CARTERS INC
Form 10-Q
October 30, 2008

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

(X) QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE QUARTERLY PERIOD ENDED SEPTEMBER 27, 2008 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 jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

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 (X) 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 (X) 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 October 30, 2008
Common stock, par value $0.01 per share	56,315,141

CARTER'S, INC.
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PART I – FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

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

		September 27, 2008		December 29, 2007
ASSETS				
Current assets:				
Cash and cash equivalents	$	59,660	$	49,012
Accounts receivable, net		160,094		119,707
Finished goods inventories, net		214,359		225,494
Prepaid expenses and other current assets		12,667		9,093
Assets held for sale		3,500		6,109
Deferred income taxes		24,921		24,234
Total current assets		475,201		433,649
Property, plant, and equipment, net		76,377		75,053
Tradenames		305,733		308,233
Cost in excess of fair value of net assets acquired		136,570		136,570
Deferred debt issuance costs, net		3,892		4,743
Licensing agreements, net		6,174		8,915
Other assets		8,310		7,505
Total assets	$	1,012,257	$	974,668
LIABILITIES AND STOCKHOLDERS' EQUITY				
Current liabilities:				
Current maturities of long-term debt	$	4,379	$	3,503
Accounts payable		58,624		56,589
Other current liabilities		58,174		46,666
Total current liabilities		121,177		106,758
Long-term debt		335,399		338,026
Deferred income taxes		112,873		113,706
Other long-term liabilities		32,134		34,049
Total liabilities		601,583		592,539
Commitments and contingencies				
Stockholders' equity:				
Preferred stock; par value $.01 per share; 100,000 shares authorized; none issued or outstanding at September 27, 2008 and December 29, 2007		--		--
		565		576

Common stock, voting; par value $.01 per share; 150,000,000 shares authorized; 56,533,319 and 57,663,315 shares issued and outstanding at September 27, 2008 and December 29, 2007, respectively		
Additional paid-in capital	213,546	232,356
Accumulated other comprehensive income	2,324	2,671
Retained earnings	194,239	146,526
Total stockholders' equity	410,674	382,129
Total liabilities and stockholders' equity	$ 1,012,257	$ 974,668

See accompanying notes to the unaudited condensed consolidated financial statements

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

	For the three-month periods ended		For the nine-month periods ended	
	September 27, 2008	September 29, 2007	September 27, 2008	September 29, 2007
Net sales	$ 436,419	$ 410,949	$ 1,068,066	$ 1,018,852
Cost of goods sold	281,752	265,093	708,903	671,198
Gross profit	154,667	145,856	359,163	347,654
Selling, general, and administrative expenses	104,536	94,241	289,019	267,122
Intangible asset impairment (Note 4)	--	--	--	154,886
Executive retirement charges (Note14)	--	--	5,325	--
Facility write-down and closure costs (Note 11)	2,609	256	2,609	5,233
Royalty income	(9,576)	(8,649)	(24,693)	(22,894)
Operating income (loss)	57,098	60,008	86,903	(56,693)
Interest expense, net	4,048	6,021	13,357	17,453
Income (loss) before income taxes	53,050	53,987	73,546	(74,146)
Provision for income taxes	19,675	19,369	25,833	25,074
Net income (loss)	$ 33,375	$ 34,618	$ 47,713	$ (99,220)
Basic net income (loss) per common share	$ 0.60	$ 0.60	$ 0.85	$ (1.71)
Diluted net income (loss) per common share	$ 0.58	$ 0.58	$ 0.82	$ (1.71)
Basic weighted-average number of shares outstanding	56,015,725	57,745,717	56,462,515	58,010,633
Diluted weighted-average number of shares outstanding	57,963,941	59,975,130	58,490,406	58,010,633

See accompanying notes to the unaudited condensed consolidated financial statements

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

	For the nine-month periods ended September 27, 2008	September 29, 2007
Cash flows from operating activities:		
Net income (loss)	$ 47,713	$ (99,220)
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:		
Depreciation and amortization	20,576	22,526
Amortization of debt issuance costs	851	872
Non-cash intangible asset impairment charges	--	154,886
Non-cash stock-based compensation expense	6,756	4,653
Income tax benefit from exercised stock options	(3,457)	(7,797)
Loss on disposal of property, plant, and equipment	383	620
Deferred income taxes	(1,399)	(8,890)
Non-cash facility write-down and closure costs (Note 11)	2,609	2,450
Effect of changes in operating assets and liabilities:		
Accounts receivable	(40,387)	(49,454)
Inventories	11,135	(52,941)
Prepaid expenses and other assets	(4,722)	(5,302)
Accounts payable and other liabilities	17,295	(1,020)
Net cash provided by (used in) operating activities	57,353	(38,617)
Cash flows from investing activities:		
Capital expenditures	(19,197)	(13,228)
Proceeds from sale of property, plant, and equipment	--	53
Net cash used in investing activities	(19,197)	(13,175)
Cash flows from financing activities:		
Payments on term loan	(1,751)	(2,627)
Share repurchase (Note 8)	(29,774)	(47,406)
	--	117,600

Borrowings from revolving loan facility		
Payments on revolving loan facility	--	(96,000)
Income tax benefit from exercised stock options	3,457	7,797
Proceeds from exercise of stock options	560	2,576
Other	--	10,561
Net cash used in financing activities	(27,508)	(7,499)
Net increase (decrease) in cash and cash equivalents	10,648	(59,291)
Cash and cash equivalents, beginning of period	49,012	68,545
Cash and cash equivalents, end of period	$ 59,660	$ 9,254

See accompanying notes to the unaudited condensed consolidated financial statements

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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 income (loss)	Retained earnings	Total stockholders' equity
Balance at December 29, 2007	$ 576	$ 232,356	$ 2,671	$ 146,526	$ 382,129
Income tax benefit from exercised stock options	--	3,457	--	--	3,457
Exercise of stock options (579,445 shares)	6	554	--	--	560
Stock-based compensation expense	--	6,306	--	--	6,306
Issuance of common stock (43,386 shares)	1	629	--	--	630
Share repurchase (1,898,183 shares) (Note 8)	(18)	(29,756)	--	--	(29,774)
Comprehensive income (loss):					
Net income	--	--	--	47,713	47,713
Unrealized loss on interest rate swap, net of tax benefit of $199	--	--	(375)	--	(375)
Unrealized gain on interest rate collar, net of tax of $28	--	--	28	--	28
Total comprehensive (loss) income	--	--	(347)	47,713	47,366
Balance at September 27, 2008	$ 565	$ 213,546	$ 2,324	$ 194,239	$ 410,674

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, 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 to our Carter’s and OshKosh retail stores that market our brand name 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 statement of our financial position as of September 27, 2008, the results of our operations for the three and nine-month periods ended September 27, 2008 and September 29, 2007, cash flows for the nine-month periods ended September 27, 2008 and September 29, 2007, and changes in stockholders’ equity for the nine-month period ended September 27, 2008. Operating results for the three and nine-month periods ended September 27, 2008 are not necessarily indicative of the results that may be expected for the fiscal year ending January 3, 2009. Our accompanying condensed consolidated balance sheet as of December 29, 2007 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 December 29, 2007.

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 third quarter and first nine months of fiscal 2008 reflect our financial position as of September 27, 2008. The third quarter and first nine months of fiscal 2007 ended on September 29, 2007.

Certain prior year amounts have been reclassified for comparative purposes.

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

NOTE 3 – COMPREHENSIVE INCOME (LOSS):

Comprehensive income (loss) is summarized as follows:

(dollars in thousands)	For the three-month periods ended		For the nine-month periods ended	
	September 27, 2008	September 29, 2007	September 27, 2008	September 29, 2007
Net income (loss)	$ 33,375	$ 34,618	$ 47,713	$ (99,220)
Unrealized gain (loss) on interest rate swap, net of taxes of $110, $(584), $(199), and $(606)	188	(1,018)	(375)	(1,058)
Unrealized gain (loss) on interest rate collar, net of taxes of $203, $(117), $28, and $(84)	345	(204)	28	(146)
Settlement of pension asset, net of tax benefit of $75	--	--	--	(132)
Total comprehensive income (loss)	$ 33,908	$ 33,396	$ 47,366	$ (100,556)

NOTE 4 – COST IN EXCESS OF FAIR VALUE OF NET ASSETS ACQUIRED AND OTHER INTANGIBLE ASSETS:

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

In connection with the 2001 acquisition, we adopted the provisions of Statement of Financial Accounting Standards ("SFAS") No. 141, "Business Combinations" ("SFAS 141"), and applied the required provisions of SFAS No. 142, "Goodwill and other Intangible Assets" ("SFAS 142"). Accordingly, our Carter's tradename and cost in excess of fair value of net assets acquired have been concluded to have indefinite lives and are not being amortized.

In connection with the acquisition of OshKosh B'Gosh, Inc. on July 14, 2005 (the "Acquisition"), the Company recorded cost in excess of fair value of net assets acquired, tradename, licensing, and leasehold interest assets in accordance with SFAS 141. During the second quarter of fiscal 2007, as a result of negative trends in sales and profitability of the Company's OshKosh B'Gosh wholesale and retail segments and re-forecasted projections for such segments for the balance of fiscal 2007, the Company conducted an interim impairment assessment on the value of the intangible assets that the Company recorded in connection with the Acquisition. This assessment was performed in accordance with SFAS 142. Based on this assessment, impairment charges of approximately $36.0 million and $106.9 million were recorded to reflect the impairment of the cost in excess of fair value of net assets acquired for the OshKosh wholesale and retail segments, respectively. In addition, an impairment charge of $12.0 million was recorded to reflect the impairment of the value ascribed to the OshKosh tradename asset. For cost in excess of fair value of net assets acquired, the fair value was determined using the expected present value of future cash flows. For the OshKosh tradename, the fair value was determined using a discounted cash flow analysis which examined the hypothetical cost savings that accrue as a result of our ownership of the tradename.

During the first nine months of fiscal 2008, approximately $1.5 million of tax contingencies recorded in connection with the Acquisition were reversed due to settlement with taxing authorities and closure of applicable statute of limitations. This reversal resulted in a corresponding reduction to the OshKosh tradename asset of $2.5 million and a reduction in the related deferred tax liability of $1.0 million in accordance with Emerging Issues Task Force ("EITF") Issue No. 93-7, "Uncertainties Related to Income Taxes in a Purchase Business Combination" ("EITF 93-7").

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

NOTE 4 – COST IN EXCESS OF FAIR VALUE OF NET ASSETS ACQUIRED AND OTHER INTANGIBLE ASSETS: (Continued)

The Company's intangible assets were as follows:

		September 27, 2008			December 29, 2007		
(dollars in thousands)	Weighted-average useful life	Gross amount	Accumulated amortization	Net amount	Gross amount	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	$ 88,000	$ --	$ 88,000
OshKosh licensing agreements	4.7 years	$ 19,100	$ 12,926	$ 6,174	$ 19,100	$ 10,185	$ 8,915
Leasehold interests	4.1 years	$ 1,833	$ 1,492	$ 341	$ 1,833	$ 1,149	$ 684

Amortization expense for intangible assets was approximately $1.0 million and $3.1 million for the three and nine-month periods ended September 27, 2008 and $1.0 million and $3.4 million for the three and nine-month periods ended September 29, 2007. Annual amortization expense for the OshKosh licensing agreements and leasehold interests is expected to be as follows:

(dollars in thousands)

Fiscal Year	Estimated amortization expense
2008 (period from September 28 through January 3, 2009)	$ 1,021
2009	3,717
2010	1,777
Total	$ 6,515

NOTE 5 – INCOME TAXES:

The Company and its subsidiaries file income tax returns in the United States and in various states and local jurisdictions. The Internal Revenue Service has recently completed an income tax examination for fiscal 2004 and 2005, and has recently begun its audit of fiscal 2006. In most cases, the Company is no longer subject to state and local tax authority examinations for years prior to fiscal 2004.

During the first nine months of fiscal 2008, we recognized approximately $1.6 million in tax benefits due to the completion of the Internal Revenue Service audit for fiscal 2004 and 2005. In addition, we recognized approximately $0.9 million of pre-Acquisition uncertainties previously reserved for upon completion of these audits. These pre-Acquisition uncertainties have been reflected as a reduction in the OshKosh tradename asset in accordance with EITF 93-7. We also recognized approximately $0.3 million in tax benefits due to various statute closures, primarily state and local jurisdictions during the third quarter of fiscal 2008 and approximately $0.6 million of pre-Acquisition uncertainties previously reserved for upon the closure of applicable statute of limitations. These pre-Acquisition uncertainties have been reflected as a reduction in the OshKosh tradename asset in accordance with EITF 93-7.

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

NOTE 5 – INCOME TAXES: (Continued)

As of September 27, 2008, the Company had gross unrecognized tax benefits of approximately $7.0 million. The Company's reserve for unrecognized tax benefits as of September 27, 2008 includes approximately $5.4 million of reserves which, if ultimately recognized, will impact the Company's effective tax rate in the period settled. The reserve for unrecognized tax benefits also includes $1.2 million of reserves which, if ultimately recognized, would be reflected as an adjustment to the Carter's cost in excess of fair value of net assets acquired or the OshKosh tradename asset and $0.4 million for 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.

Included in the reserves for unrecognized tax benefits are approximately $0.6 million of reserves for which the statute of limitations is expected to expire in the third quarter of fiscal 2009. Such exposures relate primarily to state and local income tax matters. If these tax benefits are ultimately recognized, such recognition may impact our annual effective tax rate for fiscal 2009 and the tax rate in the quarter in which the benefits are recognized.

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 $0.5 million of interest accrued as of September 27, 2008.

NOTE 6 – FAIR VALUE MEASUREMENTS:

Effective December 30, 2007 (the first day of our 2008 fiscal year), the Company adopted 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-1	Quoted prices in active markets for identical assets or liabilities
Level-2	Quoted prices for similar assets and liabilities in active markets or inputs that are observable
Level-3	Inputs that are unobservable (for example, cash flow modeling inputs based on assumptions)

The following table summarizes assets and liabilities measured at fair value on a recurring basis at September 27, 2008, as required by SFAS 157:

(dollars in millions)	Level 1	Level 2	Level 3
Assets			

Investments	$	--	$	--	$	--
Liabilities						
Interest rate swap	$	--	$	0.9	$	--
Interest rate collar	$	--	$	0.5	$	--

Our senior credit facility requires us to hedge at least 25% of our variable rate debt under the term loan. 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 variable rate term loan debt. The interest rate swap agreement matures on July 30, 2010. As of September 27, 2008, approximately $59.4 million of our outstanding term loan debt was hedged under this agreement.

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

NOTE 6 – FAIR VALUE MEASUREMENTS: (Continued)

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

Both our interest rate swap and collar 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.

NOTE 7 – 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 other liabilities are net of these expected employee contributions. Additionally, we have an obligation under a defined benefit plan covering certain former officers and their spouses. 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 net periodic post-retirement benefit cost charged to operations are as follows:

	For the three-month periods ended		For the nine-month periods ended	
(dollars in thousands)	September 27, 2008	September 29, 2007	September 27, 2008	September 29, 2007
Service cost – benefits attributed to service during the period	$ 26	$ 26	$ 79	$ 78
Interest cost on accumulated post-retirement benefit obligation	132	131	395	391
Total net periodic post-retirement benefit cost	$ 158	$ 157	$ 474	$ 469

The components of net periodic pension benefit cost charged to operations are as follows:

	For the three-month periods ended		For the nine-month periods ended	
(dollars in thousands)	September 27, 2008	September 29, 2007	September 27, 2008	September 29, 2007
	$ 13	$ 13	$ 39	$ 43

Interest cost on accumulated pension benefit obligation								
Actuarial gain		--		(53)		--		(53)
Total net periodic pension benefit cost	$	13	$	(40)	$	39	$	(10)

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

NOTE 7 – EMPLOYEE BENEFIT PLANS: (Continued)

The Company acquired two defined benefit pension plans in connection with the Acquisition. The benefits for certain current and former employees of OshKosh under these pension plans were frozen as of December 31, 2005. During the second quarter of fiscal 2007, the Company liquidated one of these plans, the OshKosh B'Gosh Collective Bargaining Pension Plan (the "Plan"), distributed each participant's balance, and the remaining net assets of $2.2 million were contributed to the Company's defined contribution plan to offset future employer contributions. In connection with the liquidation of the Plan, the Company recorded a pre-tax gain of approximately $0.3 million related to the Plan settlement during the second quarter of fiscal 2007.

The Company's net periodic pension benefit included in the statements of operations is comprised of:

	For the three-month periods ended		For the nine-month periods ended	
(dollars in thousands)	September 27, 2008	September 29, 2007	September 27, 2008	September 29, 2007
Interest cost on accumulated pension benefit obligation	$ 562	$ 551	$ 1,686	$ 1,654
Expected return on assets	(943)	(897)	(2,830)	(3,213)
Amortization of actuarial gain	(19)	(34)	(57)	(104)
Gain on settlement	--	--	--	(276)
Total net periodic pension benefit	$ (400)	$ (380)	$ (1,201)	$ (1,939)

NOTE 8 – 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 third quarter and first nine months of fiscal 2008, the Company repurchased and retired approximately $10 million and $30 million, or 578,098 and 1,898,183 shares, of its common stock at an average price of $16.81 and $15.69 per share, respectively. During the third quarter and first nine months of fiscal 2007, the Company repurchased and retired approximately $7 million and $47 million, or 338,100 and 1,985,519 shares, of its common stock at an average price of $21.87 and $23.88 per share, respectively. Since inception of the program and through the first nine months of fiscal 2008, the Company repurchased and retired approximately $87 million, or 4,371,402 shares, of its common stock at an average price of $19.96 per share. Accordingly, we have reduced common stock by the par value of such shares and have deducted the remaining excess repurchase price over par value from additional paid-in capital.

During the first nine months of fiscal 2008, the Company issued 43,386 shares of common stock at a fair market value of $14.52 to its non-management board members. Accordingly, we recognized $630,000 in stock-based compensation expense. We received no proceeds from the issuance of these shares.

During the third quarter and first nine months of fiscal 2007, the Company issued 2,062 shares and 23,482 shares of common stock at a fair market value of $21.82 and $25.21 to its non-management board members and recognized $45,000 and $585,000 in stock-based compensation expense, respectively. We received no proceeds from the issuance of these shares.

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

NOTE 9 – 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 nine-month period ended September 27, 2008.

	Assumptions
Volatility	34.16%
Risk-free interest rate	3.49%
Expected term (years)	5.62
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.

The following table summarizes our stock option and restricted stock activity during the nine-month period ended September 27, 2008:

	Time-based stock options	Performance-based stock options	Retained stock options	Restricted stock
Outstanding, December 29, 2007	4,315,689	620,000	661,870	372,283
Granted	532,250	--	--	152,606
Exercised	(31,089)	--	(548,356)	--
Vested restricted stock	--	--	--	(39,850)
Forfeited	(17,150)	(400,000)	--	(7,250)
Expired	(8,450)	--	--	--
Outstanding, September 27, 2008	4,791,250	220,000	113,514	477,789
Exercisable, September 27, 2008	3,623,170	--	113,514	--

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 14, "Executive Retirement Charges").

During the three-month period ended September 27, 2008, we granted 495,000 time-based stock options with a weighted-average Black-Scholes fair value of $5.81 and a weighted-average exercise price of $15.23. In connection with these grants, we recognized approximately $165,000 in stock-based compensation expense.

During the nine-month period ended September 27, 2008, we granted 532,250 time-based stock options with a weighted-average Black-Scholes fair value of $5.89 and a weighted-average exercise price of $15.35. In connection with these grants, we recognized approximately $194,000 in stock-based compensation expense.

During the three-month period ended September 27, 2008, we granted 127,500 shares of restricted stock to employees with a weighted-average fair value on the date of grant of $16.59. In connection with these grants, we recognized approximately $88,000 in stock-based compensation expense.

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NOTE 9 – STOCK-BASED COMPENSATION: (Continued)

During the nine-month period ended September 27, 2008, we granted 152,606 shares of restricted stock to employees and a director with a weighted-average fair value on the date of grant of $16.59. In connection with these grants, we recognized approximately $143,000 in stock-based compensation expense.

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

(dollars in thousands)	Time-based stock options	Restricted stock	Total
2008 (period from September 28 through January 3, 2009)	$ 917	$ 751	$ 1,668
2009	2,665	2,464	5,129
2010	1,897	1,829	3,726
2011	1,276	1,298	2,574
2012	270	313	583
Total	$ 7,025	$ 6,655	$ 13,680

NOTE 10 – 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.

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NOTE 10 – SEGMENT INFORMATION: (Continued)

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

(dollars in thousands)	For the three-month periods ended September 27, 2008	% of Total	September 29, 2007	% of Total	For the nine-month periods ended September 27, 2008	% of Total	September 29, 2007	% of Total
Net sales:								
Wholesale-Carter's	$ 151,848	34.8%	$ 149,918	36.4%	$ 364,002	34.1%	$ 355,865	34.9%
Wholesale-OshKosh	22,801	5.2%	28,197	6.9%	55,010	5.1%	63,417	6.2%
Retail-Carter's	112,508	25.8%	102,429	24.9%	291,566	27.3%	253,530	24.9%
Retail-OshKosh	72,568	16.6%	62,800	15.3%	166,816	15.6%	157,533	15.5%
Mass Channel-Carter's	76,694	17.6%	67,605	16.5%	190,672	17.9%	188,507	18.5%
Total net sales	$ 436,419	100.0%	$ 410,949	100.0%	$ 1,068,066	100.0%	$ 1,018,852	100.0%
Operating income (loss):		% of segment net sales		% of segment net sales		% of segment net sales		% of segment net sales
Wholesale-Carter's	$ 29,520	19.4%	$ 33,484	22.3%	$ 63,086	17.3%	$ 70,972	19.9%
Wholesale-OshKosh	1,546	6.8%	2,624	9.3%	(5,290)	(9.6)%	(1,010)	(1.6)%
OshKosh cost in excess of fair value of net assets acquired-impairment	--	--	--	--	--	--	(35,995)	(56.8)%
Net Wholesale-OshKosh	1,546	6.8%	2,624	9.3%	(5,290)	(9.6)%	(37,005)	(58.4)%
Retail-Carter's	20,367	18.1%	19,599	19.1%	42,167	14.5%	33,235	13.1%
Retail-OshKosh	9,810	13.5%	2,541	4.0%	431	0.3%	(478)	(0.3)%
OshKosh cost in excess of fair value of net assets acquired-impairment	--	--	--	--	--	--	(106,891)	(67.9)%
Net Retail-OshKosh	9,810	13.5%	2,541	4.0%	431	0.3%	(107,369)	(68.2)%

Mass Channel-Carter’s		10,055		13.1%	12,898	19.1%	24,576		12.9%	30,043		15.9%
Mass Channel-OshKosh (a)		764		--	615	--	1,923		--	1,503		--
Segment operating income (loss)		72,062		16.5%	71,761	17.5%	126,893		11.9%	(8,621)		(0.8)%
Other reconciling items		(14,964)	(b)	(3.4)%	(11,753)	(2.9)%	(39,990)	(b),(c)	(3.7)%	(36,072)	(d)	(3.5)%
OshKosh tradename impairment		--		--	--	--	--		--	(12,000)		(1.2)%
Net other reconciling items		(14,964)		(3.4)%	(11,753)	(2.9)%	(39,990)		(3.7)%	(48,072)		(4.7)%
Total operating income (loss)	$	57,098		13.1%	$ 60,008	14.6%	$ 86,903		8.1%	$ (56,693)		(5.6)%

(a

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

(b) Includes $2.6 million related to the write-down of the carrying value of the OshKosh distribution center (see Note 11).

(c) Includes $5.3 million in executive retirement charges in connection with Mr. Rowan’s retirement (see Note 14).

(d) Includes $7.4 million in closure costs related to the closure of our OshKosh distribution center, including $2.1 million in accelerated depreciation (see Note 11).

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)
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NOTE 11 – FACILITY CLOSURE AND RESTRUCTURING COSTS:

OshKosh Distribution Facility

The Company continually evaluates opportunities to reduce its supply chain complexity and lower costs. In the first quarter of fiscal 2007, the Company determined that OshKosh brand products could be effectively distributed through its other distribution facilities and third-party logistics providers. On February 15, 2007, the Company's Board of Directors approved management's plan to close the Company's White House, Tennessee distribution facility, which was utilized to distribute the Company's OshKosh brand products.

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 were impaired as of the end of January 2007, as it became "more likely than not" that the expected life of the OshKosh distribution facility would be significantly shortened. Accordingly, we wrote down the assets to their estimated recoverable fair value as of the end of January 2007. The adjusted asset values were subject to accelerated depreciation over their remaining estimated useful life. Distribution operations at the OshKosh facility ceased as of April 5, 2007, at which point the land, building, and equipment assets of $6.1 million were reclassified as held for sale. Over the past year, the Company has been actively trying to sell this facility for its appraised value. However, due to recent declines in the commercial real estate market, the Company lowered the anticipated selling price of the facility during the third quarter of fiscal 2008 and has written down the carrying value of the facility by $2.6 million to reflect the new anticipated selling price.

During the first nine months of fiscal 2007, we recorded closure costs of $7.4 million, consisting of asset impairment charges of $2.4 million related to a write-down of the related land, building, and equipment, $2.0 million of severance charges, $2.1 million of accelerated depreciation (included in selling, general, and administrative expenses), and $0.9 million of other closure costs.

Acquisition Restructuring

In connection with the Acquisition, management developed a plan to restructure and integrate the operations of OshKosh. In accordance with EITF No. 95-3, "Recognition of Liabilities in Connection with a Purchase Business Combination," liabilities were established for OshKosh severance, lease termination costs associated with the closure of 30 OshKosh retail stores, contract termination costs, and other exit and facility closure costs.

The following table summarizes restructuring reserves related to the Acquisition which were included in other current liabilities on the accompanying unaudited condensed consolidated balance sheet:

(dollars in thousands)	Severance and other exit costs	Lease termination costs	Total
Balance at December 29, 2007	$ 489	$ 674	$ 1,163
Payments	(458)	--	(458)
Balance at March 29, 2008	31	674	705

Payments	(53)	--	(53)
Adjustments	42	(42)	--
Balance at June 28, 2008	20	632	652
Payments	(31)	(632)	(663)
Adjustments	11	--	11
Balance at September 27, 2008	$ --	$ --	$ --

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NOTE 12 – EARNINGS PER SHARE:

Basic net income (loss) per share is calculated by dividing net income (loss) for the period by the weighted-average common shares outstanding for the period. Diluted net income (loss) 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 following table summarizes the shares from these potentially dilutive securities, calculated using the treasury stock method:

(dollars in thousands, except per share data)	For the three-month periods ended September 27, 2008	For the three-month periods ended September 29, 2007	For the nine-month periods ended September 27, 2008	For the nine-month periods ended September 29, 2007
Net income (loss)	$ 33,375	$ 34,618	$ 47,713	$ (99,220)
Weighted-average number of common and common equivalent shares outstanding:				
Basic number of common shares outstanding	56,015,725	57,745,717	56,462,515	58,010,633
Dilutive effect of unvested restricted stock	84,593	60,190	84,119	--
Dilutive effect of stock options	1,863,623	2,169,223	1,943,772	--
Diluted number of common and common equivalent shares outstanding	57,963,941	59,975,130	58,490,406	58,010,633
Basic net income (loss) per common share	$ 0.60	$ 0.60	$ 0.85	$ (1.71)
Diluted net income (loss) per common share	$ 0.58	$ 0.58	$ 0.82	$ (1.71)