CELADON GROUP INC
Form 10-Q
April 30, 2007

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

FORM 10-Q

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

For the quarterly period ended March 31, 2007

or

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

Commission file number: 000-23192

CELADON GROUP, INC.
(Exact name of registrant as specified in its charter)

Delaware	**13-3361050**
(State or other jurisdiction of incorporation or organization)	(IRS Employer Identification No.)
9503 East 33rd Street **One Celadon Drive** **Indianapolis, IN**	**46235-4207**
(Address of principal executive offices)	(Zip Code)

(317) 972-7000
(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes [X] No [ ]

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

Large accelerated filer [ ]   Accelerated filer [X]   Non-accelerated filer [ ]

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12-b2 of the Exchange Act).

Yes [ ] No [X]

As of April 24, 2007 (the latest practicable date), 23,512,495 shares of the registrant's common stock, par value $0.033 per share, were outstanding.

CELADON GROUP, INC.

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Part I. Financial Information

Item I. Financial Statements

CELADON GROUP, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS
March 31, 2007 and June 30, 2006
(Dollars in thousands except per share and par value amounts)

	March 31, 2007 (unaudited)	June 30, 2006
A S S E T S		
Current assets:		
Cash and cash equivalents	$ 1,813	$ 1,674
Trade receivables, net of allowance for doubtful accounts of $1,247 and $1,269 at March 31, 2007 and June 30, 2006	56,132	55,462
Prepaid expenses and other current assets	11,892	10,132
Tires in service	2,763	2,737
Equipment held for resale	11,781	---
Income tax receivable	518	5,216
Deferred income taxes	1,351	1,867
Total current assets	86,250	77,088
Property and equipment	201,948	121,733
Less accumulated depreciation and amortization	39,238	30,466
Net property and equipment	162,710	91,267
Tires in service	1,418	1,569
Goodwill	19,137	19,137
Other assets	1,088	1,005
Total assets	$ 270,603	$ 190,066
L I A B I L I T I E S A N D S T O C K H O L D E R S' E Q U I T Y		
Current liabilities:		
Accounts payable	$ 7,930	$ 4,369
Accrued salaries and benefits	13,564	16,808
Accrued insurance and claims	7,464	7,048
Accrued fuel expense	5,878	6,481
Other accrued expenses	12,423	12,018
Current maturities of long-term debt	10,200	975
Current maturities of capital lease obligations	3,808	507
Total current liabilities	61,267	48,206
Long-term debt, net of current maturities	27,358	9,608
Capital lease obligations, net of current maturities	25,552	933
Deferred income taxes	15,517	9,867

Minority interest		25		25
Stockholders’ equity:				
Preferred stock, $1.00 par value, authorized 179,985 shares; no shares issued and outstanding		---		---
Common stock, $0.033 par value, authorized 40,000,000 shares; issued 23,509,308 and 23,111,367 shares at March 31, 2007 and June 30, 2006		776		763
Retained earnings		49,200		32,092
Additional paid-in capital		92,968		90,828
Accumulated other comprehensive loss		(2,060)		(2,256)
Total stockholders’ equity		140,884		121,427
Total liabilities and stockholders’ equity	$	270,603	$	190,066

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

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CELADON GROUP, INC.
CONDENSED CONSOLIDATED STATEMENTS OF INCOME
(Dollars in thousands except per share amounts)
(Unaudited)

	For the three months ended March 31,		For the nine months ended March 31,	
	2007	2006	2007	2006
Revenue:				
Freight revenue	$ 105,162	$ 100,844	$ 320,281	$ 307,072
Fuel surcharges	15,238	14,469	50,717	46,450
	120,400	115,313	370,998	353,522
Operating expenses:				
Salaries, wages, and employee benefits	35,829	35,697	107,558	106,028
Fuel	27,547	25,289	84,921	79,436
Operations and maintenance	8,321	7,087	23,573	21,811
Insurance and claims	3,299	3,620	10,829	10,967
Depreciation and amortization	6,679	3,199	14,163	9,283
Revenue equipment rentals	7,281	9,718	25,301	30,344
Purchased transportation	16,908	16,272	53,059	51,935
Costs of products and services sold	1,480	1,349	5,342	3,990
Professional and consulting fees	537	644	1,524	2,197
Communications and utilities	1,248	1,007	3,549	3,050
Operating taxes and licenses	2,136	1,891	6,385	6,104
General and other operating	1,515	1,574	4,556	4,539
Total operating expenses	112,780	107,347	340,760	329,684
Operating income	7,620	7,966	30,238	23,838
Other (income) expense:				
Interest income	(1)	(41)	(16)	(119)
Interest expense	996	227	2,058	727
Other (income) expense, net	35	3	39	29
Income before income taxes	6,590	7,777	28,157	23,201
Provision for income taxes	2,660	3,100	11,049	9,041
Net income	$ 3,930	$ 4,677	$ 17,108	$ 14,160
Earnings per common share:				
Diluted earnings per share	$ 0.17	$ 0.20	$ 0.72	$ 0.61
Basic earnings per share	$ 0.17	$ 0.20	$ 0.73	$ 0.62
Average shares outstanding:				
Diluted	23,739	23,496	23,657	23,333
Basic	23,483	22,928	23,391	22,750

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

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CELADON GROUP, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
For the nine months ended March 31, 2007 and 2006
(Dollars in thousands)
(Unaudited)

	2007	2006
Cash flows from operating activities:		
Net income	$ 17,108	$ 14,160
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	14,399	9,452
Gain on sale of equipment	(236)	(169)
Stock based compensation	1,080	2,484
Deferred income taxes	6,166	(1,682)
Provision for doubtful accounts	288	556
Changes in assets and liabilities:		
Trade receivables	(959)	2,620
Income tax recoverable	4,698	(905)
Tires in service	125	764
Prepaid expenses and other current assets	(1,761)	(3,147)
Other assets	230	(138)
Accounts payable and accrued expenses	823	(3,593)
Income tax payable	----	(265)
Net cash provided by operating activities	41,961	20,137
Cash flows from investing activities:		
Purchase of property and equipment	(50,386)	(47,407)
Proceeds on sale of property and equipment	30,238	32,447
Purchase of businesses, net of cash	(29,457)	---
Net cash used in investing activities	(49,605)	(14,960)
Cash flows from financing activities:		
Proceeds from issuances of common stock	785	900
Proceeds from bank borrowings and debt	10,250	---
Payments on long-term debt	(2,113)	(1,095)
Principal payments under capital lease obligations	(1,139)	(773)
Net cash provided by (used in) provided by financing activities	7,783	(968)
Increase in cash and cash equivalents	139	4,209
Cash and cash equivalents at beginning of period	1,674	11,115
Cash and cash equivalents at end of period	$ 1,813	$ 15,324
Supplemental disclosure of cash flow information:		
Interest paid	$ 2,004	$ 717
Income taxes paid	$ 899	$ 12,215

Supplemental disclosure of non-cash flow investing activities:				
Lease obligation/debt incurred in the purchase of equipment	$	47,898	$	1,876

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

CELADON GROUP, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
March 31, 2007
(Unaudited)

1. Basis of Presentation

The accompanying unaudited condensed consolidated financial statements include the accounts of Celadon Group, Inc. and its majority owned subsidiaries (the "Company"). All material intercompany balances and transactions have been eliminated in consolidation.

The unaudited condensed consolidated financial statements have been prepared in accordance with generally accepted accounting principles ("GAAP") in the United States of America pursuant to the rules and regulations of the Securities and Exchange Commission ("SEC") for interim financial statements. Certain information and footnote disclosures have been condensed or omitted pursuant to such rules and regulations. In the opinion of management, the accompanying unaudited financial statements reflect all adjustments (all of a normal recurring nature), which are necessary for a fair presentation of the financial condition and results of operations for these periods. The results of operations for the interim period are not necessarily indicative of the results for a full year. These condensed consolidated financial statements and notes thereto should be read in conjunction with the Company's condensed consolidated financial statements and notes thereto, included in the Company's Annual Report on Form 10-K for the fiscal year ended June 30, 2006.

The preparation of the financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

2. New Accounting Pronouncements

In February 2007, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities* ("SFAS 159"). SFAS 159 permits entities to choose to measure certain financial assets and liabilities at fair value. Unrealized gains and losses on items for which the fair value option has been elected are reported in earnings. SFAS 159 is effective for fiscal years beginning after November 15, 2007. The Company is currently assessing the expected impact of adopting SFAS 159 on our consolidated financial position and results of operations when it becomes effective.

In September 2006, the SEC issued Staff Accounting Bulletin 108 *Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements* ("SAB 108"). SAB 108 provides interpretive guidance on how the effects of the carryover or reversal of prior year misstatements should be considered in quantifying a current year misstatement. The SEC staff believes that registrants should quantify errors using both a balance sheet and an income statement approach and evaluate whether either approach results in quantifying a misstatement that, when all relevant quantitative and qualitative factors are considered, is material. The guidance in SAB 108 must be applied to annual financial statements for fiscal years ending after November 15, 2006. The Company is currently assessing the impact of adopting SAB 108 but does not expect that it will have a material effect on our consolidated financial position or results of operations.

In September 2006, FASB issued Statement of Financial Accounting Standards ("SFAS") No. 157, *Fair Value Measurements* ("SFAS 157"). SFAS 157 defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles ("GAAP") and expands disclosures about fair value measurements. This statement was published due to the different definitions of fair value and the limited guidance for applying those definitions in GAAP that are among the many accounting pronouncements that require fair value measurements. SFAS 157 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. This statement is effective for financial statements issued for fiscal years beginning after November 15, 2007. Additionally, prospective application of this statement is required as of the beginning of the fiscal year in which it is initially applied. SFAS 157 is not expected to have a material impact upon our financial position, results of operations and cash flows.

CELADON GROUP, INC.
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In June 2006, FASB issued Interpretation No. 48, *Accounting for Uncertainty in Income Taxes, an interpretation of FASB Statement No. 109* ("FIN 48"). FIN 48 prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN 48 also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure and transition. Our effective date of this interpretation is July 1, 2007, the first fiscal year beginning after December 15, 2006. We are continuing to evaluate the impact of the adoption of FIN 48 on our consolidated financial statements.

In September 2006, FASB issued SFAS No. 158, *Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans-an amendment of FASB Statements No. 87, 88, 106, and 132(R).* This statement requires an employer to recognize the overfunded or underfunded status of a defined benefit postretirement plan (other than a multiemployer plan) as an asset or liability in its statement of financial position and to recognize changes in that funded status in the year in which the changes occur through comprehensive income of a business entity. This statement also requires an employer to measure the funded status of a plan as of the date of its year-end statement of financial position, with limited exceptions. The provisions of SFAS No. 158 are effective as of the end of the fiscal year ending after December 15, 2006. As of March 31, 2007, management believes that SFAS No. 158 will have no effect on the financial position, results of operations, and cash flows of the Company.

3. Stock Splits

In fiscal 2006, the Board of Directors approved two three-for-two stock splits, effected in the form of a fifty percent (50%) stock dividend. The stock split distribution dates were February 15, 2006 and June 15, 2006 to stockholders of record as of the close of business on February 1, 2006 and June 1, 2006. Unless otherwise indicated, all share and per share amounts have been adjusted to give retroactive effect to these stock-splits.

4. Earnings Per Share

The difference in basic and diluted weighted average shares is due to the assumed exercise of outstanding stock options. A reconciliation of the basic and diluted earnings per share calculation was as follows (amounts in thousands, except per share amounts):

	For three months ended March 31,		For nine months ended March 31,	
	2007	**2006**	**2007**	**2006**
Net income	$ 3,930	$ 4,677	$ 17,108	$ 14,160
Denominator				
Weighted average number of common shares outstanding	23,483	22,928	23,391	22,750
Equivalent shares issuable upon exercise of stock options	256	568	266	583
Diluted shares	23,739	23,496	23,657	23,333

Earnings per share				
Basic	$ 0.17	$ 0.20	$ 0.73	$ 0.62
Diluted	$ 0.17	$ 0.20	$ 0.72	$ 0.61

CELADON GROUP, INC.
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5. Segment Information and Significant Customers

The Company operates in two segments, transportation and e-commerce. The Company generates revenue in the transportation segment, primarily by providing truckload-hauling services through its subsidiaries Celadon Trucking Services Inc. ("CTSI"), Celadon Logistics Services, Inc (“CLSI”), Servicios de Transportacion Jaguar, S.A. de C.V., ("Jaguar"), and Celadon Canada, Inc. ("CelCan"). The Company provides certain services over the Internet through its e-commerce subsidiary TruckersB2B, Inc. ("TruckersB2B"). The e-commerce segment generates revenue by providing discounted fuel, tires, and other products and services to small and medium-sized trucking companies. The Company evaluates the performance of its operating segments based on operating income (amounts below in thousands).

	Transportation	E-commerce	Consolidated
Three months ended March 31, 2007			
Operating revenue	$ 118,203	$ 2,197	$ 120,400
Operating income	7,272	348	7,620
Three months ended March 31, 2006			
Operating revenue	$ 113,231	$ 2,082	$ 115,313
Operating income	7,547	419	7,966
Nine months ended March 31, 2007			
Operating revenue	$ 363,330	$ 7,668	$ 370,998
Operating income	29,034	1,204	30,238
Nine months ended March 31, 2006			
Operating revenue	$ 347,383	$ 6,139	$ 353,522
Operating income	22,705	1,133	23,838

Information as to the Company’s operating revenue by geographic area is summarized below (in thousands). The Company allocates operating revenue based on country of origin of the tractor hauling the freight:

	For the three months ended March 31,		For the nine months ended March 31,	
	2007	2006	2007	2006
Operating revenue:				
United States	$ 99,373	$ 95,177	$ 305,575	$ 289,391
Canada	13,654	13,629	43,888	43,364
Mexico	7,373	6,507	21,535	20,767
Total	$ 120,400	$ 115,313	$ 370,998	$ 353,522

No customer accounted for more than 10% of the Company’s total revenue during any of its two most recent fiscal years or interim periods presented above.

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6. Stock Based Compensation

On July 1, 2005, the Company adopted SFAS 123(R) which requires all share-based payments to employees, including grants of employee stock options, be recognized in the financial statements based upon a grant-date fair value of an award. In January 2006, shareholders approved the 2006 Omnibus Plan ("2006 Plan"), that provides various vehicles to compensate the Company's key employees. The 2006 Plan utilizes such vehicles as stock options, restricted stock grants, and stock appreciation rights ("SARs"). The 2006 Plan authorized the Company to grant 1,687,500 shares. In fiscal 2007, the Company granted 20,000 stock options and 68,160 restricted shares. The Company is authorized to grant an additional 800,871 shares.

The following table summarizes the expense components of our stock based compensation program:

	For three months ended March 31,		For nine months ended March 31,	
	2007	**2006**	**2007**	**2006**
Stock options expense	$ 247	$ 282	$ 734	$ 282
Restricted stock expense	223	141	530	328
Stock appreciation rights expense	103	312	(1,775)	1,950
Total stock related compensation expense	$ 573	$ 735	$ (511)	$ 2,560

The Company has granted a number of stock options under various plans. Options granted to employees have been granted with an exercise price equal to the market price on the grant date and expire on the tenth anniversary of the grant date. The majority of options granted to employees vest 25 percent per year, commencing with the first anniversary of the grant date. Options granted to non-employee directors have been granted with an exercise price equal to the market price on the grant date, vest over three or four years, commencing with the first anniversary of the grant date, and expire on the tenth anniversary of the grant date.

A summary of the activity of the Company's stock option plans as of March 31, 2007 and changes for the nine months then ended is presented below:

Options	Shares	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Term	Aggregate Intrinsic Value
Outstanding at July 1, 2006	1,446,710	$ 7.44	---	---
Granted	20,000	$ 18.84	---	---
Exercised	(329,872)	$ 2.68	---	---
Forfeited or expired	---	---	---	---

Outstanding at March 31, 2007	1,136,838	$	9.02	7.09	$	8,728,302
Exercisable at March 31, 2007	620,938	$	5.68	5.66	$	6,841,190

The fair value of each option grant is estimated on the date of grant using the Black-Scholes option-pricing model with the following weighted-average assumptions:

	Fiscal 2007	Fiscal 2006
Weighted average grant date fair value	$9.97	$12.58
Dividend yield	0	0
Expected volatility	64.2%	50.1%
Risk-free interest rate	4.92%	4.35%
Expected lives	4 years	4 years

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Restricted Shares

	Number of Shares	Weighted Average Grant Date Fair Value
Unvested at July 1, 2006	274,230	$8.96
Granted	68,160	16.79
Vested	---	---
Forfeited	---	---
Unvested at March 31, 2007	342,390	$10.52

Restricted shares granted to employees have been granted with a share price equal to the market price on the grant date and vest by 25 percent per year, commencing with the first anniversary of the grant date. In addition, certain financial targets must be met for these shares to vest. Restricted shares granted to non-employee directors have been granted with an exercise price equal to the market price on the grant date and vest on the date of the Company's next annual meeting.

As of March 31, 2007, the Company had $2.7 million and $2.4 million of total unrecognized compensation expense related to stock options and restricted stock, respectively, that is expected to be recognized over the remaining period of approximately 3.4 years for stock options and 2.1 years for restricted stock.

Stock Appreciation Rights

	Number of Shares	Weighted Average Grant Date Fair Value
Unvested at July 1, 2006	571,437	$7.73
Granted	---	---
Paid	(7,871)	$4.48
Forfeited	(309,176)	$7.10
Unvested at March 31, 2007	254,390	$8.59

SARs granted to employees vest on a 3 or 4 year vesting schedule. In addition, certain financial targets must be met for the SARs to vest. During the first quarter of fiscal 2007, the Company gave SARs grantees the opportunity to enter into an alternative fixed compensation arrangement whereby the grantee would forfeit all rights to SARs compensation in exchange for a guaranteed quarterly payment for the remainder of the underlying SARs term. This alternative arrangement is subject to continued service to the Company or one of its subsidiaries. The number of forfeited SARs reported above reflects entry into this alternative arrangement. These fixed payments will be accrued quarterly from July 1, 2006 to March 31, 2009. The Company offered this alternative arrangement to mitigate the volatility to earnings from stock price variance on the SARs.

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(Unaudited)

7. Comprehensive Income

Comprehensive income consisted of the following components for the third quarter of fiscal 2007 and 2006, respectively, and the nine months ended March 31, 2007 and 2006, respectively (in thousands):

	Three months ended March 31,		Nine months ended March 31,	
	2007	2006	2007	2006