VALASSIS COMMUNICATIONS INC
Form 10-Q
August 09, 2007

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

x Quarterly report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the Quarterly Period Ended June 30, 2007

¨ Transition Report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
Commission File Number: 1-10991

VALASSIS COMMUNICATIONS, INC.

(Exact Name of Registrant as Specified in its Charter)

Delaware	**38-2760940**
(State or Other Jurisdiction of Incorporation or Organization)	**(IRS Employer Identification Number)**

19975 Victor Parkway

Livonia, Michigan 48152

(address of principal executive offices)

Registrant s Telephone Number: (734) 591-3000

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

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

Large accelerated filer x Accelerated filer ¨ Non-accelerated filer ¨

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act): Yes ¨ No x

As of August 1, 2007, there were 47,882,160 shares of the Registrant s Common Stock outstanding.

Part I Financial Information

Item 1. Financial Statements

VALASSIS COMMUNICATIONS, INC.

Condensed Consolidated Balance Sheets

(U.S. dollars in thousands)

(unaudited)

	June 30, 2007	Dec. 31, 2006
Assets		
Current assets:		
Cash and cash equivalents	$ 135,831	$ 52,619
Auction-rate securities		102,533
Accounts receivable (less allowance for doubtful accounts of $18,603 at June 30, 2007 and $5,001 at December 31, 2006)	456,973	339,079
Inventories:		
Raw materials	21,178	12,729
Work in progress	15,487	13,105
Prepaid expenses and other	23,752	16,681
Deferred income taxes	18,050	1,789
Refundable income taxes	11,615	3,957
Total current assets	682,886	542,492
Property, plant and equipment, gross:		
Land and buildings	80,907	55,723
Machinery and equipment	214,532	142,085
Office furniture and equipment	170,216	61,903
Automobiles	221	216
Leasehold improvements	22,088	2,949
	487,964	262,876
Less accumulated depreciation and amortization	(174,733)	(153,490)
Net property, plant and equipment	313,231	109,386
Intangible assets:		
Goodwill	885,819	173,134
Other intangibles	331,555	35,555
	1,217,374	208,689
Less accumulated amortization	(78,500)	(75,280)
Net intangible assets	1,138,874	133,409
Investments	6,802	4,899
Other assets	29,658	11,240

Total assets	$ 2,171,451	$ 801,426

See accompanying notes to condensed consolidated financial statements.

VALASSIS COMMUNICATIONS, INC.

Condensed Consolidated Balance Sheets, Continued

(U.S. dollars in thousands)

(unaudited)

	June 30, 2007	Dec. 31, 2006
Liabilities and Stockholders Equity		
Current liabilities:		
Current portion, long-term debt	$ 30,900	$
Accounts payable	301,395	268,834
Accrued interest	18,905	3,307
Accrued compensation and benefits	48,893	23,671
Accrued other expenses	43,782	17,150
Progress billings	51,253	49,258
Total current liabilities	495,128	362,220
Long-term debt	1,332,573	259,931
Other non-current liabilities	11,186	8,195
Deferred income taxes	139,876	3,506
Stockholders equity:		
Preferred stock of $0.01 par value. Authorized 25,000,000 shares; no shares issued or outstanding at June 30, 2007 and December 31, 2006		
Common stock of $0.01 par value. Authorized 100,000,000 shares; issued 63,262,596 at June 30, 2007 and 63,264,925 at December 31, 2006; outstanding 47,781,579 at June 30, 2007 and 47,783,908 at December 31, 2006	633	633
Additional paid-in capital	47,754	44,225
Retained earnings	655,270	638,209
Accumulated other comprehensive income	9,258	4,734
Treasury stock, at cost (15,481,017 shares at June 30, 2007 and 15,481,017 shares at December 31, 2006)	(520,227)	(520,227)
Total stockholders equity	192,688	167,574
Total liabilities and stockholders equity	$ 2,171,451	$ 801,426

See accompanying notes to condensed consolidated financial statements.

VALASSIS COMMUNICATIONS, INC.

Condensed Consolidated Statements of Income

(U.S. dollars in thousands, except per share data)

(unaudited)

	Three Months Ended June 30, 2007	Three Months Ended June 30, 2006	Six Months Ended June 30, 2007	Six Months Ended June 30, 2006
Revenues	$ 612,147	$ 260,593	$ 973,451	$ 508,238
Costs and expenses:				
Cost of products sold	472,822	197,972	751,839	383,241
Selling, general and administrative	96,364	30,515	150,890	63,255
Amortization expense	2,312	138	3,220	278
Total costs and expenses	571,498	228,625	905,949	446,774
Earnings from operations	40,649	31,968	67,502	61,464
Other expenses (income):				
Interest expense	25,228	2,216	35,847	5,071
Other income, net	(1,485)	(728)	(3,663)	(2,082)
Total other expenses (income)	23,743	1,488	32,184	2,989
Earnings before income taxes	16,906	30,480	35,318	58,475
Income taxes	7,130	10,791	14,309	20,729
Net earnings	$ 9,776	$ 19,689	$ 21,009	$ 37,746
Net earnings per common share, basic	$ 0.20	$ 0.41	$ 0.44	$ 0.79
Net earnings per common share, diluted	$ 0.20	$ 0.41	$ 0.44	$ 0.79
Shares used in computing net earnings per share, basic	47,781,249	47,766,605	47,780,316	47,709,701
Shares used in computing net earnings per share, diluted	47,876,878	47,863,266	47,872,659	47,811,621

See accompanying notes to condensed consolidated financial statements.

VALASSIS COMMUNICATIONS, INC.

Condensed Consolidated Statements of Cash Flows

(U.S. dollars in thousands)

(unaudited)

	Six Months Ended June 30, 2007	June 30, 2006
Cash flows from operating activities:		
Net earnings	$ 21,009	$ 37,746
Adjustments to reconcile net earnings to net cash provided by operating activities:		
Depreciation and amortization of intangibles	25,282	7,359
Amortization of bond discount and debt issue costs	1,278	232
Provision for losses on accounts receivable	2,401	125
Asset impairment	1,460	
Loss on sale of property, plant and equipment	84	18
Gain on equity investments	(855)	(185)
Stock-based compensation charge	3,530	3,185
Changes in assets and liabilities which (decrease) increase cash flow:		
Accounts receivable	65,645	12,510
Inventories	(4,687)	(3,474)
Prepaid expenses and other	4,640	(6,108)
Other liabilities	(18,549)	(150)
Other assets	23,582	(5,713)
Accounts payable	3,540	1,033
Accrued expenses and interest	(24,750)	(9,191)
Income taxes	1,420	(2,260)
Progress billings	(8,323)	(6,671)
Total adjustments	75,698	(9,290)
Net cash provided by operating activities	96,707	28,456
Cash flows from investing activities:		
Additions to property, plant and equipment	(12,225)	(4,386)
Acquisition of ADVO, net of cash acquired	(1,187,301)	
Purchases of auction-rate securities	(156,335)	(234,408)
Proceeds from sales of auction-rate securities	258,869	216,536
Investments and advances to affiliated companies	(1,000)	
Other	(360)	(212)
Net cash used in investing activities	(1,098,352)	(22,470)
Cash flows from financing activities:		
Borrowings of long-term debt	1,130,000	
Payment of debt issue costs	(19,212)	
Repayment of long term debt	(26,475)	(14,379)
Repurchase of common stock		(3,913)
Proceeds from the issuance of common stock		5,678
Net cash provided by (used in) financing activities	1,084,313	(12,614)

Effect of exchange rate changes on cash	544	1,136
Net increase (decrease) in cash	83,212	(5,492)
Cash at beginning of period	52,619	64,320
Cash at end of period	$ 135,831	$ 58,828
Supplemental disclosure of cash flow information:		
Cash paid during the period for interest	$ 18,486	$ 5,666
Cash paid during the period for income taxes	$ 13,889	$ 25,643
Non-cash financing activities:		
Stock issued under stock-based compensation plan	$ 1,393	$ 1,881

See accompanying notes to condensed consolidated financial statements.

VALASSIS COMMUNICATIONS, INC.

Notes to Condensed Consolidated Financial Statements

(unaudited)

1. **BASIS OF PRESENTATION**

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (generally accepted accounting principles) for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. In the opinion of management, the information contained herein reflects all adjustments necessary for a fair presentation of the information presented. All such adjustments are of a normal recurring nature. The results of operations for the interim periods are not necessarily indicative of results to be expected for the fiscal year. For further information, refer to the consolidated financial statements and footnotes thereto included in the Valassis Communications, Inc. (Valassis, the Company, we or our) Annual Report on Form 10-K for the year ended December 31, 2006, as amended by Amendments No. 1 and No. 2 thereto on Form 10-K/A (as amended, the Amended 2006 10-K).

2. **ACQUISITION OF ADVO**

Valassis completed the acquisition of ADVO, Inc. (ADVO) on March 2, 2007 for approximately $1.2 billion, including the refinancing of approximately $125 million in existing ADVO debt, which was financed with debt as more fully described in Note 7. Long-Term Debt.

The acquisition was accounted for as a purchase in accordance with Statement of Financial Accounting Standards (SFAS) 141, Business Combinations and ADVO s results are included in the consolidated operating results from the acquisition date. The total purchase price reflects transaction costs and is net of cash acquired. Amounts allocated to the assets acquired and liabilities assumed are based upon estimates of fair value as of the acquisition date.

The purchase price allocation for the acquisition is preliminary with respect to finalization of intangible asset and fixed asset valuations, integration accrual, and other minor items. As of June 30, 2007, the preliminary allocation of the purchase price for the acquisition was made to the following major opening balance sheet categories.

(in thousands of U.S. dollars)	**June 30, 2007**
Current assets	$ 220,118
Property, plant and equipment	214,945
Goodwill	712,685
Intangible assets	296,000
Other non-current assets	20,036
Total assets	**$ 1,463,784**
Current liabilities	$ 118,773
Non-current liabilities	157,710
Total liabilities	**$ 276,483**

VALASSIS COMMUNICATIONS, INC.

Notes to Condensed Consolidated Financial Statements

(unaudited)

The operating results for ADVO are included in the accompanying condensed consolidated statements of operations from March 2, 2007, the date of acquisition. The following unaudited pro forma condensed consolidated financial information has been prepared assuming the ADVO acquisition had occurred on January 1, 2007 and January 1, 2006, respectively.

	Three Months Ended	
($ in thousands, except per share amounts)	**June 30, 2007**	**June 30, 2006**
Revenue	$ 612,147	$ 645,470
Operating income	40,649	42,102
Net earnings	9,776	14,605
Basic earnings per share	$ 0.20	$ 0.31
Diluted earnings per share	$ 0.20	$ 0.31

	Six Months Ended	
($ in thousands, except per share amounts)	**June 30, 2007**(1)	**June 30, 2006**
Revenue	$ 1,196,954	$ 1,245,495
Operating income	37,141	79,272
Net earnings	(6,770)	25,798
Basic earnings per share	$ (0.14)	$ 0.54
Diluted earnings per share	$ (0.14)	$ 0.54

(1) Results include $23.0 million in one-time costs related to the acquisition of ADVO by Valassis.

These unaudited pro forma results are presented for comparative purposes only. The pro forma results are not necessarily indicative of what our actual results would have been had the acquisition of ADVO been completed as of the beginning of the periods presented. In addition, the pro forma results do not purport to project our future results.

3. **STOCK-BASED COMPENSATION**

Effective January 1, 2006, we adopted SFAS No. 123R, Share-Based Payment (FAS 123R). We use a Black-Scholes valuation model to determine the fair value of stock option grants and the straight-line attribution method for recognizing stock-based compensation expense under FAS 123R, which is consistent with the method we used in recognizing stock-based compensation expense for disclosure purposes under FAS 123 prior to the adoption of FAS 123R.

Stock-based compensation for the quarters ended June 30, 2007 and June 30, 2006 was $1.8 million and $1.8 million, respectively. For the six months ended June 30, 2007 and June 30, 2006, stock-based compensation expense was $3.5 million and $3.2 million, respectively. Total compensation expense related to non-vested options not yet recognized at June 30, 2007 is approximately $9.1 million, which we expect to recognize as compensation expense over the next five years.

VALASSIS COMMUNICATIONS, INC.

Notes to Condensed Consolidated Financial Statements

(unaudited)

4. **FOREIGN CURRENCY AND DERIVATIVE FINANCIAL INSTRUMENTS**

The functional currencies for our foreign operations are the applicable local currencies. Accounts of foreign operations are translated into U.S. dollars using the spot rate of the local currency on the balance sheet date for assets and liabilities and average monthly exchange rates for revenues and expenses. Translation adjustments are reflected as an adjustment to equity on a cumulative basis.

Currencies to which we have exposure are the Mexican peso, Canadian dollar, British pound and euro. Currency restrictions are not expected to have a significant effect on our cash flows, liquidity, or capital resources. We typically purchase the Mexican peso under three to twelve-month forward foreign exchange contracts to stabilize the cost of production in Mexico. Under SFAS No. 133, Accounting for Derivative Instruments and Hedging Activities (SFAS 133), our Mexican peso forward exchange contracts meet the definition of a cash flow hedge. Accordingly, changes in the fair value of the hedge are recorded as a component of other comprehensive income. For the quarter ended June 30, 2007, the recorded unrealized market value gains and losses included in other comprehensive income were immaterial. Actual exchange losses or gains are recorded against production expense when the contracts are executed. As of June 30, 2007, we had a commitment to purchase $4.6 million in Mexican pesos over the next eleven months.

Valassis entered into two interest rate swap agreements during the second quarter of 2007. These derivative agreements effectively fix interest rates on a portion of our floating rate debt and qualify for cash flow hedge accounting treatment under SFAS 133. The fair value of these derivatives was $4.1 million as of June 30, 2007. Any changes in face value will be recorded as a component of other comprehensive income. See Note 7. Long-Term Debt for further information on the interest rate swap agreements.

5. **GOODWILL AND OTHER INTANGIBLES**

Intangible assets as of June 30, 2007 are comprised of:

(in thousands of U.S. dollars)	**Intangible Assets, at Cost**	**Accumulated Amortization at June 30, 2007**	**Unamortized Balance at June 30, 2007**	**Weighted Average Useful Life (in years)**
Amortizable intangible assets	$ 183,455	$ (5,695)	$ 177,760	19.7
Non-amortizable intangible assets:				
Goodwill:				
Free-standing Inserts			18,257	
Neighborhood Targeted			5,325	
Household Targeted			32,642	
International & Services			64,864	
ADVO			712,685	
The Valassis name and other			11,341	
ADVO trade names and trademarks			116,000	
Total non-amortizable intangible assets			**961,114**(1)	
Consolidated net intangible assets			**$ 1,138,874**	

(1) Net of $21.5 million of amortization recorded prior to the adoption of SFAS No. 142 and a $51.3 million impairment charge.

VALASSIS COMMUNICATIONS, INC.

Notes to Condensed Consolidated Financial Statements

(unaudited)

6. CONTINGENCIES

Upon our completion of the acquisition of ADVO, we assumed responsibility for ADVO s pending securities class action lawsuits. In September 2006, three securities class action lawsuits (*Robert Kelleher v. ADVO, Inc., et al., Jorge Cornet v. ADVO, Inc., et al., Richard L. Field v. ADVO, Inc., et al.*) were filed against ADVO and certain of its officers in the United States District Court for the District of Connecticut by certain ADVO shareholders seeking to certify a class of all persons who purchased ADVO stock between July 6, 2006 and August 30, 2006. These complaints generally allege ADVO violated federal securities law by making a series of materially false and misleading statements concerning ADVO s business and financial results in connection with the proposed merger with Valassis and, as a result, the price of ADVO s stock was allegedly inflated.

On December 12, 2006, the *Kelleher* plaintiffs filed a Motion to Partially Lift Discovery Stay, in response to which defendants filed opposition on January 16, 2007. The presiding judge denied the plaintiff s motion to lift the stay on discovery. In addition, the court ordered the matters consolidated under a single action entitled, *Robert Kelleher et al. v. ADVO, Inc., et al.*, Civil Case No. 3:06CV01422(AVC). A revised, consolidated complaint was filed by the plaintiffs on June 8, 2007. The defendants responsive pleading is due August 24, 2007.

Under the circumstances, it is not possible for us to predict the likelihood of a favorable or unfavorable resolution of the securities class action.

Valassis is involved in various claims and legal actions arising in the ordinary course of business. In the opinion of management, the ultimate disposition of these matters will not have a material adverse effect on our financial position, results of operations or liquidity.

7. LONG-TERM DEBT

Long-term debt is summarized as follows:

(in thousands of U.S. dollars)	June 30, 2007	Dec. 31, 2006
Revolving Credit Facility	$	$
6 5/8% Senior Notes due 2009, net of discount	99,948	99,931
Senior Convertible Notes due 2033, net of discount	160,000	160,000
8 1/4% Senior Notes due 2015	540,000	
Senior Secured Term Loan B	563,525	
Senior Secured Delayed Draw Term Loan		
	$ 1,363,473	$ 259,931
Less current portion	30,900	
	$ 1,332,573	$ 259,931

On March 2, 2007, Valassis completed the offering of $540.0 million aggregate principal amount of its 8 1/4% Senior Notes due 2015 (the 2015 Notes) in connection with the financing of its acquisition of ADVO. The 2015 Notes are unsecured and bear interest at a fixed rate of 8 1/4% per annum payable semi-annually in arrears on March 1 and September 1, commencing on September 1, 2007, and mature on March 1, 2015. In July 2007, in accordance with the terms of the registration rights agreement between us and the initial purchasers of the 2015 Notes, we filed with the Securities and Exchange Commission (SEC) a registration statement pursuant to which we commenced an exchange offer to exchange the original notes issued in the private placement for a like principal amount of exchange notes registered under the Securities Act of 1933, as amended. The exchange notes will be substantially identical to the original notes, except that the exchange notes will not be subject to certain transfer restrictions.

On March 2, 2007, in connection with the acquisition of ADVO, Valassis entered into a Credit Agreement with various banking institutions. The Credit Agreement provides for: (i) a $120.0 million senior secured revolving line of credit; (ii) a $590.0 million Senior Secured Term Loan B; and (iii) a $160.0 million senior secured delayed draw term loan. As of June 30, 2007, Valassis had no borrowings under the revolving line of credit or delayed draw term loan.

VALASSIS COMMUNICATIONS, INC.

Notes to Condensed Consolidated Financial Statements

(unaudited)

On April 4, 2007 and June 29, 2007, Valassis entered into forward dated swap agreements with notional principal amounts of $300.0 million and $180.0 million, respectively. The swap agreements expire in December 2010, and effectively fix the interest rates for an aggregate of $480.0 million of our variable rate debt under the Term Loan B portion of our senior secured credit facility. Under SFAS No. 133, each contract is recorded as a cash flow hedge in which the fair value is recorded as an asset and changes in the fair value are recorded as a component of other comprehensive income. The recording of these interest rate swap agreements resulted in a $4.1 million derivative classified as Other Assets on the balance sheet.

For further information, refer to Current and Long-term Debt within Item 2.

8. SEGMENT REPORTING

Valassis has five reportable segments: Free-standing Inserts (FSI), Neighborhood Targeted, Household Targeted, International & Services and ADVO. We previously reported our Run of Press (ROP) business as a separate segment. Due to the similarity in sales and operational processes and the newly-combined sales and general management, we aggregated ROP into the Neighborhood Targeted segment effective January 1, 2007. Our five reportable segments are strategic business units that offer different products and services and are subject to regular review by our chief operating decision-makers. They are managed separately because each business requires different executional strategies and caters to different customer marketing needs.

The accounting policies of the segments are the same as those described in the summary of significant accounting policies. We evaluate performance based on earnings from operations. Assets are not allocated in all cases to reportable segments and are not used to assess the performance of a segment.

	Three Months Ended June 30,					
(in millions of U.S. dollars)	**FSI**	**Neighborhood Targeted(1)**	**Household Targeted**	**International & Services**	**ADVO**	**Total**
2007						
Revenues from external customers	$ 98.7	$ 120.2	$ 12.7	$ 29.0	$ 351.5	$ 612.1
Intersegment revenues	$ (0.8)	$ 3.6	$	$	$ 1.1	$ 3.9
Depreciation/amortization	$ 2.2	$ 0.5	$	$ 0.6	$ 14.6	$ 17.9
Segment profit	$ 5.4	$ 14.5	$ 0.5	$ 1.9	$ 19.4	$ 41.7
2006						
Revenues from external customers	$ 117.0	$ 101.8	$ 14.2	$ 27.6		$ 260.6
Intersegment revenues	$	$	$	$		$
Depreciation/amortization	$ 2.1	$ 0.5	$ 0.1	$ 0.9		$ 3.6
Segment profit	$ 20.8	$ 8.9	$ 0.1	$ 2.2		$ 32.0

VALASSIS COMMUNICATIONS, INC.

Notes to Condensed Consolidated Financial Statements

(unaudited)

(in millions of U.S. dollars)	FSI	Neighborhood Targeted(1)	Household Targeted	International & Services	ADVO(2)	Total
	Six Months Ended June 30,					
2007						
Revenues from external customers	$ 208.4	$ 220.7	$ 23.9	$ 56.9	$ 463.6	$ 973.5
Intersegment revenues	$	$ 3.6	$	$	$ 1.2	$ 4.8
Depreciation/amortization	$ 4.6	$ 1.0	$	$ 1.2	$ 18.5	$ 25.3
Segment profit (loss)	$ 15.3	$ 25.4	$ (0.5)	$ 4.6	$ 24.7	$ 69.5
2006						
Revenues from external customers	$ 232.3	$ 189.0	$ 32.4	$ 54.5		$ 508.2
Intersegment revenues	$	$	$	$		$
Depreciation/amortization	$ 4.3	$ 1.0	$ 0.2	$ 1.9		$ 7.4
Segment profit	$ 38.4	$ 16.3	$ 2.5	$ 4.3		$ 61.5

(1) Neighborhood Targeted now includes the Run of Press business.
(2) Results since the acquisition date of March 2, 2007.

Reconciliations to consolidated financial statement totals are as follows:

(in millions of U.S. dollars)	Three Months Ended June 30, 2007	Three Months Ended June 30, 2006	Six Months Ended June 30, 2007	Six Months Ended June 30, 2006
Profit for reportable segments	$ 41.7	$ 32.0	$ 69.5	$ 61.5
Unallocated amounts:				
Litigation and other costs related to the acquisition of ADVO	(1.1)		(2.0)	
Interest expense	(25.2)	(2.2)	(35.8)	(5.1)
Other income	1.5	0.7	3.6	2.1
Earnings before income taxes	$ 16.9	$ 30.5	$ 35.3	$ 58.5

Domestic and foreign revenues were as follows:

(in millions of U.S. dollars)	Three Months Ended June 30, 2007	Three Months Ended June 30, 2006	Six Months Ended June 30, 2007	Six Months Ended June 30, 2006
United States	587.5	245.7	933.5	478.7
Foreign	24.6	14.9	40.0	29.5
Total	$ 612.1	$ 260.6	$ 973.5	$ 508.2

Domestic and foreign long-lived assets (property, plant and equipment, net) were as follows:

(in millions of U.S. dollars)	June 30, 2007	Dec 31, 2006

United States	$ 292.5	$ 89.3
Foreign	20.7	20.1
Total	$ 313.2	$ 109.4

VALASSIS COMMUNICATIONS, INC.

Notes to Condensed Consolidated Financial Statements

(unaudited)

9. **EARNINGS PER SHARE**

Earnings per common share (EPS) data were computed as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
(in thousands of U.S. dollars)	**2007**	**2006**	**2007**	**2006**
Net earnings	$ 9,776	$ 19,689	$ 21,009	$ 37,746
Basic EPS:				
Weighted average common shares outstanding	47,781	47,767	47,780	47,710
Earnings per common share basic	$ 0.20	$ 0.41	$ 0.44	$ 0.79
Diluted EPS:				
Weighted average common shares outstanding	47,781	47,767	47,780	47,710
Weighted average shares purchased on exercise of dilutive options		1,409		1,467
Shares purchased with proceeds of options/unrecognized compensation	(50)	(1,346)	(53)	(1,398)
Shares contingently issuable	146	33	146	33
Shares applicable to diluted earnings	47,877	47,863	47,873	47,812
Earnings per common share diluted	$ 0.20	$ 0.41	$ 0.44	$ 0.79

Unexercised employee stock options to purchase 6.7 million shares of Valassis common stock were not included in the computations of diluted EPS for the three months ended June 30, 2007 and six months ended June 30, 2007, respectively, because the options exercise prices were greater than the average market price of our common stock during the applicable periods.

10. **GUARANTOR AND NON-GUARANTOR CONDENSED CONSOLIDATING FINANCIAL STATEMENTS**

The following information is presented in accordance with Rule 3-10 of Regulation S-X. The operating and investing activities of the separate legal entities included in the consolidated financial statements are fully interdependent and integrated. Revenues and operating expenses of the separate legal entities include intercompany charges for management and other services. The 2015 Notes issued by Valassis are guaranteed by substantially all of Valassis existing and future domestic subsidiaries on a senior unsecured basis. Each of the subsidiary guarantors is 100% owned, directly or indirectly, by Valassis and has guaranteed the 2015 Notes on a joint and several, full and unconditional basis. Non-wholly-owned subsidiaries, joint ventures, partnerships and foreign subsidiaries are not guarantors of these obligations. The subsidiary guarantors also guarantee the senior secured credit facility described in Note 7.

VALASSIS COMMUNICATIONS, INC.

Notes to Condensed Consolidated Financial Statements

(unaudited)

The following tables present the condensed consolidating balance sheets as of June 30, 2007 and December 31, 2006 and the related condensed consolidating statements of income for the three and six months ended June 30, 2007 and 2006, and the condensed consolidating statements of cash flows for the six months ended June 30, 2007 and 2006.

Condensed Consolidating Balance Sheet

June 30, 2007

(in thousands)

	Parent Company	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Consolidating Adjustments	Consolidated Total
Assets					
Current assets:					
Cash and cash equivalents	$ 21,382	$ 87,298	$ 27,151	$	$ 135,831
Accounts receivable, net	214,970	213,300	28,913	(210)	456,973
Inventories	25,847	10,783	35		36,665
Prepaid expenses and other	21,293	21,230	1,229	(20,000)	23,752
Deferred income taxes	1,051	16,629	370		18,050
Refundable income taxes	10,679	1,027	(91)		11,615
Total current assets	295,222	350,267	57,607	(20,210)	682,886
Property, plant and equipment, net	16,293	276,224	13,329	7,385	313,231
Intangible assets, net	35,544	1,103,586	6,988	(7,244)	1,138,874
Investments	1,430,091	38,118		(1,461,407)	6,802
Other assets	30,360	(692)	197	(207)	29,658
Total assets	$ 1,807,510	$ 1,767,503	$ 78,121	$ (1,481,683)	$ 2,171,451

	Parent Company	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Consolidating Adjustments	Consolidated Total
Liabilities and Stockholders Equity					
Current liabilities:					
Current portion, long-term debt	$ 30,900	$	$	$	$ 30,900
Accounts payable	171,297	125,684	19,318	(14,904)	301,395
Accrued expenses	48,649	56,747	11,556	(5,372)	111,580
Progress billings	27,897	16,580	6,776		51,253
Total current liabilities	278,743	199,011	37,650	(20,276)	495,128
Long-term debt	1,332,573				1,332,573
Other non-current liabilities		8,833	2,353		11,186
Deferred income taxes	3,506	136,370			139,876
Stockholders equity	192,688	1,423,289	38,118	(1,461,407)	192,688

Total liabilities and stockholders equity	$ 1,807,510	$ 1,767,503	$ 78,121	$ (1,481,683)	$ 2,171,451

VALASSIS COMMUNICATIONS, INC.

Notes to Condensed Consolidated Financial Statements

(unaudited)

Condensed Consolidating Balance Sheet

December 31, 2006

(in thousands)

	Parent Company	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Consolidating Adjustments	Consolidated Total
Assets					
Current assets:					
Cash and cash equivalents	$ 21,463	$ 13,173	$ 17,983	$	$ 52,619
Auction-rate securities	91,519	11,014			102,533
Accounts receivable, net	246,944	61,708	30,427		339,079
Inventories	25,834				25,834
Prepaid expenses and other	(5,043)	28,085	1,863	(8,224)	16,681
Deferred income taxes	1,094	494	201		1,789
Refundable income taxes	3,552	286	119		3,957
Total current assets	385,363	114,760	50,593	(8,224)	542,492
Property, plant and equipment, net	17,955	71,381	12,665	7,385	109,386
Intangible assets, net	35,656	98,009	6,988	(7,244)	133,409
Investments	216,595	31,696		(243,392)	4,899
Other assets	12,495	(1,244)	179	(190)	11,240
Total assets	$ 668,064	$ 314,602	$ 70,425	$ (251,665)	$ 801,426

	Parent Company	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Consolidating Adjustments	Consolidated Total
Liabilities and Stockholders Equity					
Current liabilities:					
Accounts payable	$ 169,608	$ 81,822	$ 19,701	$ (2,297)	$ 268,834
Accrued expenses	28,448	11,543	10,113	(5,976)	44,128
Progress billings	38,997	2,869	7,392		49,258
Total current liabilities	237,053	96,234	37,206	(8,273)	362,220
Long-term debt	259,931				259,931
Other non-current liabilities		6,672	1,523		8,195
Deferred income taxes	3,506				3,506
Stockholders equity	167,574	211,696	31,696	(243,392)	167,574
Total liabilities and stockholders equity	$ 668,064	$ 314,602	$ 70,425	$ (251,665)	$ 801,426

VALASSIS COMMUNICATIONS, INC.

Notes to Condensed Consolidated Financial Statements

(unaudited)

Condensed Consolidating Statement of Income

Three Months Ended June 30, 2007

(in thousands)

	Parent Company	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Consolidating Adjustments	Consolidated Total
Revenues	$ 180,032	$ 418,199	$ 26,120	$ (12,204)	$ 612,147
Cost and expenses:					
Cost of products sold	152,029	312,897	20,100	(12,204)	472,822
Selling, general and administrative	13,346	76,560	6,458		96,364
Amortization	55	2,257			2,312
Total costs and expenses	165,430	391,714	26,558	(12,204)	571,498
Earnings from operations	14,602	26,485	(438)		40,649
Other expenses (income):					
Interest expense	25,225		3		25,228
Other income, net	(201)	(1,173)	(111)		(1,485)
Total other expenses (income)	25,024	(1,173)	(108)		23,743
Earnings/(loss) before income taxes	(10,422)	27,658	(330)		16,906
Income taxes	(2,012)	8,993	149		7,130
Equity in net earnings/(loss) of subsidiary	18,186	(479)		(17,707)	
Net earnings/(loss)	$ 9,776	$ 18,186	$ (479)	$ (17,707)	$ 9,776

Condensed Consolidating Statement of Income

Three Months Ended June 30, 2006

(in thousands)

	Parent Company	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Consolidating Adjustments	Consolidated Total
Revenues	$ 175,158	$ 70,432	$ 16,367	$ (1,364)	$ 260,593
Cost and expenses:					
Cost of products sold	145,188	42,017	12,131	(1,364)	197,972

Selling, general and administrative	5,414	21,019	4,082		30,515
Amortization	55	83			138
Total costs and expenses	150,657	63,119	16,213	(1,364)	228,625
Earnings from operations	24,501	7,313	154		31,968
Other expenses (income):					
Interest expense	2,840	(469)	(155)		2,216
Other income, net	(1,116)	347	41		(728)
Total other expenses (income)	1,724	(122)	(114)		1,488
Earnings before income taxes	22,777	7,435	268		30,480
Income taxes	9,590	732	469		10,791
Equity in net earnings/(loss) of subsidiary	6,502	(201)		(6,301)	
Net earnings/(loss)	$ 19,689	$ 6,502	$ (201)	$ (6,301)	$ 19,689

VALASSIS COMMUNICATIONS, INC.

Notes to Condensed Consolidated Financial Statements

(unaudited)

Condensed Consolidating Statement of Income

Six Months Ended June 30, 2007

(in thousands)

	Parent Company	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Consolidating Adjustments	Consolidated Total
Revenues	$ 349,299	$ 595,817	$ 42,807	$ (14,472)	$ 973,451
Cost and expenses:					
Cost of products sold	293,241	440,085	32,985	(14,472)	751,839
Selling, general and administrative	26,933	113,121	10,836		150,890
Amortization	111	3,109			3,220
Total costs and expenses	320,285	556,315	43,821	(14,472)	905,949
Earnings from operations	29,014	39,502	(1,014)		67,502
Other expenses (income):					
Interest expense	35,842		5		35,847
Other income, net	(1,861)	(1,579)	(223)		(3,663)
Total other expenses (income)	33,981	(1,579)	(218)		32,184
Earnings/(loss) before income taxes	(4,967)	41,081	(796)		35,318
Income taxes	1,831	12,107	371		14,309
Equity in net earnings/(loss) of subsidiary	27,807	(1,167)		(26,640)	
Net earnings/(loss)	$ 21,009	$ 27,807	$ (1,167)	$ (26,640)	$ 21,009

Condensed Consolidating Statement of Income

Six Months Ended June 30, 2006

(in thousands)

	Parent Company	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Consolidating Adjustments	Consolidated Total
Revenues	$ 339,262	$ 139,421	$ 32,186	$ (2,631)	$ 508,238
Cost and expenses:					
Cost of products sold	276,236	85,904	23,732	(2,631)	383,241

Selling, general and administrative	18,914	36,275	8,066		63,255
Amortization	111	167			278
Total costs and expenses	295,261	122,346	31,798	(2,631)	446,774
Earnings from operations	44,001	17,075	388		61,464
Other expenses (income):					
Interest expense	5,692	(469)	(152)		5,071
Other income, net	(1,991)		(91)		(2,082)
Total other expenses (income)	3,701	(469)	(243)		2,989
Earnings before income taxes	40,300	17,544	631		58,475
Income taxes	18,192	1,561	976		20,729
Equity in net earnings/(loss) of subsidiary	15,638	(345)		(15,293)	
Net earnings/(loss)	$ 37,746	$ 15,638	$ (345)	$ (15,293)	$ 37,746

VALASSIS COMMUNICATIONS, INC.

Notes to Condensed Consolidated Financial Statements

(unaudited)

Condensed Consolidating Statement of Cash Flows

Six Months Ended June 30, 2007

(in thousands)

	Parent Company	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Consolidating Adjustments	Consolidated Total
Operating activities					
Net cash provided by operating activities	$ 14,748	$ 73,145	$ 8,814	$	$ 96,707
Investing Activities					
Additions to property, plant and equipment	(2,000)	(10,035)	(190)		(12,225)
Acquisition of ADVO, net of cash acquired	(1,187,301)				(1,187,301)
Purchases of auction rate securities	(146,262)	(10,073)			(156,335)
Proceeds from sales of auction rate securities	237,781	21,088			258,869
Investments and advances to affiliated companies	(1,000)				(1,000)
Other	(360)				