extension Presentation Linkbase Document | X | | | |

+ Attached as Exhibit 101 to this report are the following items formatted in XBRL (Extensible Business Reporting Language):

1. Consolidated Statements of Income for the three and nine months ended September 30, 2012 and September 30, 2011;
2. Consolidated Statements of Comprehensive Income for the three and nine months ended September 30, 2012 and September 30, 2011;
3. Consolidated Balance Sheets at September 30, 2012, December 31, 2011 and September 30, 2011;
4. Condensed Consolidated Statements of Cash Flows for the nine months ended September 30, 2012 and September 30, 2011; and
5. Notes to Consolidated Financial Statements.

