

ENCORE WIRE CORP /DE/

Form 10-Q

November 07, 2006

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**UNITED STATES SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549  
FORM 10-Q**

**QUARTERLY REPORT PURSUANT TO SECTION 13 or 15(d) OF THE SECURITIES  
EXCHANGE ACT OF 1934**

**For the quarterly period ended September 30, 2006**

**OR**

**TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES  
EXCHANGE ACT OF 1934**

**For the transition period from \_\_\_\_\_ to \_\_\_\_\_**

**Commission File Number: 0-20278**

**ENCORE WIRE CORPORATION**

**(Exact name of registrant as specified in its charter)**

**Delaware**

(State of Incorporation)

**75-2274963**

(I.R.S. employer identification number)

**1410 Millwood Road**

**McKinney, Texas**

(Address of principal executive offices)

**75069**

(Zip code)

**Registrant's telephone number, including area code: (972) 562-9473**

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 is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act.

Large accelerated filer

Accelerated filer

Non-accelerated filer

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes  No

Number of shares of Common Stock outstanding as of October 31, 2006: 23,274,352

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**ENCORE WIRE CORPORATION**  
**FORM 10-Q**  
**FOR THE QUARTERLY PERIOD ENDED SEPTEMBER 30, 2006**

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## ITEM 1. CONSOLIDATED FINANCIAL STATEMENTS

ENCORE WIRE CORPORATION  
CONSOLIDATED BALANCE SHEETS

In Thousands of Dollars	ASSETS	September 30, 2006 (Unaudited)	December 31, 2005 (See Note)
Current assets:			
Cash		\$ 34,683	\$ 2,622
Accounts receivable (net of allowance of \$835 and \$690)		292,078	164,930
Inventories (Note 3)		114,323	67,932
Prepaid expenses and other assets		23,937	18,628
Current deferred income taxes		4,278	1,121
Total current assets		469,299	255,233
Property, plant, and equipment, at cost:			
Land		9,468	8,375
Construction in progress		6,509	12,113
Buildings and improvements		47,065	38,063
Machinery and equipment		134,053	120,326
Furniture and fixtures		3,928	3,624
Total property, plant, and equipment		201,023	182,501
Accumulated depreciation and amortization		97,720	89,364
		103,303	93,137
Other assets		102	106
Total assets		\$ 572,704	\$ 348,476

Note: The consolidated balance sheet at December 31, 2005, as presented, is derived from the audited consolidated financial statements at that date.

See accompanying notes.

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ENCORE WIRE CORPORATION  
 CONSOLIDATED BALANCE SHEETS (continued)

In Thousands of Dollars, Except Share and Per Share Data	September 30, 2006 (Unaudited)	December 31, 2005 (See Note)
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Current liabilities:		
Trade accounts payable	\$ 31,541	\$ 17,277
Accrued liabilities	23,667	19,304
Current income taxes payable	1,393	19,540
 Total current liabilities	 56,601	 56,121
Non-current deferred income taxes	9,913	10,620
Long term notes payable	184,067	70,438
Other long term liabilities	933	762
 Stockholders' equity:		
Common stock, \$.01 par value:		
40,000,000 shares authorized, 26,028,802 and 25,939,103 shares issued	261	259
Additional paid-in capital	40,628	38,932
Treasury stock (2,758,950 and 2,758,950 shares, at cost)	(15,275)	(15,275)
Retained earnings	295,576	186,619
 Total stockholders' equity	 321,190	 210,535
 Total liabilities and stockholders' equity	 \$ 572,704	 \$ 348,476

Note: The consolidated balance sheet at December 31, 2005, as presented, is derived from the audited consolidated financial statements at that date.

See accompanying notes.

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ENCORE WIRE CORPORATION  
CONSOLIDATED STATEMENTS OF INCOME  
(Unaudited)

In Thousands, Except Per Share Data	Quarter Ended September 30,		Nine Months Ended September 30,	
	2006	2005	2006	2005
Net sales	\$ 372,915	\$ 207,459	\$ 987,011	\$ 513,917
Cost of goods sold	298,649	176,462	766,520	456,802
 Gross profit	 74,266	 30,997	 220,491	 57,115
Selling, general, and administrative expenses	16,589	12,769	46,760	33,254
 Operating income (loss)	 57,677	 18,228	 173,731	 23,861
Net interest & other expenses	2,530	1,074	5,608	2,676
 Income (loss) before income taxes	 55,147	 17,154	 168,123	 21,185
Provision (benefit) for income taxes	19,386	5,949	59,166	6,517
 Net income (loss)	 \$ 35,761	 \$ 11,205	 \$ 108,957	 \$ 14,668
 Net earnings (loss) per common and common equivalent share basic	 \$ 1.54	 \$ .48	 \$ 4.69	 \$ .63
 Weighted average common and common equivalent shares basic	 23,267	 23,111	 23,248	 23,108
 Net earnings (loss) per common and common equivalent share diluted	 \$ 1.51	 \$ .48	 \$ 4.60	 \$ .63
 Weighted average common and common equivalent shares diluted	 23,680	 23,495	 23,666	 23,447
 Cash dividends declared per share	 \$	 \$	 \$	 \$

See accompanying notes.

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ENCORE WIRE CORPORATION  
CONSOLIDATED STATEMENTS OF CASH FLOWS  
(Unaudited)

In Thousands of Dollars	Nine Months Ended September 30,	
	2006	2005
<b>OPERATING ACTIVITIES</b>		
Net income (loss)	\$ 108,957	\$ 14,668
Adjustments to reconcile net income to cash provided by (used in) operating activities:		
Depreciation and amortization	9,052	9,365
Deferred income taxes	(3,864)	784
Excess tax benefits of options exercised	(768)	
Stock based compensation	307	
Provision for bad debts	135	285
(Gain) loss on sale of equipment	34	152
Changes in operating assets and liabilities:		
Accounts receivable	(127,283)	(50,735)
Inventory	(46,391)	(11,083)
Trade accounts payable and accrued liabilities	18,627	10,398
Other assets and liabilities	(5,279)	(4,375)
Current income taxes receivable/payable	(17,379)	5,277
<b>NET CASH PROVIDED BY (USED IN) OPERATING ACTIVITIES</b>	<b>(63,852)</b>	<b>(25,264)</b>
<b>INVESTING ACTIVITIES</b>		
Purchases of property, plant and equipment	(19,351)	(10,105)
Change in long-term investments		15
Proceeds from sale of equipment	225	202
<b>NET CASH PROVIDED BY (USED IN) INVESTING ACTIVITIES</b>	<b>(19,126)</b>	<b>(9,888)</b>
<b>FINANCING ACTIVITIES</b>		
Borrowings (repayments) under notes payable	113,800	34,463
Proceeds from issuance of common stock	623	71
Excess tax benefits of options exercised	768	
Long-term financing fees	(152)	
Purchase of treasury stock		
<b>NET CASH PROVIDED BY (USED IN) FINANCING ACTIVITIES</b>	<b>115,039</b>	<b>34,534</b>

Net increase (decrease) in cash	32,061	(618)
Cash at beginning of period	2,622	2,640
Cash at end of period	\$ 34,683	\$ 2,022

See accompanying notes.

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ENCORE WIRE CORPORATION  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
(Unaudited)

**NOTE 1 BASIS OF PRESENTATION**

The unaudited consolidated financial statements of Encore Wire Corporation (the Company) have been prepared in accordance with U.S. generally accepted accounting principles for interim information and the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by U.S. generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments, consisting only of normal recurring adjustments considered necessary for a fair presentation, have been included. Results of operations for interim periods presented do not necessarily indicate the results that may be expected for the entire year. These financial statements should be read in conjunction with the audited consolidated financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 2005.

Certain reclassifications have been made to prior periods' financial statements to conform to the current presentation.

**NOTE 2 STOCK BASED COMPENSATION**

The Company has one stock option plan that provides for the grant of stock options to its employees. The Company grants stock option awards at prices equal to the market value of its stock on the date of grant. These options vest ratably over a period of five years from the time the options are granted with maximum terms of ten years.

Prior to December 31, 2005, the Company applied the disclosure-only provisions of Statement of Financial Accounting Standards No. 123, *Accounting for Stock-Based Compensation* (SFAS 123). In accordance with the provisions of SFAS 123, the Company applied Accounting Principles Board Opinion No. 25, *Accounting for Stock Issued to Employees* (APB 25), and related interpretations in accounting for its plan and, accordingly, did not recognize compensation expense for the plan because stock options were issued at exercise prices equal to the market value of its stock on the date of grant.

Effective January 1, 2006, the Company adopted Statement of Financial Accounting Standards No. 123 (revised 2004), *Share-Based Payment* (SFAS 123R), which supersedes SFAS 123 and APB 25. SFAS 123R requires all share-based payments to employees to be recognized in the financial statements based on their fair values using an option-pricing model, such as the Black-Scholes model, at the date of grant. The Company elected to use the Black-Scholes model and the modified prospective method for adoption, which requires compensation expense to be recorded for all unvested stock options beginning in the first quarter of adoption. For all unvested options outstanding as of January 1, 2006, compensation expense previously measured under SFAS No. 123, but unrecognized, will be recognized using the straight-line method over the remaining vesting period, net of forfeitures. For share-based payments granted subsequent to January 1, 2006, compensation expense, based on the fair value on the date of grant, as defined by SFAS 123R, will be recognized using the straight-line method from the date of grant over the related service period of the employee receiving the award. The Company granted 50,000 stock options during the third quarter of 2006.

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The fair value of an option award is estimated on the date of grant using a Black-Scholes options pricing model that uses assumptions detailed in the table below. We base expected volatilities on historical volatilities of our common stock. The expected life represents the weighted average period of time that options granted are expected to be outstanding giving consideration to vesting periods and management's consideration of historical exercise patterns. The risk free rate is based on the U.S. Treasury yield curve in effect at the time of grant for periods corresponding to the expected life of the option.

SFAS 123R requires the estimation of forfeitures when recognizing compensation expense and adjustment of the estimated forfeiture rate over the requisite service period should actual forfeitures differ from such estimates. Changes in estimated forfeitures are recognized through a cumulative catch-up adjustment, which is recognized in the period of change and impacts the amount of un-recognized compensation expense to be recorded in future periods.

SFAS No. 123R reduced income from continuing operations before income taxes for the three-month and nine-month periods ended September 30, 2006 by \$112,233 and \$307,216, respectively, and did not appreciably impact net income per common share. As of September 30, 2006, total unrecognized compensation cost related to stock option awards granted was \$1,118,383 and the related weighted-average period over which that cost is expected to be recognized is 4.56 years.

The following presents a summary of stock options activity and changes for the nine months ended September 30, 2006 (aggregate intrinsic value in thousands):

	<b>Number Of Shares</b>	<b>Weighted Average Exercise Price</b>	<b>Weighted Average Remaining Contractual Term</b>	<b>Aggregate Intrinsic Value</b>
Balance outstanding at December 31, 2005	639,825	\$ 6.73		
Granted	50,000	\$ 37.95		
Exercised	(88,399)	\$ 7.69		
Forfeited/Cancelled	(1,500)	\$ 7.70		
Balance outstanding at September 30, 2006	599,926	\$ 6.25	4.56	\$ 17,422
Options exercisable at September 30, 2006	478,046	\$ 5.82	3.83	\$ 14,107

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We determined the fair value of options issued during the nine months ended September 30, 2006, using the Black-Scholes option pricing model with the following weighted average assumptions:

	Nine Months Ended September 30,	
	2006	2005
Expected stock price volatility	55.7%	N/A
Expected life of options	5.0	N/A
Risk-free interest rate	3.8%	N/A
Dividend yield	0.0%	N/A

The per-share weighted average grant-date fair value of stock options granted was \$19.63 for the nine months ended September 30, 2006.

**NOTE 3 INVENTORIES**

Inventories are stated at the lower of cost, determined by the last-in, first-out (LIFO) method, or market.

Inventories consisted of the following (in thousands):

	September 30, 2006	December 31, 2005
Raw materials	\$ 25,093	\$ 11,288
Work-in-process	22,102	8,428
Finished goods	162,672	84,665
	209,867	104,381
Adjust to LIFO cost	(95,544)	(36,449)
	114,323	67,932
Lower of Cost or Market Adjustment		
	\$ 114,323	\$ 67,932

An actual valuation of inventory under the LIFO method can be made only at the end of each year based on the inventory levels and costs at that time. Accordingly, interim LIFO calculations are based on management's estimates of expected year-end inventory levels and costs. Because these are subject to many forces beyond management's control, interim results are subject to the final year-end LIFO inventory valuation.

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Net earnings (loss) per common and common equivalent share are computed using the weighted average number of shares of common stock and common stock equivalents

outstanding during each period. If dilutive, the effect of stock options, treated as common stock equivalents, is calculated using the treasury stock method.

The following tables set forth the computations of basic and diluted net earnings per share:

	Quarter Ended 9/30/06	Quarter Ended 9/30/05
Numerator:		
Net income	\$ 35,761,035	\$ 11,204,923
Denominator:		
Denominator for basic earnings per share    weighted average shares	23,267,114	23,110,539
Effect of dilutive securities:		
Employee stock options	413,107	384,793
Denominator for diluted earnings per share    weighted average shares	23,680,221	23,495,332
	Nine Months Ended 9/30/06	Nine Months Ended 9/30/05
Numerator:		
Net income	\$ 108,957,054	\$ 14,668,152
Denominator:		
Denominator for basic earnings per share    weighted average shares	23,247,618	23,107,940
Effect of dilutive securities:		
Employee stock options	418,748	338,703
Denominator for diluted earnings per share    weighted average shares	23,666,366	23,446,643

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Effective August 27, 2004, the Company, through its indirectly wholly-owned subsidiary, Encore Wire Limited, a Texas Limited partnership ( Encore Wire Limited ), refinanced its unsecured loan facility (the Financing Agreement ) and also arranged for a private placement of debt (the 2004 Note Purchase Agreement ). The Financing Agreement is with two banks, Bank of America, N.A., as Agent, and Wells Fargo Bank, National Association, and replaces the previous financing agreement. The Company is the guarantor of the indebtedness. The Financing Agreement was first amended May 16, 2006, to expand the Company's line of credit from \$85,000,000 to \$150,000,000, as disclosed in previous filings. The Financing Agreement was amended a second time on August 31, 2006, to expand the Company's line of credit from \$150,000,000 to \$200,000,000, as disclosed in the Company's press release dated September 1, 2006. The Financing Agreement, as amended, extends through August 27, 2009, and provides for maximum borrowings of the lesser of \$200,000,000 or the amount of eligible accounts receivable plus the amount of eligible finished goods and raw materials, less any reserves established by the banks. The calculated maximum borrowing amount available at September 30, 2006, as computed under the Financing Agreement, was \$200,000,000.

Concurrent with the entry into the Financing Agreement in 2004, Encore Wire Limited and the Company, through its agent bank, entered into the 2004 Note Purchase Agreement with Hartford Life Insurance Company, Great-West Life & Annuity Insurance Company, London Life Insurance Company and London Life and Casualty Reinsurance Corporation (collectively, the 2004 Purchasers ), whereby Encore Wire Limited issued and sold \$45,000,000 of 5.27% Senior Notes, Series 2004-A, due August 27, 2011 (the Fixed Rate Senior Notes ) to the 2004 Purchasers, the proceeds of which were used to repay a portion of the Company's outstanding indebtedness under its previous financing agreement. Through its agent bank, the Company then entered into an interest rate swap agreement to convert the fixed rate on the Fixed Rate Senior Notes to a variable rate based on LIBOR plus a fixed adder for the seven-year duration of these notes. As of September 30, 2006, the Company recorded a liability and a corresponding unrealized reduction to notes payable on the balance sheet of \$933,083 to account for the fair value of the interest rate swap.

On September 28, 2006, Encore Wire Limited and the Company, through its agent bank, entered into another Note Purchase Agreement (the 2006 Note Purchase Agreement ) with Metropolitan Life Insurance Company, Metlife Insurance Company of Connecticut and Great-West Life & Annuity Insurance Company, (collectively, the 2006 Purchasers ), whereby Encore Wire Limited issued and sold \$55,000,000 of Floating Rate Senior Notes, Series 2006-A, due September 30, 2011 (the Floating Rate Senior Notes ), the proceeds of which were used to repay a portion of the Company's outstanding indebtedness under its Financing Agreement.

Obligations under the Financing Agreement, the Fixed Rate Senior Notes and the Floating Rate Senior Notes are unsecured and contain customary covenants and events of default. The Company was in compliance with these covenants, as of September 30, 2006. Under the Financing Agreement, the Company is allowed to pay cash dividends. At September 30, 2006, the total balance outstanding under the Financing Agreement, the Fixed Rate Senior Notes and the Floating Rate Senior Notes was \$185,000,000. Amounts outstanding under the Financing Agreement are payable on August 27, 2009,

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with interest payments due quarterly. Interest payments on the Fixed Rate Senior Notes are due semi-annually, while interest payments on the Floating Rate Senior Notes are due quarterly.

Obligations under the Financing Agreement, the 2004 Note Purchase Agreement and the 2006 Note Purchase Agreement are the only contractual obligations or commercial borrowing commitment of the Company.

**NOTE 6 STOCK REPURCHASE AUTHORIZATION**

On November 6, 2001, the Board of Directors of the Company approved a stock repurchase program covering the purchase of up to 450,000 additional shares of its common stock dependent upon market conditions. Common stock purchases under this program were authorized through December 31, 2002, on the open market or through privately negotiated transactions at prices determined by the Chairman of the Board or the President of the Company. As of December 31, 2002, 225,300 shares had been purchased under this authorization. The Board of Directors has extended this program four times, through December 31, 2006, for the remaining 224,700 shares; however, there have been no further repurchases of stock since 2002.

**NOTE 7 CONTINGENCIES**

The Company is a party to litigation and claims that arise out of the Company's ordinary course of business. While the results of these matters cannot be predicted with certainty, the Company does not believe the final outcome of such litigation and claims will have a material adverse effect on the financial condition, the results of operation or the cash flows of the Company. The Company also believes that it has adequate insurance to cover any damages that may ultimately be awarded.

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

**General**

The Company is a low-cost manufacturer of copper electrical building wire and cable. The Company is a significant supplier of residential wire for interior wiring in homes, apartments and manufactured housing and commercial wire for commercial and industrial buildings.

The Company's operating results in any given time period are driven by several key factors, including; the volume of product produced and shipped, the cost of copper and other raw materials, the competitive pricing environment in the wire industry and the resulting influence on gross margins and the efficiency with which the Company's plant operates during the period, among others. Price competition for electrical wire and cable is intense, and the Company sells its products in accordance with prevailing market prices. Copper is the principal raw material used by the Company in manufacturing its products. Copper accounted for approximately 76.8%, 73.0% and 67.1% of the Company's cost of goods sold during fiscal 2005, 2004 and 2003, respectively. The price of copper fluctuates, based on general economic conditions, supply, demand and other factors, which has caused monthly variations in the cost of copper purchased by

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the Company. The Company cannot predict future copper prices or the effect of fluctuations in the cost of copper on the Company's future operating results.

The following discussion and analysis relates to factors that have affected the operating results of the Company for the quarterly and nine-month periods ended September 30, 2006 and 2005. Reference should also be made to the audited financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 2005.

**Results of Operations**

**Quarter Ended September 30, 2006 Compared to Quarter Ended September 30, 2005**

Net sales for the third quarter of 2006 amounted to \$372.9 million compared with net sales of \$207.5 million for the third quarter of 2005. This dollar increase was primarily the result of a 103% increase in the average price of wire sold, offsetting an 11% decrease in unit volume measured as the pounds of copper contained in the wire sold in the quarter. The average cost per pound of raw copper purchased increased 106% in the third quarter of 2006 compared to the third quarter of 2005, and was the principal reason the average sales price for wire increased. These factors resulted in increased gross margins in the third quarter of 2006 versus the third quarter of 2005. Fluctuations in sales prices are primarily a result of changing copper raw material prices and product price competition.

Cost of goods sold increased to \$298.6 million, or 80.1% of net sales, in the third quarter of 2006, compared to \$176.5 million, or 85.1% of net sales, in the third quarter of 2005. Gross profit increased to \$74.3 million, or 19.9% of net sales, in the third quarter of 2006 versus \$31.0 million, or 14.9% of net sales, in the third quarter of 2005. The increased gross profit and gross margin percentages were primarily the result of industry wide pricing trends that increased the spread between the selling price of copper wire and the purchase cost of raw copper.

Inventories are stated at the lower of cost, using the last-in, first-out (LIFO) method, or market. The Company maintains only one inventory pool for LIFO purposes as all inventories held by the Company generally relate to the Company's only business segment, the manufacture and sale of copper building wire products. As permitted by U.S. generally accepted accounting principles, the Company maintains its inventory costs and cost of goods sold on a first-in, first-out (FIFO) basis and makes a quarterly adjustment to adjust total inventory and cost of goods sold from FIFO to LIFO. The Company applies the lower of cost or market (LCM) test by comparing the LIFO cost of its raw materials, work-in-process and finished goods inventories to estimated market values, which are based primarily upon the most recent quoted market price of copper, in pound quantities, as of the end of each reporting period.

Additionally, future reductions in the quantity of inventory on hand could cause copper that is carried in inventory at costs different from the cost of copper in the period in which the reduction occurs to be included in costs of goods sold for that period.

As a result of increasing copper costs, partially offset by a decrease in the amount of inventory on hand during the third quarter of 2006, a LIFO adjustment was recorded, increasing cost of sales by \$6.8 million during the quarter.

Based on copper prices at the end of the quarter, no LCM adjustment was necessary. Future reductions in the

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price of copper could require the Company to record a LCM adjustment against the related inventory balance, which would result in a negative impact on net income.

Selling expenses for the third quarter of 2006 were \$14.7 million, or 3.9% of net sales, compared to \$10.7 million, or 5.1% of net sales, for the third quarter of 2005. The percentage decrease was due to the decrease in freight costs as a percentage of net sales, driven by the large increase in sales dollars discussed above. Freight costs increased on a per pound basis, however, primarily due to higher fuel costs in the trucking industry. General and administrative expenses for the third quarter of 2006 decreased to \$1.8 million, or 0.5% of net sales, compared to \$1.9 million, or 0.9% of net sales, in the third quarter of 2005. The general and administrative costs are semi-fixed by nature and therefore do not fluctuate proportionately with sales. The provision for bad debts was \$45,000 and \$195,000 in the third quarter of 2006 and 2005, respectively.

The net interest and other income and expense category was \$2.5 million in the third quarter of 2006 compared to \$1.1 million in the third quarter of 2005. The increase was due primarily to higher average debt balances and higher interest rates during the third quarter of 2006 than during the comparable period in 2005. Taxes were accrued at an effective rate of 35.2% in the third quarter of 2006 consistent with the Company's estimated liabilities.

As a result of the foregoing factors, the Company's net income increased to \$35.8 million in the third quarter of 2006 from \$11.2 million in the third quarter of 2005.

**Nine Months Ended September 30, 2006 compared to Nine Months Ended September 30, 2005**

Net sales for the first nine months of 2006 amounted to \$987.0 million compared with net sales of \$513.9 million for the first nine months of 2005. This dollar increase was primarily the result of a 96% increase in the average price of wire sold. The average cost per pound of raw copper purchased increased 89% in the first nine months of 2006 compared to the first nine months of 2005, and was the principal reason the average sales price for wire increased. Fluctuations in sales prices are primarily a result of changing copper raw material prices and product price competition.

Cost of goods sold increased to \$766.5 million in the first nine months of 2006, compared to \$456.8 million in the first nine months of 2005. Gross profit increased to \$220.5 million, or 22.3% of net sales, in the first nine months of 2006 versus \$57.1 million, or 11.1% of net sales, in the first nine months of 2005. The increased gross profit and gross margin percentages were primarily the result of the margin expansion in 2006 versus 2005 discussed in the quarterly analysis above.

As a result of increasing copper costs and an increased amount of inventory on hand during the first nine months of 2006, a LIFO adjustment was recorded increasing cost of sales by \$59.1 million during the period. Based on the current copper prices, there is no LCM adjustment necessary. Future reductions in the price of copper could require the Company to record a LCM adjustment against the related inventory balance, which would result in a negative impact on net income.



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Selling expenses for the first nine months of 2006 were \$40.2 million, or 4.1% of net sales, compared to \$27.4 million, or 5.3% of net sales, in the same period of 2005. The percentage decrease was due to the decrease in freight costs as a percentage of net sales, driven by the large increase in sales dollars discussed above. Freight costs increased on a per pound basis, however, primarily due to higher fuel costs in the trucking industry. General and administrative expenses increased to \$6.4 million, or 0.7% of net sales, in the first nine months of 2006 compared to \$5.6 million, or 1.1% of net sales, in the same period of 2005. The general and administrative costs are semi-fixed by nature and therefore do not fluctuate proportionately with sales, resulting in the decreased percentage to sales dollars. The provision for bad debts was \$135,000 and \$285,000 in the first nine months of 2006 and 2005, respectively. Net interest expense was \$5.6 million in the first nine months of 2006 compared to \$2.7 million in the first nine months of 2005. The increase was due primarily to higher average debt balances and higher interest rates during the first nine months of 2006 than during the comparable period of 2005.

As a result of the foregoing factors, the Company's net income increased to \$109.0 million in the first nine months of 2006 from \$14.7 million in the first nine months of 2005.

**Liquidity and Capital Resources**

The Company maintains a substantial inventory of finished products to satisfy the prompt delivery requirements of its customers. As is customary in the industry, the Company provides payment terms to most of its customers that exceed terms that it receives from its suppliers. Therefore, the Company's liquidity needs have generally consisted of operating capital necessary to finance these receivables and inventory. Capital expenditures have historically been necessary to expand the production capacity of the Company's manufacturing operations. The Company has historically satisfied its liquidity and capital expenditure needs with cash generated from operations, borrowings under its various debt arrangements and sales of its common stock. The Company uses its revolving credit facility to manage day to day operating cash needs as required by daily fluctuations in working capital. The total debt balance fluctuates daily as cash inflows differ from cash outflows.

Effective August 27, 2004, the Company, through its indirectly wholly-owned subsidiary, Encore Wire Limited, a Texas Limited partnership ( Encore Wire Limited ), refinanced its unsecured loan facility (the Financing Agreement ) and also arranged for a private placement of debt (the 2004 Note Purchase Agreement ). The Financing Agreement is with two banks, Bank of America, N.A., as Agent, and Wells Fargo Bank, National Association, and replaces the previous financing agreement. The Company is the guarantor of the indebtedness. The Financing Agreement was first amended May 16, 2006, to expand the Company's line of credit from \$85,000,000 to \$150,000,000, as disclosed in previous filings. The Financing Agreement was amended a second time on August 31, 2006, to expand the Company's line of credit from \$150,000,000 to \$200,000,000, as disclosed in the Company's press release dated September 1, 2006. The Financing Agreement, as amended, extends through August 27, 2009, and provides for maximum borrowings of the lesser of \$200,000,000 or the amount of eligible accounts receivable plus the amount of eligible finished goods and raw materials, less any reserves established by the banks. The calculated maximum borrowing amount

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available at September 30, 2006, as computed under the Financing Agreement, was \$200,000,000.

Concurrent with the entry into the Financing Agreement in 2004, Encore Wire Limited and the Company, through its agent bank, entered into the 2004 Note Purchase Agreement with Hartford Life Insurance Company, Great-West Life & Annuity Insurance Company, London Life Insurance Company and London Life and Casualty Reinsurance Corporation (collectively, the 2004 Purchasers ), whereby Encore Wire Limited issued and sold \$45,000,000 of 5.27% Senior Notes, Series 2004-A, due August 27, 2011 (the Fixed Rate Senior Notes ) to the 2004 Purchasers, the proceeds of which were used to repay a portion of the Company's outstanding indebtedness under its previous financing agreement. Through its agent bank, the Company then entered into an interest rate swap agreement to convert the fixed rate on the Fixed Rate Senior Notes to a variable rate based on LIBOR plus a fixed adder for the seven-year duration of these notes. As of September 30, 2006, the Company recorded a liability and a corresponding unrealized reduction to notes payable on the balance sheet of \$933,083 to account for the fair value of the interest rate swap.

On September 28, 2006, Encore Wire Limited and the Company, through its agent bank, entered into another Note Purchase Agreement (the 2006 Note Purchase Agreement ) with Metropolitan Life Insurance Company, Metlife Insurance Company of Connecticut and Great-West Life & Annuity Insurance Company, (collectively, the 2006 Purchasers ), whereby Encore Wire Limited issued and sold \$55,000,000 of Floating Rate Senior Notes, Series 2006-A, due September 30, 2011 (the Floating Rate Senior Notes ), the proceeds of which were used to repay a portion of the Company's outstanding indebtedness under its Financing Agreement.

Obligations under the Financing Agreement, the Fixed Rate Senior Notes and the Floating Rate Senior Notes are unsecured and contain customary covenants and events of default. The Company was in compliance with these covenants, as of September 30, 2006. Under the Financing Agreement, the Company is allowed to pay cash dividends. At September 30, 2006, the total balance outstanding under the Financing Agreement, the Fixed Rate Senior Notes and the Floating Rate Senior Notes was \$185,000,000. Amounts outstanding under the Financing Agreement are payable on August 27, 2009, with interest payments due quarterly. Interest payments on the Fixed Rate Senior Notes are due semi-annually, while interest payments on the Floating Rate Senior Notes are due quarterly.

Obligations under the Financing Agreement, the 2004 Note Purchase Agreement and the 2006 Note Purchase Agreement are the only contractual obligations or commercial borrowing commitment of the Company.

Cash used in operations was \$63.9 million in the first nine months of 2006 compared to \$25.3 million of cash used by operations in the first nine months of 2005. The increase in cash used by operations resulted primarily from the increase in accounts receivable of \$127.3 million in the first nine months of 2006 versus an increase of \$50.7 million in 2005 along with an increase in inventory of \$46.4 million in 2006 versus an increase of \$11.1 million in 2005, offset by the \$94.3 million increase in net income in the first nine months of 2006 versus the first nine months of 2005. The large increases in accounts receivable and inventory were primarily the result of the significant increases in copper prices from year to year as discussed in Results of Operations above. Copper prices

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increased the dollar value of inventory on hand and drove the sales prices for copper building wire higher, resulting in the increased accounts receivable balance. Net income increased due to the reasons highlighted in Results of Operations , above.

Cash used in investing activities increased to \$19.1 million in the first nine months of 2006 from \$9.9 million in the first nine months of 2005. In 2006, the funds were used primarily to construct the new 160,000 square foot armored cable plant and to purchase manufacturing equipment for the new plant. The \$115.0 million and the \$34.5 million of cash provided by financing activities in the first nine months of 2006 and 2005, respectively, were a result of the Company s increase in outstanding bank debt, which was used primarily to fund the Company s increased working capital requirements as discussed above.

During the remainder of 2006, the Company expects its capital expenditures will consist of additional plant and equipment for its residential and commercial wire operations, primarily related to the new armored cable plant, which was discussed in a press release, dated March 21, 2005. The armored cable plant has been constructed and a majority of the machinery planned in the initial phase of this project has been installed. The Company began shipping armored cable in July 2006. The total capital expenditures associated with these projects in 2006 are currently estimated to be in the \$20.0 to \$25.0 million range. The Company will continue to manage its working capital requirements. These requirements may increase as a result of expected continued sales increases and may be impacted by the price of copper. The Company believes that the cash flow from operations and the financing available under the amended Financing Agreement will satisfy working capital and capital expenditure requirements for the next twelve months.

**Information Regarding Forward Looking Statements**

This report on Form 10-Q contains various forward-looking statements (within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended) and information that are based on management s belief as well as assumptions made by and information currently available to management. The words believes, anticipates, plans, seeks, expects, intends and similar expressions identify the forward-looking statements. Although the Company believes that the expectations reflected in such forward-looking statements are reasonable, it can give no assurance that such expectations will prove to have been correct. Such statements 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 expected. Among the key factors that may have a direct bearing on the Company s operating results are fluctuations in the economy and in the level of activity in the building and construction industry, demand for the Company s products, the impact of price competition and fluctuations in the price of copper. For more information regarding forward looking statements see Information Regarding Forward Looking Statements in Part II, Item 7 of the Company s Annual Report on Form 10-K for the year ended December 31, 2005, which is hereby incorporated by reference.

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

There have been no material changes from the information provided in Item 7.A of the Company's Annual Report on Form 10-K for the year ended December 31, 2005.

**ITEM 4. CONTROLS AND PROCEDURES**

The Company maintains controls and procedures designed to ensure that it is able to collect the information it is required to disclose in the reports it files with the SEC, and to process, summarize and disclose this information within the time periods specified in the rules of the SEC. Based on an evaluation of the Company's disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended) as of the end of the period covered by this report conducted by the Company's management, with the participation of the Chief Executive and Chief Financial Officers, the Chief Executive and Chief Financial Officers believe that these controls and procedures are effective to ensure that the Company is able to collect, process and disclose the information it is required to disclose in the reports it files with the SEC within the required time periods. There have been no changes in the Company's internal controls over financial reporting or in other factors that have materially affected, or are reasonably likely to materially affect, internal controls over financial reporting during the period covered by this report.

**PART II. OTHER INFORMATION**

**ITEM 1A. RISK FACTORS**

There have been no material changes to the Company's risk factors as disclosed in Item 1A, Risk Factors, in the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2005.

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

**Stock Repurchase Program**

On November 6, 2001, the Board of Directors of the Company approved a stock repurchase program covering the purchase of up to 450,000 additional shares of its common stock dependent upon market conditions. Common stock purchases under this program were authorized through December 31, 2002 on the open market or through privately negotiated transactions at prices determined by the Chairman of the Board or the President of the Company. As of December 31, 2002, 225,300 shares had been purchased under this authorization. The Board of Directors has extended this program four times, through December 31, 2006, for the remaining 224,700 shares; however, there have been no further repurchases of stock since 2002.

**ITEM 6. EXHIBITS**

The information required by this Item 6 is set forth in the Index to Exhibits accompanying this Form 10-Q.

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SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on behalf by the undersigned thereunto duly authorized.

ENCORE WIRE CORPORATION

(Registrant)

Dated: November 7, 2006

/s/ DANIEL L. JONES

Daniel L. Jones, President and  
Chief Executive Officer

Dated: November 7, 2006

/s/ FRANK J. BILBAN

Frank J. Bilban, Vice President Finance,  
Treasurer and Secretary  
Chief Financial Officer

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INDEX TO EXHIBITS

Exhibit Number	Description
3.1	Certificate of Incorporation of Encore Wire Corporation, as amended through July 20, 2004 (filed on Exhibit 3.1 to the Company's Quarterly Report on Form 10-Q for the quarter ended June 30, 2004, and incorporated herein by reference).
3.2	Amended and Restated Bylaws of Encore Wire Corporation, as amended through February 20, 2006 (filed as Exhibit 3.2 to the Company's Annual Report on Form 10-K for the year ended December 31, 2005, and incorporated herein by reference).
10.1	Credit Agreement by and among Encore Wire Limited, as Borrower, Bank of America, N.A., as Agent, and Bank of America, N.A. and Wells Fargo Bank, National Association, as Lenders, dated August 27, 2004 (filed as Exhibit 10.1 to the Company's Quarterly Report on Form 10-Q for the quarter ended September 30, 2004 and incorporated herein by reference).
10.2	First Amendment to Credit Agreement of August 27, 2004, dated May 16, 2006, by and among Encore Wire Limited, as Borrower, Bank of America, N.A., as Agent, and Bank of America, N.A. and Wells Fargo Bank, National Association, as Lenders (filed as Exhibit 10.3 to the Company's Quarterly Report on Form 10-Q for the quarter ended June 30, 2006 and incorporated herein by reference).
10.3	Second Amendment to Credit Agreement of August 27, 2004, dated August 31, 2006, by and among Encore Wire Limited, as Borrower, Bank of America, N.A., as Agent, and Bank of America, N.A. and Wells Fargo Bank, National Association, as Lenders.
10.4	Note Purchase Agreement by and among Encore Wire Limited and Encore Wire Corporation, as Debtors, and Hartford Life Insurance Company, Great-West Life & Annuity Insurance Company, London Life Insurance Company and London Life and Casualty Reinsurance Corporation, as Purchasers, dated August 27, 2004 (filed as Exhibit 10.2 to the Company's Quarterly Report on Form 10-Q for the quarter ended September 30, 2004 and incorporated herein by reference).
10.5	Master Note Purchase Agreement by and among Encore Wire Limited and Encore Wire Corporation, as Debtors, and Metropolitan Life Insurance Company, Metlife Insurance Company of Connecticut and Great-West Life & Annuity Insurance Company, as Purchasers, dated September 28, 2006.
10.6*	1999 Stock Option Plan, as amended and restated, effective as of February 20, 2006 (filed as Exhibit 10.2 to the Company's Quarterly Report on Form 10-Q for the quarter ended March 31, 2006, and incorporated herein by reference).

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Exhibit Number	Description
10.7*	1989 Stock Option Plan, as amended and restated (filed as Exhibit 4.1 to the Company's Registration Statement on Form S-8 (No. 333-38729), and incorporated herein by reference), terminated except with respect to outstanding options there under.
31.1	Certification by Daniel L. Jones, President and Chief Executive Officer of Encore Wire Corporation, dated November 7, 2006 and submitted pursuant to Rule 13a-14(a)/15d-14(a) and pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification by Frank J. Bilban, Vice President-Finance, Chief Financial Officer, Treasurer and Secretary of Encore Wire Corporation, dated November 7, 2006 and submitted pursuant to Rule 13a-14(a)/15d-14(a) and pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification by Daniel L. Jones, President and Chief Executive Officer of Encore Wire Corporation, dated November 7, 2006 and submitted as required by 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	Certification by Frank J. Bilban, Vice President-Finance, Chief Financial Officer, Treasurer and Secretary of Encore Wire Corporation, dated November 7, 2006 as required by 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

\* Management contract or compensatory plan.