

PGT, Inc.  
Form 10-Q  
May 08, 2014  
Table of Contents

**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 March 29, 2014**

**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 000-52059**

**PGT, Inc.**  
**1070 Technology Drive**  
**North Venice, FL 34275**

**Registrant's telephone number: 941-480-1600**

**State of Incorporation**  
**Delaware**

**IRS Employer Identification No.**  
**20-0634715**

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 Regulation 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

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

Large accelerated filer <input type="checkbox"/>	Accelerated filer <input checked="" type="checkbox"/>
Non-accelerated filer <input type="checkbox"/> (Do not check if a smaller reporting company)	Smaller reporting company <input type="checkbox"/>

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

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

Common Stock, \$0.01 par value 47,238,685 shares, as of May 7, 2014.

**Table of Contents**

**PGT, INC.**

**TABLE OF CONTENTS**

	<b>Page Number</b>
<b><u>Part I. Financial Information</u></b>	
<b><u>Item 1. Condensed Consolidated Financial Statements (unaudited)</u></b>	
<u>Condensed Consolidated Statements of Comprehensive Income</u>	3
<u>Condensed Consolidated Balance Sheets</u>	4
<u>Condensed Consolidated Statements of Cash Flows</u>	5
<u>Notes to Condensed Consolidated Financial Statements</u>	6
<b><u>Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations</u></b>	16
<b><u>Item 3. Quantitative and Qualitative Disclosures About Market Risk</u></b>	21
<b><u>Item 4. Controls and Procedures</u></b>	21
<b><u>Part II. Other Information</u></b>	
Item 1. <u>Legal Proceedings</u>	22
Item 1A. <u>Risk Factors</u>	22
Item 2. <u>Unregistered Sales of Equity Securities and Use of Proceeds</u>	22
Item 3. <u>Defaults Upon Senior Securities</u>	23
Item 4. <u>Mine Safety Disclosure</u>	23
Item 5. <u>Other Information</u>	23
Item 6. <u>Exhibits</u>	23

**Table of Contents****PART I FINANCIAL INFORMATION****ITEM 1. CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)****PGT, INC.****CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME***(in thousands, except per share amounts)*

	<b>Three Months Ended</b>	
	<b>March 29,</b>	<b>March 30,</b>
	<b>2014</b>	<b>2013</b>
	<i>(unaudited)</i>	
Net sales	\$ 62,724	\$ 49,563
Cost of sales	42,953	32,004
Gross margin	19,771	17,559
Selling, general and administrative expenses	13,377	13,024
Gain on sale of assets held for sale		(2,195)
Income from operations	6,394	6,730
Interest expense, net	898	813
Other expense, net	177	216
Income before income taxes	5,319	5,701
Income tax expense	1,967	437
Net income	\$ 3,352	\$ 5,264
Net income per common share:		
Basic	\$ 0.07	\$ 0.10
Diluted	\$ 0.07	\$ 0.09
Weighted average shares outstanding:		
Basic	47,150	52,517
Diluted	49,727	56,893
Comprehensive income	\$ 3,262	\$ 5,106

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



**Table of Contents****PGT, INC.****CONDENSED CONSOLIDATED BALANCE SHEETS***(in thousands, except per share amounts)*

	<b>March 29, 2014</b>	<b>December 28, 2013</b>
	<i>(unaudited)</i>	
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$ 30,777	\$ 30,204
Accounts receivable, net	22,392	20,821
Inventories	15,325	12,908
Prepaid expenses	1,166	1,538
Other current assets	3,174	3,166
Deferred income taxes, net	2,333	2,763
<b>Total current assets</b>	<b>75,167</b>	<b>71,400</b>
Property, plant and equipment, net	46,340	44,123
Intangible assets, net	38,441	38,869
Other assets, net	2,050	2,240
<b>Total assets</b>	<b>\$ 161,998</b>	<b>\$ 156,632</b>
<b>LIABILITIES AND SHAREHOLDERS EQUITY</b>		
Current liabilities:		
Accounts payable and accrued liabilities	\$ 16,974	\$ 15,522
Current portion of long-term debt	4,895	4,890
<b>Total current liabilities</b>	<b>21,869</b>	<b>20,412</b>
Long-term debt, less current portion	71,470	72,365
Deferred income taxes, net	13,380	13,380
Other liabilities	1,426	1,400
<b>Total liabilities</b>	<b>108,145</b>	<b>107,557</b>
Shareholders equity:		
Preferred stock; par value \$.01 per share; 10,000 shares authorized; none outstanding		
Common stock; par value \$.01 per share; 200,000 shares authorized; 49,312 and 48,868 shares issued and 47,228 and 46,871 shares outstanding at March 29, 2014, and December 28, 2013, respectively	493	489
Additional paid-in-capital	231,744	229,269
Accumulated other comprehensive loss	(2,313)	(2,223)

Accumulated deficit	(165,062)	(168,414)
Subtotal shareholders' equity	64,862	59,121
Less treasury stock, at cost	(11,009)	(10,046)
Total shareholders' equity	53,853	49,075
Total liabilities and shareholders' equity	\$ 161,998	\$ 156,632

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

Table of Contents

## PGT, INC.

## CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

*(in thousands)*

	<b>Three Months Ended</b>	
	<b>March 29,</b>	<b>March 30,</b>
	<b>2014</b>	<b>2013</b>
	<i>(unaudited)</i>	
<b>Cash flows from operating activities:</b>		
Net income	\$ 3,352	\$ 5,264
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	986	1,235
Amortization	428	1,626
Provision for allowances of doubtful accounts	(87)	(103)
Amortization and write off of deferred financing costs	234	389
Stock-based compensation	245	316
Derivative financial instruments	433	252
Deferred income taxes	429	
Tax benefit for stock options exercised	(1,538)	
Gain on disposal of assets		(2,178)
Change in operating assets and liabilities:		
Accounts receivable	(1,852)	(4,955)
Inventories	(2,417)	(1,960)
Prepaid and other assets	486	(23)
Accounts payable, accrued and other liabilities	2,804	1,991
Net cash provided by operating activities	3,503	1,854
<b>Cash flows from investing activities:</b>		
Purchases of property, plant and equipment	(3,203)	(637)
Proceeds from disposal of asset		7,470
Net cash (used in) provided by investing activities	(3,203)	6,833
<b>Cash flows from financing activities:</b>		
Payments of long-term debt	(1,000)	(7,500)
Purchases of treasury stock	(963)	(6,091)
Tax benefit for stock options exercised	1,538	
Proceeds from exercise of stock options	698	451
Net cash provided by (used in) financing activities	273	(13,140)
Net increase (decrease) in cash and cash equivalents	573	(4,453)
Cash and cash equivalents at beginning of period	30,204	18,743



Cash and cash equivalents at end of period	\$ 30,777	\$ 14,290
--	-----------	-----------

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

---

**Table of Contents**

**PGT, INC.**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

*(unaudited)*

**NOTE 1. BASIS OF PRESENTATION**

The accompanying unaudited condensed consolidated financial statements include the accounts of PGT, Inc. and its wholly-owned subsidiary, PGT Industries, Inc. (collectively, the Company ) after elimination of intercompany accounts and transactions. These statements have been prepared in accordance with the instructions to Form 10-Q and do not include all of the information and footnotes required by United States Generally Accepted Accounting Principles ( GAAP ) for complete financial statements. In the opinion of management, all adjustments (consisting only of normal recurring adjustments) considered necessary for a fair presentation have been included. Operating results for the interim period are not necessarily indicative of the results that may be expected for the remainder of the current year or for any future periods. Each of our Company s fiscal quarters ended March 29, 2014, and March 30, 2013, consisted of 13 weeks.

The condensed consolidated balance sheet as of December 28, 2013, is derived from the audited consolidated financial statements but does not include all disclosures required by GAAP. The condensed consolidated balance sheet as of December 28, 2013, and the unaudited condensed consolidated financial statements as of and for the period ended March 29, 2014, should be read in conjunction with the more detailed audited consolidated financial statements for the year ended December 28, 2013, included in the Company s most recent Form 10-K annual report. Accounting policies used in the preparation of these unaudited condensed consolidated financial statements are consistent with the accounting policies described in the Notes to Consolidated Financial Statements included in the Company s Form 10-K.

**Recently Issued Accounting Pronouncements**

In July 2013, the Financial Accounting Standards Board (FASB) issued ASU No. 2013-11, Income Taxes: Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward Exists, which requires tax benefits to be presented in the financial statement as a reduction to deferred tax asset for a net operating loss carryforward or a tax credit carryforward. We adopted this standard in the first quarter of 2014, and it did not impact the condensed consolidated financial statements.

**NOTE 2. WARRANTY**

Most of our manufactured products are sold with warranties. Warranty periods, which vary by product components, generally range from 1 to 10 years, although the warranty period for a limited number of specifically identified components in certain applications is a lifetime. However, the majority of the products sold have warranties on components which range from 1 to 3 years. The reserve for warranties is based on management s assessment of the cost per service call, the lag time between order ship dates and warranty service dates, and the number of service calls expected to be incurred to satisfy warranty obligations on recorded net sales. The reserve is determined after assessing Company history and through specific identification. Expected future obligations are discounted to a current value using a risk-free rate for obligations with similar maturities.

During the quarter, we recorded warranty expense at a rate of 1.75% of sales. This rate is higher than the 1.50% of sales accrued in the first quarter of 2013, due to a recent increase in the number of service claims. We assess the

adequacy of our warranty accrual on a quarterly basis and adjust the previous amounts recorded, if necessary, to reflect a change in estimate of the future costs of claims yet to be serviced.

The table set forth below summarizes current period charges, any adjustment to previous estimates if necessary, as well as settlements, which represent actual costs incurred during the period, for the three months ended March 29, 2014, and March 30, 2013. The reserve is determined after assessing Company history and through specific identification. Expected future obligations are discounted to a current value using a risk-free rate for obligations with similar maturities.

**Table of Contents**

The following provides information with respect to our warranty accrual:

<b>Accrued Warranty</b>	<b>Beginning of Period</b>	<b>Charged to Expense</b>	<b>Adjustments <i>(in thousands)</i></b>	<b>Settlements</b>	<b>End of Period</b>
Three months ended March 29, 2014	\$ 2,666	\$ 1,098	\$ 90	\$ (1,198)	\$ 2,656
Three months ended March 30, 2013	\$ 3,858	\$ 744	\$ (188)	\$ (841)	\$ 3,573

**NOTE 3. INVENTORIES**

Inventories consist principally of raw materials purchased for the manufacture of our products. We have limited finished goods inventory since all products are custom, made-to-order and usually ship upon completion. Finished goods inventory costs include direct materials, direct labor, and overhead. All inventories are stated at the lower of cost (first-in, first-out method) or market value. Inventories consisted of the following:

	March 29, 2014	December 28, 2013
	<i>(in thousands)</i>	
Raw materials	\$ 12,291	\$ 11,305
Work in progress	429	329
Finished goods	2,605	1,274
Total inventories	\$ 15,325	\$ 12,908

**NOTE 4. STOCK COMPENSATION EXPENSE**

On March 28, 2014, the Board of Directors adopted, and on May 7, 2014, our stockholders approved, the PGT, Inc. 2014 Omnibus Equity Incentive Plan (the "2014 Equity Incentive Plan"). The Board of Directors determined that grants of restricted shares and other share-based awards to our officers, employees, Directors, independent contractors and consultants are an important part of our long-term incentive compensation program, which we use in order to strengthen the commitment of such individuals to the Company, motivate them to faithfully and diligently perform their responsibilities, and attract and retain competent and dedicated individuals, whose efforts will result in the long-term growth and profitability of the Company.

*2014 Omnibus Equity Incentive Plan*

The 2014 Omnibus Equity Incentive Plan, among other things:

provides 1,500,000 common shares available for grants of equity awards,

sets forth the types of awards eligible under the plan, including issuances of options, share appreciation rights, restricted shares, restricted share units, share bonuses, other share-based awards and cash awards,

identifies those eligible to receive the equity awards include company officers, employees, directors, and certain independent contractors and consultants, and

confirms that the governance and administration of such equity plan is the responsibility of the Board of Directors, or Compensation Committee at the direction of the Board.

*Exercises*

In the first quarter of 2014, there were 432,162 options exercised at a weighted average exercise price of \$1.61 per share, and 12,027 restricted shares vested at a weighted average fair value price of \$10.30 per share.

*New Issuances*

In March 2014, we issued 20,000 options and 144,262 restricted stock awards to certain executive and non-executive employees of the Company. The options vest over a five year period from March 2014, and have an exercise price of \$11.81 per share based on the NASDAQ market price of the underlying common stock on the close of business on the day the options were granted. The restricted stock awards were issued as two separate grants, the first being both performance and service based awards with a weighted average fair value on date of grant of \$11.81 per share based on the NASDAQ market price of the common stock on the close of business on

**Table of Contents**

the day the awards were granted, and vest over a three year period. The second awards were service based only, with a weighted average fair value on date of grant of \$11.81 per share based on the NASDAQ market price of the common stock on the close of business on the day the awards were granted, and vest over a three year period.

We record stock compensation expense over an award's vesting period based on the award's fair value at the date of grant. We recorded compensation expense for stock-based awards of \$0.2 million for the first quarter of 2014 and \$0.3 million for the first quarter of 2013. As of March 29, 2014, and March 30, 2013, there was \$2.0 million and \$1.0 million, respectively, of total unrecognized compensation cost related to non-vested stock options and restricted stock awards. These costs are expected to be recognized in earnings on a straight-line basis over the weighted average remaining vesting period of 2.1 years.

**NOTE 5. NET INCOME PER COMMON SHARE**

Basic EPS is determined using the two-class method and is computed by dividing net income available to common shareholders by the weighted-average number of common shares outstanding during the period. Diluted EPS reflects the dilutive effect of potential common shares from securities such as stock options.

Our weighted average shares outstanding for the three months ended March 29, 2014, and March 30, 2013, excludes underlying options of 47 thousand and 22 thousand, respectively, because their effects were anti-dilutive.

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

	<b>Three Months Ended</b>	
	<b>March 29, 2014</b>	<b>March 30, 2013</b>
	<i>(in thousands, except per share amounts)</i>	
Net income	\$ 3,352	\$ 5,264
Weighted-average common shares - Basic	47,150	52,517
Add: Dilutive effect of stock compensation plans	2,577	4,376
Weighted-average common shares - Diluted	49,727	56,893
<b>Net income per common share:</b>		
Basic	\$ 0.07	\$ 0.10
Diluted	\$ 0.07	\$ 0.09

**NOTE 6. INTANGIBLE ASSETS**

Intangible assets are as follows:

	March 29, 2014	December 28, 2013	Original Useful Life (in years)
	<i>(in thousands)</i>		
<b>Intangible assets:</b>			
Trade names	\$ 38,441	\$ 38,441	indefinite
Customer relationships	55,700	55,700	10
Less: Accumulated amortization	(55,700)	(55,272)	
Subtotal		428	
Intangible assets, net	\$ 38,441	\$ 38,869	

---

**Table of Contents****Indefinite Lived Intangible Asset**

The impairment evaluation of the carrying amount of intangible assets with indefinite lives is conducted annually, or more frequently if events or changes in circumstances indicate that an asset might be impaired. The evaluation is performed by comparing the carrying amounts of these assets to their estimated fair values. If the estimated fair value is less than the carrying amount of the intangible assets, an impairment charge is recorded to reduce the asset to its estimated fair value. The estimated fair value is determined using the relief from royalty method that is based upon the discounted projected cost savings (value) attributable to ownership of our trade names, our only indefinite lived intangible assets.

In estimating fair value, the method we use requires us to make assumptions, the most material of which are net sales projections attributable to products sold with these trade names, the anticipated royalty rate we would pay if the trade names were not owned (as a percent of net sales), and a weighted average discount rate. These assumptions are subject to change based on changes in the markets in which these products are sold, which impact our projections of future net sales and the assumed royalty rate. Factors affecting the weighted average discount rate include assumed debt to equity ratios, risk-free interest rates, and equity returns, each for market participants in our industry.

Our year-end test of trade names, performed as of December 28, 2013, utilized a weighted average royalty rate of 4.0% and a discount rate of 16.1%. As of December 28, 2013, the estimated fair value of the trade names exceeded book value by approximately 79%, or \$30.3 million. We believe our projected sales are reasonable based on available information regarding our industry and the core markets that we serve. We also believe the royalty rate is appropriate and could improve over time based on market trends and information. The discount rate was based on current financial market trends and will remain dependent on such trends in the future.

No impairment test was conducted during the quarter ended March 29, 2014, because no impairment indicators were identified.

**Amortizable Intangible Assets**

We perform an impairment test on our amortizable intangible assets any time that impairment indicators exist. As of March 29, 2014, all amortizable intangible assets have been fully amortized.

**NOTE 7. LONG-TERM DEBT**

On May 28, 2013, we entered into a Credit Agreement (the "Credit Agreement") with the various financial institutions and other persons from time to time parties thereto as lenders (the "Lenders"), SunTrust Bank, as administrative agent (in such capacity, the "Administrative Agent"), as collateral agent, as swing line lender and as a letter of credit issuer, and the other agents and parties thereto. The Credit Agreement established new senior secured credit facilities in an aggregate amount of \$105.0 million, consisting of an \$80.0 million Tranche A term loan facility maturing in five years that will amortize on a basis of 5% annually during the five-year term, and a \$25.0 million revolving credit facility maturing in five years that includes a \$5.0 million swing line facility and a \$10.0 million letter of credit facility.

Interest on all loans under the Credit Agreement is payable either quarterly or at the expiration of any LIBOR interest period applicable thereto. Borrowings under the term loans and the revolving credit facility accrue interest at a rate equal to, at our option, a base rate or LIBOR plus an applicable margin. The applicable margin is based on our leverage ratio, ranging from 300 to 350 basis points in the case of LIBOR and 200 to 250 basis points in the case of the base rate. We pay quarterly fees on the unused portion of the revolving credit facility equal to 0.50% as well as a quarterly letter of credit fee at a rate per annum equal to the applicable margin for LIBOR loans on the face amount of



any outstanding letters of credit.

On September 16, 2013, we entered into two interest rate caps and an interest rate swap to hedge a portion of our debt against volatility in future interest rates (See Note 11).

The Credit Agreement requires us to maintain a maximum leverage ratio (based on the ratio of total funded debt to consolidated EBITDA, each as defined in the Credit Agreement) and a minimum fixed charge coverage ratio (based on the ratio of consolidated EBITDA minus net cash taxes minus capital expenditures to cash interest expense plus scheduled principal payments of term loans, each as defined in the Credit Agreement), which are tested quarterly based on the last four fiscal quarters and is set at levels as described in the Credit Agreement. As of March 29, 2014, our current leverage as defined in the calculation was 1.75, and we were in compliance and expect to be in the future.

The Credit Agreement also contains a number of affirmative and restrictive covenants, including limitations on the incurrence of additional debt, liens on property, acquisitions and investments, loans and guarantees, mergers, consolidations, liquidations and dissolutions, asset sales, dividends and other payments in respect of our capital stock, prepayments of certain debt and transactions with affiliates. The Credit Agreement also contains customary events of default.

**Table of Contents**

In connection with entering into the Credit Agreement, on May 28, 2013, we terminated the credit agreement, dated as of June 23, 2011, among PGT Industries, Inc., as the borrower, the Company, as guarantor, the lenders from time to time party thereto and General Electric Capital Corporation, as administrative agent and collateral agent (the Old Credit Agreement). Proceeds from the term loan facility under the Credit Agreement were used to repay amounts outstanding under the Old Credit Agreement, repurchase shares of our common stock having an aggregate value of approximately \$50 million, and pay certain fees and expenses.

On August 5, 2013, we entered into Amendment No. 1 (the Amendment) to the Credit Agreement dated May 28, 2013. The Amendment permits us to make capital expenditures (as defined in the Credit Agreement) in an amount up to but not exceeding \$14.0 million in connection with the expansion and operation of our glass processing business and activities without reducing the amount of capital expenditures otherwise permitted.

The face value of the debt as of March 29, 2014, was \$78.0 million. Related debt issuance costs and the debt discount are being amortized to interest expense, net on the Condensed Consolidated Statements of Comprehensive Income over the term of the debt.

The contractual future maturities of long-term debt outstanding as of March 29, 2014, are as follows (excluding unamortized debt discount and issuance costs):

	<i>(in thousands)</i>
2014	\$ 4,000
2015	4,000
2016	4,000
2017	3,000
2018	63,000
Total debt	\$ 78,000

**NOTE 8. ACCUMULATED OTHER COMPREHENSIVE LOSS**

The following table shows the activity of accumulated other comprehensive loss, net of tax for the three months ended March 29, 2014, and March 30, 2013:

	<b>Aluminum Forward Contracts</b>	<b>Interest Swap</b>	<b>Total</b>
	<i>(in thousands)</i>		
Balance at December 28, 2013	\$ (1,837)	\$ (386)	\$ (2,223)
Other comprehensive loss before reclassification	(97)	(154)	(251)
Amounts reclassified from accumulated other comprehensive loss	161		161
Net current-period other comprehensive loss	64	(154)	(90)

Balance at March 29, 2014	\$ (1,773)	\$ (540)	\$ (2,313)
	<b>Aluminum Forward Contracts</b>	<b>Interest Swap</b>	<b>Total</b>
		<i>(in thousands)</i>	
Balance at December 29, 2012	\$ (1,414)	\$	\$ (1,414)
Other comprehensive loss before reclassification	(158)		(158)
Amounts reclassified from accumulated other comprehensive loss			
Net current-period other comprehensive loss	(158)		(158)
Balance at March 30, 2013	\$ (1,572)	\$	\$ (1,572)

**Table of Contents**

Reclassification out of accumulated other comprehensive loss for the three months ended March 29, 2014, and March 30, 2013:

Detail about accumulated other comprehensive loss components	Amount reclassified from Accumulated Other Comprehensive Loss		Affected line item in statement where Net Income is presented
	March 29, 2014	March 30, 2013	
	<i>(in thousands)</i>		
Aluminum Forward Contracts			
Effective Portion of aluminum forward contracts	\$ 256	\$	Cost of Sales
Tax effect	(95)		Tax expense
	\$ 161	\$	

**NOTE 9. COMMITMENTS AND CONTINGENCIES***Litigation*

Our Company is a party to various legal proceedings in the ordinary course of business. Although the ultimate disposition of those proceedings cannot be predicted with certainty, management believes the outcome of any claim that is pending or threatened, either individually or in the aggregate, will not have a materially adverse effect on our operations, financial position or cash flows.

**NOTE 10. INCOME TAXES**

We recognized income taxes at a rate of 37.0%, which is slightly lower than the statutory rate of 38.8% for the three months ended March 29, 2014. The rate is lower than the statutory rate due mainly to the estimated impact of the section 199 manufacturing deduction.

Our income tax rate was 7.7% for the three months ended March 30, 2013, as we released a portion of our deferred tax asset valuation allowance to offset a portion of our regular tax expense. As of the year ended 2013, we had no valuation allowance on our deferred tax assets.

**NOTE 11. DERIVATIVES**

We enter into aluminum forward contracts to hedge the fluctuations in the purchase price of aluminum extrusion we use in production. Our contracts are designated as cash flow hedges since they are highly effective in offsetting changes in the cash flows attributable to forecasted purchases of aluminum.

In addition, we entered into LIBOR rate hedges on September 16, 2013, to offset the changes in cash flows of the debt interest rate payments that are attributable to the fluctuations of LIBOR rates. With the exception of the time value portion of our caps, these contracts are designated as cash flow hedges since they are highly effective in offsetting the changes in the monthly interest payments attributable to the changes in interest rates during the term of the agreement.

We net cash collateral from payments of margin calls on deposit with our brokers against the liability position of open contracts for the purchase of hedge instruments on a first-in, first-out basis. For statement of cash flows presentation, we present net cash receipts from and payments to the margin account as investing activities.

**Derivative Financial Instruments Aluminum Contracts**

Guidance under the Financial Instruments topic of the Codification requires us to record our hedge contracts at fair value and consider our credit risk for contracts in a liability position, and our counter-party's credit risk for contracts in an asset position, in determining fair value. We assess our counter-party's risk of non-performance when measuring the fair value of financial instruments in an asset position by evaluating their financial position, including cash on hand, as well as their credit ratings. We assess our risk of non-performance when measuring the fair value of our financial instruments in a liability position by evaluating our credit ratings, our current liquidity, including cash on hand, and availability under our revolving credit facility as compared to the maturities of the financial liabilities. In addition, we entered into a master netting arrangement (MNA) with our commodities broker that provides for, among other things, the close-out netting of exchange-traded transactions in the event of the insolvency of either party to the MNA.

---

**Table of Contents**

We maintain a \$2.0 million line of credit with our commodities broker to cover the liability position of open contracts for the purchase of aluminum in the event that the price of aluminum falls. Should the price of aluminum fall to a level which causes our liability for open aluminum contracts to exceed \$2.0 million, we are required to fund daily margin calls to cover the excess.

At March 29, 2014, the fair value of our aluminum forward contracts was in a net liability position of \$0.6 million. We had 29 outstanding forward contracts for the purchase of 9.1 million pounds of aluminum, representing approximately 36% of our anticipated needs through June 2015, at an average price of \$0.88 per pound with maturity dates of between less than one month and fifteen months. We assessed the risk of non-performance of the Company to these contracts and recorded a de minimis adjustment to fair value as of March 29, 2014.

As of December 28, 2013, the fair value of our aluminum forward contracts was in a net liability position of approximately \$0.5 million. We had 33 outstanding forward contracts for the purchase of 9.5 million pounds of aluminum at an average price of \$0.89 per pound with maturity dates of between less than one month and eighteen months through June 2015. We assessed the risk of non-performance of the Company on these contracts and recorded a de minimis adjustment to fair value as of December 28, 2013.

Although it is our intent to have our aluminum hedges qualify as highly effective for reporting purposes, during the three months ended March 29, 2014, 12 of our 29 outstanding contracts no longer qualified as effective. Effectiveness of aluminum forward contracts is determined by comparing the change in the fair value of the forward contract to the change in the expected cash to be paid for the hedged item. The effective portion of the gain or loss on our aluminum forward contracts is reported as a component of Accumulated other comprehensive loss in the accompanying Condensed Consolidated Balance Sheets and is reclassified into earnings in the same line item in the Consolidated Statement of Comprehensive Income as the hedged item in the same period or periods during which the transaction affects earnings. When a cashflow hedge becomes ineffective, and if the forecasted hedged transaction is still probable of occurrence, amounts previously recorded in Accumulated other comprehensive loss remain in Accumulated other comprehensive loss and are recognized in earnings in the period in which the hedged transaction affects earnings. The change in value of the aluminum forward contracts occurring after ineffectiveness is recognized in Other expense, net on the Condensed Consolidated Statements of Comprehensive Income. We do not expect the gains or losses recognized in Accumulated other comprehensive loss as of March 29, 2014, that will be reclassified to earnings within the next three months to be material.

As of December 28, 2013, our aluminum hedges qualified as effective for reporting purposes and amounts were recorded in Accumulated other comprehensive loss.

**Derivative Financial Instruments – Interest Rate Contract**

On September 16, 2013, we entered into two interest rate caps and one interest rate swap. The first is a one year interest rate cap agreement with a notional amount of \$40.0 million that was designated as a cash flow hedge that protects the variable rate debt from an increase in the floating one month LIBOR rate of greater than 0.50%. The second is a two year interest rate cap agreement with a notional amount of \$20.0 million that was designated as a cash flow hedge that protects the variable rate debt from an increase in the floating one month LIBOR rate of greater than 0.50%. Effectiveness for the interest rate caps will be measured by comparing the changes in the intrinsic value of the cap with the change in the fair value of the forecasted interest payments due to changes in the LIBOR interest rate when LIBOR is greater than 0.50%. The intrinsic value portions of the interest rate caps are expected to be highly effective due to the critical terms of the cap exactly matching those of the hedged debt. The time value portion of the caps are deemed ineffective and will be marked to market in the reporting period.

The swap is a forward starting three year six months interest rate swap agreement with a notional amount of \$40.0 million that effectively converted a portion of the floating rate debt to a fixed rate of 2.15% that starts September 28, 2014, with a termination date of May 18, 2018. Since all of the critical terms of the swap and cap exactly matched those of the hedged debt, no ineffectiveness was identified in the hedging relationship. Consequently, all changes in fair value are recorded as a component of Accumulated other comprehensive income. Hedge effectiveness for the interest rate swap is evaluated on a quarterly basis by comparing changes in the cumulative gain or loss from the forward-starting interest rate swap with the cumulative changes in the discounted expected cash flows of future monthly interest related to changes of the swap rate.

**Table of Contents**

The impact of the offsetting derivative instrument is depicted below:

As of March 29, 2014

(in thousands)

Description	Gross Amounts of Assets Presented in Balance Sheet		Gross Amounts not offset in Balance Sheet		Net Amount
	Gross Amounts Recognized	Balance Sheet	Balance Sheet	Financial Instruments	
Interest rate caps	\$ 19	\$	\$ 19	\$	\$ 19

As of March 29, 2014

Description	Gross Amounts of Liabilities		Gross Amounts not offset in Balance Sheet		Net Amount
	Gross Amounts Recognized	Balance Sheet	Balance Sheet	Financial Instruments	
Aluminum forward contract	\$ 576	\$	\$ 576	\$	\$ 576
Interest rate swap	\$ 785	\$	\$ 785	\$	\$ 785

As of December 28, 2013

Description	Gross Amounts of Assets		Gross Amounts not offset in Balance Sheet		Net Amount
	Gross Amounts Recognized	Balance Sheet	Balance Sheet	Financial Instruments	
Interest rate cap	\$ 34	\$	\$ 34	\$	\$ 34

As of December 28, 2013

(in thousands)



Description	Gross Amounts not offset in Balance Sheet					Net Amount
	Gross Amounts of Recognized Liabilities	Gross Amounts offset in Balance Sheet	Net amounts of Liabilities Presented in Balance Sheet	Cash Financial Instruments	Cash Collateral Pledged	
Aluminum forward contract	\$ 479	\$	\$ 479	\$	\$	\$ 479
Interest rate swap	\$ 630	\$	\$ 630	\$	\$	\$ 630

The fair value of our derivatives are classified in the accompanying Condensed Consolidated Balance Sheets as follows:

Derivatives in a net asset (liability) position	Balance Sheet Location		March 29, 2014	December 28, 2013
			<i>(in thousands)</i>	
<b>Hedging Instruments:</b>				
Aluminum forward contracts	Accrued Liabilities		\$ (506)	\$ (441)
Aluminum forward contracts	Other Liabilities		(70)	(38)
Interest rate cap	Other Current Asset		13	21
Interest rate cap	Other Assets		6	13
Interest rate swap	Other Liabilities		(785)	(630)
<b>Total hedging instruments</b>			<b>\$ (1,342)</b>	<b>\$ (1,075)</b>

**Table of Contents**

The following represents the gains (losses) on derivative financial instruments for the three months ended March 29, 2014, and March 30, 2013, and their classifications within the accompanying Condensed Consolidated Financial Statements:

	<b>Derivatives in Cash Flow Hedging Relationships</b>			
	<b>Amount of Gain or (Loss) Recognized in OCI on Derivatives (Effective Portion) Three Months Ended</b>		<b>Amount of (Loss) Reclassified from Accumulated OCI into Income (Effective Portion)</b>	
	<b>(in thousands)</b>		<b>(in thousands)</b>	
	<b>March 29, 2014</b>	<b>March 30, 2013</b>	<b>March 29, 2014</b>	<b>March 30, 2013</b>
Aluminum contracts	\$ (192)	\$ 157	Cost of sales	\$ (256) \$
Interest rate swap	\$ (154)	\$	Interest expense, net	\$ \$

  

	<b>Amount of (Loss) Recognized in Location of Gain or (Loss) Recognized in Income on Derivatives (Ineffective Portion)</b>	
	<b>Three Months Ended</b>	
	<b>(in thousands)</b>	
	<b>March 29, 2014</b>	<b>March 30, 2013</b>
Aluminum contracts	Other Expense, net	\$ (162) \$ (252)
Interest rate swap	Other Expense, net	\$ \$

**NOTE 12. FAIR VALUE**

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants. A three-tier fair value hierarchy is used to prioritize the inputs used in measuring fair value. The hierarchy gives the highest priority to unadjusted quoted market prices in active markets for identical assets or liabilities and the lowest priority to unobservable inputs. A financial instrument's level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. The three levels of the fair value hierarchy are as follows:

Level 1 Unadjusted quoted prices in active markets that are accessible at the measurement date for identical, unrestricted assets or liabilities.

Level 2 Inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly or indirectly.

Level 3 Prices or valuations that require inputs that are both significant to the fair value measurement and unobservable.

The accounting guidance concerning fair value allows us to elect to measure financial instruments at fair value and report the changes in fair value through the Condensed Consolidated Statements of Comprehensive Income. This election can only be made at certain specified dates and is irrevocable once made. We do not have a policy regarding specific assets or liabilities to elect to measure at fair value, but rather make the election on an instrument-by-instrument basis as they are acquired or incurred.

**Table of Contents****Items Measured at Fair Value on a Recurring Basis**

The following assets and liabilities are measured in the Condensed Consolidated Balance Sheets at fair value on a recurring basis and are categorized in the table below based upon the lowest level of significant input to the valuation:

<b>Fair Value Measurements at Reporting Date of Net Asset (Liability) Using:</b> <i>(in thousands)</i>				
<b>Description</b>	<b>Quoted Prices in Active Markets (Level 1)</b>		<b>Significant Unobservable Inputs (Level 3)</b>	
	<b>March 29, 2014</b>	<b>Significant Other Observable Inputs (Level 2)</b>	<b>Significant Other Observable Inputs (Level 2)</b>	<b>Significant Unobservable Inputs (Level 3)</b>
Aluminum forward contracts	\$ (576)	\$	\$ (576)	\$
Interest rate cap	19		19	
Interest rate swap	(785)		(785)	
Derivative financial instruments, net liability	\$ (1,342)	\$	\$ (1,342)	\$

  

<b>Description</b>	<b>Quoted Prices in Active Markets (Level 1)</b>		<b>Significant Other Observable Inputs (Level 2)</b>		<b>Significant Unobservable Inputs (Level 3)</b>	
	<b>December 28, 2013</b>	<b>December 28, 2013</b>	<b>December 28, 2013</b>	<b>December 28, 2013</b>	<b>December 28, 2013</b>	<b>December 28, 2013</b>
Aluminum forward contracts	\$ (479)	\$	\$ (479)	\$	\$	\$
Interest rate cap	34		34			
Interest rate swap	(630)		(630)			
Derivative financial instruments, net liability	\$ (1,075)	\$	\$ (1,075)	\$	\$	\$

The following is a description of the methods and assumptions used to estimate the fair values of our assets and liabilities measured at fair value on a recurring basis, as well as the basis for classifying these assets and liabilities as Level 2.

Aluminum forward contracts identical to those held by us trade on the London Metal Exchange ( LME ). The LME provides a transparent forum and is the world's largest center for the trading of futures contracts for non-ferrous metals. The prices are used by the metals industry worldwide as the basis for contracts for the movement of physical material throughout the production cycle. Based on this high degree of volume and liquidity in the LME, we believe the valuation price at any measurement date for contracts with identical terms as to prompt date, trade date and trade price as those we hold at any time represents a contract's exit price to be used for purposes of determining fair value.

Interest rate cap and swap contracts identical to those held by us are sold by financial institutions. The valuation price at any measurement date for a contract with identical terms, exercise price, expiration date, settlement date, and notional quantities, as the one we hold, is used for determining the fair value.

**Fair Value of Financial Instruments**

The following table presents the carrying values and estimated fair values of financial assets and liabilities that are required to be recorded or disclosed at fair value at March 29, 2014, and December 28, 2013, respectively:

	March 29, 2014		December 28, 2013	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
<i>(in thousands)</i>				
<b>Financial assets and liabilities</b>				
Cash and cash equivalents	\$ 30,777	\$ 30,777	\$ 30,204	\$ 30,204
Accounts receivable, net	\$ 22,392	\$ 22,392	\$ 20,821	\$ 20,821
Accounts payable and accrued liabilities	\$ 16,974	\$ 16,974	\$ 15,522	\$ 15,522
Long-term debt (including current portion)	\$ 76,365	\$ 76,365	\$ 77,255	\$ 77,255

The following provides a description of the methods and significant assumptions used in estimating the fair value of our financial instruments that are not measured at fair value on a recurring basis.

*Cash and cash equivalents* The estimated fair value of these financial instruments approximates their carrying amounts due to their highly liquid or short-term nature.

---

**Table of Contents**

*Accounts receivable, net* The estimated fair value of these financial instruments approximates their carrying amounts due to their short-term nature.

*Accounts payable and accrued liabilities* The estimated fair value of these financial instruments approximate their carrying amounts due to their short-term nature.

*Debt* The estimated fair value of this debt is based on level 2 inputs of debt with similar terms and characteristics.

**NOTE 13. ASSETS HELD FOR SALE**

During the first quarter of 2013, we sold the Salisbury, North Carolina facility for approximately \$8.0 million in cash (approximately \$7.5 million net of selling costs), resulting in a gain of \$2.2 million.

**ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

The following discussion of our financial condition and results of operations should be read in conjunction with the Management's Discussion and Analysis of Financial Condition and Results of Operations and the consolidated financial statements and notes thereto for the year ended December 28, 2013, included in our most recent Form 10-K annual report as well as our reports on Forms 10-Q and 8-K and other publicly available information. All amounts herein are unaudited.

**Special Note Regarding Forward-Looking Statements**

From time to time, we have made or will make forward-looking statements within the meaning of Section 21E of the Exchange Act. These statements do not relate strictly to historical or current facts. Forward-looking statements usually can be identified by the use of words such as goal, objective, plan, expect, anticipate, intend, project, believe, may, could, or other words of similar meaning. Forward-looking statements provide our current expectations or forecasts of future events, results, circumstances or aspirations. Our disclosures in this report contain forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. We may also make forward-looking statements in our other documents filed or furnished with the Securities and Exchange Commission and in oral presentations. Forward-looking statements are based on assumptions and by their nature are subject to risks and uncertainties, many of which are outside of our control. Our actual results may differ materially from those set forth in our forward-looking statements. There is no assurance that any list of risks and uncertainties or risk factors is complete. Factors that could cause actual results to differ materially from those described in our forward-looking statements include, but are not limited to:

Changes in new home starts and home remodeling trends

The economy in the U.S. generally or in Florida where the substantial portion of our sales are generated

Raw material prices, especially aluminum

Transportation costs

Level of indebtedness

Dependence on our WinGuard branded product lines

Product liability and warranty claims

Federal and state regulations

Dependence on our manufacturing facilities

Any forward-looking statements made by us or on our behalf speak only as of the date they are made and we do not undertake any obligation to update any forward-looking statement to reflect the impact of subsequent events or circumstances. Before making any investment decision, you should carefully consider all risks and uncertainties disclosed in all our SEC filings, including our reports on Forms 8-K, 10-Q and 10-K and our registration statements under the Securities Act of 1933, as amended, all of which are accessible on the SEC's website at [www.sec.gov](http://www.sec.gov) and at <http://ir.pgtindustries.com/sec.cfm>

## **EXECUTIVE OVERVIEW**

### **Sales and Operations**

On May 7, 2014, we issued a press release, and held a conference call on May 8, 2014, to review the results of operations for the three months ended March 29, 2014. During the call, we also discussed current market conditions and progress made regarding certain business initiatives. The overview and estimates contained in this report are consistent with those given in our press release and our conference call remarks. We are neither updating nor confirming that information.

**Table of Contents**

We generated net sales of \$62.7 million, up over last year's first quarter net sales of \$49.6 million, a continuation of the sales growth that we experienced during 2013. This growth of 26.6% was primarily driven by our ability to take market share and outperform the improving Florida new construction housing market, along with sales and marketing programs targeting our WinGuard products for the repair and remodel market. As macro-economic conditions continued to improve, specifically in Florida, our mix shifted from 29% of total sales in the first quarter of 2013 being sold into new construction projects, to 35% in the first quarter of 2014. Our WinGuard new construction products lead this shift, with sales up 56% over prior year.

During the quarter, impact sales grew 26.3% over prior year, and represented 76.5% of total sales, driven by our WinGuard products with sales of \$45 million. Our percentage of impact sales is consistent with the 76.6% of total sales a year ago. In addition, our non-impact products sales grew 27.4% over prior year, with sales in both non-impact vinyl and non-impact aluminum up 33% and 28%, respectively, year over year.

Our sales growth generated a 12.6% increase in gross margin dollars; however, our gross margin percentage decreased by 3.9% primarily attributable to an increase in purchased finished glass units in excess of current internal glass capacities to support our sales growth, as well as inefficiencies in both labor costs and scrap rates resulting from hiring and training 400 new employees since the end of the 2013 first quarter. In addition, our margins were impacted from targeted large project pricing to gain market share, and a shift in mix towards new construction.

Selling, general and administrative expenses as a percent of sales decreased to 21.3%, compared to 26.3% in the first quarter of 2013, due to strong leverage on increased sales as well as a reduction of \$1.2 million in amortization expense from 2013.

In the first quarter of 2014, we posted net income of \$3.4 million compared to \$5.3 million a year ago. Net income for the first quarter of 2013 included a \$2.2 million gain on the sale of our Salisbury, North Carolina facility.

As we look forward, we expect to capitalize on improving economic conditions, especially in our core Florida market, and our investments in consumer promotions and advertising. We are in the process of constructing our new glass facility to address our internal capacity constraints, which is scheduled to be operational by the end of the third quarter of 2014. In addition, we are focusing resources on hiring and training new employees to meet demand in line with projected top line growth. We expect to continue the momentum of strong year over year sales growth in the second quarter. April sales, in fact, were up approximately 24% over prior year, and we are forecasting second quarter sales to be between \$76 million and \$78 million, compared to \$62.8 million in second quarter of 2013.

**Performance Summary**

The following table presents financial data derived from our unaudited Condensed Consolidated Statements of Comprehensive Income as a percentage of total net sales for the periods indicated:

	<b>Three Months Ended</b>			
	<i>(unaudited)</i>			
	<b>March 29,</b>		<b>March 30,</b>	
	<b>2014</b>		<b>2013</b>	
	<i>(in thousands)</i>			
Net sales	\$ 62,724	100.0%	\$ 49,563	100.0%
Cost of sales	42,953	68.5%	32,004	64.6%



Edgar Filing: PGT, Inc. - Form 10-Q

Gross margin	19,771	31.5%	17,559	35.4%
Selling, general and administrative expenses	13,377	21.3%	13,024	26.3%
Gain on sale of assets held for sale		0.0%	(2,195)	-4.4%
Income from operations	6,394	10.2%	6,730	13.6%
Interest expense, net	898	1.4%	813	1.6%
Other expense, net	177	0.3%	216	0.4%
Income before income taxes	5,319	8.5%	5,701	11.5%
Income tax expense	1,967	3.1%	437	0.9%
Net income	\$ 3,352	5.3%	\$ 5,264	10.6%

**Table of Contents**

The following table represents total sales by product category for the three months ended March 29, 2014, and March 30, 2013:

Product category:	Three Months Ended				
	March 29, 2014		March 30, 2013		% change
	Sales	% of sales	Sales	% of sales	
	<i>(in millions)</i>				
Impact Window and Door Products	\$ 47,976	76.5%	\$ 37,990	76.6%	26.3%
Other Window and Door Products	14,748	23.5%	11,573	23.4%	27.4%
Total net sales	\$ 62,724	100.0%	\$ 49,563	100.0%	26.6%

Net sales of impact window and door products, which include our WinGuard, PremierVue and Architectural Systems product lines, were \$48.0 million for the first quarter of 2014, an increase of \$10.0 million, or 26.3%, from \$38.0 million in net sales for the 2013 first quarter. WinGuard led the increased sales growth in impact products both in new construction sales by 56%, and in repair and remodel markets by 15% over the first quarter of 2013. Both new construction and repair and remodel growth rates exceeded market growth, due in part to our ability to deliver on our value proposition as well as large project pricing, designed to gain share.

Net sales of other window and door products were \$14.7 million for the first quarter of 2014, an increase of \$3.1 million, or 27.4%, from \$11.6 million in net sales for the 2013 first quarter. This increase primarily resulted from an increase in sales of our non-impact aluminum products of \$1.5 million, non-impact vinyl products, up \$1.3 million, and an increase in Eze-Breeze product sales of \$0.3 million. Our non-impact products sales increase also benefited from the growth in new construction sales, as overall revenue growth from new construction increased by 54%.

**Gross margin**

Gross margin was \$19.8 million in the first quarter of 2014, an increase of \$2.2 million in gross margin dollars, or 12.6%, from the first quarter of 2013. Gross margin as a percentage of net sales was 31.5%, a decrease of 3.9% from the 35.4% in the first quarter of 2013. The decrease in gross margin as a percentage of sales was due to an increase in material costs from purchasing finished glass in excess of our current glass capacities to support our sales growth, resulting in a decrease of 1.7%, as well as large project pricing to gain market share and a shift in mix towards new construction, resulting in a decrease of 2.1%. Additionally, operational inefficiencies in both labor and scrap rates resulting from hiring and training our new employees, negatively impacting our margin by 1.0%, and additional health care and other overhead costs, impacted our margin by 1.3%. These factors were partially offset by leveraging higher sales, and the favorable impact of the price increase announced in the third quarter of 2013, which combined to positively impact gross margin by 2.2%.

**Selling, general and administrative expenses**

Selling, general and administrative expenses were \$13.4 million for the first quarter of 2014, an increase of \$0.4 million from \$13.0 million for the first quarter of 2013. The key factors driving the increase were an increase of \$0.9 million in selling activities consistent with higher sales, and \$0.7 million in employee related costs for distribution and general administration. This was partially offset by \$1.2 million in lower amortization expense.

***Gain on sale of assets held for sale***

During the first quarter of 2013, we sold the Salisbury, North Carolina facility for approximately \$8.0 million in cash (approximately \$7.5 million net of selling costs), resulting in a gain of \$2.2 million.

***Interest expense, net***

Interest expense, net was \$0.9 million in the first quarter of 2014, an increase of \$0.1 million from \$0.8 million for the first quarter of 2013. Our interest expense increased slightly from prior year due to the increased debt balance, while offset by decreased interest rates from the new agreement, and decreased deferred financing costs.

***Other expense, net***

Other expense, net was \$0.2 million in the first quarter of 2014, in-line with the \$0.2 million in the first quarter of 2013. The amount in 2014 and 2013 primarily relates to the ineffective portion of aluminum hedges.

**Table of Contents*****Income tax expense***

We recognized income taxes at a rate of 37.0%, which is slightly lower than the statutory rate of 38.8% for the three months ended March 29, 2014. The rate is lower than the statutory rate due mainly to the estimated impact of the Section 199 manufacturing deduction.

For the three months ended March 30, 2013, our tax rate of 7.7% was lower than the statutory rate, as we released a portion of our deferred tax asset valuation allowance to offset a portion of our regular tax expense. As of year ended 2013, we had no valuation allowance on our deferred tax assets.

**Liquidity and Capital Resources**

Our principal source of liquidity is cash flow generated by operations, supplemented by borrowings under our credit facilities. This cash generating capability provides us with financial flexibility in meeting operating and investing needs. Our primary capital requirements are to fund working capital needs, meet required debt service payments on our credit facilities and fund capital expenditures, largely related to our glass plant expansion.

***Consolidated Cash Flows***

*Operating Activities.* Our sales growth resulted in an increase in working capital of \$2.3 million, mainly in accounts receivable and additional inventory needs as a result of increased sales. Cash provided by operating activities during the quarter was \$3.5 million, compared to \$1.9 million in the first three months of 2013. Disbursements to vendors and personnel were also higher in the first quarter of 2014 compared to 2013, primarily due to higher sales.

Direct cash flows from operations for the first three months of 2014 and 2013 are as follows:

	<b>Direct Cash Flows</b>	
	<b>Three Months Ended</b>	
	<b>March 29,</b>	<b>March 30,</b>
	<b>2014</b>	<b>2013</b>
	<i>(in millions)</i>	
Collections from customers	\$ 63.6	\$ 46.3
Other collections of cash	0.7	0.4
Disbursements to vendors	(36.1)	(29.9)
Personnel related disbursements	(24.0)	(14.0)
Income taxes paid		(0.1)
Debt service costs (interest)	(0.7)	(0.8)
<b>Cash provided by operations</b>	<b>\$ 3.5</b>	<b>\$ 1.9</b>

Days sales outstanding (DSO), which we calculate as average accounts receivable divided by quarterly average daily sales, was 32.1 days at March 29, 2014, compared to 31.8 days at March 30, 2013.

Inventory on hand as of March 29, 2014, increased \$1.9 million to \$15.3 million, compared to March 30, 2013. Inventory turns during the first three months of 2014 increased to 11.8 from 10.0 for the first three months of 2013.

We monitor and evaluate raw material inventory levels based on the need for each discrete item to fulfill short-term requirements calculated from current order patterns and to provide appropriate safety stock. Because all of our products are made-to-order, we have only a small amount of finished goods and work in process inventory. As a result of these factors, our inventories are not excessive, and we believe the value of such inventories will be realized through sale.

*Investing Activities.* Cash used in investing activities was \$3.2 million for the first three months of 2014, compared to cash provided by investing activities of \$6.8 million for the first three months of 2013. In 2014, the \$3.2 million in cash used included \$1.8 million on the new glass plant and \$1.4 million for the purchase of new equipment used in normal operations. In 2013, the \$6.8 million in cash provided by investing activities was due to proceeds from the sale of the Salisbury, North Carolina facility, of \$7.5 million, along with lower capital additions.

---

**Table of Contents**

*Financing activities.* Cash provided by financing activities was \$0.3 million in the first three months of 2014, primarily due to \$2.2 million from the exercise of stock options and option tax benefits, which was offset by \$1.0 million for the payment of debt and \$1.0 million for the purchase of treasury stock. Cash used in financing activities was \$13.1 million in the first three months of 2013, due to a \$7.5 million prepayment of debt and \$6.1 million for stock repurchases. This was offset by exercises of stock options totaling \$0.5 million.

*Debt Covenant.* In accordance with the Credit Agreement (defined below) we are required to meet certain financial covenants, the most restrictive of which is a maximum ratio of Total Funded Debt to Consolidated EBITDA for the trailing four quarters. This maximum ratio decreases during the term of the agreement from 3.75X to 3.0X. Consolidated EBITDA as defined in the agreement is determined as follows: Consolidated net income/(loss) plus interest expense (net of interest income), income taxes, depreciation, amortization, as well as other non-recurring items such as restructuring charges, plant consolidation costs, manufacturing inefficiencies incurred with plant consolidations, and non-cash stock compensation. We closely monitor compliance with our various debt covenants. As of March 29, 2014, our current leverage as defined in the calculation was 1.75, and we were in compliance and expect to be in the future.

*Capital Resources.* On May 28, 2013, we entered into a Credit Agreement (the *Credit Agreement*) with the various financial institutions and other persons from time to time parties thereto as lenders (the *Lenders*), SunTrust Bank, as administrative agent (in such capacity, the *Administrative Agent*), as collateral agent, as swing line lender and as a letter of credit issuer, and the other agents and parties thereto. The Credit Agreement establishes new senior secured credit facilities in an aggregate amount of \$105.0 million, consisting of an \$80.0 million Tranche A term loan facility maturing in five years that will amortize on a basis of 5% annually during the five-year term, and a \$25.0 million revolving credit facility maturing in five years that includes a \$5.0 million swing line facility and a \$10.0 million letter of credit facility. As of March 29, 2014, there were \$0.6 million of letters of credit outstanding and \$24.4 million available on the revolver.

Interest on all loans under the Credit Agreement is payable, either quarterly, or at the expiration of any LIBOR interest period applicable thereto. Borrowings under the term loans and the revolving credit facility accrue interest at a rate equal to, at our option, a base rate or LIBOR plus an applicable margin. The applicable margin is based on our leverage ratio, ranging from 300 to 350 basis points in the case of LIBOR and 200 to 250 basis points in the case of the base rate. We pay quarterly fees on the unused portion of the revolving credit facility equal to 0.50% as well as a quarterly letter of credit fee at a rate per annum equal to the applicable margin for LIBOR loans on the face amount of any outstanding letters of credit.

The Credit Agreement contains a number of affirmative and restrictive covenants, including limitations on the incurrence of additional debt, liens on property, acquisitions and investments, loans and guarantees, mergers, consolidations, liquidations and dissolutions, asset sales, dividends and other payments in respect of our capital stock, prepayments of certain debt and transactions with affiliates. The Credit Agreement also contains customary events of default.

The Credit Agreement also requires us to maintain certain maximum leverage ratios and minimum fixed charge ratios, which are tested at the end of each fiscal quarter.

PGT, Inc. has unconditionally guaranteed all loans and other obligations under the Credit Agreement and related documents, and such guarantee is secured by a lien on substantially all of the assets of our wholly owned subsidiary, PGT Industries, Inc., subject to certain limitations. PGT, Inc. has no operations or assets independent of its subsidiary.

Edgar Filing: PGT, Inc. - Form 10-Q

The face value of the debt as of March 29, 2014, was \$78.0 million. Related debt issuance costs and the debt discount are being amortized to interest expense, net on the Condensed Consolidated Statements of Comprehensive Income over the term of the debt.

The contractual future maturities of long-term debt outstanding as of March 29, 2014, are as follows (excluding unamortized debt discount and issuance costs):

	<i>(in millions)</i>
2014	\$ 4.0
2015	4.0
2016	4.0
2017	3.0
2018	63.0
Total debt	\$ 78.0

---

## **Table of Contents**

*Capital Expenditures.* Capital expenditures vary depending on prevailing business factors, including current and anticipated market conditions. For the first three months of 2014, capital expenditures were \$3.2 million, compared to \$0.6 million for the first three months of 2013. We expect to spend approximately \$18 to \$20 million on capital expenditures in 2014, including an additional \$10.7 million related to the new glass plant facility, along with continuing capital expenditures related to the new enterprise resource planning ( ERP ) system, new products and manufacturing initiatives. We anticipate that cash flows from operations and liquidity from the revolving credit facility, if needed, will be sufficient to execute our business plans.

*Hedging.* We enter into aluminum forward contracts to hedge the fluctuations in the purchase price of aluminum extrusion we use in production. We enter into these contracts by trading on the London Metal Exchange ( LME ). We trade on the LME using an international commodities broker that offers global access to all major markets. We maintain a \$2.0 million line of credit with our commodities broker to cover the liability position of open contracts for the purchase of aluminum in the event that the price of aluminum falls. Should the price of aluminum fall to a level which causes our liability for open aluminum contracts to exceed \$2.0 million, we are required to fund daily margin calls to cover the excess.

## **Contractual Obligations**

There have been no material changes, with the exception of signing a new lease on a small facility of 19,605 square feet in the Venice, Florida region during the first quarter of 2014, to the Disclosures of Contractual Obligations and Commercial Commitments table in Part II, Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations of our Form 10-K annual report for year ended December 28, 2013, as filed with the Securities and Exchange Commission on February 28, 2014.

## **Significant Accounting Policies and Critical Accounting Estimates**

Our consolidated financial statements are prepared in accordance with U.S. generally accepted accounting principles. Significant accounting policies are those that are both important to the accurate portrayal of a Company's financial condition and results and require subjective or complex judgments, often as a result of the need to make estimates about the effect of matters that are inherently uncertain. We make estimates and assumptions that affect the amounts reported in our financial statements and accompanying notes. Certain estimates are particularly sensitive due to their significance to the financial statements and the possibility that future events may be significantly different from our expectations.

We identified our significant accounting policies in our Form 10-K annual report for the year ended December 28, 2013, as filed with the Securities and Exchange Commission on February 28, 2014. There have been no changes to our critical accounting policies during the first three months of 2014.

## **ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

We utilize derivative financial instruments to hedge price movements in aluminum materials used in our manufacturing process and to hedge interest rate fluctuation associated with our debt. We entered into aluminum hedging instruments that settle at various times through June 2015 and cover approximately 36% of our anticipated need through June 2015 at an average price of \$0.88 per pound. For forward contracts for the purchase of aluminum on March 29, 2014, a 10% decrease in the price of aluminum per pound would decrease the fair value of our forward contracts of aluminum by \$0.7 million. This calculation utilizes our actual commitment of 9.1 million pounds under contract (to be settled throughout June 2015) and the market price of aluminum as of March 29, 2014, which was approximately \$0.88 per pound.



We experience changes in interest expense when market interest rates change. Changes in our debt could also increase these risks. Based on debt outstanding at March 29, 2014, a 100 basis point increase in interest rates would result in approximately \$0.6 million of additional interest costs annually, which includes the impact of our interest rate caps and swap (See Note 11 to the Condensed Consolidated Financial Statements).

#### **ITEM 4. CONTROLS AND PROCEDURES**

*Evaluation of Disclosure Controls and Procedures.* Disclosure controls and procedures are controls and other procedures that are designed to ensure that information required to be disclosed in the Company's reports filed or submitted under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms.

A control system, however, no matter how well conceived and operated can at best provide reasonable, not absolute, assurance that the objectives of the control system are met. Additionally, a control system reflects the fact that there are resource constraints, and the benefits of controls must be considered relative to costs. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of error or fraud, if any, within our Company have been detected, and due to these inherent limitations, misstatements due to error or fraud may occur and not be detected.

---

**Table of Contents**

Our Chief Executive Officer and Chief Financial Officer, with the assistance of management, evaluated the design, operation and effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act) as of the end of the period covered by this report (the Evaluation Date ). Based on that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that, as of the Evaluation Date, our disclosure controls and procedures were effective for the purposes of ensuring that information required to be disclosed in our reports filed under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms, and that such information is accumulated and communicated to management, including our Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

During the second quarter of fiscal year 2012, we started the implementation of our new Enterprise Resource Planning System ( ERP System ). We expect to continue this implementation in phases over the course of the next five months. The implementation of this ERP System has affected and will continue to affect our internal control over financial reporting by, among other things, improving user access security and automating a number of accounting, back office and reporting processes and activities. Management will continue to evaluate the operating effectiveness of related key controls during subsequent periods.

*Changes in Internal Control over Financial Reporting.* During the period covered by this report, there have been no changes in our internal control over financial reporting identified in connection with the evaluation described above that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

**PART II OTHER INFORMATION**

**ITEM 1. LEGAL PROCEEDINGS**

We are involved in various claims and lawsuits incidental to the conduct of our business in the ordinary course. We carry insurance coverage in such amounts in excess of our self-insured retention as we believe to be reasonable under the circumstances and that may or may not cover any or all of our liabilities with respect to claims and lawsuits. We do not believe that the ultimate resolution of these matters will have a material adverse impact on our financial position or results of operations.

Although our business and facilities are subject to federal, state and local environmental regulation, environmental regulation does not have a material impact on our operations. We believe that our facilities are in material compliance with such laws and regulations. As owners and lessees of real property, we can be held liable for the investigation or remediation of contamination on such properties, in some circumstances without regard to whether we knew of or were responsible for such contamination. Our current expenditures with respect to environmental investigation and remediation at our facilities are minimal, although no assurance can be provided that more significant remediation may not be required in the future as a result of spills or releases of petroleum products or hazardous substances or the discovery of previously unknown environmental conditions.

**ITEM 1A. RISK FACTORS**

In addition to the other information set forth in this report, you should carefully consider the factors discussed in Part 1, Item 1A. Risk Factors in our Form 10-K annual report for the year ended December 28, 2013, which could materially affect our business, financial condition or future results.

Additional risk and uncertainties not currently known to us or that we currently deem to be immaterial also may materially adversely affect our business, financial condition and/or operating results.

**ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS**

**Unregistered Sales of Equity Securities and Use of Proceeds**

None.

**Issuer Purchases of Equity Securities**

During the first quarter of 2014, we repurchased 85,051 shares of our common stock at an average price per share of \$11.05. During the first quarter of 2013, we repurchased 1,074,078 shares of our common stock at an average price per share of \$5.67.

---

**Table of Contents**

**ITEM 3. DEFAULTS UPON SENIOR SECURITIES**

None.

**ITEM 4. MINE SAFETY DISCLOSURE**

Not applicable

**ITEM 5. OTHER INFORMATION**

None.

**ITEM 6. EXHIBITS**

The following items are attached or incorporated herein by reference:

- 3.1 Amended and Restated Certificate of Incorporation of PGT, Inc. (incorporated herein by reference to Exhibit 3.1 to the Company's Annual Report on Form 10-K filed with the Securities and Exchange Commission on March 18, 2010, Registration No. 000-52059)
- 3.2 Amended and Restated By-Laws of PGT, Inc. (incorporated herein by reference to Exhibit 3.2 to the Company's Annual Report on Form 10-K filed with the Securities and Exchange Commission on March 18, 2010, Registration No. 000-52059)
- 4.1 Form of Specimen Certificate (incorporated herein by reference to Exhibit 4.1 to Amendment No. 2 to the Registration Statement of the Company on Form S-1, filed with the Securities and Exchange Commission on May 26, 2006, Registration No. 333-132365)
- 4.3 PGT Savings Plan (incorporated herein by reference to Exhibit 4.5 to the Company's Form S-8 Registration Statement, filed with the Securities and Exchange Commission on October 15, 2007, Registration No. 000-52059)
- 10.1 Credit Agreement, dated as of May 28, 2013, among PGT, Inc., PGT Industries, Inc., the lenders party thereto, certain other financial institutions, and SunTrust Bank, as Administrative Agent and Collateral Agent, (incorporated herein by reference to Exhibit 10.1 to Current Report on Form 8-K dated May 28, 2013, filed with the Securities and Exchange Commission on June 3, 2013, Registration No. 000-52059)
- 10.2 Amendment No. 1 to Credit Agreement, dated August 5, 2013, by and among the Company and the Lenders party thereto, and SunTrust Bank, as Administrative Agent and Collateral Agent for the Lenders, amending Credit Agreement dated May 28, 2013, (incorporated herein by reference to Exhibit 10.1 to Current Report on Form 8-K dated August 5, 2013, filed with the Securities and Exchange Commission on August 9, 2013, Registration No. 000-52059)
- 10.3 Form of PGT, Inc. 2006 Equity Incentive Plan Non-qualified Stock Option Agreement (incorporated herein by reference to Exhibit 10.8 to Amendment No. 3 to the Registration Statement of the Company on Form S-1, filed with the Securities and Exchange Commission on June 8, 2006, Registration No. 333-132365)
- 10.4 Form of Employment Agreement, between PGT Industries, Inc. and, individually, Rodney Hershberger,

## Edgar Filing: PGT, Inc. - Form 10-Q

Jeffery T. Jackson, Mario Ferrucci III, Deborah L. LaPinska, Monte Burns, David B. McCutcheon, Bradley West and Todd Antonelli (incorporated herein by reference to Exhibit 10.1 to Current Report on Form 8-K dated February 20, 2009, filed with the Securities and Exchange Commission on February 26, 2009, Registration No. 000-52059)

- 10.8 Form of PGT, Inc. 2006 Equity Incentive Plan Replacement Non-Qualified Stock Option Agreement (incorporated herein by reference to Exhibit 10.17 to the Company's Annual Report on Form 10-K filed with the Securities and Exchange Commission on March 18, 2010, Registration No. 000-5205)
- 10.9 PGT, Inc. Amended and Restated 2006 Equity Incentive Plan (incorporated herein by reference to Exhibit 10.7 to the Company's Annual Report on Form 10-K filed with the Securities and Exchange Commission on March 18, 2010, Registration No. 000-52059)
- 10.10 Supply Agreement, executed on January 24, 2014, by and between Keymark Corporation and PGT Industries, Inc. (incorporated herein by reference to Exhibit 10.1 to Current Report on Form 8-K dated January 24, 2014, filed with the Securities and Exchange Commission on January 28, 2014, Registration No. 000-52059)
- 10.11 Supply Agreement, executed on December 16, 2013, by and between PPG Industries, Inc. and PGT Industries, Inc. (incorporated herein by reference to Exhibit 10.1 to Current Report on Form 8-K dated December 16, 2013, filed with the Securities and Exchange Commission on December 20, 2013, Registration No. 000-52059)
- 10.12 Sales Contract, executed on November 12, 2013, by and between E. I. du Pont de Nemours and Company, through its Packaging and Industrial Polymers business, and PGT Industries, Inc. (incorporated herein by reference to Exhibit 10.1 to Current Report on Form 8-K dated November 12, 2013, filed with the Securities and Exchange Commission on November 13, 2013, Registration No. 000-52059)
- 10.13 Supply Agreement, executed on January 24, 2014, by and between, PGT Industries, Inc. and SAPA Extruder, Inc. (incorporated herein by reference to Exhibit 10.1 to Current Report on Form 8-K dated January 24, 2014, filed with the Securities and Exchange Commission on January 28, 2014, Registration No. 000-52059)
- 10.14 Supply Agreement, executed on April 29, 2014, by and between PGT Industries, Inc. and Royal Group, Inc., (incorporated herein by reference to Exhibit 10.1 to Current Report on Form 8-K dated April 29, 2014, filed with the Securities and Exchange Commission on May 5, 2014, Registration No. 000-52059)
- 31.1\* Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 31.2\* Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 32.1\* Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- 32.2\* Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
  
- 101.INS XBRL Instance Document\*
- 101.SCH XBRL Taxonomy Extension Schema\*
- 101.CAL XBRL Taxonomy Extension Calculation Linkbase\*
- 101.DEF XBRL Taxonomy Extension Definition\*
- 101.LAB XBRL Taxonomy Extension Label Linkbase\*
- 101.PRE XBRL Taxonomy Extension Presentation Linkbase\*

\* Filed herewith.

**Table of Contents**

**SIGNATURES**

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.

**PGT, INC.  
(Registrant)**

Date: May 8, 2014

/s/ Rodney Hershberger  
Rodney Hershberger  
Chairman, President and Chief Executive Officer

Date: May 8, 2014

/s/ Jeffrey T. Jackson  
Jeffrey T. Jackson  
Executive Vice President and Chief Financial Officer