

CARTERS INC
Form 10-Q
July 31, 2009

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 JULY 4, 2009 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:

001-31829

CARTER'S, INC.

(Exact name of Registrant as specified in its charter)

| | |
|------------------|---------------------|
| Delaware | 13-3912933 |
| (state or other | (I.R.S. Employer |
| jurisdiction of | Identification No.) |
| incorporation or | |
| organization) | |

The Proscenium
1170 Peachtree Street NE, Suite 900
Atlanta, Georgia 30309
(Address of principal executive offices, including zip code)
(404) 745-2700
(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 website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of

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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, a non-accelerated filer, or a smaller reporting company. See definition of “accelerated filer, large accelerated filer, and smaller reporting company” in Rule 12b-2 of the Exchange Act. (Check one)

Large Accelerated Filer (X) Accelerated Filer () Non-Accelerated Filer () 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 (X)

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

| Common Stock | Outstanding Shares at July 30, 2009 |
|---|---|
| Common stock, par value \$0.01 per share | 56,784,758 |

CARTER'S, INC.
INDEX

| | Page |
|---|-----------|
| <u>Part I. Financial Information</u> | |
| <u>Item 1. Financial Statements</u> | |
| <u>Unaudited Condensed Consolidated Balance Sheets as of July 4, 2009 and January 3, 2009</u> | <u>1</u> |
| <u>Unaudited Condensed Consolidated Statements of Operations for the three and six-month periods ended July 4, 2009 and June 28, 2008</u> | <u>2</u> |
| <u>Unaudited Condensed Consolidated Statements of Cash Flows for the six-month periods ended July 4, 2009 and June 28, 2008</u> | <u>3</u> |
| <u>Unaudited Condensed Consolidated Statement of Changes in Stockholders' Equity for the six-month period ended July 4, 2009</u> | <u>4</u> |
| <u>Notes to the Unaudited Condensed Consolidated Financial Statements</u> | <u>5</u> |
| <u>Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations</u> | <u>17</u> |
| <u>Item 3. Quantitative and Qualitative Disclosures about Market Risk</u> | <u>29</u> |
| <u>Item 4. Controls and Procedures</u> | <u>29</u> |
| <u>Part II. Other Information</u> | |
| <u>Item 1. Legal Proceedings</u> | <u>30</u> |
| <u>Item 1A. Risk Factors</u> | <u>30</u> |
| <u>Item 2. Unregistered Sales of Equity Securities and Use of Proceeds</u> | <u>35</u> |
| <u>Item 3. Defaults upon Senior Securities</u> | <u>35</u> |
| <u>Item 4. Submission of Matters to a Vote of Security Holders</u> | <u>35</u> |
| <u>Item 5. Other Information</u> | <u>35</u> |
| <u>Item 6. Exhibits</u> | <u>35</u> |
| <u>Signatures</u> | <u>36</u> |
| <u>Certifications</u> | <u>37</u> |

PART I - FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

CARTER'S, INC.
 CONDENSED CONSOLIDATED BALANCE SHEETS
 (dollars in thousands, except for share data)
 (unaudited)

| | July 4, 2009 | January 3, 2009 |
|---|---------------------|---------------------|
| ASSETS | | |
| Current assets: | | |
| Cash and cash equivalents | \$ 173,812 | \$ 162,349 |
| Accounts receivable, net | 96,864 | 106,060 |
| Finished goods inventories, net | 256,151 | 203,486 |
| Prepaid expenses and other current assets | 13,538 | 13,214 |
| Deferred income taxes | 25,712 | 27,982 |
| Total current assets | 566,077 | 513,091 |
| Property, plant, and equipment, net | 83,677 | 86,229 |
| Tradenames | 305,733 | 305,733 |
| Cost in excess of fair value of net assets acquired | 136,570 | 136,570 |
| Deferred debt issuance costs, net | 3,031 | 3,598 |
| Licensing agreements, net | 3,432 | 5,260 |
| Other assets | 293 | 576 |
| Total assets | \$ 1,098,813 | \$ 1,051,057 |
| LIABILITIES AND STOCKHOLDERS' EQUITY | | |
| Current liabilities: | | |
| Current maturities of long-term debt | \$ 3,503 | \$ 3,503 |
| Accounts payable | 109,944 | 79,011 |
| Other current liabilities | 42,509 | 57,613 |
| Total current liabilities | 155,956 | 140,127 |
| Long-term debt | 332,772 | 334,523 |
| Deferred income taxes | 106,361 | 108,989 |
| Other long-term liabilities | 43,082 | 40,822 |
| Total liabilities | 638,171 | 624,461 |
| Commitments and contingencies | | |
| Stockholders' equity: | | |
| Preferred stock; par value \$.01 per share; 100,000 shares authorized; none issued or outstanding at July 4, 2009 and January 3, 2009 | -- | -- |
| Common stock, voting; par value \$.01 per share; 150,000,000 shares authorized; 56,784,758 and | 568 | 563 |

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| | | |
|--|--------------|--------------|
| 56,352,111 shares issued and outstanding at July 4, 2009 and January 3, 2009, respectively | | |
| Additional paid-in capital | 217,707 | 211,767 |
| Accumulated other comprehensive loss | (6,914) | (7,318) |
| Retained earnings | 249,281 | 221,584 |
| Total stockholders' equity | 460,642 | 426,596 |
| Total liabilities and stockholders' equity | \$ 1,098,813 | \$ 1,051,057 |

See accompanying notes to the unaudited condensed consolidated financial statements

CARTER'S, INC.
 CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
 (dollars in thousands, except per share data)
 (unaudited)

| | For the | | For the | |
|---|--|------------------|--|------------------|
| | three-month periods ended July 4, 2009 | June 28, 2008 | six-month periods ended July 4, 2009 | June 28, 2008 |
| Net sales | \$ 317,909 | \$ 301,675 | \$ 674,696 | \$ 631,647 |
| Cost of goods sold | 201,619 | 202,094 | 431,059 | 427,151 |
| Gross profit | 116,290 | 99,581 | 243,637 | 204,496 |
| Selling, general, and administrative expenses | 99,843 | 92,207 | 198,973 | 184,483 |
| Workforce reduction and facility write-down and closure costs (Note 10) | 2,980 | -- | 11,400 | -- |
| Executive retirement charges (Note 13) | -- | 5,325 | -- | 5,325 |
| Royalty income | (7,472) | (7,203) | (16,234) | (15,117) |
| Operating income | 20,939 | 9,252 | 49,498 | 29,805 |
| Interest expense, net | 2,708 | 4,789 | 5,883 | 9,309 |
| Income before income taxes | 18,231 | 4,463 | 43,615 | 20,496 |
| Provision for income taxes | 6,902 | 1,684 | 15,918 | 6,158 |
| Net income | \$ 11,329 | \$ 2,779 | \$ 27,697 | \$ 14,338 |
| Basic net income per common share (Note 11) | \$ 0.20 | \$ 0.05 | \$ 0.49 | \$ 0.25 |
| Diluted net income per common share (Note 11) | \$ 0.19 | \$ 0.05 | \$ 0.47 | \$ 0.24 |

See accompanying notes to the unaudited condensed consolidated financial statements

CARTER'S, INC.
 CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
 (dollars in thousands)
 (unaudited)

| | For the | |
|---|-------------------------|------------------|
| | six-month periods ended | |
| | July 4, 2009 | June 28, 2008 |
| Cash flows from operating activities: | | |
| Net income | \$ 27,697 | \$ 14,338 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Depreciation and amortization | 16,990 | 14,150 |
| Amortization of debt issuance costs | 567 | 567 |
| Non-cash stock-based compensation expense | 3,543 | 5,055 |
| Income tax benefit from exercised stock options | (1,313) | (60) |
| Non-cash asset impairment and facility write-down charges | 3,662 | -- |
| Deferred income taxes | (401) | 552 |
| Effect of changes in operating assets and liabilities: | | |
| Accounts receivable | 9,196 | 17,114 |
| Inventories | (52,665) | (25,323) |
| Prepaid expenses and other assets | (767) | (7,120) |
| Accounts payable and other liabilities | 20,492 | 4,786 |
| Net cash provided by operating activities | 27,001 | 24,059 |
| Cash flows from investing activities: | | |
| Capital expenditures | (15,835) | (7,055) |
| Net cash used in investing activities | (15,835) | (7,055) |
| Cash flows from financing activities: | | |
| Payments on term loan | (1,751) | (875) |
| Share repurchase | -- | (20,059) |
| Income tax benefit from exercised stock options | 1,313 | 60 |
| Proceeds from exercise of stock options | 735 | 81 |
| Net cash provided by (used in) financing activities | 297 | (20,793) |
| Net increase (decrease) in cash and cash equivalents | 11,463 | (3,789) |

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| | | |
|--|------------|-----------|
| Cash and cash equivalents, beginning of period | 162,349 | 49,012 |
| Cash and cash equivalents, end of period | \$ 173,812 | \$ 45,223 |

See accompanying notes to the unaudited condensed consolidated financial statements

CARTER'S, INC.
CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN STOCKHOLDERS' EQUITY
(dollars in thousands, except for share data)
(unaudited)

| | Common stock | Additional paid-in capital | Accumulated other comprehensive (loss) income | Retained earnings | Total stockholders' equity |
|---|-----------------|----------------------------------|---|----------------------|----------------------------------|
| Balance at January 3, 2009 | \$ 563 | \$ 211,767 | \$ (7,318) | \$ 221,584 | \$ 426,596 |
| Exercise of stock options (243,016 shares) | 2 | 733 | -- | -- | 735 |
| Income tax benefit from exercised stock options | -- | 1,313 | -- | -- | 1,313 |
| Restricted stock activity | 3 | (3) | -- | -- | -- |
| Stock-based compensation expense | -- | 3,197 | -- | -- | 3,197 |
| Issuance of common stock (33,656 shares) | -- | 700 | -- | -- | 700 |
| Comprehensive income (loss): | | | | | |
| Net income | -- | -- | -- | 27,697 | 27,697 |
| Derivative hedging adjustment, net of tax of \$214 | -- | -- | 404 | -- | 404 |
| Total comprehensive income | -- | -- | 404 | 27,697 | 28,101 |
| Balance at July 4, 2009 | \$ 568 | \$ 217,707 | \$ (6,914) | \$ 249,281 | \$ 460,642 |

See accompanying notes to the unaudited condensed consolidated financial statements

CARTER'S, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(unaudited)

NOTE 1 – THE COMPANY:

Carter's, Inc., and its wholly owned subsidiaries (collectively, the "Company," "we," "us," "its," and "our") design, source, and market branded childrenswear under the Carter's, Child of Mine, Just One Year, OshKosh, OshKosh B'Gosh, and related brands. Our products are sourced through contractual arrangements with manufacturers worldwide for wholesale distribution to major domestic retailers, including the mass channel, and for our 271 Carter's and 168 OshKosh retail stores that market our branded merchandise and other licensed products manufactured by other companies.

NOTE 2 – BASIS OF PREPARATION:

The accompanying unaudited condensed consolidated financial statements comprise the consolidated financial statements of Carter's, Inc. and its subsidiaries. All intercompany transactions and balances have been eliminated in consolidation.

In our opinion, the Company's accompanying unaudited condensed consolidated financial statements contain all adjustments necessary for a fair presentation of our financial position as of July 4, 2009, the results of our operations for the three and six-month periods ended July 4, 2009 and June 28, 2008, cash flows for the six-month periods ended July 4, 2009 and June 28, 2008 and changes in stockholders' equity for the six-month period ended July 4, 2009. Operating results for the three and six-month periods ended July 4, 2009 are not necessarily indicative of the results that may be expected for the fiscal year ending January 2, 2010. Our accompanying condensed consolidated balance sheet as of January 3, 2009 is from our audited consolidated financial statements included in our most recently filed Annual Report on Form 10-K, but does not include all disclosures required by accounting principles generally accepted in the United States of America ("GAAP").

Certain information and footnote disclosure normally included in financial statements prepared in accordance with GAAP have been condensed or omitted pursuant to the rules and regulations of the Securities and Exchange Commission and the instructions to Form 10-Q. The accounting policies we follow are set forth in our most recently filed Annual Report on Form 10-K in the notes to our audited consolidated financial statements for the fiscal year ended January 3, 2009.

Our fiscal year ends on the Saturday, in December or January, nearest the last day of December. The accompanying unaudited condensed consolidated financial statements for the second quarter and first half of fiscal 2009 are as of July 4, 2009. The second quarter and first half of fiscal 2008 ended on June 28, 2008.

Certain prior year amounts have been reclassified to facilitate comparability with current year presentation.

Subsequent events were evaluated through July 30, 2009, the date these financials were available to be issued.

NOTE 3 – COST IN EXCESS OF FAIR VALUE OF NET ASSETS ACQUIRED AND OTHER INTANGIBLE ASSETS:

Cost in excess of fair value of net assets acquired as of July 4, 2009, represents the excess of the cost of the acquisition of Carter's, Inc. by Berkshire Partners LLC which was consummated on August 15, 2001 over the fair value of the net assets acquired. The Carter's cost in excess of fair value of net assets acquired is not deductible for tax purposes.

The Carter's cost in excess of fair value of net assets acquired and Carter's and OshKosh tradenames are deemed to have indefinite lives and are not being amortized.

5

CARTER'S, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(unaudited)

NOTE 3 – COST IN EXCESS OF FAIR VALUE OF NET ASSETS ACQUIRED AND OTHER INTANGIBLE ASSETS: (Continued)

The Company's intangible assets were as follows:

| (dollars in thousands) | Weighted-average useful life | Gross amount | July 4, 2009 Accumulated amortization | Net amount | Gross amount | January 3, 2009 Accumulated amortization | Net amount |
|--|------------------------------|--------------|--|------------|--------------|---|------------|
| Carter's cost in excess of fair value of net assets acquired | Indefinite | \$ 136,570 | \$ -- | \$ 136,570 | \$ 136,570 | \$ -- | \$ 136,570 |
| Carter's tradename | Indefinite | \$ 220,233 | \$ -- | \$ 220,233 | \$ 220,233 | \$ -- | \$ 220,233 |
| OshKosh tradename | Indefinite | \$ 85,500 | \$ -- | \$ 85,500 | \$ 85,500 | \$ -- | \$ 85,500 |
| OshKosh licensing agreements | 4.7 years | \$ 19,100 | \$ 15,668 | \$ 3,432 | \$ 19,100 | \$ 13,840 | \$ 5,260 |
| Leasehold interests | 4.1 years | \$ 1,833 | \$ 1,815 | \$ 18 | \$ 1,833 | \$ 1,599 | \$ 234 |

Amortization expense for intangible assets was approximately \$1.0 million for the three-month periods ended July 4, 2009 and June 28, 2008. Amortization expense for intangible assets was approximately \$2.0 million and \$2.1 million for the six-month periods ended July 4, 2009 and June 28, 2008. Amortization expense for the remainder of fiscal 2009 and fiscal 2010 for the OshKosh licensing agreements and leasehold interests is expected to be as follows:

| (dollars in thousands) | Fiscal Year | Estimated amortization Expense |
|------------------------|---|--------------------------------|
| | 2009 (period from July 5 through January 2, 2010) | \$ 1,673 |
| | 2010 | 1,777 |
| | Total | \$ 3,450 |

NOTE 4 – INCOME TAXES:

The Company and its subsidiaries file income tax returns in the United States and in various states and local jurisdictions. During the first quarter of fiscal 2009, the Internal Revenue Service completed an income tax audit for fiscal 2006, and began an audit of fiscal 2007. In most cases, the Company is no longer subject to state and local tax authority examinations for years prior to fiscal 2005.

During the first half of fiscal 2009, we recognized approximately \$1.0 million in tax benefits due to the completion of the Internal Revenue Service audit for fiscal 2006. During the first half of fiscal 2008, we recognized approximately \$1.6 million in tax benefits due to the completion of an Internal Revenue Service audit for fiscal 2004 and 2005.

As of July 4, 2009, the Company had gross unrecognized tax benefits of approximately \$7.1 million. Substantially all of the Company's reserve for unrecognized tax benefits as of July 4, 2009, if ultimately recognized, will impact the Company's effective tax rate in the period settled. The Company has recorded tax positions for which the ultimate deductibility is highly certain, but for which there is uncertainty about the timing of such deductions. Because of deferred tax accounting, changes in the timing of these deductions would not impact the annual effective tax rate, but would accelerate the payment of cash to the taxing authorities.

CARTER'S, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(unaudited)

NOTE 4 – INCOME TAXES: (Continued)

Included in the reserves for unrecognized tax benefits are approximately \$0.5 million of reserves for which the statute of limitations is expected to expire in the third quarter of fiscal 2009. If these tax benefits are ultimately recognized, such recognition may impact our annual effective tax rate for fiscal 2009 and the effective tax rate in the quarter in which the benefits are recognized. While the Internal Revenue Service has begun its audit of the Company's income tax return for fiscal 2007, the audit has not proceeded to a point where the Company can reasonably determine the outcome or completion date.

We recognize interest related to unrecognized tax benefits as a component of interest expense and penalties related to unrecognized tax benefits as a component of income tax expense. The Company had approximately \$0.6 million of interest accrued as of July 4, 2009.

NOTE 5 – FINANCIAL INSTRUMENTS:

Effective December 30, 2007 (the first day of our 2008 fiscal year), the Company adopted Statement of Financial Accounting Standards ("SFAS") SFAS No. 157, "Fair Value Measurements" ("SFAS 157"), which defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements. The fair value hierarchy for disclosure of fair value measurements under SFAS 157 is as follows:

Level- Quoted prices in active markets for identical assets
1 or liabilities

Level- Quoted prices for similar assets and liabilities in
2 active markets or inputs that are observable

Level- Inputs that are unobservable (for example, cash
3 flow modeling inputs based on assumptions)

The following table summarizes assets and liabilities measured at fair value on a recurring basis at July 4, 2009, as required by SFAS 157:

| (dollars in millions) | Level 1 | Level 2 | Level 3 |
|--------------------------------|---------|----------|---------|
| Assets | | | |
| Investments | \$ -- | \$ 130.0 | \$ -- |
| Assets held for sale | \$ -- | \$ 2.8 | \$ -- |
| Liabilities | | | |
| Interest rate hedge agreements | \$ -- | \$ 2.0 | \$ -- |

At July 4, 2009, we had approximately \$130.0 million invested in two Dreyfus Cash Management Funds, which are included in cash and cash equivalents on the accompanying unaudited condensed consolidated balance sheet. These

funds consisted of the Dreyfus Treasury Prime Cash Management fund (\$87.9 million), which invests only in U.S. Treasury Bills or U.S. Treasury Notes, and the Dreyfus Tax Exempt Cash Management fund (\$42.1 million), which invests in short-term, high quality municipal obligations that provide income exempt from federal taxes.

At July 4, 2009, the carrying value of the Company's White House, Tennessee distribution facility held for sale was estimated to be \$2.8 million. As discussed in more detail in Note 10, during the second quarter of fiscal 2009, the Company wrote down the carrying value of this property by approximately \$0.7 million to reflect the decrease in the fair market value as evidenced by recent negotiations to sell the property.

Our senior credit facility requires us to hedge at least 25% of our variable rate debt under this facility. As of July 4, 2009, approximately \$147.1 million of our \$336.3 million of outstanding debt was hedged under interest rate swap agreements.

CARTER'S, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(unaudited)

NOTE 5 – FINANCIAL INSTRUMENTS: (Continued)

On September 22, 2005, we entered into an interest rate swap agreement to receive floating interest and pay fixed interest. This interest rate swap agreement is designated as a cash flow hedge of the variable interest payments on a portion of our term loan debt. The interest rate swap agreement matures on July 30, 2010. As of July 4, 2009, approximately \$47.1 million of our outstanding term loan debt was hedged under this interest rate swap agreement.

On May 25, 2006, we entered into an interest rate collar agreement (the “collar”) with a floor of 4.3% and a ceiling of 5.5%. The collar covered \$100 million of our variable rate term loan debt and was designated as a cash flow hedge of the variable interest payments on such debt. The collar matured on January 31, 2009.

On January 30, 2009, we entered into two interest rate swap agreements in order to limit our exposure to higher interest rates. Each interest rate swap agreement covers \$50.0 million of our variable rate term loan debt, to receive floating interest and pay fixed interest. We continue to be in compliance with the 25% hedging requirement under our senior credit facility. These interest rate swap agreements are designated as cash flow hedges of the variable interest payments on a portion of our variable rate term loan debt and each mature in January 2010.

Our interest rate swap agreements are traded in the over-the-counter market. Fair values are based on quoted market prices for similar assets or liabilities or determined using inputs that use as their basis readily observable market data that are actively quoted and can be validated through external sources, including third-party pricing services, brokers, and market transactions.

The fair value of our derivative instruments in our accompanying unaudited condensed consolidated balance sheet as of July 4, 2009 was as follows:

| (dollars in millions) | Asset Derivatives | | Liability Derivatives | |
|--------------------------------|---|------------|---------------------------|------------|
| | Balance sheet location | Fair value | Balance sheet location | Fair value |
| Interest rate hedge agreements | Prepaid expenses and other current assets | -- | Other current liabilities | \$ 2.0 |

The effect of derivative instruments designated as cash flow hedges on our accompanying unaudited condensed consolidated financial statements were as follows:

| (dollars in thousands) | For the three-month period ended July 4, 2009 | | For the six-month period ended July 4, 2009 | |
|------------------------|--|--------------------------|--|--------------------------|
| | Amount of gain (loss) | Amount of gain (loss) | Amount of gain (loss) | Amount of gain (loss) |

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| | recognized in accumulated other comprehensive income (loss) on effective hedges (1) | reclassified from accumulated other comprehensive income (loss) into interest expense | recognized in accumulated other comprehensive income (loss) on effective hedges (1) | reclassified from accumulated other comprehensive income (loss) into interest expense (2) |
|-----------------------------------|---|---|---|--|
| Interest rate hedge agreements | \$ 144 | \$ -- | \$ (3) | \$ (407) |

(1) Amount recognized in accumulated other comprehensive (loss) income, net of tax of \$85,000 and net of tax benefit of \$2,000 for the three and six-month periods ended July 4, 2009, respectively.

(2) Settlement of interest rate collar agreement, net of tax of \$216,000.

CARTER'S, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(unaudited)

NOTE 6 – EMPLOYEE BENEFIT PLANS:

Under a defined benefit plan frozen in 1991, we offer a comprehensive post-retirement medical plan to current and certain future retirees and their spouses until they become eligible for Medicare or a Medicare Supplement Plan. We also offer life insurance to current and certain future retirees. Employee contributions are required as a condition of participation for both medical benefits and life insurance and our liabilities are net of these expected employee contributions. See Note 7 “Employee Benefit Plans” to our audited consolidated financial statements in our most recently filed Annual Report on Form 10-K for further information.

The components of post-retirement benefit expense charged to operations are as follows:

| (dollars in thousands) | For the | | For the | |
|---|--|------------------|--|------------------|
| | three-month periods ended July 4, 2009 | June 28, 2008 | six-month periods ended July 4, 2009 | June 28, 2008 |
| Service cost – benefits attributed to service during the period | \$ 23 | \$ 26 | \$ 46 | \$ 53 |
| Interest cost on accumulated post-retirement benefit obligation | 113 | 132 | 226 | 263 |
| Amortization net actuarial gain | (7) | -- | (14) | -- |
| Total net periodic post-retirement benefit cost | \$ 129 | \$ 158 | \$ 258 | \$ 316 |

The component of pension expense charged to operations is as follows:

| (dollars in thousands) | For the | | For the | |
|---|--|------------------|--|------------------|
| | three-month periods ended July 4, 2009 | June 28, 2008 | six-month periods ended July 4, 2009 | June 28, 2008 |
| Interest cost on accumulated pension benefit obligation | \$ 13 | \$ 13 | \$ 26 | \$ 26 |

Under a defined benefit pension plan frozen as of December 31, 2005, certain current and former employees of OshKosh are eligible to receive benefits. The net periodic pension benefit associated with this pension plan and included in the statement of operations was comprised of:

| (dollars in thousands) | For the | | For the | |
|---|--|------------------|--|------------------|
| | three-month periods ended July 4, 2009 | June 28, 2008 | six-month periods ended July 4, 2009 | June 28, 2008 |
| Interest cost on accumulated pension benefit obligation | \$ 568 | \$ 562 | \$ 1,135 | \$ 1,124 |
| Expected return on assets | (650) | (944) | (1,300) | (1,887) |

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| | | | | |
|--|-------|-----------|-------|-----------|
| Amortization of actuarial loss (gain) | 102 | (19) | 205 | (38) |
| Total net periodic pension expense (benefit) | \$ 20 | \$ (401) | \$ 40 | \$ (801) |

CARTER'S, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(unaudited)

NOTE 7 – COMMON STOCK:

On February 16, 2007, the Company's Board of Directors approved a stock repurchase program, pursuant to which the Company is authorized to purchase up to \$100 million of its outstanding common shares. Such repurchases may occur from time to time in the open market, in negotiated transactions, or otherwise. This program has no time limit. The timing and amount of any repurchases will be determined by the Company's management, based on its evaluation of market conditions, share price, and other factors.

During the first half of fiscal 2009, the Company did not repurchase any shares of its common stock. During the second quarter and first half of fiscal 2008, the Company repurchased and retired approximately 645,727 and 1,320,085 shares of its common stock at an average price of \$15.55 and \$15.20 per share, respectively. Since inception of the program and through July 4, 2009, the Company repurchased and retired approximately 4,599,580 shares, or approximately \$91.1 million, of its common stock at an average price of \$19.81 per share, leaving approximately \$8.9 million available for repurchase under the plan. We have reduced common stock by the par value of such shares repurchased and have deducted the remaining excess repurchase price over par value from additional paid-in capital.

During the second quarter and first half of fiscal 2009, the Company issued 33,656 shares of common stock at a fair market value of \$20.80 to its non-management board members. In connection with this issuance, we recognized approximately \$700,000 in stock-based compensation expense. During the second quarter and first half of fiscal 2008, the Company issued 43,386 shares of common stock at a fair market value of \$14.48 to its non-management board members. In connection with this issuance, we recognized approximately \$630,000 in stock-based compensation expense. We received no proceeds from the issuance of these shares.

NOTE 8 – STOCK-BASED COMPENSATION:

We account for stock-based compensation expense in accordance with SFAS No. 123 (revised 2004), "Share-Based Payment." The fair value of time-based or performance-based stock option grants are estimated on the date of grant using the Black-Scholes option pricing method with the following weighted-average assumptions used for grants issued during the six-month period ended July 4, 2009.

| Assumptions | | |
|-------------------------|-------|---|
| Volatility | 35.83 | % |
| Risk-free interest rate | 2.50 | % |
| Expected term (years) | 7 | |
| Dividend yield | -- | |

The fair value of restricted stock is determined based on the quoted closing price of our common stock on the date of grant.

CARTER'S, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(unaudited)

NOTE 8 – STOCK-BASED COMPENSATION: (Continued)

The following table summarizes our stock option and restricted stock activity during the six-month period ended July 4, 2009:

| | Time-based stock options | Performance-based stock options | Retained stock options | Restricted stock |
|---------------------------------|-----------------------------|------------------------------------|------------------------------|---------------------|
| Outstanding, January 3, 2009 | 4,733,080 | 220,000 | 113,514 | 444,589 |
| Granted | 448,000 | -- | -- | 208,500 |
| Exercised | (129,502) | -- | (113,514) | -- |
| Vested restricted stock | -- | -- | -- | (132,256) |
| Forfeited | (85,600) | (20,000) | -- | (52,525) |
| Expired | (36,000) | -- | -- | -- |
| Outstanding, July 4, 2009 | 4,929,978 | 200,000 | -- | 468,308 |
| Exercisable, July 4, 2009 | 3,796,558 | -- | -- | -- |

During the six-month period ended July 4, 2009, we granted 448,000 time-based stock options with a weighted-average Black-Scholes fair value of \$7.61 and a weighted-average exercise price of \$18.08. In connection with these grants, we recognized approximately \$250,000 in stock-based compensation expense.

During the six-month period ended July 4, 2009, we granted 208,500 shares of restricted stock to employees with a weighted-average fair value on the date of grant of \$18.08. In connection with these grants, we recognized approximately \$275,000 in stock-based compensation expense.

As a result of the retirement of an executive officer during the second quarter of fiscal 2008, the Company recognized approximately \$2.2 million of stock-based compensation expense as a result of the accelerated vesting of 400,000 performance-based stock options (see Note 13, "Executive Retirement Charges").

Unrecognized stock-based compensation expense related to outstanding unvested stock options and unvested restricted stock awards is expected to be recorded as follows:

| (dollars in thousands) | Time-based stock options | Restricted stock | Total |
|---|--------------------------------|---------------------|---------|
| 2009 (period from July 5 through January 2, 2010) | \$1,438 | \$1,407 | \$2,845 |

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| | | | |
|-------|---------|---------|----------|
| 2010 | 2,502 | 2,466 | 4,968 |
| 2011 | 1,938 | 2,002 | 3,940 |
| 2012 | 1,059 | 1,180 | 2,239 |
| Total | \$6,937 | \$7,055 | \$13,992 |

CARTER'S, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(unaudited)

NOTE 9 – SEGMENT INFORMATION:

We report segment information in accordance with the provisions of SFAS No. 131, “Disclosure about Segments of an Enterprise and Related Information,” which requires segment information to be disclosed based upon a “management approach.” The management approach refers to the internal reporting that is used by management for making operating decisions and assessing the performance of our reportable segments. We report our corporate expenses, workforce reduction, and facility write-down and closure costs separately as they are not included in the internal measures of segment operating performance used by the Company in order to measure the underlying performance of our reportable segments.

The table below presents certain segment information for the periods indicated:

| (dollars in thousands) | For the three-month periods ended | | | | For the six-month periods ended | | | |
|--------------------------|-----------------------------------|------------------------|---------------|------------------------|---------------------------------|------------------------|---------------|------------------------|
| | July 4, 2009 | % of Total | June 28, 2008 | % of Total | July 4, 2009 | % of Total | June 28, 2008 | % of Total |
| Net sales: | | | | | | | | |
| Carter's: | | | | | | | | |
| Wholesale | \$ 100,088 | 31.5 % | \$ 94,322 | 31.3 % | \$ 222,985 | 33.0 % | \$ 212,154 | 33.6 % |
| Retail | 110,127 | 34.6 % | 92,656 | 30.7 % | 212,057 | 31.4 % | 179,058 | 28.4 % |
| Mass Channel | 44,216 | 13.9 % | 51,054 | 16.9 % | 102,961 | 15.3 % | 113,978 | 18.0 % |
| Carter's net sales | 254,431 | 80.0 % | 238,032 | 78.9 % | 538,003 | 79.7 % | 505,190 | 80.0 % |
| OshKosh: | | | | | | | | |
| Retail | 52,160 | 16.4 % | 49,883 | 16.5 % | 103,988 | 15.4 % | 94,248 | 14.9 % |
| Wholesale | 11,318 | 3.6 % | 13,760 | 4.6 % | 32,705 | 4.9 % | 32,209 | 5.1 % |
| OshKosh net sales | 63,478 | 20.0 % | 63,643 | 21.1 % | 136,693 | 20.3 % | 126,457 | 20.0 % |
| Total net sales | \$ 317,909 | 100.0 % | \$ 301,675 | 100.0 % | \$ 674,696 | 100.0 % | \$ 631,647 | 100.0 % |
| Operating income (loss): | | | | | | | | |
| | | % of segment net sales | | % of segment net sales | | % of segment net sales | | % of segment net sales |
| Carter's: | | | | | | | | |
| Wholesale | \$ 12,352 | 12.3 % | \$ 12,663 | 13.4 % | \$ 36,531 | 16.4 % | \$ 34,222 | 16.1 % |
| Retail | 16,575 | 15.1 % | 10,358 | 11.2 % | 33,163 | 15.6 % | 21,800 | 12.2 % |
| Mass Channel | 8,639 | 19.5 % | 7,123 | 14.0 % | 16,674 | 16.2 % | 13,865 | 12.2 % |
| | 37,566 | 14.8 % | 30,144 | 12.7 % | 86,368 | 16.1 % | 69,887 | 13.8 % |

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| | | | | | | | | | |
|-------------------|-----------|----------|-----------|----------|-----------|---------|-----------|----------|--|
| Carter's | | | | | | | | | |
| operating | | | | | | | | | |
| income | | | | | | | | | |
| OshKosh: | | | | | | | | | |
| Retail | 786 | 1.5 % | (2,646) | (5.3 %) | 455 | 0.4 % | (9,379) | (10.0 %) | |
| Wholesale | (2,318) | (20.5 %) | (4,312) | (31.3 %) | (2,274) | (7.0 %) | (6,836) | (21.2 %) | |
| Mass Channel | | | | | | | | | |
| (a) | 438 | -- | 628 | -- | 1,144 | -- | 1,159 | -- | |
| OshKosh | | | | | | | | | |
| operating loss | | | | | | | | | |
| | (1,094) | (1.7 %) | (6,330) | (9.9 %) | (675) | (0.5 %) | (15,056) | (11.9 %) | |
| Segment | | | | | | | | | |
| operating | | | | | | | | | |
| income | | | | | | | | | |
| | 36,472 | 11.5 % | 23,814 | 7.9 % | 85,693 | 12.7 % | 54,831 | 8.7 % | |
| Corporate | | | | | | | | | |
| expenses (b) | | | | | | | | | |
| | (11,910) | (3.7 %) | (9,237) | (3.1 %) | (23,830) | (3.5 %) | (19,701) | (3.1 %) | |
| Workforce | | | | | | | | | |
| reduction and | | | | | | | | | |
| facility | | | | | | | | | |
| write-down and | | | | | | | | | |
| closure costs (c) | | | | | | | | | |
| | (3,623) | (1.0 %) | -- | -- | (12,365) | (1.7 %) | -- | -- | |
| Executive | | | | | | | | | |
| retirement | | | | | | | | | |
| charges (d) | | | | | | | | | |
| | -- | -- | (5,325) | (1.7 %) | -- | -- | (5,325) | (0.9 %) | |
| Net corporate | | | | | | | | | |
| expenses | | | | | | | | | |
| | (15,533) | (4.9 %) | (14,562) | (4.8 %) | (36,195) | (5.4 %) | (25,026) | (4.0 %) | |
| Total operating | | | | | | | | | |
| income | | | | | | | | | |
| | \$ 20,939 | 6.6 % | \$ 9,252 | 3.1 % | \$ 49,498 | 7.3 % | \$ 29,805 | 4.7 % | |

(a) OshKosh mass channel consists of a licensing agreement with Target Stores. Operating income consists of royalty income, net of related expenses.

(b) Corporate expenses generally include expenses related to executive management, finance, stock-based compensation, building occupancy, information technology, certain legal fees, severance and relocation, incentive compensation, consulting, and audit fees.

(c) Includes closure costs associated with our Barnesville, Georgia distribution facility including severance, asset impairment charges, other closure costs, and accelerated depreciation, asset impairment charges related to our Oshkosh, Wisconsin facility, write-down of our White House, Tennessee facility held for sale, and severance and other benefits related to the corporate workforce reduction (see Note 10).

(d) Charges associated with an executive officer's retirement (see Note 13).

CARTER'S, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(unaudited)

NOTE 10 – WORKFORCE REDUCTION AND FACILITY WRITE-DOWN AND CLOSURE COSTS:

Corporate Workforce Reduction

On April 21, 2009, the Company announced to affected employees a plan to reduce its corporate workforce (defined as excluding retail district managers, hourly retail store employees, and distribution center employees). Approximately 150 employees were affected under the plan. The plan includes consolidating the majority of our operations performed in our Oshkosh, Wisconsin office into other Company locations. This consolidation will likely result in the addition of resources in our other locations.

As a result of this corporate workforce reduction, we recorded severance charges and other one-time benefits to eligible employees of \$2.2 million in the second quarter of fiscal 2009. During the first half of fiscal 2009, we recorded charges of \$7.3 million consisting of \$5.5 million in severance charges and other benefits, and approximately \$1.8 million in asset impairment charges related to the closure of our Oshkosh, Wisconsin office. The majority of the severance payments will be paid through the end of the year.

The following table summarizes restructuring reserves related to the corporate workforce reduction which are included in other current liabilities on the accompanying unaudited condensed consolidated balance sheet:

| (dollars in thousands) | Severance and other one-time benefits |
|--------------------------|---------------------------------------|
| Balance at April 4, 2009 | \$ 3,300 |
| Provision | 2,200 |
| Payments | (900) |
| Balance at July 4, 2009 | \$ 4,600 |

Barnesville Distribution Facility Closure

On April 2, 2009, the Company announced to affected employees a plan to close its Barnesville, Georgia distribution center. Approximately 210 employees were affected by this closure. Operations at the Barnesville facility ceased on June 1, 2009.

In accordance with SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets," under a held and used model, it was determined that the distribution facility assets became impaired during March 2009, when it became "more likely than not" that the expected life of the Barnesville, Georgia distribution facility would be significantly shortened. Accordingly, we wrote down the assets to their estimated recoverable fair value in March 2009. The adjusted asset values will be subject to accelerated depreciation over their remaining estimated useful life.

In conjunction with the plan to close the Barnesville, Georgia distribution center, the Company recorded accelerated depreciation charges (included in selling, general, and administrative expenses) of approximately \$0.7 million in the

second quarter of fiscal 2009 and charges of \$4.3 million during the first half of fiscal 2009, consisting of severance of \$1.7 million, asset impairment charges of \$1.1 million related to the write-down of the related land, building, and equipment, \$1.0 million of accelerated depreciation (included in selling, general, and administrative expenses), and \$0.5 million of other closure costs.

CARTER'S, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(unaudited)

NOTE 10 – WORKFORCE REDUCTION AND FACILITY WRITE-DOWN AND CLOSURE COSTS: (Continued)

The following table summarizes restructuring reserves related to the closure of the Barnesville, Georgia distribution center which are included in other current liabilities on the accompanying unaudited condensed consolidated balance sheet:

| (dollars in thousands) | Severance | Other closure costs | Total |
|-----------------------------|-----------|---------------------------|----------|
| Balance at April 4, 2009 | \$ 1,700 | \$ 500 | \$ 2,200 |
| Provision | -- | -- | -- |
| Payments | (700) | -- | (700) |
| Balance at July 4, 2009 | \$ 1,000 | \$ 500 | \$ 1,500 |

White House Distribution Facility

During the second quarter of fiscal 2009, the Company wrote down the carrying value of its White House, Tennessee distribution facility held for sale by approximately \$0.7 million to reflect the decrease in the fair market value as evidenced by recent negotiations to sell the facility. The carrying value of the facility as of July 4, 2009 is \$2.8 million (classified as an asset held for sale within prepaid expenses and other current assets on the accompanying unaudited condensed consolidated balance sheet) to reflect the new anticipated selling price less costs to sell.

CARTER'S, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(unaudited)

NOTE 11 – EARNINGS PER SHARE:

Basic net income per share is calculated by dividing net income for the period by the weighted-average common shares outstanding for the period. Diluted net income per share includes the effect of dilutive instruments, such as stock options and restricted stock, and uses the average share price for the period in determining the number of shares that are to be added to the weighted-average number of shares outstanding. The table below summarizes the shares from these potentially dilutive securities, calculated using the treasury stock method.

The following is a reconciliation of basic common shares outstanding to diluted common and common equivalent shares outstanding:

| | For the three-month periods ended | | For the six-month periods ended | |
|---|--------------------------------------|------------------|------------------------------------|------------------|
| | July 4, 2009 | June 28, 2008 | July 4, 2009 | June 28, 2008 |
| Weighted-average number of common and common equivalent shares outstanding: | | | | |
| Basic number of common shares outstanding | 56,220,522 | 56,156,795 | 56,089,674 | 56,685,914 |
| Dilutive effect of unvested restricted stock | 122,781 | 67,533 | 116,583 | 72,352 |
| Dilutive effect of stock options | 1,787,646 | 1,939,377 | 1,727,956 | 1,983,387 |
| Diluted number of common and common equivalent shares outstanding | 58,130,949 | 58,163,705 | 57,934,213 | 58,741,653 |
| Basic net income per common share: | | | | |
| Net income | \$ 11,329,000 | \$ 2,779,000 | \$ 27,697,000 | \$ 14,338,000 |
| Income allocated to participating securities | (93,589) | (17,376) | (229,335) | (88,819) |
| Net income available to common shareholders | \$ 11,235,411 | \$ 2,761,624 | \$ 27,467,665 | \$ 14,249,181 |
| Basic net income per common share | \$ 0.20 | \$ 0.05 | \$ 0.49 | \$ 0.25 |
| Diluted net income per common share: | | | | |
| Net income | \$ 11,329,000 | \$ 2,779,000 | \$ 27,697,000 | \$ 14,338,000 |
| Income allocated to participating securities | (90,728) | (16,800) | (222,536) | (85,834) |
| Net income available to common shareholders | \$ 11,238,272 | \$ 2,762,200 | \$ 27,474,464 | \$ 14,252,166 |
| Diluted net income per common share | \$ 0.19 | \$ 0.05 | \$ 0.47 | \$ 0.24 |

For the three and six-month periods ended July 4, 2009, anti-dilutive shares of 1,166,050 and 1,290,050, respectively, and performance-based stock options of 200,000, were excluded from the computations of diluted earnings per share. For the three and six-month periods ended June 28, 2008, anti-dilutive shares of 1,052,135 and 991,385, respectively, and performance-based stock options of 620,000 were excluded from the computations of diluted earnings per share.

NOTE 12 – RECENT ACCOUNTING PRONOUNCEMENTS:

In February 2008, the Financial Accounting Standards Board (“FASB”) issued FASB Staff Position (“FSP”) No. FAS 157-2 (“FSP 157-2”), which delays the effective date of SFAS No. 157, "Fair Value Measurements," for nonfinancial assets and nonfinancial liabilities, except for items that are recognized or disclosed at fair value in the financial statements on a recurring basis (at least annually). Nonfinancial assets and nonfinancial liabilities would include all assets and liabilities other than those meeting the definition of a financial asset or financial liability as defined in paragraph 6 of SFAS No. 159, “The Fair Value Option for Financial Assets and Financial Liabilities.” This FSP defers the effective date of Statement 157 to fiscal years beginning after November 15, 2008, and interim periods within those fiscal years for items within the scope of FSP 157-2. The Company has adopted FSP 157-2 effective January 4, 2009 and has included the required disclosures in Note 5.

CARTER'S, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(unaudited)

NOTE 12 – RECENT ACCOUNTING PRONOUNCEMENTS: (Continued)

In March 2008, the FASB issued SFAS No. 161, “Disclosures about Derivative Instruments and Hedging Activities – an Amendment of FASB Statement No. 133,” which requires enhanced disclosures on the effect of derivatives on a Company’s financial statements. These disclosures were required for the Company beginning with the first quarter of fiscal 2009 consolidated financial statements. The Company has adopted the provisions of this statement effective April 4, 2009 and has included the required disclosures within Note 5.

In June 2008, the FASB issued FSP Emerging Issues Task Force (“EITF”) No. 03-6-1, “Determining Whether Instruments Granted in Share-Based Payment Transactions Are Participating Securities” (“FSP EITF 03-6-1”). FSP EITF 03-6-1 addresses whether instruments granted in share-based payment transactions are participating securities prior to vesting and, therefore, need to be included in the earnings allocation in computing earnings per share under the two-class method as described in SFAS No. 128, “Earnings per Share.” Under the guidance in FSP EITF 03-6-1, unvested share-based payment awards that contain non-forfeitable rights to dividends or dividend equivalents (whether paid or unpaid) are participating securities and shall be included in the computation of earnings per share pursuant to the two-class method. FSP EITF 03-6-1 is effective for fiscal years beginning after December 15, 2008, and interim periods within those fiscal years. All prior period earnings per share data presented shall be adjusted retrospectively. The Company has adopted the provisions of this standard effective January 4, 2009 and has included the required disclosures in Note 11.

In December 2008, the FASB issued FSP No. FAS 132(R)-1, “Employers’ Disclosures about Postretirement Benefit Plan Assets” (“FSP FAS 132(R)-1”), to provide guidance on an employers’ disclosures about plan assets of a defined benefit pension or other postretirement plan. This FSP is effective for fiscal years ending after December 15, 2009. We are currently evaluating the impact that FSP FAS 132(R)-1 will have on our consolidated financial statements.

In April 2009, the FASB issued FSP FAS 107-1 and APB Opinion No. 28-1, “Interim Disclosures about Fair Value of Financial Instruments,” which requires disclosures about fair value of financial instruments for interim reporting periods as well as in annual financial statements. The Company has adopted the provisions of this FSP effective July 4, 2009 and has included the required disclosures in Note 5.

In May 2009, the FASB issued SFAS No. 165, “Subsequent Events” (“SFAS 165”) which establishes general standards of accounting for and disclosure of events that occur after the balance sheet date but before financial statements are issued or are available to be issued. SFAS 165 applies prospectively to both interim and annual financial periods ending after June 15, 2009. The Company has adopted the provisions of this statement effective July 4, 2009 and has included the required disclosures in Note 2.

In June 2009, the FASB issued SFAS No. 168, “The FASB Accounting Standards Codification™ and the Hierarchy of Generally Accepted Accounting Principles - a replacement of FASB Statement No. 162” (“SFAS 168”). The FASB Accounting Standards Codification™ (“Codification”) will become the source of authoritative GAAP recognized by the FASB to be applied by nongovernmental entities. Rules and interpretive releases of the Securities and Exchange Commission (“SEC”) under authority of federal securities laws are also sources of authoritative GAAP for SEC registrants. On the effective date of SFAS 168, the Codification will supersede all then-existing non-SEC accounting and reporting standards. All other nongrandfathered non-SEC accounting literature not included in the Codification will become nonauthoritative under GAAP. SFAS 168 is effective for financial statements issued for interim and

annual periods ending after September 15, 2009. The Company will amend our disclosures accordingly beginning with our Quarterly Report on Form 10-Q for the three and nine-month periods ending October 3, 2009.

NOTE 13 – EXECUTIVE RETIREMENT CHARGES:

On June 11, 2008, the Company announced the retirement of an executive officer. In connection with this retirement, the Company recorded charges during the second quarter and first half of fiscal 2008 of \$5.3 million, \$3.1 million of which related to the present value of severance and benefit obligations, and \$2.2 million of which related to the accelerated vesting of stock options.

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

The following is a discussion of our results of operations and current financial position. This discussion should be read in conjunction with our unaudited condensed consolidated financial statements and the accompanying notes included elsewhere in this quarterly report.

Our fiscal year ends on the Saturday, in December or January, nearest the last day of December. The accompanying unaudited condensed consolidated financial statements for the second quarter and first half of fiscal 2009 reflect our financial position as of July 4, 2009. The second quarter and first half of fiscal 2008 ended on June 28, 2008.

RESULTS OF OPERATIONS

The following table sets forth, for the periods indicated (i) selected statement of operations data expressed as a percentage of consolidated net sales and (ii) the number of retail stores open at the end of each period:

| | Three-month periods ended | | Six-month periods ended | |
|---|---------------------------|------------------|-------------------------|------------------|
| | July 4, 2009 | June 28, 2008 | July 4, 2009 | June 28, 2008 |
| Wholesale sales: | | | | |
| Carter's | 31.5 % | 31.3 % | 33.0 % | 33.6 % |
| OshKosh | 3.6 | 4.6 | 4.9 | 5.1 |
| Total wholesale sales | 35.1 | 35.9 | 37.9 | 38.7 |
| Retail store sales: | | | | |
| Carter's | 34.6 | 30.7 | 31.4 | 28.4 |
| OshKosh | 16.4 | 16.5 | 15.4 | 14.9 |
| Total retail store sales | 51.0 | 47.2 | 46.8 | 43.3 |
| Mass channel sales | 13.9 | 16.9 | 15.3 | 18.0 |
| Consolidated net sales | 100.0 | 100.0 | 100.0 | 100.0 |
| Cost of goods sold | 63.4 | 67.0 | 63.9 | 67.6 |
| Gross profit | 36.6 | 33.0 | 36.1 | 32.4 |
| Selling, general, and administrative expenses | 31.4 | 30.6 | 29.5 | 29.2 |
| Workforce reduction and facility write-down and closure costs | 1.0 | -- | 1.7 | -- |
| Executive retirement charges | -- | 1.7 | -- | 0.9 |

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|--|--------|--------|--------|--------|
| Royalty income | (2.4) | (2.4) | (2.4) | (2.4) |
| Operating income | 6.6 | 3.1 | 7.3 | 4.7 |
| Interest expense, net | 0.9 | 1.6 | 0.8 | 1.5 |
| Income before income taxes | 5.7 | 1.5 | 6.5 | 3.2 |
| Provision for income taxes | 2.1 | 0.6 | 2.4 | 0.9 |
| Net income | 3.6 % | 0.9 % | 4.1 % | 2.3 % |
| Number of retail stores at end of period: | | | | |
| Carter's | 271 | 231 | 271 | 231 |
| OshKosh | 168 | 163 | 168 | 163 |
| Total | 439 | 394 | 439 | 394 |

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (Continued)

Three and six-month periods ended July 4, 2009 compared to the three and six-month periods ended June 28, 2008

CONSOLIDATED NET SALES

In the second quarter of fiscal 2009, consolidated net sales increased \$16.2 million, or 5.4%, to \$317.9 million and reflect growth in our Carter's brand wholesale and retail store segments and our OshKosh brand retail store segment. In the first half of fiscal 2009, consolidated net sales increased \$43.0 million, or 6.8%, to \$674.7 million and reflect growth in our Carter's and OshKosh brand wholesale and retail store segments.

| (dollars in thousands) | For the three-month periods ended | | | | For the six-month periods ended | | | | |
|------------------------|-----------------------------------|---------------|------------------|---------------|---------------------------------|---------------|------------------|---------------|--|
| | July 4, 2009 | % of Total | June 28, 2008 | % of Total | July 4, 2009 | % of Total | June 28, 2008 | % of Total | |
| Net sales: | | | | | | | | | |
| Wholesale-Carter's | \$ 100,088 | 31.5 % | \$ 94,322 | 31.3 % | \$ 222,985 | 33.0 % | \$ 212,154 | 33.6 % | |
| Wholesale-OshKosh | 11,318 | 3.6 % | 13,760 | 4.6 % | 32,705 | 4.9 % | 32,209 | 5.1 % | |
| Retail-Carter's | 110,127 | 34.6 % | 92,656 | 30.7 % | 212,057 | 31.4 % | 179,058 | 28.4 % | |
| Retail-OshKosh | 52,160 | 16.4 % | 49,883 | 16.5 % | 103,988 | 15.4 % | 94,248 | 14.9 % | |
| Mass | | | | | | | | | |
| Channel-Carter's | 44,216 | 13.9 % | 51,054 | 16.9 % | 102,961 | 15.3 % | 113,978 | 18.0 % | |
| Total net sales | \$ 317,909 | 100.0 % | \$ 301,675 | 100.0 % | \$ 674,696 | 100.0 % | \$ 631,647 | 100.0 % | |

CARTER'S WHOLESALE SALES

Carter's brand wholesale sales increased \$5.8 million, or 6.1%, in the second quarter of fiscal 2009 to \$100.1 million. The increase in Carter's brand wholesale sales was driven by an 11% increase in units shipped, partially offset by a 4% decrease in average price per unit, as compared to the second quarter of fiscal 2008.

Carter's brand wholesale sales increased \$10.8 million, or 5.1%, in the first half of fiscal 2009 to \$223.0 million. The increase in Carter's brand wholesale sales was driven by a 4% increase in units shipped and a 1% increase in average price per unit, as compared to the first half of fiscal 2008.

The increase in units shipped during the second quarter and first half of fiscal 2009 was primarily driven by increased off-price sales and strong over-the-counter performance at our wholesale customers. The decrease in average price per unit during the second quarter of fiscal 2009 reflects a higher mix of off-price sales which generally carry lower selling prices and higher provisions for markdown support.

OSHKOSH WHOLESALE SALES

OshKosh brand wholesale sales decreased \$2.4 million, or 17.7%, in the second quarter of fiscal 2009 to \$11.3 million and reflects a 30% decrease in units shipped partially offset by an 18% increase in average price per unit as compared to the second quarter of fiscal 2008.

OshKosh brand wholesale sales increased \$0.5 million, or 1.5%, in the first half of fiscal 2009 to \$32.7 million and reflects a 12% increase in average price per unit partially offset by a 9% decrease in units shipped as compared to the first half of fiscal 2008.

The decrease in units shipped during the second quarter and first half of fiscal 2009 relate primarily to a reduction in off-price shipments. The increase in average price per unit during the second quarter and first half of fiscal 2009 reflect reduced levels of off-price shipments and lower levels of customer support.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (Continued)

MASS CHANNEL SALES

Mass channel sales decreased \$6.8 million, or 13.4%, in the second quarter of fiscal 2009 to \$44.2 million. The decrease was due to an \$8.6 million, or 28.9%, decrease in sales of our Child of Mine brand to Walmart, partially offset by a \$1.8 million, or 8.5%, increase in sales of our Just One Year brand to Target. The decrease in Child of Mine brand sales resulted from a reduction in floor space. The increase in Just One Year brand sales was driven largely by improved product performance and timing of product launches as compared to similar launches last year.

Mass channel sales decreased \$11.0 million, or 9.7%, in the first half of fiscal 2009 to \$103.0 million. The decrease was due to an \$11.7 million, or 17.9%, decrease in sales of our Child of Mine brand to Walmart, partially offset by a \$0.6 million, or 1.3%, increase in sales of our Just One Year brand to Target. The decrease in Child of Mine brand sales resulted primarily from a reduction in floor space. The increase in sales of our Just One Year brand was due to improved product performance and new door growth. We anticipate our mass channel sales could decline approximately 10% in fiscal 2009 as compared to fiscal 2008, primarily due to lower sales of our Child of Mine brand due to strategic assortment changes made by Walmart.

CARTER'S RETAIL STORES

Carter's retail store sales increased \$17.5 million, or 18.9%, in the second quarter of fiscal 2009 to \$110.1 million. The increase was driven by incremental sales of \$10.9 million generated by new store openings and a comparable store sales increase of 8.1%, or \$6.3 million. On a comparable store basis, transactions increased 8.0%, units per transaction increased 3.3%, and average prices decreased 3.1% as compared to the second quarter of fiscal 2008.

Carter's retail store sales increased \$33.0 million, or 18.4%, in the first half of fiscal 2009 to \$212.1 million. The increase was driven by incremental sales of \$19.2 million generated by new store openings and a comparable store sales increase of 6.7%, or \$13.7 million. On a comparable store basis, transactions increased 5.3%, units per transaction increased 1.6%, and average prices decreased 0.3% as compared to the first half of fiscal 2008.

We attribute the increases in transactions during the second quarter and first half of fiscal 2009 to strong product performance in all product categories, changes in our merchandising strategies including a higher mix of opening price point items (high-volume, entry level basic products), a better assortment of in-season merchandise on the floor, in-store product presentation, and merchandising and marketing efforts. The decrease in average prices during the second quarter and first half of fiscal 2009 were due to our new opening price point strategy.

The Company's comparable store sales calculations include sales for all stores that were open during the comparable fiscal period, including remodeled stores and certain relocated stores. If a store relocates within the same center with no business interruption or material change in square footage, the sales of such store will continue to be included in the comparable store calculation. If a store relocates to another center, or there is a material change in square footage, such store is treated as a new store. Stores that are closed during the period are included in the comparable store sales calculation up to the date of closing.

There were a total of 271 Carter's retail stores as of July 4, 2009. During the second quarter of fiscal 2009, we opened 11 Carter's retail stores. During the first half of fiscal 2009, we opened 18 Carter's retail stores. In total, we plan to open 25 Carter's retail stores and close one Carter's retail store during fiscal 2009.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (Continued)

OSHKOSH RETAIL STORES

OshKosh retail store sales increased \$2.3 million, or 4.6%, in the second quarter of fiscal 2009 to \$52.2 million. The increase reflects a comparable store sales increase of 2.6%, or \$1.1 million, and incremental sales of \$1.1 million generated by new store openings, partially offset by the impact of store closings of \$0.2 million. On a comparable store basis, transactions increased 7.2% and average prices decreased 2.5%. We attribute the increase in transactions to strong product performance, our new opening price point strategy, and a better assortment of in-season merchandise on the floor. The decrease in average prices is attributable to our new opening price point strategy.

OshKosh retail store sales increased \$9.7 million, or 10.3%, in the first half of fiscal 2009 to \$104.0 million. The increase reflects a comparable store sales increase of 6.7%, or \$7.9 million, and incremental sales of \$2.0 million generated by new store openings, partially offset by the impact of store closings of \$0.3 million. On a comparable store basis, transactions increased 6.2% and average prices increased 3.2%. We attribute the increase in transactions to strong product performance, our new opening price point strategy, and improved in-store product presentation. The increase in average prices was driven by more significant prior year markdowns to clear excess goods in the first quarter of fiscal 2008.

There were a total of 168 OshKosh retail stores as of July 4, 2009. During the second quarter and first half of fiscal 2009, we opened three OshKosh retail stores. We plan to open six OshKosh retail stores and close one OshKosh retail store during fiscal 2009.

GROSS PROFIT

Gross profit increased \$16.7 million, or 16.8%, to \$116.3 million in the second quarter of fiscal 2009. Gross profit as a percentage of net sales was 36.6% in the second quarter of fiscal 2009 as compared to 33.0% in the second quarter of fiscal 2008. Our gross profit increased \$39.1 million, or 19.1%, to \$243.6 million in the first half of fiscal 2009. Gross profit as a percentage of net sales was 36.1% in the first half of fiscal 2009 as compared to 32.4% in the first half of fiscal 2008.

These increases in gross profit as a percentage of net sales reflect:

- (i) a greater mix of consolidated retail sales which, on average, have a higher gross margin than sales in our wholesale and mass channel segments;
- (ii) lower levels of excess inventory charges related to strong demand from off-price accounts, more favorable loss rates, and improved inventory management; and
- (iii) growth in OshKosh wholesale gross margin due to lower levels of customer support.

The Company includes distribution costs in its selling, general, and administrative expenses. Accordingly, the Company's gross profit may not be comparable to other companies that include such distribution costs in their cost of goods sold.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (Continued)

SELLING, GENERAL, AND ADMINISTRATIVE EXPENSES

Selling, general, and administrative expenses in the second quarter of fiscal 2009 increased \$7.6 million, or 8.3%, to \$99.8 million. As a percentage of net sales, selling, general, and administrative expenses in the second quarter of fiscal 2009 were 31.4% as compared to 30.6% in the second quarter of fiscal 2008. Selling, general, and administrative expenses in the first half of fiscal 2009 increased \$14.5 million, or 7.9%, to \$199.0 million. As a percentage of net sales, selling, general, and administrative expenses in the first half of fiscal 2009 were 29.5% as compared to 29.2% in the first half of fiscal 2008.

These increases in selling, general, and administrative expenses as a percentage of net sales reflect:

- (i) higher retail store expenses as a percentage of consolidated net sales related to new store openings; and
- (ii) higher provisions for incentive compensation.

Partially offsetting these increases were:

- (i) lower levels of bad debt expense; and
- (ii) reducing discretionary spending and increased overall focus on our corporate cost structure.

WORKFORCE REDUCTION AND FACILITY WRITE-DOWN AND CLOSURE COSTS

As a result of the corporate workforce reduction, we recorded severance charges and other one-time benefits to eligible employees of \$2.2 million in the second quarter of fiscal 2009. During the first half of fiscal 2009, we recorded charges of \$7.3 million consisting of \$5.5 million in severance charges and other benefits, and approximately \$1.8 million in asset impairment charges related to the closure of our Oshkosh, Wisconsin corporate office. The majority of the severance payments will be paid through the end of the year.

In conjunction with the plan to close the Barnesville, Georgia distribution center, the Company recorded accelerated depreciation charges (included in selling, general, and administrative expenses) of approximately \$0.7 million in the second quarter of fiscal 2009 and charges of \$4.3 million during the first half of fiscal 2009, consisting of severance of \$1.7 million, asset impairment charges of \$1.1 million related to the write-down of the related land, building, and equipment, \$1.0 million of accelerated depreciation (included in selling, general, and administrative expenses), and \$0.5 million of other closure costs.

During the second quarter of fiscal 2009, the Company wrote down the carrying value of its White House, Tennessee distribution facility held for sale by approximately \$0.7 million to reflect the decrease in the fair market value as evidenced by recent negotiations to sell the facility. The carrying value of the facility as of July 4, 2009 is \$2.8 million (classified as an asset held for sale within prepaid expenses and other current assets on the accompanying unaudited condensed consolidated balance sheet) to reflect the new anticipated selling price less costs to sell.

EXECUTIVE RETIREMENT CHARGES

In the second quarter of fiscal 2008, the Company announced the retirement of an executive officer. In connection with this retirement, the Company recorded charges during the second quarter of fiscal 2008 of \$5.3 million, \$3.1

million of which related to the present value of severance and benefit obligations, and \$2.2 million of which related to the accelerated vesting of stock options.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (Continued)

ROYALTY INCOME

We license the use of our Carter's, Just One Year, Child of Mine, OshKosh B'Gosh, OshKosh, and Genuine Kids from OshKosh brand names. Royalty income from these brands in the second quarter of fiscal 2009 was approximately \$7.5 million (including \$1.9 million of international royalty income), an increase of 3.7%, or \$0.3 million, as compared to the second quarter of fiscal 2008. This increase was driven by increased sales by our international licensees and Carter's brand domestic licensees.

Royalty income from these brands in the first half of fiscal 2009 was approximately \$16.2 million (including \$4.0 million of international royalty income), an increase of 7.4%, or \$1.1 million, as compared to the first half of fiscal 2008. This increase was driven by increased sales by our international licensees and Carter's brand domestic licensees.

OPERATING INCOME

Operating income increased \$11.7 million to \$20.9 million in the second quarter of fiscal 2009. Our operating income increased \$19.7 million, or 66.1% to \$49.5 million in the first half of fiscal 2009. These increases in operating income were due to the factors described above.

INTEREST EXPENSE, NET

Interest expense in the second quarter of fiscal 2009 decreased \$2.1 million, or 43.5%, to \$2.7 million. The decrease is primarily attributable to lower effective interest rates. Weighted-average borrowings in the second quarter of fiscal 2009 were \$336.9 million at an effective interest rate of 3.31% as compared to weighted-average borrowings in the second quarter of fiscal 2008 of \$340.7 million at an effective interest rate of 6.21%. In the second quarter of fiscal 2009, we recorded \$0.5 million in interest expense related to our interest rate swap agreements. In the second quarter of fiscal 2008, we recorded \$0.5 million in interest expense related to our interest rate swap agreement and \$0.5 million in interest expense related to our interest rate collar agreement.

Interest expense in the first half of fiscal 2009 decreased \$3.4 million, or 36.8%, to \$5.9 million. The decrease is primarily attributable to lower effective interest rates. Weighted-average borrowings in the first half of fiscal 2009 were \$337.3 million at an effective interest rate of 3.59% as compared to weighted-average borrowings in the first half of fiscal 2008 of \$341.1 million at an effective interest rate of 6.01%. In the first half of fiscal 2009, we recorded \$0.9 million in interest expense related to our interest rate swap agreements and \$0.5 million in interest expense related to our interest rate collar agreement. In the first half of fiscal 2008, we recorded \$0.6 million in interest expense related to our interest rate swap agreement and \$0.5 million in interest expense related to our interest rate collar agreement.

INCOME TAXES

Our effective tax rate was 37.9% for the second quarter of fiscal 2009 and 37.7% for the second quarter of fiscal 2008.

Our effective tax rate was 36.5% for the first half of fiscal 2009 and 30.0% in the first half of fiscal 2008. This change was a result of the reversal of \$1.6 million of reserves for certain tax exposures following the completion of an Internal Revenue Service examination for fiscal 2004 and 2005 in the first half of fiscal 2008 as compared to the reversal of \$1.0 million related to the completion of an Internal Revenue Service examination for fiscal 2006 in the first half of fiscal 2009.

NET INCOME

As a result of the factors described above, our net income for the second quarter of fiscal 2009 increased \$8.6 million to \$11.3 million as compared to \$2.8 million in the second quarter of fiscal 2008. Our net income for the first half of fiscal 2009 increased \$13.4 million to \$27.7 million as compared to \$14.3 million for the first half of fiscal 2008.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (Continued)

FINANCIAL CONDITION, CAPITAL RESOURCES, AND LIQUIDITY

Our primary cash needs are working capital and capital expenditures. Our primary source of liquidity will continue to be cash and cash equivalents on hand, cash flow from operations, and borrowings under our revolver, and we expect that these sources will fund our ongoing requirements for working capital and capital expenditures. These sources of liquidity may be impacted by events described in our risk factors, as further discussed in Item 1A of this Form 10-Q.

Net accounts receivable at July 4, 2009 were \$96.9 million compared to \$102.6 million at June 28, 2008 and \$106.1 million at January 3, 2009. The decrease as compared to June 28, 2008 primarily reflects lower levels of mass channel sales. Due to the seasonal nature of our operations, the net accounts receivable balance at July 4, 2009 is not comparable to the net accounts receivable balance at January 3, 2009.

Net inventories at July 4, 2009 were \$256.2 million compared to \$250.8 million at June 28, 2008 and \$203.5 million at January 3, 2009. The increase of \$5.3 million, or 2.1%, as compared to June 28, 2008 is due to an increase in our retail store base and the timing of wholesale shipments, partially offset by net working capital needs. Due to the seasonal nature of our operations, net inventories at July 4, 2009 are not comparable to net inventories at January 3, 2009.

Net cash provided by operating activities for the first half of fiscal 2009 was \$27.0 million compared to \$24.1 million in the first half of fiscal 2008. The increase in operating cash flow primarily reflects the growth in earnings partially offset by increased levels of inventory.

We invested \$15.8 million in capital expenditures during the first half of fiscal 2009 compared to \$7.1 million during the first half of fiscal 2008. We plan to invest approximately \$40 million in capital expenditures during fiscal 2009, primarily for retail store openings and remodelings (including retail store fixtures), fixtures for our wholesale customers, investments in our supply chain, and investments in information technology.

On February 16, 2007, the Company's Board of Directors approved a stock repurchase program, pursuant to which the Company is authorized to purchase up to \$100 million of its outstanding common shares. During the first half of fiscal 2009, the Company did not repurchase any of its common stock. Since inception of the program and through July 4, 2009, the Company repurchased and retired 4,599,580 shares, or approximately \$91.1 million, of its common stock at an average price of \$19.81 per share, leaving approximately \$8.9 million available for repurchase under the plan. Such repurchases may occur from time to time in the open market, in negotiated transactions, or otherwise. This program has no time limit. The timing and amount of any repurchases will be determined by management, based on its evaluation of market conditions, share price, and other factors.

At July 4, 2009, we had approximately \$336.3 million in term loan borrowings and no borrowings outstanding under our revolver (together with the term loan, our "Senior Credit Facility"), exclusive of approximately \$8.6 million of outstanding letters of credit. Principal borrowings under our term loan are due and payable in quarterly installments of \$0.9 million through June 30, 2012, with the remaining balance of \$325.8 million due on July 14, 2012. Weighted-average borrowings in the first half of fiscal 2009 were \$337.3 million at an effective interest rate of 3.59% as compared to weighted-average borrowings in the first half of fiscal 2008 of \$341.1 million at an effective interest rate of 6.01%.

The Senior Credit Facility contains and defines financial covenants, including a minimum interest coverage ratio, maximum leverage ratio, and a fixed charge coverage ratio. As of July 4, 2009, the Company is in compliance with

all debt covenants. The Senior Credit Facility also sets forth mandatory and optional prepayment conditions, including an annual excess cash flow requirement, as defined, that may result in our use of cash to reduce our debt obligations. There was no excess cash flow payment required for fiscal 2008 or 2007. Our obligations under the Senior Credit Facility are collateralized by a first priority lien on substantially all of our assets, including the assets of our domestic subsidiaries.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (Continued)

Our Senior Credit Facility requires us to hedge at least 25% of our debt under this facility using interest rate swaps or other similar instruments. As of July 4, 2009, \$147.1 million, or 44%, of our Senior Credit Facility borrowings were subject to interest rate swap agreements.

Our operating results are subject to risk from interest rate fluctuations on our Senior Credit Facility, which carries variable interest rates. As of July 4, 2009, our outstanding debt aggregated approximately \$336.3 million, of which \$189.2 million, or 56%, was subject to variable interest rates. An increase or decrease of 1% in the applicable rate would increase or decrease our annual interest cost by approximately \$1.9 million, exclusive of variable rate debt subject to our swap agreements, and could have an adverse effect on our earnings and cash flow.

Based on our current outlook, we believe that cash generated from operations and available cash, together with amounts available under our revolver, will be adequate to meet our working capital needs and capital expenditure requirements for the foreseeable future, although no assurance can be given in this regard. We may, however, need to refinance all or a portion of the principal amount, if any, outstanding under our revolver on or before July 14, 2011 and amounts outstanding under our term loan on or before July 14, 2012.

The continuing volatility in the financial markets and the related economic downturn in markets throughout the world could have a material adverse effect on our business. While we currently generate significant cash flows from our ongoing operations and have access to credit through amounts available under our revolver, credit markets have recently experienced significant disruptions and certain leading financial institutions have either declared bankruptcy or have shown significant deterioration in their financial stability. Further deterioration in the financial markets could make future financing difficult or more expensive. If any of the financial institutions that are parties to our revolver were to declare bankruptcy or become insolvent, they may be unable to perform under their agreements with us. This could leave us with reduced borrowing capacity. In addition, tighter credit markets may lead to business disruptions for certain of our suppliers, contract manufacturers or trade customers and consequently, could disrupt our business.

EFFECTS OF INFLATION AND DEFLATION

We are affected by inflation and changing prices primarily through purchasing product from our global suppliers, increased operating costs and expenses, and fluctuations in interest rates. The effects of inflation on our net sales and operations have not been material in recent years. In recent years, there has been deflationary pressure on selling prices. If deflationary price trends outpace our ability to obtain price reductions from our global suppliers, our profitability may be affected.

SEASONALITY

We experience seasonal fluctuations in our sales and profitability, with generally lower sales and gross profit in the first and second quarters of our fiscal year. Over the past five fiscal years, excluding the impact of our acquisition of OshKosh B'Gosh, Inc. in fiscal 2005, approximately 57% of our consolidated net sales were generated in the second half of our fiscal year. Accordingly, our results of operations for the first and second quarters of any year are not indicative of the results we expect for the full year.

As a result of this seasonality, our inventory levels and other working capital requirements generally begin to increase during the second quarter and into the third quarter of each year.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

Our discussion and analysis of our financial condition and results of operations are based upon our consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues, expenses, and related disclosure of contingent assets and liabilities. We base our estimates on historical experience and on various other assumptions that we believe are reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (Continued)

Our significant accounting policies are described in Note 2 to our audited consolidated financial statements contained in our most recently filed Annual Report on Form 10-K. The following discussion addresses our critical accounting policies and estimates, which are those policies that require management's most difficult and subjective judgments, often as a result of the need to make estimates about the effect of matters that are inherently uncertain.

Revenue recognition: We recognize wholesale and mass channel revenue after shipment of products to customers, when title passes, when all risks and rewards of ownership have transferred, the sales price is fixed or determinable, and collectibility is reasonably assured. In certain cases, in which we retain the risk of loss during shipment, revenue recognition does not occur until the goods have reached the specified customer. In the normal course of business, we grant certain accommodations and allowances to our wholesale and mass channel customers in order to assist these customers with inventory clearance or promotions. Such amounts are reflected as a reduction of net sales and are recorded based upon historical trends and annual forecasts. Retail store revenues are recognized at the point of sale. We reduce revenue for customer returns and deductions. We also maintain an allowance for doubtful accounts for estimated losses resulting from the inability of our customers to make payments and other actual and estimated deductions. If the financial condition of our customers were to deteriorate, resulting in an impairment of their ability to make payments, an additional allowance could be required. Past due balances over 90 days are reviewed individually for collectibility. Our credit and collections department reviews all other balances regularly. Account balances are charged off against the allowance when we believe it is probable the receivable will not be recovered.

We contract with a third-party service to provide us with the fair value of cooperative advertising arrangements entered into with certain of our major wholesale and mass channel customers. Such fair value is determined based upon, among other factors, comparable market analysis for similar advertisements. In accordance with Emerging Issues Task Force ("EITF") Issue No. 01-09, "Accounting for Consideration Given by a Vendor to a Customer/Reseller," we have included the fair value of these arrangements of approximately \$0.8 million and \$1.6 million in the second quarter and first half of fiscal 2009 and \$0.2 million and \$0.9 million in the second quarter and first half of fiscal 2008 as a component of selling, general, and administrative expenses in the accompanying unaudited condensed consolidated statements of operations rather than as a reduction of revenue. Amounts determined to be in excess of the fair value of these arrangements are recorded as a reduction of net sales.

Inventory: We provide reserves for slow-moving inventory equal to the difference between the cost of inventory and the estimated market value based upon assumptions about future demand and market conditions. If actual market conditions are less favorable than those we project, additional write-downs may be required.

Cost in excess of fair value of net assets acquired and tradename: As of July 4, 2009, we had approximately \$136.6 million in Carter's cost in excess of fair value of net assets acquired and \$305.7 million of aggregate value related to the Carter's and OshKosh tradename assets. The fair value of the Carter's tradename was estimated at the acquisition of Carter's, Inc. by Berkshire Partners LLC which was consummated on August 15, 2001, using a discounted cash flow analysis, which examined the hypothetical cost savings that accrue as a result of our ownership of the tradename. The fair value of the OshKosh tradename was also estimated at its acquisition date using an identical discounted cash flow analysis. The tradenames were determined to have indefinite lives.

The carrying values of these assets are subject to annual impairment reviews in accordance with Statement of Financial Accounting Standards ("SFAS") No. 142, "Goodwill and other Intangible Assets," as of the last day of each fiscal year. Factors affecting such impairment reviews include the continued market acceptance of our offered products and the development of new products. Impairment reviews may also be triggered by any significant events or changes in circumstances.

Accrued expenses: Accrued expenses for workers' compensation, incentive compensation, health insurance, and other outstanding obligations are assessed based on actual commitments, statistical trends, and estimates based on projections and current expectations, and these estimates are updated periodically as additional information becomes available.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (Continued)

Loss contingencies: We record accruals for various contingencies including legal exposures as they arise in the normal course of business. In accordance with SFAS No. 5, "Accounting for Contingencies," we determine whether to disclose and accrue for loss contingencies based on an assessment of whether the risk of loss is remote, reasonably possible or probable. Our assessment is developed in consultation with our internal and external counsel and other advisors and is based on an analysis of possible outcomes under various strategies. Loss contingency assumptions involve judgments that are inherently subjective and can involve matters that are in litigation, which, by its nature is unpredictable. We believe that our assessment of the probability of loss contingencies is reasonable, but because of the subjectivity involved and the unpredictable nature of the subject matter at issue, our assessment may prove ultimately to be incorrect, which could materially impact our consolidated financial statements.

Accounting for income taxes: As part of the process of preparing the accompanying unaudited condensed consolidated financial statements, we are required to estimate our actual current tax exposure (state, federal, and foreign). We assess our income tax positions and record tax benefits for all years subject to examination based upon management's evaluation of the facts, circumstances, and information available at the reporting dates. For those uncertain tax positions where it is "more likely than not" that a tax benefit will be sustained, we have recorded the largest amount of tax benefit with a greater than 50% likelihood of being realized upon ultimate settlement with a taxing authority that has full knowledge of all relevant information. For those income tax positions where it is not "more likely than not" that a tax benefit will be sustained, no tax benefit has been recognized in the financial statements. Where applicable, associated interest is also recognized. We also assess permanent and temporary differences resulting from differing bases and treatment of items for tax and accounting purposes, such as the carrying value of intangibles, deductibility of expenses, depreciation of property, plant, and equipment, stock-based compensation expense, and valuation of inventories. Temporary differences result in deferred tax assets and liabilities, which are included within our consolidated balance sheets. We must then assess the likelihood that our deferred tax assets will be recovered from future taxable income. Actual results could differ from this assessment if sufficient taxable income is not generated in future periods. To the extent we determine the need to establish a valuation allowance or increase such allowance in a period, we must include an expense within the tax provision in the accompanying unaudited condensed consolidated statement of operations.

Employee benefit plans: We sponsor a defined benefit pension, defined contribution, and other post-retirement plans. Major assumptions used in the accounting for these employee benefit plans include the discount rate, expected return on the pension fund assets, and health care cost increase projections. See Note 7 "Employee Benefit Plans" to our audited consolidated financial statements in our most recently filed Annual Report on Form 10-K for further details on rates and assumptions.

Stock-based compensation arrangements: The Company accounts for stock-based compensation in accordance with the fair value recognition provisions of SFAS No. 123 (revised 2004), "Share-Based Payment" ("SFAS 123R"). The Company adopted SFAS 123R using the modified prospective application method of transition. The Company uses the Black-Scholes option pricing model, which requires the use of subjective assumptions. These assumptions include the following:

Volatility – This is a measure of the amount by which a stock price has fluctuated or is expected to fluctuate. The Company uses actual monthly historical changes in the market value of our stock since the Company's initial public offering on October 29, 2003, supplemented by peer company data for periods prior to our initial public offering covering the expected life of stock options being valued. An increase in the expected volatility will increase compensation expense.

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Risk-free interest rate – This is the U.S. Treasury rate as of the grant date having a term equal to the expected term of the stock option. An increase in the risk-free interest rate will increase compensation expense.

Expected term – This is the period of time over which the stock options granted are expected to remain outstanding and is based on historical experience and estimated future exercise behavior. Separate groups of employees that have similar historical exercise behavior are considered separately for valuation purposes. An increase in the expected term will increase compensation expense.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (Continued)

Dividend yield – The Company does not have plans to pay dividends in the foreseeable future. An increase in the dividend yield will decrease compensation expense.

Forfeitures – The Company estimates forfeitures of stock-based awards based on historical experience and expected future activity.

Changes in the subjective assumptions can materially affect the estimate of fair value of stock-based compensation and consequently, the related amount recognized in the accompanying unaudited condensed consolidated statement of operations.

The Company accounts for its performance-based awards in accordance with SFAS 123R and records stock-based compensation expense over the vesting term of the awards that are expected to vest based on whether it is probable that the performance criteria will be achieved. The Company reassesses the probability of vesting at each reporting period for awards with performance criteria and adjusts stock-based compensation expense based on its probability assessment.

RECENT ACCOUNTING PRONOUNCEMENTS

In February 2008, the Financial Accounting Standards Board (“FASB”) issued FASB Staff Position (“FSP”) No. FAS 157-2 (“FSP 157-2”), which delays the effective date of SFAS No. 157, “Fair Value Measurements,” for nonfinancial assets and nonfinancial liabilities, except for items that are recognized or disclosed at fair value in the financial statements on a recurring basis (at least annually). Nonfinancial assets and nonfinancial liabilities would include all assets and liabilities other than those meeting the definition of a financial asset or financial liability as defined in paragraph 6 of SFAS No. 159, “The Fair Value Option for Financial Assets and Financial Liabilities.” This FSP defers the effective date of Statement 157 to fiscal years beginning after November 15, 2008, and interim periods within those fiscal years for items within the scope of FSP 157-2. The Company has adopted FSP 157-2 effective January 4, 2009 and has included the required disclosures within Note 5 to the accompanying unaudited condensed consolidated financial statements.

In March 2008, the FASB issued SFAS No. 161, “Disclosures about Derivative Instruments and Hedging Activities – an Amendment of FASB Statement No. 133,” which requires enhanced disclosures on the effect of derivatives on a Company’s financial statements. These disclosures were required for the Company beginning with the first quarter of fiscal 2009 consolidated financial statements. The Company has adopted the provisions of this statement effective April 4, 2009 and has included the required disclosures within Note 5 to the accompanying unaudited condensed consolidated financial statements.

In June 2008, the FASB issued FSP EITF No. 03-6-1, “Determining Whether Instruments Granted in Share-Based Payment Transactions Are Participating Securities” (“FSP EITF 03-6-1”). FSP EITF 03-6-1 addresses whether instruments granted in share-based payment transactions are participating securities prior to vesting and, therefore, need to be included in the earnings allocation in computing earnings per share under the two-class method as described in SFAS No. 128, “Earnings per Share.” Under the guidance in FSP EITF 03-6-1, unvested share-based payment awards that contain non-forfeitable rights to dividends or dividend equivalents (whether paid or unpaid) are participating securities and shall be included in the computation of earnings per share pursuant to the two-class method. FSP EITF 03-6-1 is effective for fiscal years beginning after December 15, 2008, and interim periods within those fiscal years. All prior period earnings per share data presented shall be adjusted retrospectively. The Company has adopted the provisions of this standard effective January 4, 2009 and has included the required disclosures in Note

11 to the accompanying unaudited condensed consolidated financial statements.

In December 2008, the FASB issued FSP No. FAS 132(R)-1, “Employers’ Disclosures about Postretirement Benefit Plan Assets” (“FSP FAS 132(R)-1”), to provide guidance on an employers’ disclosures about plan assets of a defined benefit pension or other postretirement plan. This FSP is effective for fiscal years ending after December 15, 2009. We are currently evaluating the impact that FSP FAS 132(R)-1 will have on our consolidated financial statements.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (Continued)

In April 2009, the FASB issued FSP FAS 107-1 and APB Opinion No. 28-1, "Interim Disclosures about Fair Value of Financial Instruments," which requires disclosures about fair value of financial instruments for interim reporting periods as well as in annual financial statements. The Company has adopted the provisions of this FSP effective July 4, 2009 and has included the required disclosures in Note 5 to the accompanying unaudited condensed consolidated financial statements.

In May 2009, the FASB issued SFAS No. 165, "Subsequent Events" ("SFAS 165"), which establishes general standards of accounting for and disclosure of events that occur after the balance sheet date but before financial statements are issued or are available to be issued. SFAS 165 applies prospectively to both interim and annual financial periods ending after June 15, 2009. The Company has adopted the provisions of this statement effective July 4, 2009 and has included the required disclosures within Note 2 to the accompanying unaudited condensed consolidated financial statements.

In June 2009, the FASB issued SFAS No. 168, "The FASB Accounting Standards Codification TM and the Hierarchy of Generally Accepted Accounting Principles - a replacement of FASB Statement No. 162" ("SFAS 168"). The FASB Accounting Standards CodificationTM ("Codification") will become the source of authoritative accounting principles generally accepted in the United States of America ("GAAP") recognized by the FASB to be applied by nongovernmental entities. Rules and interpretive releases of the Securities and Exchange Commission ("SEC") under authority of federal securities laws are also sources of authoritative GAAP for SEC registrants. On the effective date of SFAS 168, the Codification will supersede all then-existing non-SEC accounting and reporting standards. All other nongrandfathered non-SEC accounting literature not included in the Codification will become nonauthoritative under GAAP. SFAS 168 is effective for financial statements issued for interim and annual periods ending after September 15, 2009. The Company will amend our disclosures accordingly beginning with our Quarterly Report on Form 10-Q for the three and nine-month periods ending October 3, 2009.

FORWARD-LOOKING STATEMENTS

Statements contained herein that relate to our future performance, including, without limitation, statements with respect to our anticipated results of operations or level of business for fiscal 2009 or any other future period, are forward-looking statements within the meaning of the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. Such statements are based on current expectations only and are subject to certain risks, uncertainties, and assumptions. Should one or more of these risks or uncertainties materialize, or should underlying assumptions prove incorrect, actual results may vary materially from those anticipated, estimated, or projected. These risks are described herein under Item 1A of Part II. We undertake no obligation to publicly update or revise any forward-looking statements or other information, whether as a result of new information, future events, or otherwise.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

CURRENCY AND INTEREST RATE RISKS

In the operation of our business, we have market risk exposures including those related to foreign currency risk and interest rates. These risks and our strategies to manage our exposure to them are discussed below.

We contract for production with third parties primarily in Asia and South and Central America. While these contracts are stated in United States dollars, there can be no assurance that the cost for the future production of our products will not be affected by exchange rate fluctuations between the United States dollar and the local currencies of these contractors. Due to the number of currencies involved, we cannot quantify the potential impact of future currency fluctuations on net income (loss) in future years. In order to manage this risk, we currently source products from approximately 100 vendors worldwide, providing us with flexibility in our production should significant fluctuations occur between the United States dollar and various local currencies. To date, such exchange fluctuations have not had a material impact on our financial condition or results of operations. We do not hedge foreign currency exchange rate risk.

Our operating results are subject to risk from interest rate fluctuations on our Senior Credit Facility, which carries variable interest rates. As of July 4, 2009, our outstanding debt aggregated approximately \$336.3 million, of which \$189.2 million bore interest at a variable rate. An increase or decrease of 1% in the applicable rate would increase or decrease our annual interest cost by approximately \$1.9 million, exclusive of variable rate debt subject to our interest rate swap agreements, and could have an adverse effect on our net income (loss) and cash flow.

OTHER RISKS

We enter into various purchase order commitments with full-package suppliers. We can cancel these arrangements, although in some instances, we may be subject to a termination charge reflecting a percentage of work performed prior to cancellation. As we rely exclusively on our full-package global sourcing network, we could incur more of these termination charges, which could increase our cost of goods sold and have a material impact on our business.

ITEM 4. CONTROLS AND PROCEDURES

(a) Evaluation of Disclosure Controls and Procedures

Our Chief Executive Officer and Chief Financial Officer have evaluated the effectiveness of the design and operation of our disclosure controls and procedures (as defined under Rules 13a-15(e) and 15d-15(e) promulgated under the Securities Exchange Act of 1934, as amended) as of the end of the period covered by this report. Based upon that evaluation, our Chief Executive Officer and Chief Financial Officer have concluded that our disclosure controls and procedures are effective.

(b) Changes in Internal Control over Financial Reporting

There were no changes in the Company's internal controls over financial reporting during the period covered by this report that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

PART II – OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS:

A class action lawsuit was filed on September 19, 2008 in the United States District Court for the Northern District of Georgia. The Amended Complaint filed on May 12, 2009 in that lawsuit asserts claims under Sections 10(b), 20(a), and 20A of the 1934 Securities Exchange Act, and alleges that between February 1, 2006 and July 24, 2007, the Company made misrepresentations regarding the successful integration of OshKosh into the Company's business, and that the share price of the Company's stock later fell when the market learned that the integration had not been as successful as represented. Plaintiff Plymouth County Retirement System filed an unopposed motion to be appointed lead counsel on November 18, 2008, and that motion was granted on March 13, 2009. Defendants filed a motion to dismiss the Amended Complaint for failure to state a claim under the federal securities laws on July 17, 2009. The parties are in the process of briefing the Defendants' motion to dismiss. The Company intends to vigorously defend this claim.

A class action lawsuit was filed on September 29, 2008 in United States District Court for the Northern District of Illinois against the Company claiming breach of contract arising from certain advertising and pricing practices with respect to Carter's brand products purchased by consumers at Carter's retail stores nationally. The complaint seeks damages and injunctive relief. Plaintiff has since filed an amended complaint, alleging breach of contract on behalf of a nationwide class and Illinois Consumer Fraud Act claims on behalf of Illinois consumers. On February 3, 2009 the same plaintiff's attorney filed a second, nearly identical action against the Company in the same court but in the name of a different plaintiff. The parties filed an agreed upon motion to consolidate this second action with the first case and to stay the need for response in the second case until after the court had ruled upon a pending motion to dismiss the first case. On April 15, 2009, the Amended Complaint in the first case was dismissed for failure to state a claim for breach of contract and for failure to adequately allege damages. The Company subsequently filed a motion to dismiss the second case on the same grounds, which the Court granted on April 29, 2009. The plaintiffs filed a notice of appeal in each action on May 1, 2009. The appeals have been consolidated and are pending.

The Company is subject to various other claims and pending or threatened lawsuits in the normal course of our business. We are not currently party to any other legal proceedings that we believe would have a material adverse effect on our financial position, results of operations or cash flows.

ITEM 1A. RISK FACTORS:

You should carefully consider each of the following risk factors as well as the other information contained in this Quarterly Report on Form 10-Q and other filings with the Securities and Exchange Commission in evaluating our business. The risks and uncertainties described below are not the only we face. Additional risks and uncertainties not presently known to us or that we currently consider immaterial may also impact our business operations. If any of the following risks actually occur, our operating results may be affected.

Risks Relating to Our Business

The loss of one or more of our major customers could result in a material loss of revenues.

In the second quarter and first half of fiscal 2009, we derived approximately 37% and 39% of our consolidated net sales from our top eight customers, including mass channel customers. We do not enter into long-term sales contracts with our major customers, relying instead on long-standing relationships and on our position in the marketplace. As a

result, we face the risk that one or more of our major customers may significantly decrease its or their business with us or terminate its or their relationships with us. Any such decrease or termination of our major customers' business could result in a material decrease in our sales and operating results.

The acceptance of our products in the marketplace is affected by consumers' tastes and preferences, along with fashion trends.

We believe that continued success depends on our ability to provide a unique and compelling value proposition for our consumers in the Company's distribution channels. There can be no assurance that the demand for our products will not decline, or that we will be able to successfully evaluate and adapt our product to be aware of consumers' tastes and preferences or fashion trends. If consumers' tastes and preferences are not aligned with our product offerings, promotional pricing may be required to move seasonal merchandise. Increased use of promotional pricing would have a material adverse affect on our sales, gross margin, and results of operations.

The value of our brand, and our sales, could be diminished if we are associated with negative publicity.

Although our employees, agents, and third-party compliance auditors periodically visit and monitor the operations of our vendors, independent manufacturers, and licensees, we do not control these vendors, independent manufacturers, licensees, or their labor practices. A violation of our vendor policies, licensee agreements, labor laws, or other laws by these vendors, independent manufacturers, or licensees could interrupt or otherwise disrupt our supply chain or damage our brand image. As a result, negative publicity regarding our Company, brands or products, including licensed products, could adversely affect our reputation and sales.

In addition, the Company's brand image, which is associated with providing a consumer product with outstanding quality and name recognition, makes it valuable as a royalty source. The Company is able to generate royalty income from the sale of licensed products that bear its Carter's, Child of Mine, Just One Year, OshKosh, Genuine Kids from OshKosh, and related trademarks. The Company also generates foreign royalty income as our OshKosh B'Gosh label carries an international reputation for quality and American style. While the Company takes significant steps to ensure the reputation of its brand is maintained through its license agreements, there can be no guarantee that the Company's brand image will not be negatively impacted through its association with products outside of the Company's core apparel products.

The Company's databases containing personal information of our retail customers could be breached, which could subject us to adverse publicity, litigation, and expenses. In addition, if we are unable to comply with security standards created by the banks and payment card industry, our operations could be adversely affected.

Database privacy, network security, and identity theft are matters of growing public concern. In an attempt to prevent unauthorized access to our network and databases containing confidential, third-party information, we have installed privacy protection systems, devices, and activity monitoring on our network. Nevertheless, if unauthorized parties gain access to our networks or databases, they may be able to steal, publish, delete, or modify our private and sensitive third-party information. In such circumstances, we could be held liable to our customers or other parties or be subject to regulatory or other actions for breaching privacy rules. This could result in costly investigations and litigation, civil or criminal penalties, and adverse publicity that could adversely affect our financial condition, results of operations, and reputation. Further, if we are unable to comply with the security standards, established by banks and the banks and payment card industry, we may be subject to fines, restrictions, and expulsion from card acceptance programs, which could adversely affect our retail operations.

There are deflationary pressures on the selling price of apparel products.

Due, among other things, to the actions of discount retailers, the worldwide supply of low cost garment sourcing, and the reaction of many retailers to lower consumer spending, the average selling price of children's apparel continues to decrease. To the extent these deflationary pressures are not offset by reductions in manufacturing costs, there would be an affect on the Company's gross margin. Additionally, the inability to leverage certain fixed costs of the

Company's design, sourcing, distribution, and support costs over its gross sales base could have an adverse impact on the Company's operating results.

Our business is sensitive to overall levels of consumer spending, particularly in the young children's apparel segment.

Consumers' demand for young children's apparel, specifically brand name apparel products, is impacted by the overall level of consumer spending. Consumer spending is impacted, among other things, by employment levels, gasoline and utility costs, business conditions, availability of consumer credit, tax rates, interest rates, levels of consumer indebtedness, and overall levels of consumer confidence. Recent and further reductions in the level of consumer spending could have a material adverse affect on the Company's sales and results of operations.

We face risks associated with the current global credit crisis and related economic downturn.

The continuing volatility in the financial markets and the related economic downturn in markets throughout the world could have a material adverse effect on our business. While we currently generate significant cash flows from our ongoing operations and have access to credit through amounts available under our revolving credit facility, credit markets have recently experienced significant disruptions and certain leading financial institutions have either declared bankruptcy or have shown significant deterioration in their financial stability. Further deterioration in the financial markets could make future financing difficult or more expensive. If any of the financial institutions that are parties to our revolver were to declare bankruptcy or become insolvent, they may be unable to perform under their agreements with us. This could leave us with reduced borrowing capacity. In addition, tighter credit markets may lead to business disruptions for certain of our suppliers, contract manufacturers or trade customers and consequently, could disrupt our business.

We source substantially all of our products through foreign production arrangements. Our dependence on foreign supply sources could result in disruptions to our operations in the event of political instability, unfavorable economic conditions, international events, or new foreign regulations and such disruptions may increase our cost of goods sold and decrease gross profit.

We source substantially all of our products through a network of vendors primarily in Asia, coordinated by our sourcing agents. The following could disrupt our foreign supply chain, increase our cost of goods sold, decrease our gross profit, or impact our ability to get products to our customers:

- financial instability of one of our major vendors;
- political instability or other international events resulting in the disruption of trade in foreign countries from which we source our products;
- increases in transportation costs as a result of increased fuel prices;
- the imposition of new regulations relating to imports, duties, taxes, and other charges on imports;
- the occurrence of a natural disaster, unusual weather conditions, or an epidemic, the spread of which may impact our ability to obtain products on a timely basis;
- changes in the United States customs procedures concerning the importation of apparel products;
- unforeseen delays in customs clearance of any goods;
- disruption in the global transportation network such as a port strike, world trade restrictions, or war;
- the application of foreign intellectual property laws;

- the ability of our vendors to secure sufficient credit to finance the manufacturing process including the acquisition of raw materials; and
- exchange rate fluctuations between the United States dollar and the local currencies of foreign contractors.

These and other events beyond our control could interrupt our supply chain and delay receipt of our products into the United States.

We source all of our products through a network of vendors. We have limited control over these vendors and we may experience delays, product recalls or loss of revenues if our products do not meet our quality standards or regulatory requirements.

Our vendors, independent manufacturers and licensees may not continue to provide products that are consistent with our standards. We have occasionally received, and may in the future continue to receive, shipments of product that fail to conform to our quality control standards. A failure in our quality control program may result in diminished product quality, which may result in increased order cancellations and returns, decreased consumer demand for our products, or product recalls, any of which may have a material adverse affect on our results of operations and financial condition. In addition, notwithstanding our strict quality control procedures, because we do not control our vendors, products that fail to meet our standards, or other unauthorized products, could end up in the marketplace without our knowledge. This could materially harm our brand and our reputation in the marketplace.

Our products are subject to regulation of and regulatory standards set by various governmental authorities with respect to quality and safety. Regulations and standards in this area are currently in place. These regulations and standards may change from time to time. Our inability to comply on a timely basis with regulatory requirements could result in significant fines or penalties, which could adversely affect our reputation and sales. Issues with the quality and safety of merchandise we sell in our stores, regardless of our culpability, or customer concerns about such issues, could result in damage to our reputation, lost sales, uninsured product liability claims or losses, merchandise recalls, and increased costs.

We operate in a highly competitive market and the size and resources of some of our competitors may allow them to compete more effectively than we can, resulting in a loss of market share and, as a result, a decrease in revenue and gross profit.

The baby and young children's apparel market is highly competitive. Both branded and private label manufacturers compete in the baby and young children's apparel market. Our primary competitors in our wholesale and mass channel businesses include Disney, Gerber, and private label product offerings. Our primary competitors in the retail store channel include Old Navy, The Gap, The Children's Place, Gymboree, and Disney. Because of the fragmented nature of the industry, we also compete with many other manufacturers and retailers. Some of our competitors have greater financial resources and larger customer bases than we have and are less financially leveraged than we are. As a result, these competitors may be able to:

- adapt to changes in customer requirements more quickly;
- take advantage of acquisition and other opportunities more readily;
- devote greater resources to the marketing and sale of their products; and
- adopt more aggressive pricing strategies than we can.

The Company's retail success and future growth is dependent upon identifying locations and negotiating appropriate lease terms for retail stores.

The Company's retail stores are located in leased retail locations across the country. Successful operation of a retail store depends, in part, on the overall ability of the retail location to attract a consumer base sufficient to make store sales volume profitable. If the Company is unable to identify new retail locations with consumer traffic sufficient to support a profitable sales level, retail growth may consequently be limited. Further, if existing outlet and strip centers do not maintain a sufficient customer base that provides a reasonable sales volume, there could be a material adverse

impact on the Company's sales, gross margin, and results of operations.

Our leverage could adversely affect our financial condition.

On July 4, 2009, we had total debt of approximately \$336.3 million.

Our indebtedness could have negative consequences. For example, it increases our vulnerability to interest rate risk and could:

- limit our ability to obtain additional financing to fund future working capital, capital expenditures, and other general corporate requirements, or to carry out other aspects of our business plan;
- require us to dedicate a substantial portion of our cash flow from operations to pay principal of, and interest on, our indebtedness, thereby reducing the availability of that cash flow to fund working capital, capital expenditures, or other general corporate purposes, or to carry out other aspects of our business plan;
- limit our flexibility in planning for, or reacting to, changes in our business and the industry; and
- place us at a competitive disadvantage compared to our competitors that have less debt.

In addition, our Senior Credit Facility contains financial and other restrictive covenants that may limit our ability to engage in activities that may be in our long-term best interests such as selling assets, strategic acquisitions, paying dividends, and borrowing additional funds. Our failure to comply with those covenants could result in an event of default which, if not cured or waived, could result in the acceleration of all of our debt which could leave us unable to meet some or all of our obligations.

Profitability could be negatively impacted if we do not adequately forecast the demand for our products and, as a result, create significant levels of excess inventory or insufficient levels of inventory.

If the Company does not adequately forecast demand for its products and purchases inventory to support an inaccurate forecast, the Company could experience increased costs due to the need to dispose of excess inventory or lower profitability due to insufficient levels of inventory.

We may not achieve sales growth plans, cost savings, and other assumptions that support the carrying value of our intangible assets.

As of July 4, 2009, the Company had Carter's cost in excess of fair value of net assets acquired of \$136.6 million, a \$220.2 million Carter's brand tradename asset, and an \$85.5 million OshKosh brand tradename asset on its unaudited condensed consolidated balance sheet. The carrying value of these assets is subject to annual impairment reviews as of the last day of each fiscal year or more frequently, if deemed necessary, due to any significant events or changes in circumstances.

Estimated future cash flows used in these impairment reviews could be negatively impacted if we do not achieve our sales plans, planned cost savings, and other assumptions that support the carrying value of these intangible assets, which could result in potential impairment of the remaining asset value.

The Company's success is dependent upon retaining key individuals within the organization to execute the Company's strategic plan.

The Company's ability to attract and retain qualified executive management, marketing, merchandising, design, sourcing, operations, and support function staffing is key to the Company's success. If the Company were unable to attract and retain qualified individuals in these areas, an adverse impact on the Company's growth and results of operations may result.

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

N/A

ITEM 3. DEFAULTS UPON SENIOR SECURITIES:

N/A

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS:

The Company held its Annual Meeting of Shareholders on May 14, 2009 (the “Annual Meeting”) for which proxies were solicited pursuant to Regulation 14A of the Securities Exchange Act of 1934, as amended. The following matters were voted on by the Company’s stockholders:

Paul Fulton, John R. Welch, and Thomas E. Whiddon were elected as Class III directors to each serve for a three-year term. The following is a schedule of the votes cast:

| Nominee | Total votes for | Total votes withheld |
|----------------------|--------------------|-------------------------|
| Paul Fulton | 32,662,671 | 18,186,204 |
| John R. Welch | 32,715,873 | 18,133,002 |
| Thomas E. Whiddon | 48,149,436 | 2,699,439 |

The directors continuing to serve after the Annual Meeting were: Class I directors – William J. Montgoris and David Pulver, Class II directors - Bradley M. Bloom, Michael D. Casey, and A. Bruce Cleverly, and Class III directors - Paul Fulton, John R. Welch, and Thomas E. Whiddon.

The holders of Carter’s, Inc.’s common stock duly approved the Company’s Amended and Restated 2003 Equity Incentive Plan. A total of 36,619,271 votes were cast in favor, 10,981,887 votes were cast against, 8,944 votes were abstentions, and 3,238,773 votes were broker non-votes.

The appointment of PricewaterhouseCoopers LLP as the Company’s independent registered public accounting firm was ratified.

| Total votes for | Total votes against | Total votes abstained |
|--------------------|---------------------------|-----------------------------|
| 50,760,941 | 63,417 | 24,516 |

ITEM 5. OTHER INFORMATION:

N/A

ITEM 6. EXHIBITS:

(a) Exhibits:

| Exhibit Number | Description of Exhibits |
|----------------|--|
| 31.1 | Rule 13a-15(e)/15d-15(e) and 13a-15(f)/15d-15(f) Certification |
| 31.2 | Rule 13a-15(e)/15d-15(e) and 13a-15(f)/15d-15(f) Certification |
| 32 | Section 1350 Certification |

SIGNATURES

Pursuant to the requirements of the Securities and Exchange Act of 1934, the Registrants have duly caused this report to be signed on their behalf by the undersigned thereunto duly authorized.

CARTER'S, INC.

Date: July 30, 2009 /s/ MICHAEL D. CASEY
Michael D. Casey
Chief Executive Officer
(Principal Executive Officer)

Date: July 30, 2009 /s/ RICHARD F. WESTENBERGER
Richard F. Westenberger
Executive Vice President and Chief Financial Officer
(Principal Financial and Accounting Officer)