GNC HOLDINGS, INC.
Form 10-Q
May 10, 2011
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-Q

(Mark one)

[**X**] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended **March 31, 2011**

[ ] 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: **333-144396**

GNC Holdings, Inc.

(Exact name of registrant as specified in its charter)

Delaware (State or other jurisdiction of Incorporation or organization)	**20-8536244** (I.R.S. Employer Identification No.)
300 Sixth Avenue **Pittsburgh, Pennsylvania** (Address of principal executive offices)	**15222** (Zip Code)

Registrant s telephone number, including area code: **(412) 288-4600**

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). [ ] Yes [ ] No

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

Large accelerated filer [ ] Accelerated filer [ ] Non-accelerated filer[**X**] 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 [**X**] No

As of May 4, 2011, the number of outstanding shares of Class A common stock, par value $0.001 per share (the Class A common stock), and the number of outstanding shares of Class B common stock, par value $0.001 per share (the Class B common stock), of GNC Holdings, Inc. were 90,063,598 shares and 13,782,311 shares, respectively.

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PART I - FINANCIAL INFORMATION

Item 1. Financial Statements

GNC HOLDINGS, INC. AND SUBSIDIARIES

Consolidated Balance Sheets

(in thousands, including share data)

	March 31, 2011 (unaudited)	December 31, 2010
Current assets:		
Cash and cash equivalents	$ 373,857	$ 193,902
Receivables, net	104,270	102,874
Inventories (Note 3)	419,512	381,949
Prepaids and other current assets	40,445	40,569
Total current assets	938,084	719,294
Long-term assets:		
Goodwill (Note 4)	625,672	625,241
Brands (Note 4)	720,000	720,000
Other intangible assets, net (Note 4)	145,542	147,224
Property, plant and equipment, net	192,056	193,428
Deferred financing fees, net	17,177	14,129
Other long-term assets	5,375	5,767
Total long-term assets	1,705,822	1,705,789
Total assets	$ 2,643,906	$ 2,425,083
Current liabilities:		
Accounts payable	$ 156,203	$ 98,662
Accrued payroll and related liabilities	25,568	25,656
Accrued interest (Note 5)	2,983	13,372
Current portion, long-term debt (Note 5)	13,592	28,070
Deferred revenue and other current liabilities	82,555	69,065
Total current liabilities	280,901	234,825
Long-term liabilities:		
Long-term debt (Note 5)	1,188,001	1,030,429
Deferred tax liabilities, net	289,134	288,015
Other long-term liabilities	31,704	33,950
Total long-term liabilities	1,508,839	1,352,394
Total liabilities	1,789,740	1,587,219
Preferred stock, $0.001 par value, 60,000 shares authorized:		
Series A, 30,500 shares designated, 30,134 shares issued, 29,867 shares outstanding and 267 shares held in treasury at March 31, 2011, and December 31, 2010	222,613	218,381
Stockholders equity:		
Common stock, $0.001 par value, 150,000 shares authorized:		
Class A, 59,968 shares issued and 59,199 shares outstanding and 769 shares held in treasury at March 31, 2011 and December 31, 2010	60	60
Class B, 28,169 shares issued and outstanding at March 31, 2011 and December 31, 2010	28	28
Paid-in-capital	452,526	451,728
Retained earnings	176,915	171,224

Treasury stock, at cost	(2,277)	(2,277)
Accumulated other comprehensive income (loss)	4,301	(1,280)
Total stockholders equity	631,553	619,483
Total liabilities and stockholders equity	$ 2,643,906	$ 2,425,083

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

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GNC HOLDINGS, INC. AND SUBSIDIARIES

Consolidated Statements of Operations

(unaudited)

(in thousands, except per share data)

	Three months ended March 31,	
	2011	**2010**
Revenue	$ 506,008	$ 465,019
Cost of sales, including costs of warehousing, distribution and occupancy	322,161	299,120
Gross profit	183,847	165,899
Compensation and related benefits	71,273	67,833
Advertising and promotion	14,207	15,454
Other selling, general and administrative	28,483	25,505
Foreign currency gain	(167)	(76)
Transaction related costs	12,362	-
Operating income	57,689	57,183
Interest expense, net (Note 5)	38,376	16,612
Income before income taxes	19,313	40,571
Income tax expense	9,390	14,910
Net income	$ 9,923	$ 25,661
Income per share - Basic and Diluted:		
Net income	$ 9,923	$ 25,661
Preferred stock dividends	(4,232)	(4,962)
Net income available to common shareholders	$ 5,691	$ 20,699
Earnings per share:		
Basic	$ 0.07	$ 0.24
Diluted	$ 0.06	$ 0.24
Weighted average common shares outstanding:		
Basic	87,367	87,339
Diluted	90,088	87,574

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

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GNC HOLDINGS, INC. AND SUBSIDIARIES

Consolidated Statement of Stockholders Equity and Comprehensive Income (Loss)

(unaudited)

(in thousands, including share data)

	Class A Common Stock		Class B Common Stock					Accumulated Other	Total
	Shares	**Dollars**	**Shares**	**Dollars**	**Treasury Stock**	**Paid-in-Capital**	**Retained Earnings**	**Comprehensive Income/(Loss)**	**Stockholders Equity**
Balance at December 31, 2010	**59,199**	**$ 60**	**28,169**	**$ 28**	**$ (2,277)**	**$ 451,728**	**$ 171,224**	**$ (1,280)**	**$ 619,483**
Comprehensive income (loss):									
Net income	-	-	-	-	-	-	9,923	-	9,923
Unrealized gain on derivatives designated and qualified as cash flow hedges, net of tax of $2,718	-	-	-	-	-	-	-	4,751	4,751
Foreign currency translation adjustments	-	-	-	-	-	-	-	830	830
Comprehensive income									*15,504*
Preferred stock dividends	-	-	-	-	-	-	(4,232)	-	(4,232)
Non-cash stock-based compensation	-	-	-	-	-	798	-	-	798
Balance at March 31, 2011	**59,199**	**$ 60**	**28,169**	**$ 28**	**$ (2,277)**	**$ 452,526**	**$ 176,915**	**$ 4,301**	**$ 631,553**
Balance at December 31, 2009	**59,170**	**$ 60**	**28,169**	**$ 28**	**$ (2,474)**	**$ 448,556**	**$ 95,263**	**$ (7,199)**	**$ 534,234**
Comprehensive income (loss):									
Net income	-	-	-	-	-	-	25,661	-	25,661
Unrealized gain on derivatives designated and qualified as cash flow hedges, net of tax of $159	-	-	-	-	-	-	-	279	279
Foreign currency translation adjustments	-	-	-	-	-	-	-	950	950
Comprehensive income									*26,890*
Issuance of class A common stock	**14**	-	-	-	-	90	-	-	90
Preferred stock dividends	-	-	-	-	-	-	(4,962)	-	(4,962)
Non-cash stock-based compensation	-	-	-	-	-	842	-	-	842
Balance at March 31, 2010	**59,184**	**$ 60**	**28,169**	**$ 28**	**$ (2,474)**	**$ 449,488**	**$ 115,962**	**$ (5,970)**	**$ 557,094**

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

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GNC HOLDINGS, INC. AND SUBSIDIARIES

Consolidated Statements of Cash Flows

(unaudited)

(in thousands)

	Three months ended March 31, 2011	2010
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	$ 9,923	$ 25,661
Adjustments to reconcile net income to net cash provided by operating activities:		
Write-off of deferred financing fees - early debt extinguishment	13,402	-
Amortization of original issue discount - early debt extinguishment	1,556	-
Depreciation expense	9,576	9,564
Amortization of intangible assets	1,909	2,186
Amortization of deferred financing fees	896	1,056
Amortization of original issue discount	108	99
Increase in provision for inventory losses	4,568	1,946
Non-cash stock-based compensation	798	842
Increase (decrease) in provision for losses on accounts receivable	151	(122)
Changes in assets and liabilities:		
Increase in receivables	(2,221)	(2,082)
Increase in inventory	(40,799)	(20,846)
Decrease in other working capital	2,131	10,218
Increase in accounts payable	57,603	47,144
Decrease in interest payable	(10,389)	(8,474)
Increase in accrued liabilities	15,397	4,926
Net cash provided by operating activities	64,609	72,118
CASH FLOWS FROM INVESTING ACTIVITIES:		
Capital expenditures	(7,768)	(7,313)
Franchise store conversions	-	4
Store acquisition costs	(608)	(230)
Net cash used in investing activities	(8,376)	(7,539)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Payment of 2007 Senior Credit Facilty	(644,382)	-
Redemption of Senior Toggle Notes	(300,000)	-
Redemption of Senior Subordinated Notes	(110,000)	-
Issuance of Class A Common Stock	-	90
Borrowings on 2011 Senior Credit Facility	1,196,200	-
Payments on long-term debt	(389)	(599)
Financing fees	(17,346)	-
Net cash provided by (used in) financing activities	124,083	(509)
Effect of exchange rate on cash and cash equivalents	(361)	(39)
Net increase in cash and cash equivalents	179,955	64,031
Beginning balance, cash and cash equivalents	193,902	89,948
Ending balance, cash and cash equivalents	$ 373,857	$ 153,979

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

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GNC HOLDINGS, INC. AND SUBSIDIARIES

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

NOTE 1. NATURE OF BUSINESS

General Nature of Business. GNC Holdings, Inc., formerly GNC Acquisition Holdings Inc., a Delaware corporation (Holdings , and collectively with its subsidiaries and, unless the context requires otherwise, its and their respective predecessors, the Company), is a leading specialty retailer of nutritional supplements, which include: vitamins, minerals and herbal supplements (VMHS), sports nutrition products, diet products and other wellness products.

The Company s organizational structure is vertically integrated as the operations consist of purchasing raw materials, formulating and manufacturing products and selling the finished products through its three primary segments: retail, franchising and manufacturing/wholesale. Corporate retail store operations are located in North America and Puerto Rico, and in addition the Company offers products domestically through GNC.com and www.drugstore.com. Franchise stores are located in the United States and 48 international countries (including distribution centers where retail sales are made). The Company operates its primary manufacturing facilities in South Carolina and distribution centers in Arizona, Pennsylvania and South Carolina. The Company manufactures the majority of its branded products, but also merchandises various third party products. Additionally, the Company licenses the use of its trademarks and trade names.

The processing, formulation, packaging, labeling and advertising of the Company s products are subject to regulation by one or more federal agencies, including the Food and Drug Administration (FDA), Federal Trade Commission (FTC), Consumer Product Safety Commission, United States Department of Agriculture and the Environmental Protection Agency. These activities are also regulated by various agencies of the states and localities in which the Company s products are sold.

NOTE 2. BASIS OF PRESENTATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accompanying unaudited consolidated financial statements have been prepared in accordance with the rules and regulations of the Securities and Exchange Commission (SEC). Accordingly, certain information and footnote disclosures normally included in the annual financial statements prepared in accordance with accounting principles generally accepted in the United States (GAAP) have been omitted. These interim consolidated financial statements should be read in conjunction with the consolidated financial statements and notes included in the prospectus (the Prospectus) contained in the Company s Registration Statement on Form S-1, as amended (Registration No. 333-169618), which was declared effective on March 31, 2011 (the Registration Statement). There have been no material changes to the application of critical accounting policies and significant judgments and estimates since December 31, 2010.

The accompanying unaudited consolidated financial statements include all adjustments (consisting of a normal and recurring nature) that management considers necessary for a fair statement of financial information for the interim periods. Interim results are not necessarily indicative of the results that may be expected for the remainder of the year ending December 31, 2011.

Principles of Consolidation. The consolidated financial statements include the accounts of Holdings, all of its subsidiaries and a variable interest entity. All material intercompany transactions have been eliminated in consolidation.

Use of Estimates. The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions. Accordingly, these estimates and assumptions affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Some of the most significant estimates pertaining to the Company include the valuation of inventories, the allowance for doubtful accounts, income tax valuation allowances and the recoverability of long-lived assets. On a regular basis, management reviews its estimates utilizing currently available information, changes in facts and circumstances, historical experience and reasonable assumptions. After such reviews and if deemed appropriate, those estimates are adjusted accordingly. Actual results could differ from those estimates.

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GNC HOLDINGS, INC. AND SUBSIDIARIES

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

Financial Instruments and Derivatives. As part of the Company s financial risk management program, it has historically used certain derivative financial instruments to reduce its exposure to market risk for changes in interest rates primarily in respect of its long-term debt obligations. The Company has not historically entered into, and does not intend to enter into, derivative transactions for speculative purposes and holds no derivative instruments for trading purposes. Floating-to-fixed interest rate swap agreements, designated as cash flow hedges of interest rate risk, were entered into from time to time to hedge the Company s exposure to interest rate changes on a portion of the Company s floating rate debt. The interest rate swap agreements converted a portion of the Company s floating rate debt to fixed rate debt. Interest rate floors designated as cash flow hedges involve the receipt of variable-rate amounts from a counterparty if interest rates fall below the strike rate on the contract in exchange for an upfront premium. The Company recorded the fair value of these contracts as an asset or a liability, as applicable, in the balance sheet, with the offset to accumulated other comprehensive income (loss), net of tax. The Company measured hedge effectiveness by assessing the changes in the fair value or expected future cash flows of the hedged item. The ineffective portions, if any, were recorded in interest expense in the current period.

Derivatives designated as hedging instruments were recorded in the consolidated balance sheet at fair value as follows:

	Balance Sheet Location	Fair Value March 31, 2011 (unaudited)		December 31, 2010	
		(in thousands)			
Interest Rate Products	Other current liabilities	$	-	$	4,395
Interest Rate Products	Other long-term liabilities	$	-	$	3,074

For the period ended December 31, 2010, the Company had interest rate swap agreements outstanding that effectively converted notional amounts of an aggregate $550.0 million of debt from floating to fixed interest rates. The four outstanding agreements were to mature between April 2011 and September 2012. Amounts related to derivatives were reported in accumulated other comprehensive income (loss) and reclassified to interest expense as interest payments were made on the Company s variable-rate debt. In conjunction with a refinancing transaction (the Refinancing) on March 4, 2011, the Company repaid in full the 2007 Senior Credit Facility (the 2007 Senior Credit Facility), its outstanding Senior Notes and its outstanding Senior Subordinated Notes (as defined below), and the four agreements were settled and terminated for an aggregate cash payment of $8.7 million. During the first quarter of 2011, $8.1 million of accumulated unrealized losses on the swaps was reclassified to interest expense, of which $5.8 million was accelerated due to the debt retirement and swap terminations on March 4, 2011. No such derivative instruments are currently outstanding.

Components of gains and losses recorded in the consolidated balance sheet and consolidated income statements for the three months ended March 31, 2011 and 2010 were as follows:

Derivatives in Cash Flow Hedging Relationships	Amount of Gain or (Loss) Recognized in OCI on Derivative (Effective Portion)		Location of Gain or (Loss) Reclassified from Accumulated OCI into Income (Effective Portion)	Amount of Gain or (Loss) Reclassified from Accumulated OCI into Income (Effective Portion)	
		(unaudited) (in thousands)			
2011					
Interest Rate Products	$	(639)	Interest income (expense)	$	(8,108)
2010					
Interest Rate Products	$	(3,659)	Interest income (expense)	$	(4,097)

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GNC HOLDINGS, INC. AND SUBSIDIARIES

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

Transaction Related Cost. The Company recognizes transaction related costs as expenses in the period incurred. For the three months ending March 31, 2011, the Company recognized $12.4 million of these expenses.

Recently Issued Accounting Pronouncements

As of March 31, 2011, there were no recently issued accounting standard that are expected to have a material impact on the Company s consolidated financial statements.

NOTE 3. INVENTORIES

Inventories at each respective period consisted of the following:

	March 31, 2011 (unaudited)	December 31, 2010
	(in thousands)	
Finished product ready for sale	$ 345,595	$ 319,212
Work-in-process, bulk product and raw materials	66,952	57,165
Packaging supplies	6,965	5,572
	$ 419,512	$ 381,949

NOTE 4. GOODWILL AND INTANGIBLE ASSETS, NET

Goodwill represents the excess of purchase price over the fair value of identifiable net assets of acquired entities. In accordance with the standard on intangibles and goodwill, goodwill and intangible assets with indefinite useful lives are not amortized, but instead are tested for impairment at least annually. Other intangible assets with finite lives are amortized on a straight-line or declining balance basis over periods not exceeding 35 years.

For the three months ended March 31, 2011, the Company acquired ten franchise stores. These acquisitions were accounted for utilizing the acquisition method of accounting and the Company recorded the acquired inventory, fixed assets, franchise rights and goodwill, with an applicable reduction to receivables and cash. The total purchase price associated with these acquisitions was

$1.5 million, of which $0.6 million was paid in cash.

The following table summarizes the Company s goodwill activity:

	Retail	Franchising	Manufacturing/ Wholesale	Total
		(in thousands)		
Balance at December 31, 2010	$ 305,097	$ 117,303	$ 202,841	$ 625,241
Acquired franchise stores	431	-	-	431
Balance at March 31, 2011 (unaudited)	$ 305,528	$ 117,303	$ 202,841	$ 625,672

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GNC HOLDINGS, INC. AND SUBSIDIARIES

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

The following table summarizes the Company s intangible asset activity:

	Retail Brand	Franchise Brand	Operating Agreements (in thousands)	Franchise Rights	Total
Balance at December 31, 2010	$ 500,000	$ 220,000	$ 146,223	$ 1,001	$ 867,224
Acquired franchise stores	-	-	-	227	227
Amortization expense	-	-	(1,713)	(196)	(1,909)