

CARTERS INC  
Form 10-Q  
April 27, 2012

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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 MARCH 31, 2012 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  
(state or other jurisdiction of  
incorporation or organization)

13-3912933  
(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 has submitted electronically and posted on its corporate website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the Registrant was required to submit and post such files). 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 "large accelerated filer, 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 ( )

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 April 27, 2012

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Common stock, par value \$0.01 per share

58,938,891



CARTER'S, INC.  
INDEX

	Page
<u>Part I. Financial Information</u>	
Item 1. <u>Financial Statements</u>	
<u>Unaudited Condensed Consolidated Balance Sheets as of March 31, 2012, December 31, 2011, and April 2, 2011</u>	<u>1</u>
<u>Unaudited Condensed Consolidated Statements of Operations for the three-month periods ended March 31, 2012 and April 2, 2011</u>	<u>2</u>
<u>Unaudited Condensed Consolidated Statements of Comprehensive Income for the three-month periods ended March 31, 2012 and April 2, 2011</u>	<u>3</u>
<u>Unaudited Condensed Consolidated Statement of Changes in Stockholders' Equity for the three-month period ended March 31, 2012</u>	<u>4</u>
<u>Unaudited Condensed Consolidated Statements of Cash Flows for the three-month periods ended March 31, 2012 and April 2, 2011</u>	<u>5</u>
<u>Notes to the Unaudited Condensed Consolidated Financial Statements</u>	<u>6</u>
Item 2. <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	<u>20</u>
Item 3. <u>Quantitative and Qualitative Disclosures about Market Risk</u>	<u>32</u>
Item 4. <u>Controls and Procedures</u>	<u>32</u>
<u>Part II. Other Information</u>	
Item 1. <u>Legal Proceedings</u>	<u>33</u>
Item 1A. <u>Risk Factors</u>	<u>33</u>
Item 2. <u>Unregistered Sales of Equity Securities and Use of Proceeds</u>	<u>39</u>
Item 3. <u>Defaults upon Senior Securities</u>	<u>39</u>
Item 4. <u>Mine Safety Disclosures</u>	<u>39</u>
Item 5. <u>Other Information</u>	<u>39</u>
Item 6. <u>Exhibits</u>	<u>39</u>
<u>Signatures</u>	<u>40</u>
Certifications	

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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)

	March 31, 2012	December 31, 2011	April 2, 2011
<b>ASSETS</b>			
Current assets:			
Cash and cash equivalents	\$300,535	\$233,494	\$248,871
Accounts receivable, net	178,668	157,754	160,057
Finished goods inventories, net	265,691	347,215	217,458
Prepaid expenses and other current assets	16,425	18,519	19,650
Deferred income taxes	24,114	25,165	26,667
 Total current assets	 785,433	 782,147	 672,703
Property, plant, and equipment, net	127,736	122,346	92,553
Tradenames	306,109	306,176	305,733
Goodwill	189,696	188,679	136,570
Deferred debt issuance costs, net	2,447	2,624	3,155
Other intangible assets, net	244	258	—
Other assets	399	479	322
 Total assets	 \$1,412,064	 \$1,402,709	 \$1,211,036
<b>LIABILITIES AND STOCKHOLDERS’ EQUITY</b>			
Current liabilities:			
Current maturities of long-term debt	\$—	\$—	\$—
Accounts payable	67,610	102,804	53,077
Other current liabilities	51,484	49,949	49,640
 Total current liabilities	 119,094	 152,753	 102,717
Long-term debt	236,000	236,000	236,000
Deferred income taxes	113,773	114,421	112,453
Other long-term liabilities	100,555	93,826	46,873
 Total liabilities	 569,422	 597,000	 498,043
Commitments and contingencies			
Stockholders’ equity:			
Preferred stock; par value \$.01 per share; 100,000 shares authorized; none issued or outstanding at March 31, 2012, December 31, 2011, and April 2, 2011	—	—	—
Common stock, voting; par value \$.01 per share; 150,000,000 shares authorized; 58,938,891, 58,595,421, and 57,761,103 shares issued and outstanding at March 31, 2012, December 31, 2011, and April 2, 2011, respectively	589	586	578

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Additional paid-in capital	235,198	231,738	211,531
Accumulated other comprehensive loss	(10,087	) (11,282	) (1,890
Retained earnings	616,942	584,667	502,774
Total stockholders' equity	842,642	805,709	712,993
Total liabilities and stockholders' equity	\$1,412,064	\$1,402,709	\$1,211,036

See accompanying notes to the unaudited condensed consolidated financial statements.

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

	For the three-month periods ended	
	March 31, 2012	April 2, 2011
Net sales	\$551,662	\$469,000
Cost of goods sold	356,923	310,915
Gross profit	194,739	158,085
Selling, general, and administrative expenses	149,705	113,780
Royalty income	(8,766	) (9,329
Operating income	53,800	53,634
Interest expense, net	1,957	1,850
Foreign currency loss	306	—
Income before income taxes	51,537	51,784
Provision for income taxes	19,262	19,661
Net income	\$32,275	\$32,123
Basic net income per common share (Note 13)	\$0.55	\$0.56
Diluted net income per common share (Note 13)	\$0.54	\$0.55

See accompanying notes to the unaudited condensed consolidated financial statements.

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

	For the three-month periods ended	
	March 31, 2012	April 2, 2011
Net income	\$32,275	\$32,123
Other comprehensive income:		
Cumulative foreign currency translation adjustments	1,195	—
Comprehensive income	\$33,470	\$32,123

See accompanying notes to the unaudited condensed consolidated financial statements.

## CARTER'S, INC.

## CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN STOCKHOLDERS' EQUITY

(dollars in thousands, except for share data)

(unaudited)

	Common stock	Additional paid-in capital	Accumulated other comprehensive (loss) income	Retained earnings	Total stockholders' equity	
Balance at December 31, 2011	\$586	\$231,738	\$(11,282	) \$584,667	\$805,709	
Exercise of stock options (81,425 shares)	1	1,681	—	—	1,682	
Withholdings from vesting of restricted stock (49,855 shares)	(1	) (2,246	) —	—	(2,247	)
Income tax benefit from stock-based compensation	—	1,535	—	—	1,535	
Restricted stock activity	3	(3	) —	—	—	
Stock-based compensation expense	—	2,493	—	—	2,493	
Net income	—	—	—	32,275	32,275	
Cumulative foreign currency translation adjustments	—	—	1,195	—	1,195	
Balance at March 31, 2012	\$589	\$235,198	\$(10,087	) \$616,942	\$842,642	

See accompanying notes to the unaudited condensed consolidated financial statements.



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

	For the three-month periods ended	
	March 31, 2012	April 2, 2011
Cash flows from operating activities:		
Net income	\$32,275	\$32,123
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	8,495	8,130
Non-cash revaluation of contingent consideration	692	—
Amortization of Bonnie Togs tradename and non-compete agreements	94	—
Amortization of debt issuance costs	177	177
Non-cash stock-based compensation expense	2,868	2,151
Income tax benefit from stock-based compensation	(1,535)	(407)
Loss on disposal/sale of property, plant, and equipment	391	100
Deferred income taxes	201	3,353
Effect of changes in operating assets and liabilities:		
Accounts receivable	(20,807)	(38,604)
Inventories	82,000	81,051
Prepaid expenses and other assets	2,215	(2,284)
Accounts payable and other liabilities	(24,624)	(76,496)
Net cash provided by operating activities	82,442	9,294
Cash flows from investing activities:		
Capital expenditures	(16,381)	(6,813)
Proceeds from sale of property, plant, and equipment	6	—
Net cash used in investing activities	(16,375)	(6,813)
Cash flows from financing activities:		
Borrowings under revolving credit facility	2,500	—
Payments on revolving credit facility	(2,500)	—
Income tax benefit from stock-based compensation	1,535	407
Withholdings from vesting of restricted stock	(2,247)	(1,406)
Proceeds from exercise of stock options	1,682	7
Net cash provided by (used in) financing activities	970	(992)
Effect of exchange rate changes on cash	4	—
Net increase in cash and cash equivalents	67,041	1,489
Cash and cash equivalents, beginning of period	233,494	247,382
Cash and cash equivalents, end of period	\$300,535	\$248,871

See accompanying notes to the unaudited condensed consolidated financial statements.

5

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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 You, Precious Firsts, OshKosh, and other brands. Our products are sourced through contractual arrangements with manufacturers worldwide for wholesale distribution to major domestic and international retailers and for our 372 Carter's, 168 OshKosh, and 69 Canadian retail stores that market our brand name merchandise and other licensed products manufactured by other companies.

On June 30, 2011, Northstar Canadian Operations Corp. ("Northstar"), a newly formed Canadian corporation and a wholly owned subsidiary of The William Carter Company ("TWCC") (a wholly owned subsidiary of Carter's, Inc.), purchased all of the outstanding shares of capital stock of the entities comprising Bonnie Togs (the "Acquisition"), a Canadian specialty retailer focused exclusively on the children's apparel and accessories marketplace. Bonnie Togs sells products under the Carter's and OshKosh brands, as well as other brands. Prior to the Acquisition, Bonnie Togs was Carter's principal licensee in Canada since 2007 and was a significant international licensee of the Company.

As a result of the acquisition of Bonnie Togs, the Company reevaluated and realigned certain of its reportable segments, please see Note 12, "Segment Information."

Our unaudited condensed consolidated balance sheet as of March 31, 2012 and audited consolidated balance sheet as of December 31, 2011 include Bonnie Togs. Bonnie Togs results are included in our unaudited condensed consolidated statements of operations effective the second quarter of fiscal 2011.

NOTE 2 – BASIS OF PREPARATION:

The accompanying unaudited condensed consolidated financial statements include the accounts of Carter's, Inc. and its wholly owned 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 March 31, 2012, the results of our operations for the three-month periods ended March 31, 2012 and April 2, 2011, comprehensive income for the three-month periods ended March 31, 2012 and April 2, 2011, changes in stockholders' equity for the three-month period ended March 31, 2012, and cash flows for the three-month periods ended March 31, 2012 and April 2, 2011. Except as otherwise disclosed, all such adjustments consist only of those of a normal recurring nature. Operating results for the three-month period ended March 31, 2012 are not necessarily indicative of the results that may be expected for the fiscal year ending December 29, 2012. Our accompanying condensed consolidated balance sheet as of December 31, 2011 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 ("SEC") 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 31, 2011.

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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 first quarter of fiscal 2012 reflects our financial position as of March 31, 2012. The first quarter of fiscal 2011 ended on April 2, 2011.

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

6

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

NOTE 3 – ACQUISITION OF BONNIE TOGS:

As noted above, on June 30, 2011, Northstar purchased all of the outstanding shares of capital stock of Bonnie Togs for total consideration of up to CAD \$95 million, of which USD \$61.2 million was paid in cash at closing. The sellers may also be paid contingent consideration ranging from zero to CAD \$35 million if the Canadian business meets certain earnings targets for the period beginning July 1, 2011 and ending on June 27, 2015. Sellers may receive a portion of the contingent consideration of up to CAD \$25 million if interim earnings targets are met through June 2013 and June 2014, respectively. Any such payments are not recoverable by the Company in the event of any failure to meet overall targets.

As of March 31, 2012, the Company had a discounted contingent consideration liability of approximately \$26.8 million based upon the high probability that Bonnie Togs will attain its earnings targets and is included in other long-term liabilities on the accompanying audited consolidated balance sheet. The fair value of the discounted contingent consideration liability as of December 31, 2011 was approximately \$25.6 million. The \$1.2 million change in the fair value of the liability is reflected as \$0.7 million in accretion expense and \$0.5 million in other comprehensive income resulting from an unfavorable foreign currency translation adjustment. The Company determined the fair value of the contingent consideration based upon a probability-weighted discounted cash flow analysis. The Company will continue to revalue the contingent consideration at each reporting date.

The following table summarizes the fair values of the assets acquired and liabilities assumed at June 30, 2011, the date of the Acquisition:

(U.S. dollars in thousands)

Current assets	\$40,668
Property, plant, and equipment	13,485
Bonnie Togs Goodwill	54,982
Bonnie Togs tradename	623
Non-compete agreements	311
Total assets acquired	110,069
Current liabilities	18,231
Non-current liabilities	6,693
Total liabilities assumed	24,924
Net assets acquired	\$85,145

In connection with the Acquisition, the Company recorded total acquired intangible assets of approximately \$55.9 million, including \$55.0 million of Bonnie Togs goodwill, \$0.6 million related to the Bonnie Togs tradename (life of two years), and \$0.3 million related to non-compete agreements for certain executives (life of four years).

The following unaudited pro forma summary presents information as if Bonnie Togs had been acquired on January 2, 2010 and assumes that there were no other changes in our operations. The pro forma information does not necessarily reflect the actual results that would have occurred had the Company operated the Canadian business since January 2, 2010, nor is it necessarily indicative of the future results of operations of the combined companies.

(dollars in thousands, except share data)	Three-month period ended April 2, 2011
Pro forma net sales	\$487,897

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Pro forma net income	\$32,623
Pro forma basic earnings per share	\$0.57
Pro forma diluted earnings per share	\$0.56

7

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

NOTE 4 – ACCUMULATED OTHER COMPREHENSIVE INCOME (LOSS):

The components of accumulated other comprehensive income (loss) consisted of the following:

(dollars in thousands)	March 31, 2012	December 31, 2011	April 2, 2011
Cumulative foreign currency translation adjustments	\$(1,929	) \$(3,124	) \$—
Pension/post-retirement liability adjustment	(8,158	) (8,158	) (1,890
Total accumulated other comprehensive loss	\$(10,087	) \$(11,282	) \$(1,890

NOTE 5 – LONG-TERM DEBT:

Long-term debt consisted of the following:

(dollars in thousands)	March 31, 2012	December 31, 2011	April 2, 2011
Revolving credit facility	\$236,000	\$236,000	\$236,000
Current maturities	—	—	—
Total long-term debt	\$236,000	\$236,000	\$236,000

On October 15, 2010, the Company entered into a \$375 million (\$130 million sub-limit for letters of credit and a swing line sub-limit of \$40 million) revolving credit facility with Bank of America as sole lead arranger and administrative agent, JP Morgan Chase Bank as syndication agent, and other financial institutions. This revolving credit facility was immediately drawn upon to pay off the Company's former term loan of \$232.2 million and pay transaction fees and expenses of \$3.8 million, leaving approximately \$130 million available under the revolver for future borrowings (net of letters of credit of approximately \$8.6 million). In connection with the repayment of the Company's former term loan, in the fourth quarter of fiscal 2010 the Company wrote off approximately \$1.2 million in unamortized debt issuance costs. In addition, in connection with the revolving credit facility, the Company recorded \$3.5 million of debt issuance costs to be amortized over the term of the revolving credit facility (five years). On December 22, 2011, the Company and lenders amended and restated the revolving credit facility to, among other things, provide a U.S. dollar revolving facility of \$340 million (\$130 million sub-limit for letters of credit and a swing line sub-limit of \$40 million) and a \$35 million multicurrency revolving facility (\$15 million sub-limit for letters of credit and a swing line sub-limit of \$5 million), which is available for borrowings by either TWCC or our Canadian subsidiary, in U.S. dollars or Canadian dollars. The term of the revolving credit facility expires October 15, 2015. At March 31, 2012, we had approximately \$236.0 million in revolver borrowings (fair value approximates book value), exclusive of \$14.5 million of outstanding letters of credit, at an effective interest rate of 2.49%.

The revolving credit facility provides for two pricing options for U.S. dollar facility revolving loans: (i) revolving loans on which interest is payable quarterly at a base rate equal to the highest of (x) the Federal Funds Rate plus ½ of 1%, (y) the rate of interest in effect for such day as publicly announced from time to time by Bank of America, N.A. as its prime rate, or (z) the Eurodollar Rate plus 1%, plus, in each case, an applicable margin initially equal to 1.25%, which may be adjusted based upon a leverage-based pricing grid ranging from 1.00% to 1.50% and (ii) revolving loans on which interest accrues for one, two, three, six or if, generally available, nine or twelve month interest periods (but is payable not less frequently than every three months) at a rate of interest per annum equal to an adjusted British Bankers Association LIBOR rate, plus an applicable margin initially equal to 2.25%, which may be adjusted based

upon a leverage-based pricing grid ranging from 2.00% to 2.50%.

The revolving credit facility also provides for two pricing options for multicurrency facility revolving loans denominated in U.S. dollars: (i) revolving loans on which interest is payable quarterly at a base rate equal to the highest of (x) the Federal Funds Rate plus  $\frac{1}{2}$  of 1%, (y) the rate of interest in effect for such day as publicly announced from time to time by Bank of America, N.A., Canada Branch in Toronto as its reference rate for loans in U.S. dollars to its Canadian borrowers, or (z) the Eurodollar Rate plus 1%, plus, in each case, an applicable margin initially equal to 1.25%, which may be adjusted based upon a leverage-based pricing grid ranging from 1.00% to 1.50% and (ii) revolving loans on which interest accrues for one, two, three, six or if, generally available, nine or twelve month interest periods (but is payable not less frequently than every three months) at a rate of interest per annum equal to an adjusted British Bankers Association LIBOR rate, plus an applicable margin initially equal to 2.25%, which may be adjusted based upon a leverage-based pricing grid ranging from 2.00% to 2.50%.



CARTER'S, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(unaudited)

NOTE 5 – LONG-TERM DEBT: (Continued)

In addition, the revolving credit facility provides for two pricing options for multicurrency facility revolving loans denominated in Canadian dollars: (i) revolving loans on which interest is payable quarterly at a base rate equal to the highest of (x) the rate of interest in effect for such day as publicly announced from time to time by Bank of America, N.A., Canada Branch in Toronto as its prime rate for loans in Canadian Dollars to Canadian Borrowers and (y) the rate of interest in effect for such day for Canadian dollar bankers' acceptances having a term of one month that appears on the Reuters Screen CDOR Page plus ½ of 1%, plus, in each case, an applicable margin initially equal to 1.25%, which may be adjusted based upon a leverage-based pricing grid ranging from 1.00% to 1.50%, and (ii) revolving loans on which interest accrues for one, two, three, six or if, generally available, nine or twelve month interest periods (but is payable not less frequently than every three months) at a rate of interest per annum equal to an adjusted British Bankers Association LIBOR rate, plus an applicable margin initially equal to 2.25%, which may be adjusted based upon a leverage-based pricing grid ranging from 2.00% to 2.50%.

Amounts outstanding under the revolving credit facility currently accrue interest at a LIBOR rate plus 2.25%.

The revolving credit facility contains and defines financial covenants, including a lease adjusted leverage ratio (defined as, with certain adjustments, the ratio of the Company's consolidated indebtedness plus six times rent expense to consolidated net income before interest, taxes, depreciation, amortization, and rent expense ("EBITDAR")) to exceed (x) if such period ends on or before December 31, 2014, 3.75:1.00 and (y) if such period ends after December 31, 2014, 3.50:1.00; and consolidated fixed charge coverage ratio (defined as, with certain adjustments, the ratio of consolidated EBITDAR to consolidated fixed charges (defined as interest plus rent expense)), for any such period to be less than 2.75:1.00. As of March 31, 2012, the Company believes it was in compliance with its financial debt covenants.

Provisions in our senior credit facility currently restrict the ability of our operating subsidiary, TWCC, from paying cash dividends to our parent company, Carter's, Inc., in excess of \$15.0 million unless TWCC and its consolidated subsidiaries meet certain leverage ratio and minimum availability requirements under the credit facility, which materially restricts Carter's, Inc. from paying cash dividends on our common stock. We do not anticipate paying cash dividends on our common stock in the foreseeable future but intend to retain future earnings, if any, for reinvestment in the future operation and expansion of our business and related development activities. Any future decision to pay cash dividends will be at the discretion of our Board of Directors and will depend upon our financial condition, results of operations, terms of financing arrangements, capital requirements, and any other factors as our Board of Directors deems relevant.

NOTE 6 – GOODWILL AND OTHER INTANGIBLE ASSETS:

In connection with the Acquisition, the Company recorded estimates of goodwill and other intangible assets including a Bonnie Togs tradename and non-compete agreements for certain executives of Bonnie Togs, in accordance with accounting guidance on business combinations.

Goodwill as of March 31, 2012, represents the excess of the cost of the acquisition of Carter's, Inc., which was consummated on August 15, 2001, and the acquisition of Bonnie Togs, which was consummated on June 30, 2011, over the fair value of the net assets acquired. Our goodwill is not deductible for tax purposes. The OshKosh tradename

was recorded in connection with the acquisition of OshKosh on July 14, 2005 and adjusted in fiscal 2007 to reflect the impairment of the value. Our Carter's and Bonnie Togs goodwill and Carter's and OshKosh tradenames are deemed to have indefinite lives and are not being amortized. The Bonnie Togs tradename and non-compete agreements for certain executives have definite lives and are being amortized over two and four years, respectively.

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

## NOTE 6 – GOODWILL AND OTHER INTANGIBLE ASSETS: (Continued)

The Company's intangible assets were as follows:

(dollars in thousands)	Weighted-average useful life	March 31, 2012			December 31, 2011		
		Gross amount	Accumulated amortization	Net amount	Gross amount	Accumulated amortization	Net amount
Carter's goodwill (1)	Indefinite	\$ 136,570	\$—	\$ 136,570	\$ 136,570	\$—	\$ 136,570
Bonnie Togs goodwill (2)	Indefinite	\$ 53,126	\$—	\$ 53,126	\$ 52,109	\$—	\$ 52,109
Carter's tradename	Indefinite	\$ 220,233	\$—	\$ 220,233	\$ 220,233	\$—	\$ 220,233
OshKosh tradename	Indefinite	\$ 85,500	\$—	\$ 85,500	\$ 85,500	\$—	\$ 85,500
Bonnie Togs tradename	2 years	\$ 376	\$ 225	\$ 151	\$ 592	\$ 150	\$ 442
Non-compete agreements	4 years	\$ 300	\$ 56	\$ 244	\$ 295	\$ 37	\$ 258

## April 2, 2011

(dollars in thousands)	Weighted-average useful life	Gross amount	Accumulated amortization	Net amount
Carter's goodwill (1)	Indefinite	\$ 136,570	\$—	\$ 136,570
Carter's tradename	Indefinite	\$ 220,233	\$—	\$ 220,233
OshKosh tradename	Indefinite	\$ 85,500	\$—	\$ 85,500

(1) \$45.9 million of which relates to the Carter's wholesale segment, \$82.0 million of which relates to the Carter's retail segment, and \$8.6 million of which relates to the international segment.

(2) Relates to the international segment.

The following is a reconciliation of Bonnie Togs intangible assets:

(dollars in thousands)	Bonnie Togs Goodwill	Bonnie Togs Tradename	Non-compete agreements
Gross Balance at December 31, 2011	\$ 52,109	\$ 592	\$ 295
Purchase accounting adjustments	—	—	—
Foreign currency exchange adjustments	1,017	9	5
Gross Balance at March 31, 2012	\$ 53,126	\$ 601	\$ 300

Amortization expense for intangible assets subject to amortization was approximately \$0.1 million for the three-month period ended March 31, 2012.

NOTE 7 – INCOME TAXES:

The Company and its subsidiaries file income tax returns in the United States and in various states and local jurisdictions. The Company's Canadian subsidiary, will file income tax returns in Canada and various Canadian provinces. The Internal Revenue Service completed its income tax audit for fiscal 2009 during fiscal 2011. In most cases, the Company is no longer subject to state and local tax authority examinations for years prior to fiscal 2007.

As of March 31, 2012, the Company had gross unrecognized tax benefits of approximately \$8.9 million, \$6.2 million of which, if ultimately recognized, will impact the Company's effective tax rate in the period settled. The Company has recorded tax positions for which the ultimate deductibility is highly certain, but for which there is uncertainty about the timing of such deductions. Because of deferred tax accounting, changes in the timing of these deductions would not impact the annual effective tax rate, but would accelerate the payment of cash to the taxing authorities.

CARTER'S, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(unaudited)

## NOTE 7 – INCOME TAXES: (Continued)

Included in the reserves for unrecognized tax benefits are approximately \$2.0 million of reserves for which the statute of limitations is expected to expire within the next fiscal year. If these tax benefits are ultimately recognized, such recognition, net of federal income taxes, may impact our annual effective tax rate for fiscal 2012 and the effective 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. During the first quarter of fiscal 2012 and 2011, the Company recognized interest expense on uncertain tax positions of approximately \$0.1 million. The Company had approximately \$0.6 million, \$0.5 million, and \$0.7 million of interest accrued as of March 31, 2012, December 31, 2011, and April 2, 2011, respectively.

## NOTE 8 – FAIR VALUE MEASUREMENTS:

The Company accounts for its fair value measurements in accordance with accounting guidance 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 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:

(dollars in millions)	March 31, 2012			December 31, 2011			April 2, 2011		
	Level 1	Level 2	Level 3	Level 1	Level 2	Level 3	Level 1	Level 2	Level 3
<b>Assets</b>									
Investments	\$50.2	\$—	\$—	\$50.2	\$—	\$—	\$175.4	\$—	\$—
Foreign exchange forward contracts	\$—	\$—	\$—	\$0.6	\$—	\$—	\$—	\$—	\$—
<b>Liabilities</b>									
Foreign exchange forward contracts	\$0.1	\$—	\$—	\$—	\$—	\$—	\$—	\$—	\$—
Revolving credit facility	\$236.0	\$—	\$—	\$236.0	\$—	\$—	\$236.0	\$—	\$—
Contingent consideration	\$—	\$—	\$26.8	\$—	\$—	\$25.6	\$—	\$—	\$—

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

NOTE 8 – FAIR VALUE MEASUREMENTS: (Continued)

The following summarizes the significant unobservable inputs for our Level 3 fair value measurements at March 31, 2012:

(dollars in millions)	Fair Value	Valuation technique	Unobservable inputs	Amount	
Contingent consideration	\$26.8	Discounted cash flow	Estimated contingent consideration payment	\$35	
			Discount rate	18	%
			Probability assumption	100	%

At March 31, 2012 and December 31, 2011, we had approximately \$50.2 million of cash invested in money market deposit accounts. At April 2, 2011, we had approximately \$50.4 million of cash invested in money market deposit accounts and \$125.0 million in U.S. Treasury bills.

As of March 31, 2012, December 31, 2011, and April 2, 2011, the fair value of the Company's outstanding borrowings under the revolving credit facility of \$236.0 million approximates book value.

In connection with the Acquisition, the Company acquired open forward foreign exchange contracts which were undesignated hedges used to reduce its risk from cash flows associated with U.S. dollar denominated inventory purchases. As part of its overall strategy to manage the level of exposure to the risk of foreign currency exchange rate fluctuations, primarily exposure to changes in the value of the U.S. dollar in relation to the Canadian dollar, the Company hedges a portion of its foreign currency exposures anticipated over the ensuing twelve-month period. The Company uses foreign exchange contracts that generally have maturities of up to 12 months to provide continuing coverage throughout the hedging period.

As of March 31, 2012, the Company had contracts for the purchase of \$18.5 million of U.S. dollars at fixed rates. The fair value of these forward contracts was a liability of \$0.1 million. The Company accounts for these foreign exchange contracts as undesignated positions in accordance with accounting standards on derivatives and hedging. As such, these positions are marked to fair value through earnings at each reporting date.

During the first quarter of fiscal 2012, the Company also recorded a \$0.6 million loss on the mark-to-market of open foreign currency exchange contracts and a \$0.3 million gain on the remeasurement of Bonnie Togs' foreign denominated payables.

The fair value of the discounted contingent consideration liability was approximately \$26.8 million as of March 31, 2012 and \$25.6 million as of December 31, 2011. The \$1.2 million change in fair value during the first quarter of fiscal 2012, reflects accretion expense of approximately \$0.7 million and \$0.5 million in accumulated other comprehensive income reflecting a unfavorable foreign currency translation adjustment. The Company determined the fair value of the contingent consideration based upon a probability-weighted discounted cash flow analysis. Changes in the estimated earnout payment, discount rate, or probability assumptions used could materially impact the fair value of the contingent consideration.



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

## NOTE 8 – FAIR VALUE MEASUREMENTS: (Continued)

The fair value of our derivative instruments in our accompanying unaudited condensed consolidated balance sheets were as follows:

(dollars in millions)	Asset Derivatives		Liability Derivatives	
	Balance sheet location	Fair value	Balance sheet location	Fair value
March 31, 2012	Prepaid expenses and other current assets	\$—	Other current liabilities	\$0.1
December 31, 2011	Prepaid expenses and other current assets	\$0.6	Other current liabilities	\$—
April 2, 2011	Prepaid expenses and other current assets	\$—	Other current liabilities	\$—

The effect of undesignated derivative instruments on our accompanying unaudited condensed consolidated financial statements was as follows:

(dollars in thousands)	Loss recognized in earnings	
	For the three-month periods ended March 31, 2012	April 2, 2011
Foreign exchange forward contracts	\$600	\$—

## NOTE 9 – EMPLOYEE BENEFIT PLANS:

Under a defined benefit plan frozen in 1991, we offer a comprehensive post-retirement medical plan to current and certain future retirees and their spouses until they become eligible for Medicare or a Medicare Supplement Plan. We also offer life insurance to current and certain future retirees. Employee contributions are required as a condition of participation for both medical benefits and life insurance and our liabilities are net of these expected employee contributions. See Note 8 “Employee Benefit Plans” to our audited consolidated financial statements in our most recently filed Annual Report on Form 10-K for further information.

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

(dollars in thousands)	For the three-month periods ended



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	March 31, 2012	April 2, 2011
Service cost – benefits attributed to service during the period	\$17	\$18
Interest cost on accumulated post-retirement benefit obligation	53	106
Amortization net actuarial gain	(18	) (5
Total net periodic post-retirement benefit cost	\$52	\$119

13

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

## NOTE 9 – EMPLOYEE BENEFIT PLANS: (Continued)

We have an obligation under a defined benefit plan covering certain former officers and their spouses. The component of pension expense charged to operations is as follows:

(dollars in thousands)	For the three-month periods ended	
	March 31, 2012	April 2, 2011
Interest cost on accumulated pension benefit obligation	\$20	\$8

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

(dollars in thousands)	For the three-month periods ended	
	March 31, 2012	April 2, 2011
Interest cost on accumulated pension benefit obligation	\$597	\$614
Expected return on assets	(713	) (778
Amortization of actuarial loss	178	—
Total net periodic pension expense (benefit)	\$62	\$(164

## NOTE 10 – COMMON STOCK:

During fiscal 2007, the Company's Board of Directors approved a share repurchase authorization, pursuant to which the Company was authorized to purchase up to \$100 million of its outstanding common shares. During fiscal 2010, the Company's Board of Directors approved a share repurchase authorization, pursuant to which the Company is authorized to purchase up to an additional \$100 million of its outstanding common shares. As of August 13, 2010, the Company had repurchased outstanding shares in the amount totaling the entire \$100 million authorized by the Board of Directors on February 16, 2007.

The Company did not repurchase any shares of its common stock during the first quarters of fiscal 2012 and 2011 pursuant to any repurchase authorization. Since inception of the repurchase program and through the first quarter of fiscal 2012, the Company repurchased and retired 6,658,410 shares, or approximately \$141.1 million, of its common stock at an average price of \$21.19 per share. We have reduced common stock by the par value of such shares repurchased and have deducted the remaining excess repurchase price over par value from additional paid-in capital. Future repurchases may occur from time to time in the open market, in negotiated transactions, or otherwise. The timing and amount of any repurchases will be determined by the Company's management, based on its evaluation of market conditions, share price, other investment priorities, and other factors.

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

## NOTE 11 – STOCK-BASED COMPENSATION:

Under the Company's Amended and Restated Equity Incentive Plan (the "Plan"), the compensation committee of our Board of Directors may award incentive stock options (ISOs and non-ISOs), stock appreciation rights (SARs), restricted stock, unrestricted stock, stock deliverable on a deferred basis (including restricted stock units), and performance-based stock awards. 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 three-month period ended March 31, 2012.

	Assumptions	
Volatility	34.82	%
Risk-free interest rate	1.38	%
Expected term (years)	5.9	
Dividend yield	—	
Grant-date fair value	\$15.09	

The fair value of restricted stock and restricted stock units (collectively, "restricted stock awards") 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 awards activity during the three-month period ended March 31, 2012:

	Stock options	Restricted stock awards
Outstanding, December 31, 2011	1,992,700	617,401
Granted	343,600	323,800
Exercised	(81,425)	) —
Vested restricted stock	—	(133,207)
Forfeited	(1,800)	) (900)
Expired	—	—
Outstanding, March 31, 2012	2,253,075	807,094
Exercisable, March 31, 2012	1,216,550	—

During the three-month period ended March 31, 2012, we granted 343,600 stock options with a weighted-average Black-Scholes fair value of \$15.09 per share and a weighted-average exercise price of \$42.61 per share. In connection with this grant, we recognized approximately \$129,000 in stock-based compensation expense during the three-month period ended March 31, 2012.

During the three-month period ended March 31, 2012, we granted 323,800 restricted stock awards with a weighted-average exercise price of \$42.61 per share. In connection with these grants, we recognized approximately

\$373,000 in stock-based compensation expense during the three-month period ended March 31, 2012.

During the three-month period ended March 31, 2012, the Company granted our Chief Executive Officer 100,000 performance-based restricted shares at a fair market value of \$42.61 per share. In addition, the Company granted our other executive officers 52,000 performance-based restricted shares at a fair market value of \$42.61 per share. Vesting of these shares is contingent upon meeting specific performance targets and would occur, if ever, in fiscal 2015. Currently, the Company believes that these targets will be achieved and, accordingly, we will continue to record compensation expense until the restricted shares vest or the Company's assessment of achievement of the performance criteria changes.

CARTER'S, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(unaudited)

## NOTE 11 – STOCK-BASED COMPENSATION: (Continued)

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

(dollars in thousands)	Stock options	Restricted stock awards	Total
2012 (period from April 1 through December 29, 2012)	\$3,184	\$6,241	\$9,425
2013	3,588	7,332	\$10,920
2014	2,612	6,267	\$8,879
2015	1,448	3,370	\$4,818
Total	\$10,832	\$23,210	\$34,042

## NOTE 12 – SEGMENT INFORMATION:

We report segment information in accordance with accounting guidance on segment reporting, which requires segment information to be disclosed based upon a “management approach.” The management approach refers to the internal reporting that is used by management for making operating decisions and assessing the performance of our reportable segments. We report our corporate expenses and acquisition-related expenses separately as they are not included in the internal measures of segment operating performance used by the Company in order to measure the underlying performance of our reportable segments.

As a result of the Acquisition, the Company realigned certain of its reportable segments. Effective October 1, 2011, the Company's reportable segments include Carter's retail, Carter's wholesale, OshKosh retail, OshKosh wholesale, and international. Prior periods presented have been recast to conform to the current year presentation.

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

## NOTE 12 – SEGMENT INFORMATION: (Continued)

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

(dollars in thousands)	For the three-month periods ended		April 2, 2011	% of Total		
	March 31, 2012	% of Total				
Net sales:						
Carter's Wholesale	\$249,485	45.2	% \$241,619	51.5		%
Carter's Retail (a)	177,204	32.1	% 137,862	29.4		%
Total Carter's	426,689	77.3	% 379,481	80.9		%
OshKosh Retail (a)	57,988	10.5	% 53,994	11.5		%
OshKosh Wholesale	20,274	3.7	% 20,076	4.3		%
Total OshKosh	78,262	14.2	% 74,070	15.8		%
International (b)	46,711	8.5	% 15,449	3.3		%
Total net sales	\$551,662	100.0	% \$469,000	100.0		%
Operating income (loss):						
			% of segment net sales		% of segment net sales	
Carter's Wholesale	\$40,271	16.1	% \$37,142	15.4		%
Carter's Retail (a)	30,534	17.2	% 26,664	19.3		%
Total Carter's	70,805	16.6	% 63,806	16.8		%
OshKosh Retail (a)	(7,459 )	(12.9 )	% (5,402 )	(10.0 )		%
OshKosh Wholesale	120	0.6	% 1,563	7.8		%
Total OshKosh	(7,339 )	(9.4 )	% (3,839 )	(5.2 )		%
International (b)	7,467	(c) 16.0	% 4,978	32.2		%
Total segment operating income	70,933	12.9	% 64,945	13.8		%
Corporate expenses (d)	(17,133 )	(e) (3.1 )	% (11,311 )	(f) (2.4 )		%
Total operating income	\$53,800	9.8	% \$53,634	11.4		%

(a) Includes eCommerce results.

(b) Net sales include international retail and wholesale sales. Operating income includes international licensing income.

(c) Includes a \$0.7 million charge associated with the revaluation of the Company's contingent consideration.

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

Includes \$1.1 million in facility closure-related costs related to closure of a distribution facility located in (e) Hogansville, Georgia. These costs include approximately \$1.0 million of severance-related charges and \$0.1 million of accelerated depreciation (recorded in selling, general, and administrative expenses).

(f) Includes \$1.0 million of professional service fees associated with the Acquisition for the three-month period ended April 2, 2011.

In the first quarters of fiscal 2012 and 2011, no customers accounted for 10% or more of our consolidated net sales.

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

## NOTE 13 – EARNINGS PER SHARE:

The Company calculates basic and diluted net income per common share in accordance with accounting guidance which requires earnings per share to be calculated pursuant to the two-class method for unvested share-based payment awards that contain non-forfeitable rights to dividends or dividend equivalents (whether paid or unpaid).

Basic net income per share is calculated by dividing net income for the period by the weighted-average common shares outstanding for the period. Diluted net income per share includes the effect of dilutive instruments, such as stock options and restricted stock awards, 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 is a reconciliation of basic common shares outstanding to diluted common and common equivalent shares outstanding:

	For the three-month periods ended	
	March 31, 2012	April 2, 2011
Weighted-average number of common and common equivalent shares outstanding:		
Basic number of common shares outstanding	58,057,275	57,049,228
Dilutive effect of unvested restricted stock	178,708	141,851
Dilutive effect of stock options	604,735	694,932
Diluted number of common and common equivalent shares outstanding	58,840,718	57,886,011
Basic net income per common share:		
Net income	\$32,275,000	\$32,123,000
Income allocated to participating securities	(442,525	) (364,477
Net income available to common shareholders	\$31,832,475	\$31,758,523
Basic net income per common share	\$0.55	\$0.56
Diluted net income per common share:		
Net income	\$32,275,000	\$32,123,000
Income allocated to participating securities	(438,025	) (360,140
Net income available to common shareholders	\$31,836,975	\$31,762,860
Diluted net income per common share	\$0.54	\$0.55

For the three-month periods ended March 31, 2012 and April 2, 2011, anti-dilutive and performance-based restricted shares of 610,950 and 945,050, respectively, were excluded from the computations of diluted earnings per share.



CARTER'S, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(unaudited)

NOTE 14 – FACILITY CLOSURE:

Consistent with the Company's strategy to strengthen our distribution capabilities, we decided to close our Hogansville, Georgia facility in 2013 and will open a new, larger multi-channel distribution facility in Braselton, Georgia in June 2012. On March 14, 2012, the Company announced to affected employees its plan to close the Hogansville facility. Approximately 210 employees are affected by this closure.

In conjunction with the plan to close the Hogansville distribution facility, the Company recorded approximately \$1.1 million in closing-related costs during the first quarter of fiscal 2012, consisting of severance of \$1.0 million and \$0.1 million of accelerated depreciation (included in selling, general, and administrative expenses). As of March 31, 2012, there was approximately \$1.1 million of restructuring reserves included in other long-term liabilities on the accompanying unaudited condensed consolidated balance sheet related to this closure. The Company expects to incur additional closure-related charges of approximately \$1.8 million for one-time termination benefits (\$1.1 million in fiscal 2012 and \$0.7 million in fiscal 2013) and \$1.6 million in accelerated depreciation (\$1.1 million in fiscal 2012 and \$0.5 million in fiscal 2013), and other closure costs of \$1.0 million in fiscal 2013. The salvage value of this facility is estimated to be \$2.0 million.

When the Company determined that it was probable that the Hogansville facility would be closed, an impairment test was performed under the "held and used" model. We determined that the assets were not impaired; however, the estimated useful lives of the assets were reassessed and depreciation was accelerated over the expected remaining shutdown period.

NOTE 15 – RECENT ACCOUNTING PRONOUNCEMENTS:

In May 2011, the Financial Accounting Standards Board ("FASB") issued updated accounting guidance related to fair value measurements and disclosures that result in common fair value measurements and disclosures between GAAP and International Financial Reporting Standards. This guidance includes amendments that clarify the intent about the application of existing fair value measurements and disclosures, while other amendments change a principle or requirement for fair value measurements or disclosures. This guidance is effective for interim and annual periods beginning after December 15, 2011. The Company has included the required disclosures within Note 8, Fair Value Measurements.

In June 2011, the FASB issued guidance to amend the presentation of comprehensive income to allow an entity the option to present the total of comprehensive income, the components of net income, and the components of other comprehensive income either in a single continuous statement of comprehensive income or in two separate but consecutive statements. In both instances, an entity is required to present each component of net income along with total net income, each component of other comprehensive income along with a total for other comprehensive income, and a total amount for comprehensive income. The guidance eliminates the option to present the components of other comprehensive income as part of the statement of changes in stockholders' equity. In December 2011, the FASB issued guidance to indefinitely defer provisions requiring reclassification adjustments out of other comprehensive income to be presented on the face of the financial statements. The other portions of the original guidance remain unchanged. These standards are effective for interim and annual periods beginning after December 15, 2011, and are to be applied retrospectively. The Company has included such disclosures within this quarterly report.

In September 2011, the FASB issued new guidance on testing goodwill for impairment. This guidance gives companies the option to perform a qualitative assessment to first assess whether the fair value of a reporting unit is less than its carrying amount. If an entity determines it is not more likely than not that the fair value of the reporting unit is less than its carrying amount, then performing the two-step impairment test is unnecessary. This guidance is effective for fiscal years beginning after December 15, 2011. The Company does not believe the adoption of this guidance will have a material impact on its consolidated financial statements.

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

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

Our fiscal year ends on the Saturday, in December or January, nearest the last day of December. The accompanying unaudited condensed consolidated financial statements for the first quarter of fiscal 2012 reflect our financial position as of March 31, 2012. The first quarter of fiscal 2011 ended on April 2, 2011.

On June 30, 2011, we acquired Bonnie Togs, a Canadian children's apparel retailer and an international licensee. Specifically, the Company purchased all of the outstanding shares of capital stock of Bonnie Togs (the "Acquisition") for total consideration of up to CAD \$95 million, of which USD \$61.2 million was paid in cash at closing. The sellers may also be paid contingent consideration ranging from zero to CAD \$35 million if the Canadian business meets certain earnings targets for the period beginning July 1, 2011 and ending on June 27, 2015. Sellers may receive a portion of the contingent consideration of up to CAD \$25 million if interim earnings targets are met through June 2013 and June 2014, respectively. Any such payments are not recoverable by the Company in the event of any failure to meet overall targets.

As of March 31, 2012, the Company had a discounted contingent consideration liability of approximately \$26.8 million based upon the high probability that Bonnie Togs will attain its earnings targets and is included in other long-term liabilities on the accompanying audited consolidated balance sheet. The fair value of the discounted contingent consideration liability as of December 31, 2011 was approximately \$25.6 million. The \$1.2 million change in the fair value of the liability is reflected as \$0.7 million in accretion expense and \$0.5 million in other comprehensive income resulting from an unfavorable foreign currency translation adjustment. The Company determined the fair value of the contingent consideration based upon a probability-weighted discounted cash flow analysis. The Company will continue to revalue the contingent consideration at each reporting date.

As a result of the Acquisition, the Company realigned certain of its reportable segments. Effective October 1, 2011, the Company's reportable segments include Carter's retail, Carter's wholesale, OshKosh retail, OshKosh wholesale, and international. Prior periods presented have been recast to conform to the current year presentation.

In connection with the Acquisition, we acquired certain definite-lived intangible assets comprised of a Bonnie Togs tradename and non-compete agreements which resulted in amortization expense of \$0.1 million in the first quarter of fiscal 2012.

Our unaudited condensed consolidated statements of operations for the three-month period ended April 2, 2011 do not include the results of Bonnie Togs.

In conjunction with the plan to close the Hogansville, Georgia distribution facility, the Company recorded approximately \$1.1 million in closing-related costs during first quarter of fiscal 2012, consisting of severance of \$1.0 million and \$0.1 million of accelerated depreciation (included in selling, general, and administrative expenses). As of March 31, 2012, there was approximately \$1.1 million of restructuring reserves included in other long-term liabilities on the accompanying unaudited condensed consolidated balance sheet related to this closure. The Company expects to incur additional closure-related charges of approximately \$1.8 million for one-time termination benefits (\$1.1 million in fiscal 2012 and \$0.7 million in fiscal 2013) and \$1.6 million in accelerated depreciation (\$1.1 million in fiscal 2012 and \$0.5 million in fiscal 2013), and other closure costs of \$1.0 million in fiscal 2013. The salvage value of this facility is estimated to be \$2.0 million.



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

## RESULTS OF OPERATIONS

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

	Three-month periods ended			
	March 31, 2012	April 2, 2011		
Net sales				
Carter's Wholesale	45.2	% 51.5		%
Carter's Retail	32.1	% 29.4		%
Total Carter's	77.3	% 80.9		%
OshKosh Retail	10.5	% 11.5		%
OshKosh Wholesale	3.7	% 4.3		%
Total OshKosh	14.2	% 15.8		%
International	8.5	% 3.3		%
Consolidated net sales	100.0	% 100.0		%
Cost of goods sold	64.7	% 66.3		%
Gross profit	35.3	% 33.7		%
Selling, general, and administrative expenses	27.1	% 24.3		%
Royalty income	(1.6)	)% (2.0)		)%
Operating income	9.8	% 11.4		%
Interest expense, net	0.4	% 0.4		%
Foreign currency loss	0.1	% —		%
Income before income taxes	9.3	% 11.0		%
Provision for income taxes	3.4	% 4.2		%
Net income	5.9	% 6.8		%
Number of retail stores at end of period:				
Carter's	372	316		
OshKosh	168	179		
International	69	—		
Total	609	495		

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

Three-month period ended March 31, 2012 compared to the three-month period ended April 2, 2011

CONSOLIDATED NET SALES

In the first quarter of fiscal 2012, consolidated net sales increased \$82.7 million, or 17.6%, to \$551.7 million and primarily reflect the acquisition of Bonnie Togs and growth in all of our segments.

(dollars in thousands)	For the three-month periods ended					
	March 31, 2012	% of Total	April 2, 2011	% of Total		
Net sales:						
Carter's Wholesale	\$249,485	45.2	% \$241,619	51.5	%	
Carter's Retail	177,204	32.1	% 137,862	29.4	%	
Total Carter's	426,689	77.3	% 379,481	80.9	%	
OshKosh Retail	57,988	10.5	% 53,994	11.5	%	
OshKosh Wholesale	20,274	3.7	% 20,076	4.3	%	
Total OshKosh	78,262	14.2	% 74,070	15.8	%	
International	46,711	8.5	% 15,449	3.3	%	
Total net sales	\$551,662	100.0	% \$469,000	100.0	%	

CARTER'S WHOLESALE SALES

Carter's wholesale sales increased \$7.9 million, or 3.3%, in the first quarter of fiscal 2012 to \$249.5 million. This growth was driven primarily by an 11% increase in average price per unit, partially offset by a 7% decrease in units shipped as compared to the first quarter of fiscal 2011. The increase in average price per unit was driven by price increases on our product offerings sold within this segment and lower levels of off-price channel sales. The decrease in units shipped was primarily due to a decrease in shipments in the off-price channel, partially offset by continued strong demand for our Child of Mine product offerings.

CARTER'S RETAIL SALES

Carter's retail store sales increased \$39.3 million, or 28.5%, in the first quarter of fiscal 2012 to \$177.2 million. The increase was driven by incremental sales of \$17.8 million generated by new store openings and \$14.1 million generated by eCommerce sales, and a comparable store sales increase of \$8.5 million, or 6.7%, partially offset by the impact of store closings of \$1.0 million. On a comparable store basis, average prices increased 11.4% as a result of planned price increases, units per transaction decreased 6.6%, and transactions increased 2.6% due primarily to strong product performance across all categories.

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

During the first quarter of fiscal 2012, the Company opened 16 Carter's retail stores and closed three stores. There were a total of 372 Carter's retail stores as of March 31, 2012. In total, the Company plans to open approximately 63 and close seven Carter's retail stores during fiscal 2012.

#### OSHKOSH RETAIL SALES

OshKosh retail store sales increased \$4.0 million, or 7.4%, in the first quarter of fiscal 2012 to \$58.0 million. The increase reflects incremental sales of \$3.5 million generated by eCommerce sales, a comparable store sales increase of \$2.3 million, or

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

4.7%, and \$0.5 million generated by new store openings, partially offset by the impact of store closings of \$2.2 million. On a comparable store basis, average prices increased 11.7% as a result of planned price increases, units per transaction decreased 6.0%, and transactions decreased 0.3%.

During the first quarter of fiscal 2012, the Company closed two OshKosh retail stores. There were a total of 168 OshKosh retail stores as of March 31, 2012. In total, the Company plans to open approximately seven and close 13 OshKosh retail stores during fiscal 2012.

#### OSHKOSH WHOLESALE SALES

OshKosh wholesale sales increased \$0.2 million, or 1.0%, in the first quarter of fiscal 2012 to \$20.3 million. This increase reflects a 20% increase in average price per unit, partially offset by a 16% decrease in units shipped as compared to the first quarter of fiscal 2011.

The increases in average price per unit primarily reflect price increases on our product offerings sold within this segment as compared to the first quarter of fiscal 2011. The decrease in units shipped during the first quarter of fiscal 2012 was due to a decrease in shipments in the off-price channel.

#### INTERNATIONAL SALES

International sales increased \$31.3 million, or 202.4%, in the first quarter of fiscal 2012 to \$46.7 million. The increase reflects a full quarter of sales from our Canadian operations and higher international wholesale sales driven primarily by expansion with our multi-national customers and growth in South America.

During the first quarter of fiscal 2012, the Company opened four retail stores in Canada. There were a total of 69 retail stores in Canada as of March 31, 2012. In fiscal 2012, the Company plans to open a total of 18 retail stores in Canada and anticipates no store closures.

#### GROSS PROFIT

Our gross profit increased \$36.7 million, or 23.2%, to \$194.7 million in the first quarter of fiscal 2012. Gross margin increased 160 basis points from 33.7% in the first quarter of fiscal 2011 to 35.3% in the first quarter of fiscal 2012. The improvement in gross profit as a percentage of net sales reflects volume growth primarily in our direct to consumer channels and price increases, partially offset by higher product costs of approximately \$35 million in the first quarter of fiscal 2012. The product cost increases are primarily related to increases in cotton prices and labor rates.

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

#### SELLING, GENERAL, AND ADMINISTRATIVE EXPENSES

Selling, general, and administrative expenses in the first quarter of fiscal 2012 increased \$35.9 million, or 31.6%, to \$149.7 million. As a percentage of net sales, selling, general, and administrative expenses increased 280 basis points from 24.3% to 27.1% in the first quarter of fiscal 2012.



The increase in selling, general, and administrative expenses as a percentage of net sales reflects:

\$10.6 million in Bonnie Togs selling, general and administrative expenses;

approximately \$5.2 million in higher provisions for performance-based compensation;

\$1.1 million in closure costs, primarily severance-related costs and accelerated depreciation, associated with the closure of our distribution facility in Hogansville, Georgia; and

\$0.7 million of accretion expense associated with the revaluation of the Bonnie Togs contingent consideration.

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

Partially offsetting these increases were:

a 70 basis points decrease (from 11.9% to 11.2%) in our U.S. retail store expenses as compared to the first quarter of fiscal 2011; and

Approximately \$1.0 million in professional service fees recorded in the first quarter of fiscal 2011 in connection with our Bonnie Togs acquisition.

#### ROYALTY INCOME

We license the use of our Carter's, Just One You, Child of Mine, OshKosh B'gosh, OshKosh, and Genuine Kids from OshKosh brand names. Royalty income from these brands in the first quarter of fiscal 2012 was approximately \$8.8 million (including \$1.8 million of international royalty income), a decrease of \$0.6 million, or 6.0%, as compared to the first quarter of fiscal 2011. The decrease was primarily due to the absence of international royalty income in the first quarter of fiscal 2012 from our former licensee, Bonnie Togs which was acquired in June 2011.

#### OPERATING INCOME

Operating income increased \$0.2 million, or 0.3%, to \$53.8 million in the first quarter of fiscal 2012. The increase in operating income was due to the factors described above.

#### INTEREST EXPENSE, NET

Interest expense in the first quarter of fiscal 2012 increased \$0.1 million, or 5.8%, to \$2.0 million, compared to the first quarter of fiscal 2011. Weighted-average borrowings for the first quarter of fiscal 2012 were comparable at \$236.0 million at an effective interest rate of 3.22%, including amortization of debt issuance costs, as compared to weighted-average borrowings for the first quarter of fiscal 2011 of \$236.0 million at an effective interest rate of 3.24%, including amortization of debt issuance costs.

#### FOREIGN CURRENCY LOSS

During the first quarter of fiscal 2012, the Company recorded \$0.3 million net loss related to our Canadian subsidiary's mark-to-market of open foreign currency exchange contracts and Bonnie Togs' foreign denominated payables.

#### INCOME TAXES

Our effective tax rate was 37.4% for the first quarter of fiscal 2012 as compared to 38.0% for the first quarter of fiscal 2011. The decrease in our effective rate is primarily attributable to our Canadian operations which carry a lower overall effective tax rate.

#### NET INCOME

As a result of the factors described above, our net income for the first quarter of fiscal 2012 increased \$0.2 million, or 0.5%, to \$32.3 million as compared to \$32.1 million in the first quarter of fiscal 2011.



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

FINANCIAL CONDITION, CAPITAL RESOURCES, AND LIQUIDITY

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

Net accounts receivable at March 31, 2012 were \$178.7 million compared to \$160.1 million at April 2, 2011 and \$157.8 million at December 31, 2011. The increase of \$18.6 million, or 11.6%, as compared to April 2, 2011 primarily reflects an increase in sales in the first quarter of fiscal 2012 compared to the first quarter of fiscal 2011 and reflects the incremental receivables associated with Bonnie Togs. Due to the seasonal nature of our operations, the net accounts receivable balance at March 31, 2012 is not comparable to the net accounts receivable balance at December 31, 2011.

Net inventories at March 31, 2012 were \$265.7 million compared to \$217.5 million at April 2, 2011 and \$347.2 million at December 31, 2011. The increase of \$48.2 million, or 22.2%, as compared to April 2, 2011 is primarily due to higher product costs, timing of product launches, the Acquisition, and business growth. Due to the seasonal nature of our operations, net inventories at March 31, 2012 are not comparable to net inventories at December 31, 2011.

Product costs can vary depending on the underlying cost of raw materials, such as cotton and polyester, and the level of labor and transportation costs. A substantial portion of the Company's products utilize cotton based fabrics, the cost of which reached historically high levels in fiscal 2011. Additionally, labor costs have increased across Asia, particularly in China, where the Company currently sources approximately 50% of its products. Furthermore, transportation costs to bring product to the United States have risen due to higher fuel costs and limited capacity in the marketplace. The Company purchases finished goods largely from foreign suppliers and pays its suppliers in U.S. currency. Consequently, the Company's product costs have been adversely impacted by the devaluation of the U.S. dollar relative to foreign currencies. These inflationary and currency risk factors have resulted in higher costs of goods sold and inventory values, and have adversely impacted our profitability and cash flows from operations. We expect that higher product costs will continue to adversely impact our profitability and cash flow through at least the first half of fiscal 2012.

Net cash provided by operating activities for the first quarter of fiscal 2012 was \$82.4 million compared to net cash provided by operating activities of \$9.3 million in the first quarter of fiscal 2011. The increase in operating cash flow primarily reflects favorable changes in net working capital.

We invested \$16.4 million in capital expenditures during the first quarter of fiscal 2012 compared to \$6.8 million during the first quarter of fiscal 2011. We plan to invest approximately \$90 - \$100 million in capital expenditures in fiscal 2012, primarily for U.S. and international retail store openings and remodelings and in expanding our distribution capacity with the addition of the Braselton, Georgia facility.

During fiscal 2007, the Company's Board of Directors approved a share repurchase authorization, pursuant to which the Company was authorized to purchase up to \$100 million of its outstanding common shares. During fiscal 2010, the Company's Board of Directors approved a share repurchase authorization, pursuant to which the Company is authorized to purchase up to an additional \$100 million of its outstanding common shares. As of August 13, 2010, the Company had repurchased outstanding shares in the amount totaling the entire \$100 million authorized by the Board

of Directors on February 16, 2007.

The Company did not repurchase any shares of its common stock during the three-month periods ended March 31, 2012 and April 2, 2011 pursuant to any repurchase authorization other than the shares of common stock from the Company's employees to satisfy tax withholding obligations upon vesting of restricted stock to such employees. Since inception of the repurchase program and through fiscal 2011, the Company repurchased and retired 6,658,410 shares, or approximately \$141.1 million, of its common stock at an average price of \$21.19 per share. We have reduced common stock by the par value of such shares repurchased and have deducted the remaining excess repurchase price over par value from additional paid-in capital. Future repurchases may occur from time to time in the open market, in negotiated transactions, or otherwise. The timing and amount of any repurchases will be determined by the Company's management, based on its evaluation of market conditions, share price, other investment priorities, and other factors.

25

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

On October 15, 2010, the Company entered into a \$375 million (\$130 million sub-limit for letters of credit and a swing line sub-limit of \$40 million) revolving credit facility with Bank of America as sole lead arranger and administrative agent, JP Morgan Chase Bank as syndication agent, and other financial institutions. This revolving credit facility was immediately drawn upon to pay off the Company's former term loan of \$232.2 million and pay transaction fees and expenses of \$3.8 million, leaving approximately \$130 million available under the revolver for future borrowings (net of letters of credit of approximately \$8.6 million). In connection with the repayment of the Company's former term loan, in the fourth quarter of fiscal 2010 the Company wrote off approximately \$1.2 million in unamortized debt issuance costs. In addition, in connection with the revolving credit facility, the Company recorded \$3.5 million of debt issuance costs to be amortized over the term of the revolving credit facility (five years). On December 22, 2011, the Company and lenders amended and restated the revolving credit facility to, among other things, provide a U.S. dollar revolving facility of \$340 million (\$130 million sub-limit for letters of credit and a swing line sub-limit of \$40 million) and a \$35 million multicurrency revolving facility (\$15 million sub-limit for letters of credit and a swing line sub-limit of \$5 million), which is available for borrowings by either TWCC or our Canadian subsidiary, in U.S. dollars or Canadian dollars. The term of the revolving credit facility expires October 15, 2015.

The revolving credit facility provides for two pricing options for U.S. dollar facility revolving loans: (i) revolving loans on which interest is payable quarterly at a base rate equal to the highest of (x) the Federal Funds Rate plus ½ of 1%, (y) the rate of interest in effect for such day as publicly announced from time to time by Bank of America, N.A. as its prime rate, or (z) the Eurodollar Rate plus 1%, plus, in each case, an applicable margin initially equal to 1.25%, which may be adjusted based upon a leverage-based pricing grid ranging from 1.00% to 1.50% and (ii) revolving loans on which interest accrues for one, two, three, six or if, generally available, nine or twelve month interest periods (but is payable not less frequently than every three months) at a rate of interest per annum equal to an adjusted British Bankers Association LIBOR rate, plus an applicable margin initially equal to 2.25%, which may be adjusted based upon a leverage-based pricing grid ranging from 2.00% to 2.50%.

The revolving credit facility provides for two pricing options for multicurrency facility revolving loans denominated in U.S. dollars: (i) revolving loans on which interest is payable quarterly at a base rate equal to the highest of (x) the Federal Funds Rate plus ½ of 1%, (y) the rate of interest in effect for such day as publicly announced from time to time by Bank of America, N.A., Canada Branch in Toronto as its reference rate for loans in U.S. dollars to its Canadian borrowers, or (z) the Eurodollar Rate plus 1%, plus, in each case, an applicable margin initially equal to 1.25%, which may be adjusted based upon a leverage-based pricing grid ranging from 1.00% to 1.50% and (ii) revolving loans on which interest accrues for one, two, three, six or if, generally available, nine or twelve month interest periods (but is payable not less frequently than every three months) at a rate of interest per annum equal to an adjusted British Bankers Association LIBOR rate, plus an applicable margin initially equal to 2.25%, which may be adjusted based upon a leverage-based pricing grid ranging from 2.00% to 2.50%.

The revolving credit facility provides for two pricing options for multicurrency facility revolving loans denominated in Canadian dollars: (i) revolving loans on which interest is payable quarterly at a base rate equal to the highest of (x) the rate of interest in effect for such day as publicly announced from time to time by Bank of America, N.A., Canada Branch in Toronto as its prime rate for loans in Canadian Dollars to Canadian Borrowers and (y) the rate of interest in effect for such day for Canadian dollar bankers' acceptances having a term of one month that appears on the Reuters Screen CDOR Page plus ½ of 1%, plus, in each case, an applicable margin initially equal to 1.25%, which may be adjusted based upon a leverage-based pricing grid ranging from 1.00% to 1.50%, and (iii) revolving loans on which interest accrues for one, two, three, six or if, generally available, nine or twelve month interest periods (but is payable not less frequently than every three months) at a rate of interest per annum equal to an adjusted British Bankers Association LIBOR rate, plus an applicable margin initially equal to 2.25%, which may be adjusted based upon a

leverage-based pricing grid ranging from 2.00% to 2.50%.

Amounts outstanding under the revolving credit facility currently accrue interest at a LIBOR rate plus 2.25%.

The revolving credit facility contains and defines financial covenants, including a lease adjusted leverage ratio (defined as, with certain adjustments, the ratio of the Company's consolidated indebtedness plus six times rent expense to consolidated net income before interest, taxes, depreciation, amortization, and rent expense ("EBITDAR")) to exceed (x) if such period ends on or before December 31, 2014, 3.75:1.00 and (y) if such period ends after December 31, 2014, 3.50:1.00; and consolidated fixed charge coverage ratio (defined as, with certain adjustments, the ratio of consolidated EBITDAR to consolidated fixed charges (defined as interest plus rent expense)), for any such period to be less than 2.75:1.00. As of March 31, 2012, the Company believes it was in compliance with its financial debt covenants.

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

At March 31, 2012, we had approximately \$236.0 million in revolver borrowings, exclusive of \$14.5 million of outstanding letters of credit. Weighted-average borrowings for the first quarter of fiscal 2012 were \$236.0 million at an effective interest rate of 3.22%, including amortization of debt issuance costs, as compared to weighted-average borrowings for the first quarter of fiscal 2011 of \$236.0 million at an effective interest rate of 3.24%, including amortization of debt issuance costs.

Our operating results are subject to risk from interest rate fluctuations on our revolving credit facility, which carries variable interest rates. As of March 31, 2012, our outstanding variable rate debt aggregated approximately \$236.0 million. An increase or decrease of 1% in the applicable rate would increase or decrease our annual interest cost by approximately \$2.4 million and could have an adverse effect on our net income (loss) and cash flow.

On June 30, 2011, Northstar purchased all of the outstanding shares of capital stock of Bonnie Togs for total consideration of up to CAD \$95 million, of which USD \$61.2 million was paid in cash at closing. The sellers may also be paid contingent consideration ranging from zero to CAD \$35 million if the Canadian business meets certain earnings targets for the period beginning July 1, 2011 and ending on June 27, 2015. Sellers may receive a portion of the contingent consideration of up to CAD \$25 million if interim earnings targets are met through June 2013 and June 2014, respectively. Any such payments are not recoverable in the event of any failure to meet overall targets.

As of March 31, 2012, the Company had a discounted contingent consideration liability of approximately \$26.8 million based upon the high probability that Bonnie Togs will attain its earnings targets and is included in other long-term liabilities on the accompanying audited consolidated balance sheet. The fair value of the discounted contingent consideration liability as of December 31, 2011 was approximately \$25.6 million. The \$1.2 million change in the fair value of the liability is reflected as \$0.7 million in accretion expense and \$0.5 million in other comprehensive income resulting from an unfavorable foreign currency translation adjustment. The Company determined the fair value of the contingent consideration based upon a probability-weighted discounted cash flow analysis. The Company will continue to revalue the contingent consideration at each reporting date.

In conjunction with the plan to close the Hogansville, Georgia distribution facility, the Company recorded approximately \$1.1 million in closing-related costs during first quarter of fiscal 2012, consisting of severance of \$1.0 million and \$0.1 million of accelerated depreciation (included in selling, general, and administrative expenses). As of March 31, 2012, there was approximately \$1.1 million of restructuring reserves included in other long-term liabilities on the accompanying unaudited condensed consolidated balance sheet related to this closure. The Company expects to incur additional closure-related charges of approximately \$1.8 million for one-time termination benefits (\$1.1 million in fiscal 2012 and \$0.7 million in fiscal 2013) and \$1.6 million in accelerated depreciation (\$1.1 million in fiscal 2012 and \$0.5 million in fiscal 2013), and other closure costs of \$1.0 million in fiscal 2013. The salvage value of this facility is estimated to be \$2.0 million.

Based on our current outlook, we believe that cash generated from operations and available cash, together with amounts available under our revolving credit facility, will be adequate to meet our working capital needs and capital expenditure requirements for the foreseeable future, although no assurance can be given in this regard. We may, however, need to refinance all or a portion of the principal amount, if any, outstanding under our revolving credit facility on or before October 15, 2015.

EFFECTS OF INFLATION AND DEFLATION



The Company is subject to both inflationary and deflationary risks. With respect to inflation, the Company is experiencing higher product costs, driven by increases in underlying component costs, such as cotton, polyester, labor rates, fuel, and transportation costs. The Company expects product costs will remain at elevated levels for at least the first half of fiscal 2012. The Company's product costs have also been adversely impacted by the devaluation of the U.S. dollar relative to foreign currencies. These inflationary and currency risk factors have resulted in higher costs of goods sold and inventory values. Although we raised our selling prices on many of our products, we were unable to fully absorb these cost increases and our profitability was adversely impacted. We do not expect in the near term to be able to fully absorb these inflated costs and our profitability may continue to be adversely impacted.

In recent years, the Company has also experienced deflationary pressure on its selling prices, in part driven by intense price competition in the young children's apparel industry. In this environment there is a risk that customers will not accept our price increases.

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

SEASONALITY

We experience seasonal fluctuations in our sales and profitability due to the timing of certain holidays and key retail shopping periods, generally resulting in lower sales and gross profit in the first half of our fiscal year. More of our consolidated net sales over the past five fiscal years, excluding the effect of the Acquisition in fiscal 2011, have typically been generated in the second half of our fiscal year (approximately 57%). Accordingly, our results of operations during the first half of the year may not be indicative of the results we expect for the full year.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

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

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

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

We contract with a third-party service to provide us with the fair value of cooperative advertising arrangements entered into with certain of our major wholesale customers. Such fair value is determined based upon, among other factors, comparable market analysis for similar advertisements. In accordance with accounting guidance on consideration given by a vendor to a customer/reseller, we have included the fair value of these arrangements of approximately \$0.6 million in the first quarter of fiscal 2012, and \$0.2 million in the first quarter of fiscal 2011, as a component of selling, general, and administrative expenses on the accompanying unaudited condensed consolidated

statements of operations rather than as a reduction of revenue. Amounts determined to be in excess of the fair value of these arrangements are recorded as a reduction of net sales.

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

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

Goodwill and tradename: As of March 31, 2012, we had approximately \$189.7 million in Carter's and Bonnie Togs goodwill and \$306.1 million of aggregate value related to the Carter's, OshKosh, and Bonnie Togs tradename assets. The fair value of the Carter's tradename was estimated using a discounted cash flow analysis at the time of the acquisition of Carter's, Inc. which was consummated on August 15, 2001. The particular discounted cash flow approach utilized the hypothetical cost savings that accrue as a result of our ownership of the tradename. The fair value of the OshKosh tradename was estimated at its acquisition date, July 14, 2005, using an identical discounted cash flow analysis. The Carter's and OshKosh tradenames were determined to have indefinite lives. The Bonnie Togs tradename was also estimated using an identical discounted cash flow analysis at the time of acquisition on June 30, 2011. The Bonnie Togs tradename was determined to have a definite life and is being amortized over two years.

The carrying values of the goodwill and indefinite lived tradename assets are subject to annual impairment reviews in accordance with accounting guidance on goodwill and other intangible assets, as of the last day of each fiscal year. Impairment reviews may also be triggered by any significant events or changes in circumstances affecting our business. Factors affecting such impairment reviews include the continued market acceptance of our offered products and the development of new products. We use discounted cash flow models to determine the fair value of these assets, using assumptions we believe hypothetical marketplace participants would use. For indefinite-lived intangible assets, if the carrying amount exceeds the fair value, an impairment charge is recognized in the amount equal to that excess.

We perform impairment tests of our goodwill at our reporting unit level, which is consistent with our operating segments. The goodwill impairment test consists of a two-step process, if necessary. The first step is to compare the fair value of a reporting unit to its carrying value, including goodwill. We use discounted cash flow models to determine the fair value of a reporting unit. The assumptions used in these models are consistent with those we believe hypothetical marketplace participants would use. If the fair value of a reporting unit is less than its carrying value, the second step of the impairment test must be performed in order to determine the amount of impairment loss, if any. The second step compares the implied fair value of the reporting unit goodwill with the carrying amount of that goodwill. If the carrying amount of the reporting unit's goodwill exceeds its implied fair value, an impairment charge is recognized in an amount equal to that excess. The loss recognized cannot exceed the carrying amount of goodwill.

A deterioration of macroeconomic conditions may not only negatively impact the estimated operating cash flows used in our cash flow models, but may also negatively impact other assumptions used in our analyses, including, but not limited to, the estimated cost of capital and/or discount rates. Additionally, as discussed above, in accordance with accounting guidance, we are required to ensure that assumptions used to determine fair value in our analyses are consistent with the assumptions a hypothetical marketplace participant would use. As a result, the cost of capital and/or discount rates used in our analyses may increase or decrease based on market conditions and trends, regardless of whether our actual cost of capital has changed. Therefore, we may recognize an impairment of an intangible asset or assets even though realized actual cash flows are approximately equal to or greater than our previously forecasted amounts.

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

Loss contingencies: We record accruals for various contingencies including legal exposures as they arise in the normal course of business. In accordance with accounting guidance on contingencies, we determine whether to disclose and accrue for loss contingencies based on an assessment of whether the risk of loss is remote, reasonably possible or probable. Our assessment is developed in consultation with our internal and external counsel and other advisors and is based on an analysis of possible outcomes under various strategies. Loss contingency assumptions involve judgments that are inherently subjective and can involve matters that are in litigation, which, by its nature is unpredictable. We believe that our assessment of the probability of loss contingencies is reasonable, but because of the subjectivity involved and the unpredictable nature of the subject matter at issue, our assessment may prove ultimately to be incorrect, which could materially impact our consolidated financial statements.

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

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

Foreign currency: The functional currency of the Company's foreign operations is the local currency. Assets and liabilities are translated into U.S. dollars using the current exchange rates in effect at the balance sheet date, while revenues and expenses are translated at the average exchange rates for the period. The resulting translation adjustments are recorded as a component of accumulated other comprehensive income within stockholders' equity.

Employee benefit plans: We sponsor a defined contribution plan, a frozen defined benefit pension plan and other unfunded post-retirement plans. The defined benefit pension and post-retirement plans require an actuarial valuation to determine plan obligations and related periodic costs. We use independent actuaries to assist with these calculations. Plan valuations require economic assumptions, including expected rates of return on plan assets, discount rates to value plan obligations, employee demographic assumptions including mortality rates, and changes in health care costs. The actuarial assumptions used may differ materially from actual results due to changing market and economic conditions. Actual results that differ from the actuarial assumptions are reflected as unrecognized gains and losses. Unrecognized gains and losses that exceed 10% of the greater of the plan's projected benefit obligations or market value of assets are amortized to earnings over the estimated service life of the remaining plan participants.

The most significant assumption used to determine the Company's projected benefit obligation under its post-retirement life and medical plan under which retirement benefits were frozen in 1991 is the discount rate used to determine the plan's projected benefit obligation.

See Note 8, "Employee Benefits Plans," to our audited consolidated financial statements, in our most recently filed Annual Report in Form 10-K for further details on rates and assumptions.

Stock-based compensation arrangements: The Company accounts for stock-based compensation in accordance with the fair value recognition provisions of accounting guidance on share-based payments. The Company adopted this guidance using the modified prospective application method of transition. The Company uses the Black-Scholes option pricing model, which requires the use of subjective assumptions. These assumptions include the following:

Volatility – This is a measure of the amount by which a stock price has fluctuated or is expected to fluctuate. The Company uses actual monthly historical changes in the market value of our stock covering the expected life of stock

options being valued. An increase in the expected volatility will increase compensation expense.

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

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

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

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

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

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

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

FORWARD-LOOKING STATEMENTS

Statements contained herein that relate to our future performance, including, without limitation, statements with respect to our anticipated results of operations or level of business for fiscal 2012 or any other future period, are forward-looking statements within the meaning of the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. Such statements are based on current expectations only and are subject to certain risks, uncertainties, and assumptions. Should one or more of these risks or uncertainties materialize, or should underlying assumptions prove incorrect, actual results may vary materially from those anticipated, estimated, or projected. These risks are described herein under Item 1A of Part II. We undertake no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events, or otherwise.



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

#### CURRENCY AND INTEREST RATE RISKS

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

We contract for production with third parties primarily in Asia. While these contracts are stated in United States dollars, there can be no assurance that the cost for the future production of our products will not be affected by exchange rate fluctuations between the United States dollar and the local currencies of these contractors. Due to the number of currencies involved, we cannot quantify the potential impact of future currency fluctuations on net income (loss) in future years. In order to manage this risk, we source products from over 100 vendors in over 15 countries, providing us with flexibility in our production should significant fluctuations occur between the United States dollar and various local currencies. To date, such exchange fluctuations have not had a material impact on our financial condition or results of operations.

Transactions by our Canadian subsidiary may be denominated in a currency other than the entity's functional currency, which is the Canadian dollar. Fluctuations in exchange rates, primarily between the United States dollar and the Canadian dollar, may affect our results of operations, financial position, and cash flows. We employ foreign exchange contracts to hedge foreign currency exchange rate risk associated with the procurement of U.S. dollar denominated finished goods destined for the Canadian market. These foreign exchange contracts are marked to market at the end of each reporting period, which could result in earnings volatility.

Our operating results are subject to risk from interest rate fluctuations on our revolving credit facility, which carries variable interest rates. As of March 31, 2012, our outstanding variable rate debt aggregated approximately \$236.0 million. An increase or decrease of 1% in the applicable rate would increase or decrease our annual interest cost by \$2.4 million and could have an adverse effect on our net income (loss) and cash flow.

#### OTHER RISKS

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

### ITEM 4. CONTROLS AND PROCEDURES

#### Evaluation of Disclosure Controls and Procedures

Our Chief Executive Officer and Chief Financial Officer have evaluated the effectiveness of the design and operation of our disclosure controls and procedures (as defined under Rules 13a-15(e) and 15d-15(e) promulgated under the Securities Exchange Act of 1934, as amended (the "Exchange Act")) as of the end of the period covered by this report. Based upon that evaluation, our Chief Executive Officer and Chief Financial Officer have concluded that our disclosure controls and procedures are effective as of March 31, 2012.

#### Changes in Internal Control over Financial Reporting

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

financial reporting.

32

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## PART II – OTHER INFORMATION

### ITEM 1. LEGAL PROCEEDINGS:

A shareholder class action lawsuit was filed on September 19, 2008 in the United States District Court for the Northern District of Georgia entitled Plymouth County Retirement System v. Carter's, Inc., No. 1:08-CV-02940-JOF (the "Plymouth Action"). The Amended Complaint filed on May 12, 2009 in the Plymouth Action asserted claims under Sections 10(b), 20(a), and 20A of the 1934 Securities Exchange Act, and alleged that between February 1, 2006 and July 24, 2007, the Company and certain current and former executives made material misrepresentations to investors regarding the successful integration of OshKosh into the Company's business, and that the share price of the Company's stock later fell when the market learned that the integration had not been as successful as represented. Defendants in the Plymouth Action filed a motion to dismiss the Amended Complaint for failure to state a claim under the federal securities laws on July 17, 2009, and briefing of that motion was complete on October 22, 2009.

A separate shareholder class action lawsuit was filed on November 17, 2009 in the United States District Court for the Northern District of Georgia entitled Mylroie v. Carter's, Inc., No. 1:09-CV-3196-JOF (the "Mylroie Action"). The initial Complaint in the Mylroie Action asserted claims under Sections 10(b) and 20(a) of the 1934 Securities Exchange Act, and alleged that between April 27, 2004 and November 10, 2009, the Company and certain current and former executives made material misstatements to investors regarding the Company's accounting for discounts offered to some wholesale customers. The Court consolidated the Plymouth Action and the Mylroie Action on November 24, 2009 (the "Consolidated Action"). On March 15, 2010, the plaintiffs in the Consolidated Action filed their amended and consolidated complaint. The Company filed a motion to dismiss on April 30, 2010, and briefing of the motion was complete on July 23, 2010.

On March 16, 2011, the United States District Court for the Northern District of Georgia granted without prejudice the Company's motion to dismiss all of the claims in the amended and consolidated complaint in the Consolidated Action for failure to state a claim under the federal securities laws. The plaintiffs filed a second amended and consolidated complaint on July 20, 2011. On December 21, 2011, the Company reached an agreement to settle the Consolidated Action for an amount which has been paid by the Company's insurance providers. The settlement agreement includes no admission of liability or wrongdoing by the Company or by any other defendants and provides for a full and complete release of all related claims that were or could have been brought against the Company, its subsidiaries, and any and all current and former directors, officers, and employees of the Company and its subsidiaries. On January 19, 2012, the Court granted preliminary approval of the settlement and ordered that notice be provided to the proposed settlement class (as defined in the settlement agreement). The Court has scheduled a hearing for May 31, 2012 to determine whether the settlement will receive final approval.

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

### ITEM 1A. RISK FACTORS:

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



## Risks Relating to Our Business

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

In the first quarter of fiscal 2012, we derived approximately 29% of our consolidated net sales from our top four customers. We do not enter into long-term sales contracts with our major customers, relying instead on long-standing relationships and on our position in the marketplace. As a result, we face the risk that one or more of our major customers may significantly decrease their business with us or terminate their relationship with us. Any such decrease or termination of our major customers' business could result in a material decrease in our sales and operating results.

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

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

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

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

In addition, the Company's brand image, which is associated with providing a consumer product with outstanding quality and name recognition, makes it valuable as a royalty source. The Company is able to generate royalty income from the sale of licensed products that bear its Carter's, Just One You, Precious Firsts, Child of Mine, OshKosh, OshKosh Est. 1895, Genuine Kids, and related trademarks. While the Company takes significant steps to ensure the reputation of its brand is maintained through its license agreements, there can be no guarantee that the Company's brand image will not be negatively impacted through its association with products outside of the Company's core apparel products.

We may incur substantial costs as a result of litigation, investigations or other proceedings, including those related to our previously filed restatements.

We are currently involved in litigation matters and investigations and may be subject to additional actions in the future. As disclosed in the Company's amended and restated Annual Report on Form 10-K for fiscal 2008, we announced on November 10, 2009, that our Audit Committee, with the assistance of outside counsel, had commenced a review of customer margin support provided by the Company and an investigation into undisclosed margin support commitments and related matters. The Company self-reported information concerning this investigation to the SEC in the fourth quarter of fiscal 2009 and has also been informed that the United States Attorney's Office is conducting an investigation into this matter. In December 2010, the Company and the SEC entered into a non-prosecution agreement pursuant to which the SEC agreed not to charge the Company with any violations of the federal securities laws, commence any enforcement action against the Company, or require the Company to pay any financial penalties in connection with the SEC's investigation of customer margin support provided by the Company, conditioned upon the

Company's continued cooperation with the SEC's investigation and with any related enforcement proceedings. The Company has incurred, and expects to continue to incur, substantial expenses for legal and accounting services due to the SEC and United States Attorney's Office investigations and any resulting litigation. These matters have diverted in the past, and may continue to divert in the future, management's time and attention away from operations and cause the Company to continue to incur substantial costs. The Company also may bear additional costs to the extent it is required, under the terms of organizational documents or under Delaware law, to indemnify former officers of the Company in respect of costs they incur in connection with any proceedings related to these matters.

At this point, the Company is unable to predict the duration, costs, scope or result of these matters.

As described in more detail in Part II - Item 1 of this filing, the Company is also currently subject to a class action lawsuit, as well as various other claims and pending or threatened lawsuits in the normal course of our business. We have only limited amounts of insurance, which may not provide coverage to offset a negative judgment or a settlement payment, which could be substantial. We may be unable to obtain additional insurance in the future, or we may be unable to do so on favorable terms. Our insurers may also dispute our claims for coverage. Further, these lawsuits may result in diversion of management's time and attention, the expenditure of large amounts of cash on legal fees and other expenses, and injury to our reputation, all of which may adversely affect our operations and financial condition.

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

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

Increased production costs and deflationary pressures on our selling prices may adversely affect our results.

The Company's product costs, driven by inflation in significant component costs such as cotton, polyester, labor, fuel, and transportation, have increased and may remain at elevated levels or increase further. Our product costs have also been adversely impacted by the devaluation of the U.S. dollar relative to foreign currencies. These inflationary and currency risk factors have resulted in higher costs of goods sold and inventory values. Although we have raised our selling prices on many of our products, we do not expect in the near term to be able to fully absorb these cost increases, and we expect our profitability to continue to be adversely impacted. In recent years, the Company has also experienced deflationary pressure on its selling prices, in part driven by intense price competition in the young children's apparel industry.

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

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

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

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

• financial instability of one or more of our major vendors;

• political instability or other international events resulting in the disruption of trade in foreign countries from which we source our products;

• increases in transportation costs as a result of increased fuel prices or significant changes in the relationship between



carrier capacity and shipper demand;

• interruptions in the supply, or increases in the cost of raw materials, including cotton, fabric, and trim items;

• significant changes in the cost of labor in our sourcing locations;

• the imposition of new regulations relating to imports, duties, taxes, and other charges on imports;

• the occurrence of a natural disaster, unusual weather conditions, or an epidemic, the spread of which may impact our ability to obtain products on a timely basis;

• changes in the United States customs procedures concerning the importation of apparel products;

• unforeseen delays in customs clearance of any goods;

• disruption in the global transportation network such as a port strike, capacity withholding, world trade restrictions, or war;

• the application of foreign intellectual property laws;

• the ability of our vendors to secure sufficient credit to finance the manufacturing process including the acquisition of raw materials; and

• exchange rate fluctuations between the Company's and/or its subsidiaries' functional currency and the currencies paid to foreign contractors.

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

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

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

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



Any significant disruption to our eCommerce business, including order acceptance and processing, order fulfillment, web-hosting, warehousing, and call center operations, could result in lost sales and could harm our brand and our reputation in the marketplace.

The operation of our eCommerce business depends on the ability to maintain the efficient and uninterrupted operation of online order-taking and fulfillment operations. We currently rely on a third party to host our eCommerce website, process and manage web orders, warehouse inventory sold through our eCommerce website, fulfill our eCommerce sales to our customers, and operate a call center supporting our eCommerce business, and we intend to transition fulfillment services in-house in the second half of fiscal 2012. Any significant disruption in the operations of our eCommerce business or in our ability to transition fulfillment services, could result in lost sales and could harm our brand and our reputation in the marketplace.

The loss of a sourcing agent could negatively impact our ability to timely deliver our inventory supply and disrupt our business, which may adversely affect our operating results.

One sourcing agent currently manages approximately 75% of our inventory purchases. Although we believe that other buying agents could be retained, or we could procure some of the inventory directly, the loss of this buying agent could delay our ability to timely receive inventory supply and disrupt our business, which could result in a material adverse effect on our operating results.

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

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

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

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

The Company's retail stores are located in leased retail locations across the United States and Canada. Successful operation of a retail store depends, in part, on the overall ability of the retail location to attract a consumer base sufficient to make store sales volume profitable. If the Company is unable to identify new retail locations with consumer traffic sufficient to support a profitable sales level, retail growth may consequently be limited. Further, if existing outlet and brand stores do not maintain a sufficient customer base that provides a reasonable sales volume or the Company is unable to negotiate appropriate lease terms for the retail stores, there could be a material adverse impact on the Company's sales, gross margin, and results of operations.

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

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

37

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We face various risks arising from our recent acquisition of Bonnie Togs, a Canadian children's apparel retailer. We may fail to realize growth opportunities and other benefits from the acquisition of Bonnie Togs, and we may fail to successfully integrate the Bonnie Togs business with our existing business, either of which could adversely affect our financial condition and results of operations.

We may fail to realize growth opportunities and other benefits from the acquisition of Bonnie Togs. We have no prior experience operating a retail business in Canada, and we may not be as successful in operating and growing this business in Canada as we have been in the United States. We may be unable to continue existing, or to develop new, vendor and customer relationships, and enhance our position in Canada. Further, our operations in Canada are subject to the various risks and uncertainties to which our United States retail operations are subject. Our ability to successfully integrate Bonnie Togs is subject to risks, including delays or difficulties in completing integration and higher than expected costs. In connection with the integration efforts, our management's attention and our resources could be diverted from other business concerns. If integration difficulties arise, the diversion of attention and resources may be increased. Any of these may adversely affect our financial condition and results of operations.

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

As of March 31, 2012, the Company had goodwill of \$136.6 million for Carter's and \$53.1 million for Bonnie Togs, and tradename assets of \$220.2 million for the Carter's brand, \$85.5 million for the OshKosh brand, and \$0.4 million for the Bonnie Togs brand on its unaudited condensed consolidated balance sheet. The carrying value of these assets is subject to annual impairment reviews as of the last day of each fiscal year or more frequently, if deemed necessary, due to any significant events or changes in circumstances.

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

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

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

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

## Share Repurchases

The following table provides information about shares acquired from employees during the first quarter of fiscal 2012 to satisfy the required withholding of taxes in connection with the vesting of restricted stock:

Period	Total number of shares purchased (1)	Average price paid per share	Total number of shares purchased as part of publicly announced plans or programs	Approximate dollar value of shares that may yet be purchased under the plans or programs
January 1, 2012 through January 28, 2012	—	\$—	—	Not applicable
January 29, 2012 through February 25, 2012	36,394	\$43.61	—	Not applicable
February 26, 2012 through March 31, 2012	13,461	\$48.60	—	Not applicable
Total	49,855	\$45.02	—	Not applicable

(1) All of the shares were surrendered by our employees to satisfy required tax withholding upon the vesting of restricted stock awards.

## ITEM 3. DEFAULTS UPON SENIOR SECURITIES:

N/A

## ITEM 4. MINE SAFETY DISCLOSURES:

N/A

## ITEM 5. OTHER INFORMATION:

N/A

## ITEM 6. EXHIBITS:

(a) Exhibits:

Exhibit Number    Description of Exhibits

10.21                    Lease Agreement dated March 29, 2012 between The William Carter Company and Duke Secured Financing 2009-1 ALZ, LLC.

31.1 Rule 13a-15(e)/15d-15(e) and 13a-15(f)/15d-15(f) Certification

31.2 Rule 13a-15(e)/15d-15(e) and 13a-15(f)/15d-15(f) Certification

32 Section 1350 Certification

39

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SIGNATURES

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

CARTER'S, INC.

Date : April 27, 2012

/s/ MICHAEL D. CASEY  
Michael D. Casey  
Chief Executive Officer  
(Principal Executive Officer)

Date : April 27, 2012

/s/ RICHARD F. WESTENBERGER  
Richard F. Westenberger  
Executive Vice President and  
Chief Financial Officer  
(Principal Financial and Accounting Officer)