

GNC HOLDINGS, INC.  
Form 10-Q  
October 21, 2011  
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# UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

## Form 10-Q

(Mark one)

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

For the quarterly period ended **September 30, 2011**

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: **333-144396**

## GNC Holdings, Inc.

(Exact name of registrant as specified in its charter)

**Delaware**  
(State or other jurisdiction of  
Incorporation or organization)

**300 Sixth Avenue**  
**Pittsburgh, Pennsylvania**  
(Address of principal executive offices)

**20-8536244**  
(I.R.S. Employer  
Identification No.)

**15222**  
(Zip Code)

Registrant's telephone number, including area code: **(412) 288-4600**

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, 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  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 the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act:

Large accelerated filer       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  No

As of October 17, 2011, the number of outstanding shares of Class A common stock, par value \$0.001 per share (the Class A common stock), and the number of outstanding shares of Class B common stock, par value \$0.001 per share (the Class B common stock), of GNC Holdings, Inc. were 92,023,956 shares and 13,782,311 shares, respectively.

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Table of Contents**PART I - FINANCIAL INFORMATION****Item 1. Financial Statements****GNC HOLDINGS, INC. AND SUBSIDIARIES****Consolidated Balance Sheets**

(in thousands, including share data)

|  | <b>September 30,<br/>2011<br/>(unaudited)</b> | <b>December 31,<br/>2010</b> |
|--|---|------------------------------|
| Current assets:  |   |                              |
| Cash and cash equivalents  | \$ 146,107                                    | \$ 193,902                   |
| Receivables, net   | 118,074                                       | 102,874                      |
| Inventories (Note 3)   | 416,282                                       | 381,949                      |
| Prepays and other current assets   | 34,102  | 40,569                       |
| Total current assets   | 714,565                                       | 719,294                      |
| Long-term assets:  |   |                              |
| Goodwill (Note 4)  | 637,394                                       | 625,241                      |
| Brands (Note 4)  | 720,000                                       | 720,000                      |
| Other intangible assets, net (Note 4)  | 151,550                                       | 147,224                      |
| Property, plant and equipment, net   | 192,808                                       | 193,428                      |
| Deferred financing fees, net   | 12,173  | 14,129                       |
| Other long-term assets   | 7,225   | 5,767                        |
| Total long-term assets   | 1,721,150                                     | 1,705,789                    |
| Total assets   | \$ 2,435,715                                  | \$ 2,425,083                 |
| Current liabilities:   |   |                              |
| Accounts payable   | 137,372                                       | 98,662                       |
| Accrued payroll and related liabilities  | 30,094  | 25,656                       |
| Accrued interest (Note 5)  | 1,768   | 13,372                       |
| Current portion, long-term debt (Note 5)   | 1,592   | 28,070                       |
| Deferred revenue and other current liabilities   | 71,046  | 69,065                       |
| Total current liabilities  | 241,872                                       | 234,825                      |
| Long-term liabilities:   |   |                              |
| Long-term debt (Note 5)  | 900,290                                       | 1,030,429                    |
| Deferred tax liabilities, net  | 286,899                                       | 288,015                      |
| Other long-term liabilities  | 35,064  | 33,950                       |
| Total long-term liabilities  | 1,222,253                                     | 1,352,394                    |
| Total liabilities  | 1,464,125                                     | 1,587,219                    |
| Preferred stock, \$0.001 par value, 60,000 shares authorized:<br>Series A, 30,500 shares designated, 30,134 shares issued, 29,867 shares<br>outstanding and 267 shares held in treasury at December 31, 2010 | -   | 218,381                      |
| Stockholders' equity:  |   |                              |
| Common stock, \$0.001 par value, 150,000 shares authorized:<br>Class A, 91,927 shares issued and 91,158 shares outstanding and 769<br>shares held in treasury at September 30, 2011 and 59,968 shares issued | 91  | 60                           |

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and 59,199 shares outstanding and 769 shares held in treasury at  
December 31, 2010

Class B, 13,782 shares and 28,169 issued and outstanding at  
September 30, 2011 and December 31, 2010, respectively

|   |              |              |
|---|--------------|--------------|
| Paid-in-capital                               | 14           | 28           |
| Retained earnings                             | 710,480      | 451,728      |
| Treasury stock, at cost                       | 261,088      | 171,224      |
| Accumulated other comprehensive income (loss) | (2,277)      | (2,277)      |
| Total stockholders' equity                    | 2,194        | (1,280)      |
|   | 971,590      | 619,483      |
| Total liabilities and stockholders' equity    | \$ 2,435,715 | \$ 2,425,083 |

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

Table of Contents**GNC HOLDINGS, INC. AND SUBSIDIARIES****Consolidated Statements of Operations****(unaudited)****(in thousands, except per share data)**

|  | Three months ending September 30, |            | Nine months ended September 30, |              |
|--|-----------------------------------|------------|---------------------------------|--------------|
|  | 2011                              | 2010       | 2011                            | 2010         |
| Revenue  | \$ 538,028                        | \$ 465,660 | \$ 1,562,571                    | \$ 1,386,409 |
| Cost of sales, including cost of warehousing, distribution and occupancy | 343,129                           | 302,601    | 992,908                         | 893,839      |
| Gross profit   | 194,899                           | 163,059    | 569,663                         | 492,570      |
| Compensation and related benefits  | 72,375                            | 69,194     | 219,011                         | 204,668      |
| Advertising and promotion  | 12,433                            | 10,854     | 40,031                          | 40,430       |
| Other selling, general and administrative                                | 26,629                            | 24,313     | 84,530                          | 75,276       |
| Foreign currency loss (gain)   | 225                               | (92)       | 106                             | (149)        |
| Transaction related costs  | 637                               | -          | 12,999                          | -            |
| Operating income   | 82,600                            | 58,790     | 212,986                         | 172,345      |
| Interest expense, net (Note 5)   | 10,418                            | 16,296     | 64,517                          | 49,182       |
| Income before income taxes   | 72,182                            | 42,494     | 148,469                         | 123,163      |
| Income tax expense (Note 10)   | 23,519                            | 15,825     | 53,879                          | 45,422       |
| Net income   | \$ 48,663                         | \$ 26,669  | \$ 94,590                       | \$ 77,741    |
| <b>Income per share - Basic and Diluted:</b>                             |                                   |            |                                 |              |
| Net income   | \$ 48,663                         | \$ 26,669  | \$ 94,590                       | \$ 77,741    |
| Preferred stock dividends  | -                                 | (5,213)    | (4,726)                         | (15,261)     |
| Net income available to common shareholders                              | \$ 48,663                         | \$ 21,456  | \$ 89,864                       | \$ 62,480    |
| Earnings per share:  |                                   |            |                                 |              |
| Basic  | \$ 0.47                           | \$ 0.25    | \$ 0.91                         | \$ 0.72      |
| Diluted  | \$ 0.45                           | \$ 0.24    | \$ 0.89                         | \$ 0.70      |
| Weighted average common shares outstanding:                              |                                   |            |                                 |              |
| Basic  | 104,390                           | 87,357     | 98,223                          | 87,350       |
| Diluted  | 107,351                           | 88,374     | 100,858                         | 88,644       |

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

Table of Contents**GNC HOLDINGS INC. AND SUBSIDIARIES****Consolidated Statement of Stockholders Equity and Comprehensive Income (Loss)**

(in thousands, including share data)

|  | Common Stock   |                 | Treasury Stock | Paid-in-Capital | Retained Earnings | Accumulated Other Comprehensive Income/(Loss) | Total Stockholders Equity |                   |                   |
|--|----------------|-----------------|----------------|-----------------|-------------------|---|---------------------------|-------------------|-------------------|
|  | Class A Shares | Class B Dollars |                |                 |                   |   |                           | Class B Shares    | Class A Dollars   |
| <b>Balance at December 31, 2010</b>  | <b>59,199</b>  | <b>\$ 60</b>    | <b>28,169</b>  | <b>\$ 28</b>    | <b>\$ (2,277)</b> | <b>\$ 451,728</b>                             | <b>\$ 171,224</b>         | <b>\$ (1,280)</b> | <b>\$ 619,483</b> |
| <i>Comprehensive income (loss):</i>  |                |                 |                |                 |                   |   |                           |                   |                   |
| Net income   | -              | -               | -              | -               | -                 | -   | 94,590                    | -                 | 94,590            |
| Unrealized gain on derivatives designated and qualified as cash flow hedges, net of tax of \$2,718 | -              | -               | -              | -               | -                 | -   | -                         | 4,751             | 4,751             |
| Foreign currency translation adjustments   | -              | -               | -              | -               | -                 | -   | -                         | (1,277)           | (1,277)           |
| <i>Comprehensive income</i>  |                |                 |                |                 |                   |   |                           |                   | <i>98,064</i>     |
| Issuance of common stock   | 16,000         | 16              | -              | -               | -                 | 237,237                                       | -                         | -                 | 237,253           |
| Conversion of stock  | 14,387         | 14              | (14,387)       | (14)            | -                 | -   | -                         | -                 | -                 |
| Preferred stock dividends  | -              | -               | -              | -               | -                 | -   | (4,726)                   | -                 | (4,726)           |
| Exercise of stock options  | 1,572          | 1               | -              | -               | -                 | 18,620  | -                         | -                 | 18,621            |
| Non-cash stock-based compensation  | -              | -               | -              | -               | -                 | 2,895   | -                         | -                 | 2,895             |
| <b>Balance at September 30, 2011 (unaudited)</b>   | <b>91,158</b>  | <b>\$ 91</b>    | <b>13,782</b>  | <b>\$ 14</b>    | <b>\$ (2,277)</b> | <b>\$ 710,480</b>                             | <b>\$ 261,088</b>         | <b>\$ 2,194</b>   | <b>\$ 971,590</b> |
| <b>Balance at December 31, 2009</b>  | <b>59,170</b>  | <b>\$ 60</b>    | <b>28,169</b>  | <b>\$ 28</b>    | <b>\$ (2,474)</b> | <b>\$ 448,556</b>                             | <b>\$ 95,263</b>          | <b>\$ (7,199)</b> | <b>\$ 534,234</b> |
| <i>Comprehensive income (loss):</i>  |                |                 |                |                 |                   |   |                           |                   |                   |
| Net income   | -              | -               | -              | -               | -                 | -   | 77,741                    | -                 | 77,741            |
| Unrealized gain on derivatives designated and qualified as cash flow hedges, net of tax of \$1,367 | -              | -               | -              | -               | -                 | -   | -                         | 2,389             | 2,389             |



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|  |               |              |               |              |                   |                   |                   |                   |                   |
|--|---------------|--------------|---------------|--------------|-------------------|-------------------|-------------------|-------------------|-------------------|
| Foreign currency translation adjustments         | -             | -            | -             | -            | -                 | -                 | -                 | 501               | 501               |
| <i>Comprehensive income</i>                      |               |              |               |              |                   |                   |                   |                   | <i>80,631</i>     |
| Issuance of common stock                         | 29            | -            | -             | -            | 197               | 4                 | -                 | -                 | 201               |
| Purchase of treasury stock                       | -             | -            | -             | -            | -                 | -                 | -                 | -                 | -                 |
| Preferred stock dividends                        | -             | -            | -             | -            | -                 | -                 | (15,261)          | -                 | (15,261)          |
| Non-cash stock-based compensation                | -             | -            | -             | -            | -                 | 2,376             | -                 | -                 | 2,376             |
| <b>Balance at September 30, 2010 (unaudited)</b> | <b>59,199</b> | <b>\$ 60</b> | <b>28,169</b> | <b>\$ 28</b> | <b>\$ (2,277)</b> | <b>\$ 450,936</b> | <b>\$ 157,743</b> | <b>\$ (4,309)</b> | <b>\$ 602,181</b> |

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

Table of Contents**GNC HOLDINGS, INC. AND SUBSIDIARIES****Consolidated Statements of Cash Flows****(unaudited)****(in thousands)**

|   | <b>Nine Months Ended</b>      |                               |
|---|-------------------------------|-------------------------------|
|   | <b>September 30,<br/>2011</b> | <b>September 30,<br/>2010</b> |
| <b><u>CASH FLOWS FROM OPERATING ACTIVITIES:</u></b>                               |                               |                               |
| Net income  | \$ 94,590                     | \$ 77,741                     |
| Adjustments to reconcile net income to net cash provided by operating activities: |                               |                               |
| Write-off of deferred financing fees - early debt extinguishment                  | 17,418                        | -                             |
| Amortization of original issue discount - early debt extinguishment               | 2,437                         | -                             |
| Depreciation expense  | 28,558                        | 27,940                        |
| Amortization of intangible assets   | 5,786                         | 5,915                         |
| Amortization of deferred financing fees   | 1,884                         | 3,195                         |
| Amortization of original issue discount   | 311                           | 304                           |
| Increase in provision for inventory losses  | 14,582                        | 10,877                        |
| Non-cash stock based compensation   | 2,895                         | 2,376                         |
| Increase (decrease) in provision for losses on accounts receivable                | 309                           | (859)                         |
| Increase (decrease) in net deferred taxes   | 59                            | (1,381)                       |
| Changes in assets and liabilities:  |                               |                               |
| Increase in receivables   | (15,423)                      | (9,659)                       |
| Increase in inventory   | (46,418)                      | (36,974)                      |
| Increase in accounts payable  | 36,155                        | 3,725                         |
| Decrease in interest payable  | (11,604)                      | (8,978)                       |
| Increase in accrued liabilities   | 12,975                        | 22,756                        |
| Other working capital   | 1,866                         | 619                           |
| <b>Net cash provided by operating activities</b>                                  | <b>146,380</b>                | <b>97,597</b>                 |
| <b><u>CASH FLOWS FROM INVESTING ACTIVITIES:</u></b>                               |                               |                               |
| Capital expenditures  | (27,808)                      | (20,969)                      |
| Acquisition of Lucky Vitamin, net of cash acquired                                | (20,998)                      | -                             |
| Other   | (1,437)                       | (278)                         |
| <b>Net cash used in investing activities</b>                                      | <b>(50,243)</b>               | <b>(21,247)</b>               |
| <b><u>CASH FLOWS FROM FINANCING ACTIVITIES:</u></b>                               |                               |                               |
| Payment of 2007 Senior Credit Facility  | (644,382)                     | -                             |
| Repurchase of Class A Preferred Stock   | (223,107)                     | -                             |
| Payment of 2011 Senior Credit Facility  | (300,000)                     | -                             |
| Redemption of Senior Toggle Notes   | (300,000)                     | -                             |
| Redemption of Senior Subordinated Notes   | (110,000)                     | -                             |
| Issuance of new equity  | 237,253                       | 233                           |
| Borrowings on 2011 Senior Credit Facility   | 1,196,200                     | -                             |
| Proceeds from exercised stock options   | 11,125                        | -                             |
| Tax benefit from exercise of stock options  | 8,379                         | -                             |
| Payments on long-term debt  | (1,184)                       | (1,340)                       |
| Deferred financing fees   | (17,346)                      | -                             |
| <b>Net cash used in financing activities</b>                                      | <b>(143,062)</b>              | <b>(1,107)</b>                |
| Effect of exchange rate on cash   | (870)                         | 33                            |
| Net (decrease) increase in cash   | (47,795)                      | 75,276                        |
| Beginning balance, cash   | 193,902                       | 89,948                        |
| Ending balance, cash  | \$ 146,107                    | \$ 165,224                    |

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

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**GNC HOLDINGS, INC. AND SUBSIDIARIES**

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)**

**NOTE 1. NATURE OF BUSINESS**

**General Nature of Business.** GNC Holdings, Inc., formerly GNC Acquisition Holdings Inc., a Delaware corporation ( Holdings ), and collectively with its subsidiaries and, unless the context requires otherwise, its and their respective predecessors, the Company ), is a leading specialty retailer of nutritional supplements, which include: vitamins, minerals and herbal supplements ( VMHS ), sports nutrition products, diet products and other wellness products.

The Company s organizational structure is vertically integrated as the operations consist of purchasing raw materials, formulating and manufacturing products and selling the finished products through its three primary segments: retail, franchising and manufacturing/wholesale. Corporate retail store operations are located in North America and Puerto Rico, and in addition the Company offers products domestically through GNC.com, www.drugstore.com, and beginning in September 2011, LuckyVitamin.com. Franchise stores are located in the United States and 52 international countries (including distribution centers where retail sales are made). The Company operates its primary manufacturing facilities in South Carolina and distribution centers in Arizona, Pennsylvania and South Carolina. The Company manufactures the majority of its branded products, but also merchandises various third party products. Additionally, the Company licenses the use of its trademarks and trade names.

The processing, formulation, packaging, labeling and advertising of the Company s products are subject to regulation by one or more federal agencies, including the Food and Drug Administration ( FDA ), Federal Trade Commission ( FTC ), Consumer Product Safety Commission, United States Department of Agriculture and the Environmental Protection Agency. These activities are also regulated by various agencies of the states and localities in which the Company s products are sold.

In March 2011, General Nutrition Centers, Inc. ( Centers ), a wholly owned subsidiary of Holdings, entered into the 2011 Senior Credit Facility, consisting of a \$1.2 billion Term Loan Facility and an \$80.0 million Revolving Credit Facility, and utilized the proceeds to repay all outstanding indebtedness under the 2007 Senior Credit Facility, the Senior Notes, and the Senior Subordinated Notes.

In April 2011, Holdings consummated an initial public offering of 16.0 million shares of its Class A common stock (the IPO ), at an IPO price of \$16.00 per share. The net proceeds from the IPO, together with cash on hand, were used to redeem all outstanding Series A preferred stock, repay approximately \$300.0 million of outstanding borrowings under the Term Loan Facility, and pay approximately \$11.1 million to satisfy obligations under the ACOF Management Services Agreement and the Class B common stock (see Note 12).

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On August 31, 2011, the Company acquired substantially all of the assets and assumed certain liabilities of S&G Properties, LLC d/b/a LuckyVitamin.com and What s The Big Deal?, Inc. d/b/a Gary s World of Wellness (collectively referred to as Lucky Vitamin ), an online retailer of health and wellness products. The aggregate purchase price of Lucky Vitamin was approximately \$21 million.

On September 7, 2011, the Company filed a registration statement related to a proposed offering of shares of its Class A common stock to be sold exclusively by participating selling stockholders (the proposed Secondary Offering ).

### **NOTE 2. BASIS OF PRESENTATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

The accompanying unaudited consolidated financial statements have been prepared in accordance with the rules and regulations of the Securities and Exchange Commission ( SEC ). Accordingly, certain information and footnote disclosures normally included in the annual financial statements prepared in accordance with accounting principles generally accepted in the United States ( GAAP ) have been omitted. These interim consolidated financial statements should be read in conjunction with the consolidated financial statements and notes included in the prospectus (the Prospectus ) contained in the Company s Registration Statement on Form S-1, as amended (Registration No. 333-169618), which was declared effective on March 31, 2011 (the Registration Statement ). There have been no material changes to the application of critical accounting policies and significant judgments and estimates since December 31, 2010.

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**GNC HOLDINGS, INC. AND SUBSIDIARIES**

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)**

The accompanying unaudited consolidated financial statements include all adjustments (consisting of a normal and recurring nature) that management considers necessary for a fair statement of financial information for the interim periods. Interim results are not necessarily indicative of the results that may be expected for the remainder of the year ending December 31, 2011.

**Principles of Consolidation.** The consolidated financial statements include the accounts of Holdings, all of its subsidiaries and a variable interest entity. All material intercompany transactions have been eliminated in consolidation.

**Use of Estimates.** The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions. Accordingly, these estimates and assumptions affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Some of the most significant estimates pertaining to the Company include the valuation of inventories, the allowance for doubtful accounts, income tax valuation allowances and the recoverability of long-lived assets. On a regular basis, management reviews its estimates utilizing currently available information, changes in facts and circumstances, historical experience and reasonable assumptions. After such reviews and if deemed appropriate, those estimates are adjusted accordingly. Actual results could differ from those estimates.

**Financial Instruments and Derivatives.** As part of the Company's financial risk management program, it has historically used certain derivative financial instruments to reduce its exposure to market risk for changes in interest rates primarily in respect of its long-term debt obligations. The Company has not historically entered into, and does not intend to enter into, derivative transactions for speculative purposes and holds no derivative instruments for trading purposes. Floating-to-fixed interest rate swap agreements, designated as cash flow hedges of interest rate risk, were entered into from time to time to hedge the Company's exposure to interest rate changes on a portion of the Company's floating rate debt. The interest rate swap agreements converted a portion of the Company's floating rate debt to fixed rate debt. Interest rate floors designated as cash flow hedges involve the receipt of variable-rate amounts from a counterparty if interest rates fall below the strike rate on the contract in exchange for an upfront premium. The Company recorded the fair value of these contracts as an asset or a liability, as applicable, in the balance sheet, with the offset to accumulated other comprehensive income (loss), net of tax. The Company measured hedge effectiveness by assessing the changes in the fair value or expected future cash flows of the hedged item. The ineffective portions, if any, were recorded in interest expense in the current period.

For the period ended December 31, 2010, the Company had interest rate swap agreements outstanding that effectively converted notional amounts of an aggregate \$550.0 million of debt from floating to fixed interest rates. The four outstanding agreements were to mature between April 2011 and September 2012. Unrealized gains and losses related to derivatives were reported in accumulated other comprehensive income (loss) and reclassified to interest expense as interest payments were made on the Company's variable-rate debt. In conjunction with a refinancing transaction (the Refinancing) on March 4, 2011, the Company repaid in full the 2007 Senior Credit Facility (the 2007 Senior Credit Facility), its outstanding Senior Notes and its outstanding Senior Subordinated Notes (as defined below), and the four agreements were settled and terminated for an aggregate cash payment of \$8.7 million. During the first quarter of 2011, \$8.1 million of accumulated unrealized losses on the swaps was

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reclassified to interest expense, of which \$5.8 million was accelerated due to the debt retirement and swap terminations on March 4, 2011. No such derivative instruments are currently outstanding. At December 31, 2010, the Company had recorded the fair value of the hedging instrument of \$4.4 million and \$3.1 million in other current liabilities and other long-term liabilities, respectively.

Table of Contents**GNC HOLDINGS, INC. AND SUBSIDIARIES****NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)**

Components of gains and losses recorded in the consolidated balance sheet and consolidated income statements for the three and nine months ended September 30, 2011 and 2010 were as follows:

|  | Three Months Ended<br>September 30, |            | Nine Months Ended<br>September 30, |            |
|--|-------------------------------------|------------|------------------------------------|------------|
|  | 2011                                | 2010       | 2011                               | 2010       |
|  | (unaudited)<br>(in thousands)       |            |                                    |            |
| Loss recognized in OCI on derivative<br>Reclassified from accumulated OCI into<br>income | \$ -                                | \$ (1,988) | \$ (639)                           | \$ (7,262) |
| Other comprehensive income   | -                                   | 3,344      | 8,108                              | 11,018     |
|  | \$ -                                | \$ 1,356   | \$ 7,469                           | \$ 3,756   |

**Transaction Related Costs.** The Company recognizes transaction related costs as expenses in the period incurred. For the three and nine months ended September 30, 2011, the Company recognized \$0.6 million and \$13.0 million, respectively, of expenses related to the IPO and the proposed Secondary Offering.

**Recently Issued Accounting Pronouncements**

In September 2011, the FASB issued updated guidance on the periodic testing of goodwill for impairment. This guidance will allow companies to assess qualitative factors to determine if it is more likely than not that goodwill will be impaired and whether it is necessary to perform the two-step goodwill impairment test required under current accounting standards. This new guidance is effective for the Company for fiscal years beginning after December 15, 2011, with early adoption permitted. The Company is currently evaluating this guidance, but does not expect the adoption will have a material effect on Company's consolidated financial statements.

**NOTE 3. INVENTORIES**

Inventories at each respective period consisted of the following:



|   | September 30,<br>2011<br>(unaudited) | December 31,<br>2010 |
|---|--------------------------------------|----------------------|
|   | (in thousands)                       |                      |
| Finished product ready for sale                 | \$ 337,710                           | \$ 319,212           |
| Work-in-process, bulk product and raw materials | 71,628                               | 57,165               |
| Packaging supplies                              | 6,944                                | 5,572                |
| Total   | \$ 416,282                           | \$ 381,949           |

**NOTE 4. GOODWILL AND INTANGIBLE ASSETS, NET**

Goodwill represents the excess of purchase price over the fair value of identifiable net assets of acquired entities. In accordance with the standard on intangibles and goodwill, goodwill and intangible assets with indefinite useful lives are not amortized, but instead are tested for impairment at least annually. Other intangible assets with finite lives are amortized on a straight-line basis over periods not exceeding 35 years.

For the nine months ended September 30, 2011, the Company acquired 22 franchise stores. These acquisitions were accounted for utilizing the acquisition method of accounting and the Company recorded the acquired inventory, fixed assets, franchise rights and goodwill, with an applicable reduction to receivables and cash. The total purchase price associated with these acquisitions was \$2.1 million, of which \$0.8 million was paid in cash.

On August 31, 2011, the Company acquired substantially all of the assets and assumed certain liabilities of Lucky Vitamin, which was accounted for as a business combination. The total purchase price for this acquisition was approximately \$21 million. Of the purchase price, \$11.5 million was preliminarily allocated to goodwill, \$9.6 million to amortizable intangible assets, \$2.6 million to current assets acquired, \$0.7 million to property and equipment acquired, and \$3.9 million to net assumed current liabilities.

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The Company's acquisition of Lucky Vitamin completed during the nine months ended September 30, 2011 did not have a material impact on the Company's consolidated financial statements, and therefore pro forma disclosures have not been presented.

The following table summarizes the Company's goodwill activity:

|  | <b>Retail</b>         | <b>Franchising</b> | <b>Manufacturing/<br/>Wholesale</b> | <b>Total</b> |
|--|-----------------------|--------------------|-------------------------------------|--------------|
|  | <b>(in thousands)</b> |                    |                                     |              |
| Balance at December 31, 2010                 | \$ 305,097            | \$ 117,303         | \$ 202,841                          | \$ 625,241   |
| Acquired franchise stores                    | 686                   | -                  | -                                   | 686          |
| Acquisition of Lucky Vitamin                 | 11,467                | -                  | -                                   | 11,467       |
| Balance at September 30, 2011<br>(unaudited) | \$ 317,250            | \$ 117,303         | \$ 202,841                          | \$ 637,394   |

The following table summarizes the Company's intangible asset activity:

|  | <b>Retail<br/>Brand</b> | <b>Franchise<br/>Brand</b> | <b>Operating<br/>Agreements</b> | <b>Other<br/>Intangibles</b> | <b>Total</b> |
|--|-------------------------|----------------------------|---------------------------------|------------------------------|--------------|
|  | <b>(in thousands)</b>   |                            |                                 |                              |              |
| Balance at December 31, 2010                 | \$ 500,000              | \$ 220,000                 | \$ 146,223                      | \$ 1,001                     | \$ 867,224   |
| Acquired franchise stores                    | -                       | -                          | -                               | 512                          | 512          |
| Acquisition of Lucky Vitamin                 | -                       | -                          | -                               | 9,600                        | 9,600        |
| Amortization expense                         | -                       | -                          | (5,140)                         | (646)                        | (5,786)      |
| Balance at September 30, 2011<br>(unaudited) | \$ 500,000              | \$ 220,000                 | \$ 141,083                      | \$ 10,467                    | \$ 871,550   |

The following table reflects the gross carrying amount and accumulated amortization for each major intangible asset:

|                       | <b>Estimated<br/>Life<br/>in years</b> | <b>Cost</b> | <b>September 30, 2011<br/>Accumulated<br/>Amortization<br/>(unaudited)</b> | <b>Carrying<br/>Amount</b> | <b>Cost</b> | <b>December 31, 2010<br/>Accumulated<br/>Amortization</b> | <b>Carrying<br/>Amount</b> |
|-----------------------|--|-------------|--|----------------------------|-------------|---|----------------------------|
| <b>(in thousands)</b> |  |             |  |                            |             |   |                            |
| Brands - retail       | -                                      | \$ 500,000  | \$ -   | \$ 500,000                 | \$ 500,000  | \$ -  | \$ 500,000                 |
| Brands - franchise    | -                                      | 220,000     | -  | 220,000                    | 220,000     | -   | 220,000                    |
| Retail agreements     | 25-35                                  | 31,000      | (4,933)  | 26,067                     | 31,000      | (4,143)   | 26,857                     |

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|                          |      |            |             |            |            |             |            |
|--------------------------|------|------------|-------------|------------|------------|-------------|------------|
| Franchise agreements     | 25   | 70,000     | (12,717)    | 57,283     | 70,000     | (10,617)    | 59,383     |
| Manufacturing agreements | 25   | 70,000     | (12,717)    | 57,283     | 70,000     | (10,617)    | 59,383     |
| Other intangibles        | 5-15 | 10,600     | (633)       | 9,967      | 1,150      | (550)       | 600        |
| Franchise rights         | 1-5  | 4,213      | (3,263)     | 950        | 3,702      | (2,701)     | 1,001      |
| Total                    |      | \$ 905,813 | \$ (34,263) | \$ 871,550 | \$ 895,852 | \$ (28,628) | \$ 867,224 |

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**GNC HOLDINGS, INC. AND SUBSIDIARIES**

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)**

The following table represents future estimated amortization expense of other intangible assets, net, with definite lives at September 30, 2011:

| Years ending December 31, | Estimated<br>amortization<br>expense<br>(unaudited)<br>(in thousands) |
|---------------------------|---|
| 2011                      | \$ 1,944  |
| 2012                      | 8,257   |
| 2013                      | 8,052   |
| 2014                      | 7,775   |
| 2015                      | 7,681   |
| Thereafter                | 117,841   |
| Total                     | \$ 151,550  |

**NOTE 5. LONG-TERM DEBT / INTEREST EXPENSE**

Long-term debt at each respective period consisted of the following:

|                             | September 30,<br>2011<br>(unaudited) | December 31,<br>2010 |
|-----------------------------|--------------------------------------|----------------------|
|                             | (in thousands)                       |                      |
| 2011 Senior Credit Facility | \$ 897,318                           | \$ -                 |
| 2007 Senior Credit Facility | -                                    | 644,382              |
| Senior Notes                | -                                    | 298,372              |
| Senior Subordinated Notes   | -                                    | 110,000              |

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|                          |            |              |
|--------------------------|------------|--------------|
| Mortgage                 | 4,539      | 5,711        |
| Capital leases           | 25         | 34           |
| Total Debt               | 901,882    | 1,058,499    |
| Less: current maturities | (1,592)    | (28,070)     |
| Long-term Debt           | \$ 900,290 | \$ 1,030,429 |

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The Company's net interest expense for each respective period was as follows:

|  | Three months ended<br>September 30, |           | Nine months ended<br>September 30, |           |
|--|-------------------------------------|-----------|------------------------------------|-----------|
|  | 2011                                | 2010      | 2011                               | 2010      |
|  | (unaudited)<br>(in thousands)       |           |                                    |           |
| 2011 Senior Credit Facility:                   |                                     |           |                                    |           |
| Term Loan                                      | \$ 9,775                            | \$ -      | \$ 23,765                          | \$ -      |
| Revolver                                       | 160                                 | -         | 368                                | -         |
| Deferred fees writedown - early extinguishment | -                                   | -         | 17,418                             | -         |
| OID writedown - early extinguishment           | -                                   | -         | 2,437                              | -         |
| Deferred financing fees amortization           | 483                                 | 1,071     | 1,884                              | 3,195     |
| Mortgage                                       | 230                                 | 110       | 550                                | 341       |
| OID amortization                               | 76                                  | 103       | 311                                | 304       |
| Interest income                                | (306)                               | (171)     | (783)                              | (469)     |
| Senior Notes                                   | -                                   | 4,874     | 4,808                              | 14,583    |
| Senior Subordinated Notes                      | -                                   | 2,957     | 3,054                              | 8,869     |
| Termination of interest rate swaps             | -                                   | -         | 5,819                              | -         |
| 2007 Senior Credit Facility:                   |                                     |           |                                    |           |
| Term Loan                                      | -                                   | 7,241     | 4,815                              | 22,024    |
| Revolver                                       | -                                   | 111       | 71                                 | 335       |
| Interest expense, net                          | \$ 10,418                           | \$ 16,296 | \$ 64,517                          | \$ 49,182 |

Accrued interest at each respective period consisted of the following:

|                             | September 30,<br>2011<br>(unaudited) | December 31,<br>2010 |
|-----------------------------|--------------------------------------|----------------------|
|                             | (in thousands)                       |                      |
| 2011 Senior Credit Facility | \$ 1,768                             | \$ -                 |
| 2007 Senior Credit Facility | -                                    | 4,173                |
| Senior Notes                | -                                    | 5,717                |
| Senior Subordinated Notes   | -                                    | 3,482                |
| Total                       | \$ 1,768                             | \$ 13,372            |

On March 4, 2011, Centers entered into the 2011 Senior Credit Facility, consisting of a \$1.2 billion term loan facility (the Term Loan Facility ) and an undrawn \$80.0 million revolving credit facility (the Revolving Credit Facility ) and, together with the Term Loan Facility, the 2011 Senior Credit Facility ). The Term Loan Facility will mature in March 2018. The Revolving Credit Facility will mature in March 2016. Interest is accrued at a rate, at the Company's option, per annum equal to (A) the sum of (i) the greatest of (a) the prime rate (as publicly announced by JPMorgan Chase Bank, N.A. as its prime rate in effect), (b) the federal funds effective rate plus 0.50%, (c) one month Adjusted LIBO Rate plus 1.0% and, (d) 2.25% plus (ii) Applicable Margin of 2.0% or (B) the sum of (i) the greatest of (a) Adjusted LIBO Rate or (b) 1.25% plus (ii) Applicable Margin of 3.0%. Additionally, the Company is required to pay a commitment fee to the lenders under the Revolving Credit Facility in respect of unutilized revolving loan commitments at a rate of 0.5% per annum, as well as letter of credit fees of 3.0% to lenders and 0.25% to the issuing bank. As of September 30, 2011, \$8.2 million of the Revolving Credit Facility was pledged to secure letters of credit. The 2011 Senior Credit Facility is collateralized by first priority pledges (subject to permitted liens) of the equity interests of each of Centers and Centers' domestic subsidiaries. In connection with the Refinancing on March 4, 2011, the Company incurred \$17.3 million in deferred financing costs. The \$1.2 billion Term Loan Facility was recorded net of original issue discount of \$3.8 million. The Company used part of the net proceeds from the IPO to repay \$300.0 million of outstanding borrowings under the Term Loan Facility. In conjunction with the \$300.0 million prepayment, the Company recognized early extinguishment costs from deferred financing costs and original issue discount of \$4.0 million and \$0.9 million, respectively.

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**GNC HOLDINGS, INC. AND SUBSIDIARIES**

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The 2011 Senior Credit Facility contains customary covenants, including incurrence covenants and certain other limitations on the ability of GNC Corporation, Centers, and Centers subsidiaries to incur additional debt, guarantee other obligations, grant liens on assets, make investments or acquisitions, dispose of assets, make optional payments or modifications of other debt instruments, pay dividends or other payments on capital stock, engage in mergers or consolidations, enter into sales and leaseback transactions, enter into arrangements that restrict GNC Corporation s, Centers and Centers subsidiaries ability to pay dividends or grant liens, engage in transactions with affiliates, and change the passive holding company status of GNC Corporation. The Revolving Credit Facility also requires that, to the extent borrowings outstanding thereunder exceed \$25.0 million, Centers and its domestic subsidiaries meet a senior secured debt ratio of consolidated senior secured debt to consolidated EBITDA (as defined in the Revolving Credit Facility). Such ratio test is 4.75 to 1.00 for the period from June 30, 2011 through and including March 31, 2013, and 4.25 to 1.00 thereafter.

As of September 30, 2011, the Company believes that it is in compliance with all covenants under the 2011 Senior Credit Facility.

At December 31, 2010, the interest rate for the 2007 Senior Credit Facility was 2.5%. At December 31, 2010, the interest rate for the Senior Notes was 5.8%. In connection with the Refinancing on March 4, 2011, the 2007 Senior Credit Facility, Senior Notes and Senior Subordinated Notes were repaid.

**NOTE 6. FINANCIAL INSTRUMENTS**

At September 30, 2011 and December 31, 2010, the Company s financial instruments consisted of cash and cash equivalents, receivables, franchise notes receivable, accounts payable and long-term debt. The carrying amount of cash and cash equivalents, receivables, accounts payable and accrued liabilities approximates their fair value because of the short maturity of these instruments. Based on the interest rates currently available and their underlying risk, the carrying value of the franchise notes receivable approximates their fair value. These fair values are reflected net of reserves, which are recognized according to Company policy. The Company determined the estimated fair values of its debt by using currently available market information and estimates and assumptions where appropriate. As considerable judgment is required to determine these estimates, changes in the assumptions or methodologies may have an effect on these estimates. The carrying amount and estimated fair values of the Company s financial instruments are as follows:

| <b>September 30, 2011</b> |                   | <b>December 31, 2010</b> |                   |
|---------------------------|-------------------|--------------------------|-------------------|
| <b>Carrying Amount</b>    | <b>Fair Value</b> | <b>Carrying Amount</b>   | <b>Fair Value</b> |

(unaudited)



(in thousands)

|  |            |            |            |            |
|--|------------|------------|------------|------------|
| Cash and cash equivalents                  | \$ 146,107 | \$ 146,107 | \$ 193,902 | \$ 193,902 |
| Receivables, net                           | 118,074    | 118,074    | 102,874    | 102,874    |
| Franchise notes receivable, net            | 6,300      | 6,300      | 4,496      | 4,496      |
| Accounts payable                           | 137,372    | 137,372    | 98,662     | 98,662     |
| Long-term debt (including current portion) | 901,882    | 874,826    | 1,058,499  | 1,007,070  |

**NOTE 7. COMMITMENTS AND CONTINGENCIES****Litigation**

The Company is engaged in various legal actions, claims and proceedings arising in the normal course of business, including claims related to breach of contracts, products liabilities, intellectual property matters and employment-related matters resulting from the Company's business activities. As with most actions such as these, an estimation of any possible and/or ultimate liability cannot always be determined.

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**GNC HOLDINGS, INC. AND SUBSIDIARIES**

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)**

The Company continues to assess the requirement to account for additional contingencies in accordance with the standard on contingencies. If the Company is required to make a payment in connection with an adverse outcome in these matters, it could have a material impact on its financial condition, operating results, and cash flows.

As a manufacturer and retailer of nutritional supplements and other consumer products that are ingested by consumers or applied to their bodies, the Company has been and is currently subjected to various product liability claims. Although the effects of these claims to date have not been material to the Company, it is possible that current and future product liability claims could have a material adverse impact on its business, financial condition or cash flows. The Company currently maintains product liability insurance with a deductible/retention of \$3.0 million per claim with an aggregate cap on retained loss of \$10.0 million. The Company typically seeks and has obtained contractual indemnification from most parties that supply raw materials for its products or that manufacture or market products it sells. The Company also typically seeks to be added, and has been added, as an additional insured under most of such parties' insurance policies. The Company is also entitled to indemnification by a former owner of the Company for certain losses arising from claims related to products containing ephedra or Kava Kava sold prior to December 5, 2003. However, any such indemnification or insurance is limited by its terms and any such indemnification, as a practical matter, is limited to the creditworthiness of the indemnifying party and its insurer, and the absence of significant defenses by the insurers. The Company may incur material products liability claims, which could increase its costs and adversely affect its reputation, revenues and operating income.

*Hydroxycut Claims.* On May 1, 2009, the FDA issued a warning on several Hydroxycut-branded products manufactured by Lovate Health Sciences U.S.A., Inc. (Lovate). The FDA warning was based on 23 reports of liver injuries from consumers who claimed to have used the products between 2002 and 2009. As a result, Lovate voluntarily recalled 14 Hydroxycut-branded products. Following the recall, the Company was named, among other defendants, in approximately 85 lawsuits related to Hydroxycut-branded products in 14 states. Lovate previously accepted the Company's tender request for defense and indemnification under its purchasing agreement with the Company and, as such, Lovate has accepted the Company's request for defense and indemnification in the Hydroxycut matters. The Company's ability to obtain full recovery in respect of any claims against the Company in connection with products manufactured by Lovate under the indemnity is dependent on Lovate's insurance coverage, the creditworthiness of its insurer, and the absence of significant defenses by such insurer. To the extent the Company is not fully compensated by Lovate's insurer, it can seek recovery directly from Lovate. The Company's ability to fully recover such amounts may be limited by the creditworthiness of Lovate.

As of September 30, 2011, there were 76 pending lawsuits related to Hydroxycut in which the Company had been named: 70 individual, largely personal injury claims and six putative class action cases, generally inclusive of claims of consumer fraud, misrepresentation, strict liability and breach of warranty. As any liabilities that may arise from these matters are not probable or reasonably estimable at this time, no liability has been accrued in the accompanying financial statements.

By court order dated October 6, 2009, the United States Judicial Panel on Multidistrict Litigation consolidated pretrial proceedings of many of the pending actions in the Southern District of California (In re: Hydroxycut Marketing and Sales Practices Litigation, MDL No. 2087).

*Pro-Hormone/Androstenedione Cases.* The Company is currently defending three lawsuits (the Andro Actions ) in New Jersey, New York and Pennsylvania relating to the sale by the Company of certain nutritional products, between 1999 and 2004, alleged to contain the ingredients commonly known as Androstenedione, Androstenediol, Norandrostenedione, and Norandrostenediol (collectively, Andro Products ). In each of the Andro Actions, plaintiffs sought, or are seeking, to certify a class and obtain damages on behalf of the class representatives and all those similarly-situated who purchased from the Company certain nutritional supplements alleged to contain one or more Andro Products. During the first quarter of 2011, the sole Andro Action filed in California was settled for an immaterial amount, pending approval by the court. Unlike the other states in which the plaintiffs reside, California law prohibits one of the ingredients; therefore, the Company does not believe that the outcome in California provides a basis for determining the potential outcome of the other Andro Actions. As any liabilities that may arise from these other Andro Actions are not probable or reasonably estimable at this time, no liability has been accrued in the accompanying financial statements.

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**GNC HOLDINGS, INC. AND SUBSIDIARIES**

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)**

**Commitments**

The Company maintains certain purchase commitments with various vendors to ensure its operational needs are fulfilled. As of September 30, 2011, such future purchase commitments consisted of \$3.7 million of advertising commitments. Other commitments related to the Company's business operations cover varying periods of time and are not significant. All of these commitments are expected to be fulfilled with no adverse consequences to the Company's operations of financial condition.

**Environmental Compliance**

In March 2008, the South Carolina Department of Health and Environmental Control (the DHEC) requested that the Company investigate contamination associated with historical activities at its South Carolina facility. These investigations have identified chlorinated solvent impacts in soils and groundwater that extend offsite from our facility. The Company is awaiting DHEC approval of the scope of additional investigations in order to understand the extent of these impacts and develop appropriate remedial measures for DHEC approval. At this stage of the investigation, however, it is not possible to estimate the timing and extent of any remedial action that may be required, the ultimate cost of remediation, or the amount of the Company's potential liability.

In addition to the foregoing, the Company is subject to numerous federal, state, local and foreign environmental and health and safety laws and regulations governing its operations, including the handling, transportation, and disposal of the Company's non-hazardous and hazardous substances and wastes, as well as emissions and discharges from its operations into the environment, including discharges to air, surface water and groundwater. Failure to comply with such laws and regulations could result in costs for remedial actions, penalties, or the imposition of other liabilities. New laws, changes in existing laws or the interpretation thereof, or the development of new facts or changes in their processes could also cause the Company to incur additional capital and operation expenditures to maintain compliance with environmental laws and regulations and environmental permits. The Company also is subject to laws and regulations that impose liability and cleanup responsibility for releases of hazardous substances into the environment without regard to fault or knowledge about the condition or action causing the liability. Under certain of these laws and regulations, such liabilities can be imposed for cleanup of previously owned or operated properties, or for properties to which substances or wastes that were sent in connection with current or former operations at its facilities. The presence of contamination from such substances or wastes could also adversely affect the Company's ability to sell or lease its properties, or to use them as collateral for financing. From time to time, the Company has incurred costs and obligations for correcting environmental and health and safety noncompliance matters and for remediation at or relating to certain of its properties or properties at which its waste has been disposed. The Company believes it has complied with, and is currently complying with, its environmental obligations pursuant to environmental and health and safety laws and regulations and that any liabilities for noncompliance will not have a material adverse effect on its business, financial performance, or cash flows. However, it is difficult to predict future liabilities and obligations, which could be material.

**NOTE 8. STOCK-BASED COMPENSATION PLANS**

The Company has outstanding stock-based compensation awards that were granted by the Holdings Compensation Committee of Holdings Board of Directors (the Compensation Committee ) under the following two stock-based employee compensation plans:

- the GNC Holdings, Inc. 2011 Stock and Incentive Plan (the 2011 Stock Plan ) adopted in March 2011; and
- the GNC Acquisition Holdings Inc. 2007 Stock Incentive Plan adopted in March 2007 (as amended, the 2007 Stock Plan ).

Both plans have provisions that allow for the granting of stock options, restricted stock and other stock based awards and are available to certain eligible employees, directors, consultants or advisors as determined by the Compensation Committee. Stock options under the plans were granted with exercise prices at or above fair market value on the date of grant, typically vest over a four- or five-year period and expire seven or ten years from the date of grant.

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**GNC HOLDINGS, INC. AND SUBSIDIARIES**

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Up to 8.5 million shares of Class A common stock may be issued under the 2011 Stock Plan (subject to adjustment to reflect certain transactions and events specified in the 2011 Stock Plan for any award grant). If any award granted under the 2011 Stock Plan expires, terminates or is cancelled without having been exercised in full, the number of shares underlying such unexercised award will again become available for awards under the 2011 Stock Plan. The total number of shares of Class A common stock available for awards under the 2011 Stock Plan will be reduced by (i) the total number of stock options or stock appreciation rights exercised, regardless of whether any of the shares of Class A common stock underlying such awards are not actually issued to the participant as the result of a net settlement, and (ii) any shares of Class A common stock used to pay any exercise price or tax withholding obligation. In addition, the number of shares of Class A common stock that are subject to restricted stock, performance shares or other stock-based awards that are not subject to the appreciation of the value of a share of Class A common stock ( Full Share Awards ) that may be granted under the 2011 Stock Plan is limited by counting shares granted pursuant to such awards against the aggregate share reserve as 1.8 shares for every share granted. If any stock option, stock appreciation right or other stock-based award that is not a Full Share Award is cancelled, expires or terminates unexercised for any reason, the shares covered by such awards will again be available for the grant of awards under the 2011 Stock Plan. If any shares of Class A common stock that are subject to restricted stock, performance shares or other stock-based awards that are Full Share Awards are forfeited for any reason, 1.8 shares of Class A common stock will again be available for the grant of awards under the 2011 Stock Plan.

The Company will not grant any additional awards under the 2007 Stock Plan. No stock appreciation rights, restricted stock, deferred stock or performance shares were granted under the 2007 Stock Plan. The Company granted 100,625 and 1,705,625 options and 7,784 and 110,344 shares of restricted stock for the three and nine months ended September 30, 2011, respectively, under the 2011 Stock Plan.

The Company utilizes the Black Scholes model to calculate the fair value of options under both of the Holdings' plans. The resulting compensation cost is recognized in the Company's financial statements over the option vesting period. The Company recognized \$0.6 million and \$0.8 million of non-cash stock-based compensation expense for the three months ended September 30, 2011 and 2010, respectively. The Company recognized \$2.9 million and \$2.4 million of non-cash stock-based compensation expense for the nine months ended September 30, 2011 and 2010, respectively. At September 30, 2011, there was \$9.8 million of total unrecognized compensation cost related to non-vested stock-based compensation for all awards previously made that are expected to be recognized over a weighted average period of approximately 6.2 years.

During the nine months ended, September 30, 2011 the total intrinsic value of awards exercised was \$22.8 million and the total amount of cash received from the exercise of options was \$11.1 million. The tax impact associated with the exercise of awards for the nine months ended September 30, 2011 was a benefit of \$8.4 million and was recorded to additional capital. During the nine months ended September 30, 2010, there were no options exercised.

The following table sets forth a summary of stock options under all plans for the nine months ended September 30, 2011:

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|                                   | <b>Total Options</b> | <b>Weighted<br/>Average<br/>Exercise Price</b> | <b>Weighted Average<br/>Remaining<br/>Contractual Term<br/>(In Years)</b> | <b>Aggregate<br/>Intrinsic Value<br/>(in Thousands)</b> |
|-----------------------------------|----------------------|--|---|---|
| Outstanding at December 31, 2010  | 9,344,188            | \$ 7.60  |   |   |
| Granted                           | 1,705,625            | 19.40  |   |   |
| Exercised                         | (1,573,189)          | 7.07   |   |   |
| Forfeited                         | (951,091)            | 13.30  |   |   |
| Expired                           | (5,800)              | 10.81  |   |   |
| Outstanding at September 30, 2011 | 8,519,733            | \$ 9.42  | 6.1   | \$ 91,139   |
| Exercisable at September 30, 2011 | 5,862,292            | \$ 7.11  | 5.7   | \$ 76,251   |

The Black Scholes model utilizes the following assumptions in determining a fair value: price of underlying stock, award exercise price, expected term, risk-free interest rate, expected dividend yield and expected stock price volatility over the award's expected term. Due to the utilization of these assumptions, the existing models do not necessarily represent the definitive fair value of awards for future periods. As Holdings has had minimal exercises of stock options under its plans, the option term has been estimated by considering both the vesting period, which typically for both plans has been five or four years, and the contractual term, which historically has been either seven or ten years. Until the IPO, the fair value of the stock was estimated based upon the net enterprise value of the Company, discounted to reflect the lack of liquidity and control associated with the stock. Following the consummation of the IPO, the fair value of the stock was based upon the closing price of the Class A common stock as reported on the New York Stock Exchange (the NYSE). Volatility is estimated based upon the Company utilizing its current peer group average to estimate the expected volatility.

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The assumptions used in the Company's Black Scholes valuation related to stock option grants made during the nine months ended September 30, 2011 were as follows:

|  |                 |
|--|-----------------|
| Dividend yield                               | 0.00%           |
| Expected option life                         | 4.5 - 7.0 years |
| Volatility factor percentage of market price | 38.5% - 39.2%   |
| Discount rate                                | 1.5% - 2.9%     |

The following table sets forth a summary of restricted stock units granted under the 2011 Stock Plan and related information for the nine months ended September 30, 2011:

|                                   | <b>Restricted<br/>Stock<br/>Units</b> | <b>Weighted<br/>Average<br/>Fair Value</b> |
|-----------------------------------|---------------------------------------|--|
| Granted                           | 110,344                               | \$ 19.24                                   |
| Vested                            | -                                     | -  |
| Forfeited                         | (24,305)                              | 18.98                                      |
| Outstanding at September 30, 2011 | 86,039                                | \$ 19.31                                   |

**NOTE 9. SEGMENTS**

The Company has three reportable segments. This information is utilized by the Company's management to assess performance and allocate assets accordingly. The Company's management evaluates segment operating results based on several indicators. The primary key performance indicators are sales and operating income or loss for each segment. Operating income or loss, as evaluated by management, excludes certain items that are managed at the consolidated level, such as distribution and warehousing, impairments and other corporate costs. The following table represents key financial information for each of the Company's reportable segments, identifiable by the distinct operations and management of each: Retail, Franchising and Manufacturing/Wholesale. The Retail reportable segment includes the Company's corporate store operations in the United States, Canada, GNC.com, and Lucky Vitamin. The Franchise reportable segment represents the Company's franchise operations, both domestically and internationally. The Manufacturing/Wholesale reportable segment represents the Company's manufacturing operations in South Carolina and the Wholesale business. This segment supplies the Retail and Franchise segments, along with various third parties, with finished products for sale. The Warehousing and Distribution and Corporate costs represent the Company's administrative expenses. The accounting policies of the segments are the same as those described in the Basis of Presentation and Summary of Significant Accounting Policies.





Table of Contents**GNC HOLDINGS, INC. AND SUBSIDIARIES****NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)**

The following table represents key financial information of the Company's segments:

|   | Three months ended            |                       | Nine months ended     |                       |
|---|-------------------------------|-----------------------|-----------------------|-----------------------|
|   | September 30,<br>2011         | September 30,<br>2010 | September 30,<br>2011 | September 30,<br>2010 |
|   | (unaudited)<br>(in thousands) |                       |                       |                       |
| <b>Revenue:</b>                                 |                               |                       |                       |                       |
| Retail  | \$ 385,231                    | \$ 338,231            | \$ 1,153,237          | \$ 1,031,899          |
| Franchise                                       | 90,884                        | 76,894                | 251,096               | 222,365               |
| Manufacturing/Wholesale:                        |                               |                       |                       |                       |
| Intersegment (1)                                | 58,430                        | 60,982                | 166,271               | 159,589               |
| Third Party                                     | 61,913                        | 50,535                | 158,238               | 132,145               |
| Sub total Manufacturing/Wholesale               | 120,343                       | 111,517               | 324,509               | 291,734               |
| Sub total segment revenues                      | 596,458                       | 526,642               | 1,728,842             | 1,545,998             |
| Intersegment elimination (1)                    | (58,430)                      | (60,982)              | (166,271)             | (159,589)             |
| <b>Total revenue</b>                            | <b>\$ 538,028</b>             | <b>\$ 465,660</b>     | <b>\$ 1,562,571</b>   | <b>\$ 1,386,409</b>   |
| <b>Operating income:</b>                        |                               |                       |                       |                       |
| Retail  | \$ 62,167                     | \$ 47,670             | \$ 189,173            | \$ 147,248            |
| Franchise                                       | 31,997                        | 25,925                | 83,291                | 70,530                |
| Manufacturing/Wholesale                         | 23,385                        | 17,901                | 60,982                | 51,140                |
| Unallocated corporate and other costs:          |                               |                       |                       |                       |
| Warehousing and distribution costs              | (15,190)                      | (13,784)              | (45,577)              | (41,450)              |
| Corporate costs (2)                             | (19,122)                      | (18,922)              | (61,884)              | (55,123)              |
| Transaction related costs                       | (637)                         | -                     | (12,999)              | -                     |
| Sub total unallocated corporate and other costs | (34,949)                      | (32,706)              | (120,460)             | (96,573)              |
| <b>Total operating income</b>                   | <b>\$ 82,600</b>              | <b>\$ 58,790</b>      | <b>\$ 212,986</b>     | <b>\$ 172,345</b>     |

(1) Intersegment revenues are eliminated from consolidated revenue.

(2) Includes \$3.5 million of executive severance for the nine months ended September 30, 2011.

**NOTE 10. INCOME TAXES**

The Company recognized \$23.5 million of income tax expense (or 32.6% of pretax income) during the three months ended September 30, 2011 compared to \$15.8 million (or 37.2% of pretax income) for the same period in 2010. For the three months ended September 30, 2011, income tax expense includes \$2.6 million, or 3.0%, of pretax income related to non-recurring tax credits and incentives.

The Company recognized \$53.9 million of income tax expense (or 36.3% of pretax income) during the nine months ended September 30, 2011 compared to \$45.4 million (or 36.9% of pretax income) for the same period in 2010. For the nine months ended September 30, 2011, income tax expense includes \$2.3 million, or 1.5% of pretax income, related to non deductible costs incurred related to the IPO. Also, the nine months ended September 30, 2011 was offset by \$2.6 million, or 1.8%, related to non-recurring tax credits and incentives.

The Company files a consolidated U.S. federal tax return and various consolidated and separate tax returns as prescribed by the tax laws of the state, local, and international jurisdictions in which it and its subsidiaries operate. The Company has been audited by the Internal Revenue Service (the IRS ) through its March 15, 2007 tax year. The Company has various state, local and international jurisdiction tax years open to examination (the earliest open period is 2003), and is also currently under audit in certain state and local jurisdictions. As of September 30, 2011, the Company believes that it has appropriately reserved for any potential federal, state, local and international income tax exposures.

The Company recorded additional unrecognized tax benefits of approximately \$1.6 million and \$0.9 million during the nine months ended September 30, 2011 and 2010, respectively. The additional unrecognized tax benefits recorded during the nine months ended September 30, 2011 are principally related to the continuation of previously taken tax positions. As of September 30, 2011 and December 31, 2010, the Company had \$10.3 million and \$8.7 million, respectively, of unrecognized tax benefits. As of September 30, 2011, the Company is not aware of any tax positions for which it is reasonably possible that the amounts of unrecognized tax benefits will significantly increase or decrease within the next 12 months. The amount of unrecognized tax benefits that, if recognized, would affect the effective tax rate is \$10.3 million. The Company recognizes accrued interest and penalties related to unrecognized tax benefits in income tax expense. The Company had accrued approximately \$3.5 million and \$2.7 million, respectively, for September 30, 2011 and December 31, 2010 in potential interest and penalties associated with uncertain tax positions. To the extent interest and penalties are not assessed with respect to the ultimate settlement of uncertain tax positions, amounts previously accrued will be reduced and reflected as a reduction of the overall income tax provision.

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**GNC HOLDINGS, INC. AND SUBSIDIARIES**

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)**

**NOTE 11. FAIR VALUE MEASUREMENT**

The standard on fair market measurement defines fair value, establishes a consistent framework for measuring fair value, and expands disclosures for each major asset and liability category measured at fair value on either a recurring or nonrecurring basis. The standard clarifies that fair value is an exit price, representing the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants. As such, fair value is a market-based measurement that should be determined based on assumptions that market participants would use in pricing an asset or liability. As a basis for considering such assumptions, the standard establishes a three-tier fair value hierarchy which prioritizes the inputs used in measuring fair value as follows:

Level 1 - observable inputs such as quoted prices in active markets for identical assets and liabilities;

Level 2 - observable inputs such as quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active, other inputs that are observable, or can be corroborated by observable market data; and

Level 3 - unobservable inputs for which there are little or no market data, which require the reporting entity to develop its own assumptions.

The following table presents the Company's financial assets and liabilities that were accounted for at fair value on a recurring basis as of September 30, 2011 by level within the fair value hierarchy:

|                             | <b>Fair Value Measurements Using</b> |         |         |
|-----------------------------|--------------------------------------|---------|---------|
|                             | Level 1                              | Level 2 | Level 3 |
|                             | <b>(unaudited)</b>                   |         |         |
|                             | <b>(in thousands)</b>                |         |         |
| Other current liabilities   | \$ -                                 | \$ -    | \$ -    |
| Other long-term liabilities | \$ 3,370                             | \$ -    | \$ -    |

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The following table presents the Company's financial assets and liabilities that were accounted for at fair value on a recurring basis as of December 31, 2010 by level within the fair value hierarchy:

|                             | <b>Fair Value Measurements Using</b> |                           |         |
|-----------------------------|--------------------------------------|---------------------------|---------|
|                             | Level 1                              | Level 2<br>(in thousands) | Level 3 |
| Other current liabilities   | \$ -                                 | \$ 4,395                  | \$ -    |
| Other long-term liabilities | \$ 3,034                             | \$ 3,074                  | \$ -    |

The following is a description of the valuation methodologies used for these items, as well as the general classification of such items pursuant to the fair value hierarchy of the standard on fair value measurements and disclosures:

*Other Current Liabilities and Other Long-term Liabilities.* Other current liabilities and long-term liabilities classified as Level 1 consist of liabilities related to the Company's non-qualified deferred compensation plan. The liabilities related to this plan are adjusted based on changes in the fair value of the underlying employee-directed investment choices. Since the employee-directed investment choices are exchange traded equity indexes with quoted prices in active markets, the liabilities are classified within Level 1 on the fair value hierarchy. Other current liabilities and long-term liabilities classified as Level 2 consisted of the Company's interest rate swaps which were terminated on March 4, 2011.

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**GNC HOLDINGS, INC. AND SUBSIDIARIES**

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)**

In addition to the above table, the Company's financial instruments also consist of cash and cash equivalents, accounts receivable, accounts payable and long-term debt. The Company did not elect to value its long-term debt with the fair value option in accordance with the standard on financial instruments. The Company believes that the recorded values of all of its other financial instruments approximate their fair values because of their nature and respective durations.

**NOTE 12. RELATED PARTY TRANSACTIONS**

*Management Services Agreement.* Together with Holdings' wholly owned subsidiary, GNC Acquisition Inc., Holdings entered into an Agreement and Plan of Merger (the *Merger Agreement*) with GNC Parent Corporation on February 8, 2007. Pursuant to the Merger Agreement and on March 16, 2007, GNC Acquisition Inc. was merged with and into GNC Parent Corporation, with GNC Parent Corporation as the surviving corporation and our wholly owned subsidiary (the *Merger*). In connection with the Merger, on March 16, 2007, Holdings entered into a Management Services Agreement (the *ACOF Management Services Agreement*) with ACOF Operating Manager II, L.P. ( *ACOF Manager* ), an affiliate of Ares Corporate Opportunities Fund II, L.P. ( *Ares* ), one of Holdings' sponsors. The ACOF Management Service Agreement provided for an annual management fee of \$750,000, payable quarterly and in advance to ACOF Manager, on a pro rata basis, until the tenth anniversary from March 16, 2007 plus any one-year extensions (which extensions occurred automatically on each anniversary date of March 16, 2007), as well as reimbursements for ACOF Manager's and its affiliates' out-of-pocket expenses in connection with the management services provided under the ACOF Management Services Agreement. For the nine months ended September 30, 2011 and 2010, \$0.2 million and \$0.6 million, respectively, had been paid pursuant to this agreement.

The ACOF Management Services Agreement provided that upon consummation of a change in control transaction or a bona fide initial public offering, ACOF Manager would receive, in lieu of quarterly payments of the annual management fee, an automatic fee equal to the net present value of the aggregate annual management fee that would have been payable to ACOF Manager during the remainder of the term of the agreement, calculated in good faith by Holdings' board of directors (the *Board*). Upon consummation of the IPO in April 2011, \$5.6 million was paid pursuant to this agreement and the agreement was terminated. This amount was accrued and expensed in transaction related costs during the period ended March 31, 2011.

*Special Dividend.* Ontario Teachers' Pension Plan Board ( *OTPP* ), as the holder of Holdings' Class B common stock, was entitled to receive an annual special dividend payment equal to an aggregate amount of \$750,000 per year when, as and if declared by the Board (the *Special Dividend*). The Special Dividend was payable in equal quarterly installments on the first day of each quarter commencing on April 1, 2007 and for ten years thereafter (the *Special Dividend Period*). For the nine months ended September 30, 2011 and 2010, \$0.2 million and \$0.6 million, respectively, was paid pursuant to this arrangement.

Upon the consummation of a change in control transaction or a bona fide initial public offering, OTPP was entitled to receive, in lieu of quarterly payments of the special dividend payments, an automatic payment equal to the net present value of the aggregate

amount of the special dividend payments that would have been payable to OTPP during the remainder of the Special Dividend Period, calculated in good faith by the Board. Upon consummation of the IPO in April 2011, \$5.6 million was paid to OTPP and the arrangement was terminated. This amount was accrued and expensed in transaction related costs during the period ended March 31, 2011.

*2007 Senior Credit Facility.* Upon consummation of the Merger, Centers entered into the 2007 Senior Credit Facility, under which various funds affiliated with Ares, were lenders. Under the 2007 Senior Credit Facility, these affiliated funds made term loans to Centers in the amount of \$65.0 million and \$62.1 million, as of the consummation of the Merger and December 31, 2010, respectively. In addition, as of December 31, 2010, an aggregate of \$2.9 million in principal and \$11.0 million in interest had been paid to affiliates of Ares in respect of amounts borrowed under the 2007 Senior Credit Facility. Borrowings under the 2007 Senior Credit Facility had accrued interest at a weighted average rate of 4.6% per year. In connection with the Refinancing and as of March 4, 2011, the remaining principal amount of \$62.1 million and an additional amount of \$0.5 million in interest was paid to affiliates of Ares.

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**GNC HOLDINGS, INC. AND SUBSIDIARIES**

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)**

*2011 Senior Credit Facility.* Various funds affiliated with Ares are lenders under the 2011 Senior Credit Facility. These affiliated funds have made term loans to Centers in the amount of \$120.0 million. In connection with the Company's repayment of \$300.0 million of outstanding borrowings under the Term Loan Facility with proceeds from the IPO, funds affiliated with Ares received approximately \$30.0 million, representing their pro rata positions in the Term Loan Facility. Interest represented \$0.1 million of the \$30.0 million paid to funds affiliated with Ares.

*Lease Agreements.* At September 30, 2011 and 2010, the Company was party to 18 and 20 lease agreements, respectively, as lessee, with Cadillac Fairview Corporation, a direct wholly owned subsidiary of OTPP, as lessor, with respect to properties located in Canada. For the nine months ended September 30, 2011 and 2010, the Company paid \$2.1 million, respectively, under the lease agreements. Each lease was negotiated in the ordinary course of business on an arm's length basis.



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**GNC HOLDINGS, INC. AND SUBSIDIARIES**

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)**

**Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations**

The following Management's Discussion and Analysis of Financial Condition and Results of Operations should be read in conjunction with Item 1, Financial Statements in Part I of this quarterly report on Form 10-Q.

**Forward-Looking Statements**

The discussion in this section includes forward-looking statements within the meaning of federal securities laws. Forward-looking statements include statements that may relate to our plans, objectives, goals, strategies, future events, future revenues or performance, capital expenditures, financing needs and other information that is not historical information. Forward-looking statements can often be identified by the use of terminology such as subject to, believe, anticipate, plan, expect, intend, estimate, project, may, will, should, would, could, can, the negatives thereof, variations thereon and similar expressions, or by discussing strategy.

All forward-looking statements, including, without limitation, our examination of historical operating trends, are based upon our current expectations and various assumptions. We believe there is a reasonable basis for our expectations and beliefs, but they are inherently uncertain. We may not realize our expectations, and our beliefs may not prove correct. Actual results could differ materially from those described or implied by such forward-looking statements. The following uncertainties and factors, among others (including those set forth under Item 1A, Risk Factors of Part II of this quarterly report on Form 10-Q), could affect future performance and cause actual results to differ materially from those matters expressed in or implied by forward-looking statements:

- significant competition in our industry;
- unfavorable publicity or consumer perception of our products;
- increases in the cost of borrowings and limitations on availability of additional debt or equity capital;
- our debt levels and restrictions in our debt agreements;
- the incurrence of material product liability and product recall costs;
- loss or retirement of key members of management;

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- costs of compliance and our failure to comply with new and existing governmental regulations, including, but not limited to, tax regulations;
- costs of litigation and the failure to successfully defend lawsuits and other claims against us;
- the failure of our franchisees to conduct their operations profitably and limitations on our ability to terminate or replace under-performing franchisees;
- economic, political and other risks associated with our international operations;
- our failure to keep pace with the demands of our customers for new products and services;
- disruptions in our manufacturing system or losses of manufacturing certifications;
- disruptions in our distribution network;
- the lack of long-term experience with human consumption of ingredients in some of our products;
- increases in the frequency and severity of insurance claims, particularly claims for which we are self-insured;
- the failure to adequately protect or enforce our intellectual property rights against competitors;
- changes in raw material costs and pricing of our products;
- failure to successfully execute our growth strategy, including any delays in our planned future growth, any inability to expand our franchise operations or attract new franchisees, or any inability to expand our company-owned retail operations;
- changes in applicable laws relating to our franchise operations;
- damage or interruption to our information systems;
- the impact of current economic conditions on our business;
- natural disasters, unusually adverse weather conditions, pandemic outbreaks, boycotts and geo-political events; and
- our failure to maintain effective internal controls.

Consequently, forward-looking statements should be regarded solely as our current plans, estimates and beliefs. You should not place undue reliance on forward-looking statements. We cannot guarantee future results, events, levels of activity, performance or achievements. We do not undertake and specifically decline any obligation to update, republish or revise forward-looking statements to reflect future events or circumstances or to reflect the occurrences of unanticipated events.

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**Business Overview**

GNC Holdings, Inc. ( Holdings ), headquartered in Pittsburgh, Pa., is a leading global specialty retailer of health and wellness products, including vitamins, minerals, and herbal supplement products, sports nutrition products and diet products, and trades on the NYSE under the symbol GNC .

As of September 30, 2011, GNC has more than 7,500 locations, of which more than 5,800 retail locations are in the United States (including 919 franchise and 2,103 Rite Aid franchise store-within-a-store locations) and franchise operations in 52 countries (including distribution centers where retail sales are made). The Company which is dedicated to helping consumers Live Well has a diversified, multi-channel business model and derives revenue from product sales through company-owned retail stores, domestic and international franchise activities, third party contract manufacturing, e-commerce and corporate partnerships. Our broad and deep product mix, which is focused on high-margin, premium, value-added nutritional products, is sold under GNC proprietary brands, including Mega Men, Ultra Mega, GNC Wellbeing, Pro Performance and Longevity Factors, and under nationally recognized third party brands.

***Revenues and Operating Performance from our Segments***

We measure our operating performance primarily through revenues and operating income from our three segments, Retail, Franchise and Manufacturing/Wholesale, and through the management of unallocated costs from our warehousing, distribution and corporate segments, as follows:

- *Retail:* Retail revenues are generated by sales to consumers at our company-owned stores and online through GNC.com. Although we believe that our retail and franchise businesses are not seasonal in nature, historically we have experienced, and expect to continue to experience, a variation in our net sales and operating results from quarter to quarter, with the first half of the year being stronger than the second half of the year. Our industry is expected to grow at an annual average rate of approximately 4.0% through 2015. As a leader in our industry, we expect our organic retail revenue to grow faster as a result of our disproportionate market share, scale economies in purchasing and advertising, strong brand awareness and vertical integration.

- *Franchise:* Franchise revenues are generated primarily from:

- (1) product sales to our franchisees;

- (2) royalties on franchise retail sales; and

- (3) franchise fees, which are charged for initial franchise awards, renewals and transfers of franchises.

As described above, our industry is expected to grow at an annual average rate of approximately 4.0% through 2015. Although we do not anticipate the number of our domestic franchise stores to grow substantially, we expect to achieve segment revenue growth consistent with projected industry growth, which will be generated by royalties on franchise retail sales and product sales to our existing franchisees. As a result of our efforts to expand our international presence and provisions in our international franchising agreements requiring franchisees to open additional stores, we have increased our international store base in recent periods and expect to continue to increase the number of our international franchise stores over the next five years. We believe this will result in additional franchise fees associated with new store openings and increased revenues from product sales to, and royalties from, franchisees.

- *Manufacturing/Wholesale:* Manufacturing/Wholesale revenues are generated through sales of manufactured products to third parties, generally for third-party private label brands; the sale of our proprietary and third-party products to and through Rite Aid and [www.drugstore.com](http://www.drugstore.com); and the sale of our proprietary products to and through PetSmart and Sam's Club. License fee revenue from the opening of a franchise store-within-a-store locations within Rite Aid stores is also recorded in this segment. Our revenues generated by our manufacturing and wholesale operations are subject to our available manufacturing capacity.

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A significant portion of our business infrastructure is comprised of fixed operating costs. Our vertically-integrated distribution network and manufacturing can support higher sales volume without significant incremental costs. We therefore expect our operating expenses to grow at a lesser rate than our revenues, resulting in positive operating leverage.

The following trends and uncertainties in our industry could affect our operating performance as follows:

- broader consumer awareness of health and wellness issues and rising healthcare costs may increase the use of the products we offer and positively affect our operating performance;
- interest in, and demand for, condition-specific products based on scientific research may positively affect our operating performance if we can timely develop and offer such condition-specific products;
- the effects of favorable and unfavorable publicity on consumer demand with respect to the products we offer may have similarly favorable or unfavorable effects on our operating performance;
- a lack of long-term experience with human consumption of ingredients in some of our products could create uncertainties with respect to the health risks, if any, related to the consumption of such ingredients and negatively affect our operating performance;
- increased costs associated with complying with new and existing governmental regulation may negatively affect our operating performance; and
- a decline in disposable income available to consumers may lead to a reduction in consumer spending and negatively affect our operating performance.

**Executive Overview**

On March 4, 2011, General Nutrition Centers Inc. (Centers), a wholly owned subsidiary of Holdings, entered into a \$1.2 billion term loan facility with a term of seven years (the Term Loan Facility) and an \$80.0 million revolving credit facility with a term of five years (the Revolving Credit Facility) and, together with the Term Loan Facility, the 2011 Senior Credit Facility). Centers used a portion of the proceeds from the Term Loan Facility to refinance its former indebtedness, including all outstanding indebtedness under its 2007 Senior Credit Facility, consisting of a \$675.0 million term loan facility (the 2007 Term Loan Facility) and a \$60.0 million senior revolving credit facility (the 2007 Revolving Credit Facility) and, together with the 2007 Term Loan Facility, the 2007 Senior Credit Facility), the Senior Notes and the Senior Subordinated Notes, and to pay related fees and expenses. As of the date hereof, the Revolving Credit Facility remains undrawn. We refer to these transactions and the use of proceeds therefrom collectively as the Refinancing.

On April 6, 2011, we completed our initial public offering (IPO) pursuant to which 25.875 million shares of Class A common stock were sold at a price of \$16.00 per share. We issued and sold 16 million shares and certain of our shareholders sold 9.875 million shares in the IPO. We used the net proceeds from the IPO, together with cash on hand (including additional funds from the Refinancing), to redeem all of our outstanding Series A preferred stock, repay \$300.0 million of outstanding borrowings under the Term Loan Facility and pay Sponsor-related obligations of approximately \$11.1 million.

On September 7, 2011, we filed a registration statement relating to a proposed offering of shares of Class A common stock to be sold exclusively by participating selling stockholders (the proposed Secondary Offering ).

In the third quarter of 2011, we generated 15.5% total revenue growth and positive domestic retail same store sales growth of 10.3%. Adjusting for expenses associated with the proposed Secondary Offering, operating income increased by 40.7% for the third quarter of 2011 compared to the same period in 2010.

Our 13.9% retail segment revenue growth for the third quarter of 2011 was driven by continued strength in the core product categories of sports and vitamins, and increased revenue from GNC.com. We believe our continued strength in the sports nutrition category reflects favorable macro fitness trends, our unique customer base and our successful new proprietary product launches. Similarly, vitamin sales have been driven primarily by increases in premium offerings including our more than 30 different Vitapakts addressing a wide range of conditions and lifestyles. GNC.com revenue increased by 38.0% in the third quarter of 2011, and we continue to realize benefits from our social media initiatives, including a growing following on Facebook. We also continue to upgrade site content and navigation, further improving our conversion rate. Internationally, the GNC brand continues to gain momentum across 52 franchise countries, resulting in growth of both number of stores and retail same store sales. With an additional 148 net new stores added at September 30, 2011 as compared to September 30, 2010, we believe this high margin business within the franchise segment will continue to drive growth.

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Our manufacturing strategy is designed to provide our stores with proprietary products at the lowest possible cost, and utilize additional capacity to promote production efficiencies and enhance our position in the third party contract business. Under this strategy, in the third quarter of 2011, we grew third party manufacturing contract sales by 13.5% and realized incremental revenue and margin contribution, which reflected contributions from our new Sam's Club and PetSmart wholesale arrangements. These arrangements also enable us to gain exposure to new customers.

From a brand marketing standpoint, we are focused on communicating our core "Live Well" theme in both magazine and print. In the first nine months of 2011, we expanded the marketing campaign to include a "best in class" theme. The campaign's branding images reflect our core customer - youthful, athletic, aspirational, and goal oriented.

**Related Parties**

For the three months ended September 30, 2011 and 2010, we had related party transactions with Ares and OTPP and their affiliates. For further discussion of these transactions, see Note 12, "Related Party Transactions" included elsewhere in this report.

**Results of Operations**

The following information presented for the three and nine months ended September 30, 2011 and 2010 was prepared by management and is unaudited and was derived from our unaudited consolidated financial statements and accompanying notes. In the opinion of management, all adjustments necessary for a fair statement of our financial position and operating results for such periods and as of such dates have been included.

As discussed in Note 9, "Segments", to our consolidated financial statements, we evaluate segment operating results based on several indicators. The primary key performance indicators are revenues and operating income or loss for each segment. Revenues and operating income or loss, as evaluated by management, exclude certain items that are managed at the consolidated level, such as warehousing and transportation costs, impairments and other corporate costs. The following discussion compares the revenues and the operating income or loss by segment, as well as those items excluded from the segment totals.

Same store sales growth reflects the percentage change in same store sales in the period presented compared to the prior year period. Same store sales are calculated on a daily basis for each store and exclude the net sales of a store for any period if the store was not open during the same period of the prior year. We also include internet sales, as generated through GNC.com and www.drugstore.com, in our domestic retail company-owned same store sales calculation. When a store's square footage has been changed as a result of reconfiguration or relocation in the same mall or shopping center, the store continues to be treated as a same store. If, during the period presented, a store was closed, relocated to a different mall or shopping center, or converted to a franchise store or a company-owned store, sales from that store up to and including the closing day or the day immediately preceding the relocation or conversion are included as same store sales as long as the store was open during the same period of the prior year. We exclude from the calculation sales during the period presented that occurred on or after the date of relocation to a different mall or shopping center or the date of a conversion.





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(Dollars in millions and percentages expressed as a percentage of total net revenue)

|  | Three Months Ended    |               |                       |               | Nine Months Ended     |               |                       |               |
|--|-----------------------|---------------|-----------------------|---------------|-----------------------|---------------|-----------------------|---------------|
|  | September 30,<br>2011 |               | September 30,<br>2010 |               | September 30,<br>2011 |               | September 30,<br>2010 |               |
|  | (unaudited)           |               |                       |               |                       |               |                       |               |
| <b>Revenues:</b>   |                       |               |                       |               |                       |               |                       |               |
| Retail   | \$ 385.2              | 71.6%         | \$ 338.2              | 72.6%         | \$ 1,153.3            | 73.8%         | \$ 1,031.9            | 74.4%         |
| Franchise  | 90.9                  | 16.9%         | 76.9                  | 16.5%         | 251.1                 | 16.1%         | 222.4                 | 16.1%         |
| Manufacturing /<br>Wholesale   | 61.9                  | 11.5%         | 50.6                  | 10.9%         | 158.2                 | 10.1%         | 132.1                 | 9.5%          |
| <b>Total net revenues</b>  | <b>538.0</b>          | <b>100.0%</b> | <b>465.7</b>          | <b>100.0%</b> | <b>1,562.6</b>        | <b>100.0%</b> | <b>1,386.4</b>        | <b>100.0%</b> |
| <b>Operating expenses:</b>   |                       |               |                       |               |                       |               |                       |               |
| Cost of sales, including<br>warehousing, distribution<br>and occupancy costs | 343.1                 | 63.8%         | 302.6                 | 65.0%         | 992.9                 | 63.5%         | 893.8                 | 64.5%         |
| Compensation and<br>related benefits   | 72.4                  | 13.5%         | 69.2                  | 14.9%         | 219.0                 | 14.0%         | 204.7                 | 14.8%         |
| Advertising and<br>promotion   | 12.4                  | 2.3%          | 10.9                  | 2.3%          | 40.0                  | 2.6%          | 40.4                  | 2.9%          |
| Other selling, general and<br>administrative expenses                        | 24.7                  | 4.6%          | 22.4                  | 4.8%          | 78.8                  | 5.0%          | 69.4                  | 5.0%          |
| Transaction related costs  | 0.6                   | 0.1%          | -                     | 0.0%          | 13.0                  | 0.9%          | -                     | 0.0%          |
| Amortization expense   | 2.0                   | 0.3%          | 1.9                   | 0.4%          | 5.8                   | 0.4%          | 5.9                   | 0.4%          |
| Foreign currency gain<br>(loss)  | 0.2                   | 0.0%          | (0.1)                 | 0.0%          | 0.1                   | 0.0%          | (0.1)                 | 0.0%          |
| <b>Total operating<br/>expenses</b>  | <b>455.4</b>          | <b>84.6%</b>  | <b>406.9</b>          | <b>87.4%</b>  | <b>1,349.6</b>        | <b>86.4%</b>  | <b>1,214.1</b>        | <b>87.6%</b>  |
| <b>Operating income:</b>   |                       |               |                       |               |                       |               |                       |               |
| Retail   | 62.2                  | 11.6%         | 47.7                  | 10.2%         | 189.2                 | 12.1%         | 147.2                 | 10.6%         |
| Franchise  | 32.0                  | 6.0%          | 25.9                  | 5.6%          | 83.3                  | 5.3%          | 70.5                  | 5.1%          |
| Manufacturing /<br>Wholesale   | 23.4                  | 4.3%          | 17.9                  | 3.9%          | 61.0                  | 3.9%          | 51.1                  | 3.7%          |
| Unallocated corporate<br>and other costs:                                    |                       |               |                       |               |                       |               |                       |               |
| Warehousing and<br>distribution costs  | (15.2)                | -2.9%         | (13.8)                | -3.0%         | (45.6)                | -2.9%         | (41.4)                | -3.0%         |
| Corporate costs  | (19.2)                | -3.5%         | (18.9)                | -4.1%         | (61.9)                | -4.0%         | (55.1)                | -4.0%         |
| Transaction related costs  | (0.6)                 | -0.1%         | -                     | 0.0%          | (13.0)                | -0.8%         | -                     | 0.0%          |
| Subtotal unallocated<br>corporate and other<br>costs, net                    | (35.0)                | -6.5%         | (32.7)                | -7.1%         | (120.5)               | -7.7%         | (96.5)                | -7.0%         |
| <b>Total operating income</b>  | <b>82.6</b>           | <b>15.4%</b>  | <b>58.8</b>           | <b>12.6%</b>  | <b>213.0</b>          | <b>13.6%</b>  | <b>172.3</b>          | <b>12.4%</b>  |
| Interest expense, net  | 10.4                  |               | 16.3                  |               | 64.5                  |               | 49.2                  |               |
| <b>Income before income<br/>taxes</b>  | <b>72.2</b>           |               | <b>42.5</b>           |               | <b>148.5</b>          |               | <b>123.1</b>          |               |
| Income tax expense   | 23.5                  |               | 15.8                  |               | 53.9                  |               | 45.4                  |               |
| <b>Net income</b>  | <b>\$ 48.7</b>        |               | <b>\$ 26.7</b>        |               | <b>\$ 94.6</b>        |               | <b>\$ 77.7</b>        |               |

**Note:** The numbers in the above table have been rounded to millions. All calculations related to the Results of Operations for the year-over-year comparisons were derived from unrounded data and could occasionally differ immaterially if you were to use the table above for these calculations.

**Comparison of the Three Months Ended September 30, 2011 and 2010**

**Revenues**

Our consolidated net revenues increased \$72.3 million, or 15.5%, to \$538.0 million for the three months ended September 30, 2011 compared to \$465.7 million for the same period in 2010. The increase was the result of increased sales in each of our segments.

*Retail.* Revenue in our Retail segment increased \$47.0 million, or 13.9%, to \$385.2 million for the three months ended September 30, 2011 compared to \$338.2 million for the same period in 2010. Domestic retail revenue increased \$41.1 million, representing a \$32.4 million, or 10.3% increase in our same store sales and a \$8.7 million increase in our non-same store sales. The increase was primarily due to sales increases in the sports nutrition, vitamin and diet categories, and also reflected an increase in sales from GNC.com of \$5.5 million, or 38.0%, to \$20.0 million for the three months ended September 30, 2011 compared to \$14.5 million for the same period in 2010. The acquisition of Lucky Vitamin on August 31, 2011 contributed \$3.8 million to the increase in sales. Canadian sales in U.S. dollars increased \$2.1 million for the three months ended September 30, 2011 compared to the same period in 2010. In local currency, Canada same store sales increased \$0.9 million and non same-store sales decreased \$0.1 million, which was improved by the effect of the weakening of the U.S. dollar from 2010 to 2011. Our company-owned store base increased by 125 domestic stores to 2,827 at September 30, 2011 compared to 2,702 at September 30, 2010, due to new store openings and franchise store acquisitions. Our Canadian store base remained consistent with 169 at September 30, 2011 and 2010.

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*Franchise.* Revenues in our Franchise segment increased \$14.0 million, or 18.2%, to \$90.9 million for the three months ended September 30, 2011 compared to \$76.9 million for the same period in 2010. Domestic franchise revenue increased by \$7.5 million compared to the same period in 2010 primarily due to an increase in product sales and royalty income. Our domestic franchisees same store retail sales improved for the three months ended September 30, 2011 by 7.8% compared to the same period in 2010. There were 919 domestic franchise stores at September 30, 2011 compared to 897 stores at September 30, 2010. International franchise revenue increased by \$5.7 million, primarily the result of increases in product sales and royalty income. Our international franchise store base increased by 148 stores to 1,549 at September 30, 2011 compared to 1,401 at September 30, 2010.

*Manufacturing/Wholesale.* Revenues in our Manufacturing/Wholesale segment, which includes third-party sales from our manufacturing facilities in South Carolina, as well as wholesale sales to Rite Aid, www.drugstore.com, Sam's Club and PetSmart increased \$11.3 million, or 22.5%, to \$61.9 million for the three months ended September 30, 2011 compared to \$50.6 million for the same period in 2010. Sales from the South Carolina plant increased by \$5.8 million, or 21.3%.

**Cost of Sales**

Consolidated cost of sales, which includes product costs, costs of warehousing and distribution and occupancy costs, increased \$40.5 million, or 13.4%, to \$343.1 million for the three months ended September 30, 2011 compared to \$302.6 million for the same period in 2010. Consolidated cost of sales, as a percentage of net revenue, was 63.8% and 65.0% for the three months ended September 30, 2011 and 2010, respectively. The increase in cost of sales was primarily due to higher sales volumes and store counts.

**Selling, General and Administrative ( SG&A ) Expenses**

Our consolidated SG&A expenses, including compensation and related benefits, advertising and promotion expense, other selling, general and administrative expenses, and amortization expense, increased \$7.7 million, or 7.4%, to \$112.1 million, for the three months ended September 30, 2011 compared to \$104.4 million for the same period in 2010. These expenses, as a percentage of net revenue, were 20.9% for the three months ended September 30, 2011 compared to 22.4% for the three months ended September 30, 2010.

*Compensation and related benefits.* Compensation and related benefits increased \$3.2 million, or 4.6%, to \$72.4 million for the three months ended September 30, 2011 compared to \$69.2 million for the same period in 2010. The increase was due primarily to support our increased store base and sales volume.

*Advertising and promotion.* Advertising and promotion expenses increased \$1.5 million, or 14.5%, to \$12.4 million for the three months ended September 30, 2011 compared to \$10.9 million during the same period in 2010. Advertising expense increased primarily as a result of an increase of \$1.7 million in media expense, partially offset by a decrease of \$0.2 million in other advertising expenses.

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*Other SG&A.* Other SG&A expenses, including amortization expense, increased \$2.4 million, or 9.5%, to \$26.7 million for the three months ended September 30, 2011 compared to \$24.3 million for the same period in 2010. This increase was due to increases in third-party commissions of \$0.5 million, credit card fees of \$0.7 million, legal and professional fees of \$0.5 million. Additionally, bad debt expense increased \$0.4 million, a result of the reversal of a portion of the allowance for bad debt in the three months ended September 30, 2010.

*Transaction related costs.* In addition to the above, we incurred \$0.6 million of non-recurring expenses principally related to the Secondary Offering.

### ***Foreign Currency (Gain) Loss***

Foreign currency (gain) loss for the three months ended September 30, 2011 and 2010 resulted primarily from accounts payable activity with our Canadian subsidiary.

### ***Operating Income***

As a result of the foregoing, consolidated operating income increased \$23.8 million, or 40.5%, to \$82.6 million for the three months ended September 30, 2011 compared to \$58.8 million for the same period in 2010. Operating income, as a percentage of net revenue, was 15.4% and 12.6% for the three months ended September 30, 2011 and 2010, respectively.

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*Retail.* Operating income increased \$14.5 million, or 30.4%, to \$62.2 million for the three months ended September 30, 2011 compared to \$47.7 million for the same period in 2010. The increase was due to higher dollar margins on increased sales, partially offset by increases in occupancy, wages and other selling expenses.

*Franchise.* Operating income increased \$6.1 million, or 23.4%, to \$32.0 million for the three months ended September 30, 2011 compared to \$25.9 million for the same period in 2010. The increase was due to higher wholesale product sales and franchise royalty income.

*Manufacturing/Wholesale.* Operating income increased \$5.5 million, or 30.6%, to \$23.4 million for the three months ended September 30, 2011 compared to \$17.9 million for the same period in 2010. The increase was due to higher wholesale product sales.

*Warehousing and distribution costs.* Unallocated warehousing and distribution costs increased \$1.4 million, or 10.2%, to \$15.2 million for the three months ended September 30, 2011 compared to \$13.8 million for the three months ended September 30, 2010. Higher fuel costs and increased wages for fulfillment of higher retail sales and wholesale businesses accounted for the increase.

*Corporate costs.* Corporate overhead costs increased \$0.3 million, or 1.6%, to \$19.2 million for the three months ended September 30, 2011 compared to \$18.9 million for the same period in 2010.

*Transaction related costs.* In addition to the above, we incurred \$0.6 million of non-recurring expenses principally related to the proposed Secondary Offering.

**Interest Expense**

Interest expense decreased \$5.9 million, or 36.1%, to \$10.4 million for the three months ended September 30, 2011 compared to \$16.3 million for the same period in 2010. This decrease was primarily attributable to decreases in interest rates on our variable rate debt in 2011 as compared to 2010 along with a reduction in outstanding debt.

**Income Tax Expense**

We recognized \$23.5 million of income tax expense (or 32.6% of pre-tax income) during the three months ended September 30, 2011 compared to \$15.8 million (or 37.2% of pre-tax income) for the same period in 2010. For the three months ended September 30, 2011, income tax expense includes \$2.6 million, or 3.0%, of pretax income related to non-recurring tax credits and

incentives.

### **Net Income**

As a result of the foregoing, consolidated net income increased \$22.0 million to \$48.7 million for the three months ended September 30, 2011 compared to \$26.7 million for the same period in 2010. Net income for the three months ended September 30, 2011 includes \$0.6 million of transaction related costs, net of tax effect, related to the proposed Secondary Offering. For the three months ended September 30, 2011, net income excluding transaction related costs related to the proposed Secondary Offering, net of tax effect, would have been \$49.1 million.

### **Comparison of the Nine Months Ended September 30, 2011 and 2010**

#### **Revenues**

Our consolidated net revenues increased \$176.2 million, or 12.7%, to \$1,562.6 million for the nine months ended September 30, 2011 compared to \$1,386.4 million for the same period in 2010. The increase was the result of increased sales in each of our segments.

*Retail.* Revenues in our Retail segment increased \$121.4 million, or 11.8%, to \$1,153.3 million for the nine months ended September 30, 2011 compared to \$1,031.9 million for the same period in 2010. Domestic retail revenue increased \$114.6 million, representing a \$90.8 million, or 9.5% increase in our same store sales and a \$23.8 million increase from our non-same store sales. The increase was primarily due to sales increases in the sports nutrition and vitamin product categories, and also included an increase in sales from GNC.com of \$16.5 million, or 38.2%, to \$59.6 million for the first nine months of 2011 compared to \$43.1 million for the same period in 2010. The acquisition of Lucky Vitamin contributed \$3.8 million to the increase in sales. Canadian sales in U.S. dollars increased \$3.0 million for the first nine months of 2011 compared to the first nine months of 2010. Canada same store sales decreased and non-same store sales were flat in local currency, which was offset by the effect of the weakening of the U.S. dollar from 2010 to 2011. Our company-owned store base increased by 125 domestic stores to 2,827 compared to 2,702 at September 30, 2010, due to new store openings and franchise store acquisitions. Our Canadian store base remained consistent with 169 stores at each of September 30, 2011 and 2010.

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*Franchise.* Revenues in our Franchise segment increased \$28.7 million, or 12.9%, to \$251.1 million for the nine months ended September 30, 2011 compared to \$222.4 million for the same period in 2010. Domestic franchise revenue increased by \$14.8 million to \$158.9 million for the nine months ended September 30, 2011 compared to \$144.1 million for the same period in 2010, primarily due to higher wholesale revenues, royalties and fees. Our domestic franchisees' same store retail sales improved for the first nine months of 2011 by 5.8% compared to the same period in 2010. There were 919 domestic franchise stores at September 30, 2011 compared to 897 stores at September 30, 2010. International franchise revenue increased by \$13.9 million, to \$92.2 million for the nine months ended September 30, 2011 from \$78.3 million, primarily the result of increases in product sales, royalties and fees. Our international franchise store base increased by 148 stores to 1,549 at September 30, 2011 compared to 1,401 at September 30, 2010.

*Manufacturing/Wholesale.* Revenues in our Manufacturing/Wholesale segment, which includes third-party sales from our manufacturing facilities in South Carolina, as well as wholesale sales to Rite Aid, PetSmart, Sam's Club and www.drugstore.com, increased \$26.1 million, or 19.7%, to \$158.2 million for the nine months ended September 30, 2011 compared to \$132.1 million for the same period in 2010. Third party contract manufacturing sales from the South Carolina manufacturing plant increased by \$10.1 million or 13.5%.

**Cost of Sales**

Consolidated cost of sales, which includes product costs, costs of warehousing and distribution and occupancy costs, increased \$99.1 million, or 11.1%, to \$992.9 million for the nine months ended September 30, 2011 compared to \$893.8 million for the same period in 2010. Consolidated cost of sales, as a percentage of net revenue, was 63.5% and 64.5% for the nine months ended September 30, 2011 and 2010, respectively. The increase in cost of sales was primarily due to higher sales volumes and store counts.

**Selling, General and Administrative ( SG&A ) Expenses**

Our consolidated SG&A expenses, including compensation and related benefits, advertising and promotion expense, other SG&A expenses and amortization expense, increased \$36.2 million, or 11.3%, to \$356.6 million, for the nine months ended September 30, 2011 compared to \$320.4 million for the same period in 2010. These expenses, as a percentage of net revenue, were 22.8% for the nine months ended September 30, 2011 compared to 23.1% for the same period in 2010.

*Compensation and related benefits.* Compensation and related benefits increased \$14.3 million, or 7.0%, to \$219.0 million for the nine months ended September 30, 2011 compared to \$204.7 million for the same period in 2010. Increases occurred in base wages of \$6.5 million to support our increased store base and sales volume, executive severance expense of \$3.5 million, incentives of \$3.2 million, and other compensation and benefits expense of \$1.1 million.

*Advertising and promotion.* Advertising and promotion expenses decreased \$0.4 million, or 1.0%, to \$40.0 million for the nine months ended September 30, 2011 compared to \$40.4 million during the same period in 2010. The decrease in advertising and promotion was primarily the result of lower media advertising expenditures partially offset by an increase in visual merchandising.

*Other SG&A.* Other SG&A expenses, including amortization expense, increased \$9.3 million, or 12.4%, to \$84.6 million for the nine months ended September 30, 2011 compared to \$75.3 million for the same period in 2010. This increase was due to increases in credit card fees of \$2.0 million, third party sales commissions of \$1.9 million, legal expenses and settlement expenses of \$3.5 million and \$0.7 million in other SG&A expenses. Additionally, bad debt expense increased \$1.2 million, a result of the reversal of a portion of the allowance for bad debt in the nine months ended September 30, 2010.

*Transaction related costs.* In addition to the above, we incurred \$13.0 million of non-recurring expenses principally related to the IPO and the proposed Secondary Offering. These consisted of a payment of \$11.1 million for the termination of Sponsor related obligations and other costs of \$1.9 million.



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**Foreign Currency (Gain) Loss**

Foreign currency (gain) loss for the nine months ended September 30, 2011 and 2010 resulted primarily from accounts payable activity with our Canadian subsidiary.

**Operating Income**

As a result of the foregoing, consolidated operating income increased \$40.7 million, or 23.6%, to \$213.0 million for the nine months ended September 30, 2011 compared to \$172.3 million for the same period in 2010. Operating income, as a percentage of net revenue, was 13.6% and 12.4% for the nine months ended September 30, 2011 and 2010, respectively. Operating income, excluding transaction related costs and executive severance expense, would have been \$229.8 million, or 14.7% of revenue, for the period ended September 30, 2011.

*Retail.* Operating income increased \$42.0 million, or 28.5%, to \$189.2 million for the nine months ended September 30, 2011 compared to \$147.2 million for the same period in 2010. The increase was due to higher margin on increased sales and a reduction in advertising expense, partially offset by increases in wages and other selling expenses.

*Franchise.* Operating income increased \$12.8 million, or 18.1%, to \$83.3 million for the nine months ended September 30, 2011 compared to \$70.5 million for the same period in 2010. The increase was due to increased wholesale product sales and royalty income.

*Manufacturing/Wholesale.* Operating income increased \$9.9 million, or 19.2%, to \$61.0 million for the nine months ended September 30, 2011 compared to \$51.1 million for the same period in 2010. This was primarily due to higher third party revenue from third party manufacturing contracts and contributions from our newer wholesale customers.

*Warehousing and distribution costs.* Unallocated warehousing and distribution costs increased \$4.2 million, or 10.0%, to \$45.6 million for the nine months ended September 30, 2011 compared to \$41.4 million for the same period in 2010. This increase was primarily due to higher fuel costs and additional wages to support higher sales volumes.

*Corporate costs.* Corporate overhead costs increased \$6.8 million, or 12.3%, to \$61.9 million for the nine months ended September 30, 2011 compared to \$55.1 million for the same period in 2010. This increase was due to increases in compensation expense and other general administrative expenses.

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*Transaction related costs.* Transaction related costs were \$13.0 million for the nine months ended September 30, 2011. These primarily consisted of a payment of \$11.1 million for termination of Sponsor related obligations and other costs of \$1.9 million.

### ***Interest Expense***

Interest expense increased \$15.3 million, or 31.2%, to \$64.5 million for the nine months ended September 30, 2011 compared to \$49.2 million for the same period in 2010. This increase included \$23.2 million of expenses related to the Refinancing: \$5.8 million in interest rate swap termination costs, \$13.4 million of deferred financing fees related to former indebtedness, \$1.6 million in original issue discount related to the Senior Toggle Notes, and \$2.4 million to defease the former Senior Notes and Senior Toggle Notes. Additionally, we recognized \$4.9 million of original issue discount and deferred financing fees expense related to the \$300 million pay down of debt in connection with the IPO in the nine months ended September 30, 2011.

### ***Income Tax Expense***

We recognized \$53.9 million of income tax expense (or 36.3% of pre-tax income) for the nine months ended September 30, 2011 compared to \$45.4 million (or 36.9% of pre-tax income) for the same period in 2010. The 2011 income tax expense includes \$2.3 million, or 1.5% of pretax income, related to non deductible costs incurred related to the IPO during the period. Also, the nine months ended September 30, 2011 was offset by \$2.6 million, or 1.8%, related to non-recurring tax credits and incentives.

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**Net Income**

As a result of the foregoing, consolidated net income increased \$16.8 million to \$94.6 million for the nine months ended September 30, 2011 compared to \$77.7 million for the same period in 2010. Net income for the nine months ended September 30, 2011 includes \$30.7 million of transaction related costs, net of tax effect, related to the Refinancing, IPO, the proposed Secondary Offering, and executive severance. For the nine months ended September 30, 2011, net income excluding transaction related costs related to the Refinancing, IPO, the proposed Secondary Offering, and executive severance, net of tax effect, would have been \$125.3 million.

**Liquidity and Capital Resources**

In March 2011, Centers entered into the 2011 Senior Credit Facility, consisting of a \$1.2 billion Term Loan Facility and an \$80.0 million Revolving Credit Facility, and utilized the proceeds to repay all outstanding indebtedness under the 2007 Senior Credit Facility, the Senior Notes and the Senior Subordinated Notes.

At September 30, 2011, we had \$146.1 million in cash and cash equivalents and \$472.7 million in working capital, compared with \$193.9 million in cash and cash equivalents and \$484.5 million in working capital at December 31, 2010. The \$11.8 million decrease in our working capital was primarily driven by a decrease in our cash which was used to repay indebtedness in connection with each of the Refinancing and the IPO, and an increase in accounts payable due to timing of payments, offset by an increase in our inventory levels due to volume.

We expect to fund our operations through internally generated cash and, if necessary, from borrowings under the Revolving Credit Facility. At September 30, 2011, we had \$71.8 million available under the Revolving Credit Facility, after giving effect to \$8.2 million utilized to secure letters of credit.

On April 6, 2011, we completed the IPO pursuant to which 25.875 million shares of Class A common stock were sold at a price of \$16.00 per share. We issued and sold 16 million shares and certain of our shareholders sold 9.875 million shares in the IPO. We used the net proceeds from the IPO, together with cash on hand (including additional funds from the Refinancing), to redeem all of our outstanding Series A preferred stock, repay \$300.0 million of outstanding borrowings under the Term Loan Facility and pay sponsor-related obligations of approximately \$11.1 million.

We expect our primary uses of cash in the near future will be debt service requirements, capital expenditures and working capital requirements.

We currently anticipate that cash generated from operations, together with amounts available under the Revolving Credit Facility, will be sufficient for the term of the 2011 Senior Credit Facility, which matures in March 2016, to meet our operating expenses, capital expenditures and debt service obligations as they become due. However, our ability to make scheduled payments of

principal on, to pay interest on, or to refinance our debt and to satisfy our other debt obligations will depend on our future operating performance, which will be affected by general economic, financial and other factors beyond our control. We are currently in compliance with our debt covenant reporting and compliance obligations under the 2011 Senior Credit Facility.

***Cash Provided by Operating Activities***

Cash provided by operating activities was \$146.4 million and \$97.6 million for the nine months ended September 30, 2011 and 2010, respectively. The increase was due primarily to the increase in net income of \$16.8 million and an increase in accounts payable of \$32.4 million due to timing of payments, offset by an increase in inventory of \$31.8 million due to sales volume.

***Cash Used in Investing Activities***

We used cash for investing activities of \$50.2 million and \$21.2 million for the nine months ended September 30, 2011 and 2010, respectively. Capital expenditures, which were primarily for new stores, improvements to our retail stores and our South Carolina manufacturing facility and corporate information systems, were \$27.8 million and \$21.0 million for the nine months ended September 30, 2011 and 2010, respectively. Also, during the nine months ended September 30, 2011, we used approximately \$21 million for the purchase of Lucky Vitamin.

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Our capital expenditures typically consist of certain periodic updates in our company-owned stores and ongoing upgrades and improvements to our manufacturing facilities and are expected to be approximately \$45 million for 2011.

***Cash Used in Financing Activities***

For the nine months ended September 30, 2011, we used cash of \$143.1 million, primarily due to repayment of indebtedness in connection with the Refinancing and the IPO. We borrowed \$1,196.2 million under the Senior Credit Facility, and utilized a portion of the funds to repay \$644.4 million under the 2007 Senior Credit Facility, \$300.0 million for the redemption of the Senior Notes, and \$110.0 million for the redemption of the Senior Subordinated Notes. We received net proceeds from the IPO of \$237.3 million and used these proceeds, together with cash on hand, to redeem all of the outstanding Class A Preferred Stock and repay \$300.0 million of the Senior Credit Facility. Additionally, we paid \$17.4 million for fees associated with the Refinancing. For the nine months ended September 30, 2010 we used cash of \$1.1 million, primarily for a payment of \$1.3 million on long-term debt, which was partially offset by an issuance of new equity for \$0.2 million in connection with the exercise of outstanding stock options.

The following is a summary of our debt:

*2011 Senior Credit Facility.* On March 4, 2011, Centers entered into the 2011 Senior Credit Facility, consisting of the Term Loan Facility and the Revolving Credit Facility. The Term Loan Facility will mature in March 2018. The Revolving Credit Facility will mature in March 2016. Interest on the 2011 Senior Credit Facility accrues at a variable rate and was 4.25% at September 30, 2011. Interest is accrued at a rate, at our option, per annum equal to (A) the sum of (i) the greatest of (a) the prime rate (as publicly announced by JPMorgan Chase Bank, N.A. as its prime rate in effect), (b) the federal funds effective rate plus 0.50%, (c) one month Adjusted LIBO Rate plus 1.0% and, (d) 2.25% plus (ii) Applicable Margin of 2.0% or (B) the sum of (i) the greatest of (a) Adjusted LIBO Rate or (b) 1.25% plus (ii) Applicable Margin of 3.0%. Effective on and after the first date on which quarterly financial statements are delivered to the lenders under and pursuant to the 2011 Senior Credit Facility following the first full quarter ending six months after the Closing Date, borrowings under the Revolving Credit Facility shall have an Applicable Margin of 1.75% for ABR Loans and 2.75% Eurodollar Loans provided the Consolidated Net Senior Secured Leverage Ratio is not greater than 3.25 to 1.00 and no event of default exists. Additionally, we are required to pay a commitment fee to the lenders under the Revolving Credit Facility in respect of unutilized revolving loan commitments at a rate of 0.5% per annum, as well as letter of credit fees of 3.0% to lenders and 0.25% to the issuing bank. As of September 30, 2011, \$8.2 million of the Revolving Credit Facility was pledged to secure letters of credit.

The 2011 Senior Credit Facility contains customary covenants, including incurrence covenants and certain other limitations on the ability of GNC Corporation, Centers, and Centers' subsidiaries to incur additional debt, guarantee other obligations, grant liens on assets, make investments or acquisitions, dispose of assets, make optional payments or modifications of other debt instruments, pay dividends or other payments on capital stock, engage in mergers or consolidations, enter into sales and leaseback transactions, enter into arrangements that restrict our subsidiaries' ability to pay dividends or grant liens, engage in transactions with affiliates, and change the passive holding company status of GNC Corporation. The Revolving Credit Facility also requires that, to the extent borrowings outstanding thereunder exceed \$25.0 million, Centers and its domestic subsidiaries meet a senior secured debt ratio of consolidated senior secured debt to consolidated EBITDA (as defined in the 2011 Senior Credit Facility). Such ratio test is 4.75 to 1.00 for the period from June 30, 2011 through and including March 31, 2013, and 4.25 to 1.00 thereafter.

As of September 30, 2011, the Company believes that it is in compliance with all covenants under the 2011 Senior Credit Facility.

*2007 Senior Credit Facility.* The 2007 Senior Credit Facility consisted of a \$675.0 million term loan facility and a \$60.0 million Revolving Credit Facility. The term loan facility was scheduled to mature in September 2013. The Revolving Credit Facility was scheduled to mature in March 2012. Interest on the 2007 Senior Credit Facility accrued at a variable rate and was 4.0% at December 31, 2010. As of December 31, 2010, \$7.9 million of the Revolving Credit Facility was pledged to secure letters of credit. At September 30, 2011, the 2007 Senior Credit Facility had been fully repaid.

*Senior Notes.* We had outstanding \$300.0 million of the Senior Notes at 99% of par value. Interest on the Senior Notes was payable semi-annually in arrears on March 15 and September 15 of each year. Interest on the Senior Notes accrued at a variable rate and was 5.8% at December 31, 2010. We had elected to make interest payments in cash. At September 30, 2011, these notes had been redeemed.

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*Senior Subordinated Notes.* We had outstanding \$110.0 million of the Senior Subordinated Notes due 2015. Interest on the Senior Subordinated Notes accrued at the rate of 10.75% per year and was payable semi-annually in arrears on March 15 and September 15 of each year. At September 30, 2011, these notes had been redeemed.

**Contractual Obligations**

There are no material changes in our contractual obligations as disclosed in our Quarterly Report on Form 10-Q for the quarter ended March 31, 2011.

**Off Balance Sheet Arrangements**

As of September 30, 2011, we had no relationships with unconsolidated entities or financial partnerships, such as entities often referred to as structured finance or special purpose entities, which would have been established for the purpose of facilitating off balance sheet arrangements or other contractually narrow or limited purposes. We are, therefore, not materially exposed to any financing, liquidity, market or credit risk that could arise if we had engaged in such relationships.

**Critical Accounting Estimates**

Our significant accounting policies are described in the notes to our consolidated financial statements under the heading "Basis of Presentation and Summary of Significant Accounting Policies" included elsewhere in this report. There have been no material changes to the application of critical accounting policies and significant judgments and estimates since those disclosed in the Prospectus.

**Recently Issued Accounting Pronouncements**

In September 2011, the FASB issued updated guidance on the periodic testing of goodwill for impairment. This guidance will allow companies to assess qualitative factors to determine if it is more likely than not that goodwill will be impaired and whether it is necessary to perform the two-step goodwill impairment test required under current accounting standards. This new guidance is effective for us for fiscal years beginning after December 15, 2011, with early adoption permitted. We are currently evaluating this guidance, but do not expect the adoption will have a material effect on our consolidated financial statements.

**Item 3. Quantitative and Qualitative Disclosures about Market Risk.**

Market risk represents the risk of changes in the value of market risk sensitive instruments caused by fluctuations in interest rates, foreign exchange rates and commodity prices. Changes in these factors could cause fluctuations in the results of our operations and cash flows. In the ordinary course of business, we are primarily exposed to foreign currency and interest rate risks. We do not use derivative financial instruments in connection with these commodity market risks.

***Foreign Currency Exchange Rate Market Risk***

We are subject to the risk of foreign currency exchange rate changes in the conversion from local currencies to the U.S. dollar of the reported financial position and operating results of our non-U.S. based subsidiaries. We are also subject to foreign currency exchange rate changes for purchases of goods and services that are denominated in currencies other than the U.S. dollar. The primary currency to which we are exposed to fluctuations is the Canadian Dollar. The fair value of our net foreign investments and our foreign denominated payables would not be materially affected by a 10% adverse change in foreign currency exchange rates for the periods presented.



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***Interest Rate Market Risk***

A portion of Centers' debt is subject to changing interest rates. Although changes in interest rates do not impact our operating income, the changes could affect the fair value of such debt and related interest payments. Based on our variable rate debt balance as of September 30, 2011, a 1% change in interest rates would have no impact on interest expense due to an interest rate floor that exists on the 2011 Senior Credit Facility.

**Item 4. Controls and Procedures.**

**Evaluation of Disclosure Controls and Procedures**

Our management, with the participation of our Chief Executive Officer ( CEO ) and Chief Financial Officer ( CFO ), has evaluated the effectiveness of our disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the Exchange Act )) as of the end of the period covered by this report. Disclosure controls and procedures are designed to provide reasonable assurance that the information required to be disclosed in the reports that we file or submit under the Exchange Act has been appropriately recorded, processed, summarized and reported on a timely basis and are effective in ensuring that such information is accumulated and communicated to our management, including our CEO and CFO, as appropriate to allow timely decisions regarding required disclosure. Based on such evaluation, our CEO and CFO have concluded that, as of September 30, 2011, our disclosure controls and procedures are effective at the reasonable assurance level.

**Changes in Internal Control Over Financial Reporting**

There have not been any changes in our internal controls over financial reporting that occurred during the last fiscal quarter, which have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

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**Part II - OTHER INFORMATION**

**Item 1. Legal Proceedings.**

We are engaged in various legal actions, claims and proceedings arising in the normal course of business, including claims related to breach of contracts, products liabilities, intellectual property matters and employment-related matters resulting from our business activities. As with most actions such as these, an estimation of any possible and/or ultimate liability cannot always be determined.

We continue to assess the requirement to account for additional contingencies in accordance with the standard on contingencies. If we are required to make a payment in connection with an adverse outcome in these matters, it could have a material impact on our financial condition, operating results, and cash flows.

As a manufacturer and retailer of nutritional supplements and other consumer products that are ingested by consumers or applied to their bodies, we have been and are currently subjected to various product liability claims. Although the effects of these claims to date have not been material to us, it is possible that current and future product liability claims could have a material adverse impact on our business, financial condition, or cash flows. We currently maintain product liability insurance with a deductible/retention of \$3.0 million per claim with an aggregate cap on retained loss of \$10.0 million. We typically seek and have obtained contractual indemnification from most parties that supply raw materials for our products or that manufacture or market products we sell. We also typically seek to be added, and have been added, as an additional insured under most of such parties' insurance policies. We are also entitled to indemnification by Numico for certain losses arising from claims related to products containing ephedra or Kava Kava sold prior to December 5, 2003. However, any such indemnification or insurance is limited by its terms and any such indemnification, as a practical matter, is limited to the creditworthiness of the indemnifying party and its insurer, and the absence of significant defenses by the insurers. We may incur material products liability claims, which could increase our costs and adversely affect our reputation, revenues and operating income.

*Hydroxycut Claims.* On May 1, 2009, the FDA issued a warning on several Hydroxycut-branded products manufactured by Iovate. The FDA warning was based on 23 reports of liver injuries from consumers who claimed to have used the products between 2002 and 2009. As a result, Iovate voluntarily recalled 14 Hydroxycut-branded products. Following the recall, we were named, among other defendants, in approximately 85 lawsuits related to Hydroxycut-branded products in 14 states. Iovate previously accepted our tender request for defense and indemnification under its purchasing agreement with us and, as such, Iovate has accepted our request for defense and indemnification in the Hydroxycut matters. Our ability to obtain full recovery in respect of any claims against us in connection with products manufactured by Iovate under the indemnity is dependent on Iovate's insurance coverage, the creditworthiness of its insurer, and the absence of significant defenses by such insurer. To the extent we are not fully compensated by Iovate's insurer, it can seek recovery directly from Iovate. Our ability to fully recover such amounts may be limited by the creditworthiness of Iovate.

During the first nine months of 2011, we were named in twenty-nine new or amended personal injury lawsuits related to Hydroxycut, generally inclusive of claims of consumer fraud, misrepresentation, strict liability and breach of warranty. None of the plaintiffs in these lawsuits asserted specific damages claims.

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The following twenty-nine personal injury matters were filed or amended during the first nine months of 2011 by individuals claiming injuries from use and consumption of Hydroxycut-branded products:

- Kelly Renner v. General Nutrition Corporation, et al., Superior Court of New Jersey, Atlantic County, L-399-11 (filed January 24, 2011);
- Orlando Jones, III, et al. v. GNC Corporation, U.S. District Court, Northern District of Alabama, 11CV350 (filed February 1, 2011);
- Lamone Griffin v. GNC, Inc., et al., Superior Court of New Jersey, Atlantic County, ATL-L-212711 (filed March 7, 2011);
- Jason Miller, et al. v. GNC Corporation, et al., Superior Court of California, County of Los Angeles, BC455783 (filed February 23, 2011);
- Shaunna Torres, et al. v. GNC Corporation, et al., Superior Court of California, County of Los Angeles, BC457615 (filed March 18, 2011);
- Teresa Paioni, et al. v. GNC Corporation, et al., Superior Court of California, County of Los Angeles, BC457616 (filed March 18, 2011);
- Sonny W. Roman v. GNC Corporation, et al., Court of Common Pleas Philadelphia County, 11-020477 (filed March 3, 2011);
- Steven D. Polley, et al. v. GNC Corporation, et al., U.S. District Court, Northern District of Alabama, 11CV1239 (filed April 11, 2011);

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- Gilbert Laureles v. General Nutrition Centers, Inc., et al., U.S. District Court, Northern District of Texas, 11CV917 (filed May 2, 2011);
- Tye Caldwell v. GNC Corporation, et al., Court of Common Pleas Philadelphia County, 11-0402972 (filed April 27, 2011);
- Henry C. Brooks v. GNC Corporation, et al., Court of Common Pleas Philadelphia County, 11-0403020 (filed April 27, 2011);
- Ronald Thompson v. GNC Corporation, et al., Court of Common Pleas Philadelphia County, 11-0403022 (filed April 27, 2011);
- Eva Hartfield, et al. v. GNC Corporation, et al., U.S. District Court, Northern District of Mississippi, 11CV99 (filed April 27, 2011);
- Kyle W. Newsom v. General Nutrition Centers, Inc., et al., U.S. District Court, Northern District of Alabama, 11CV1457 (filed May 2, 2011);
- Lshandra O. Fitzgerald v. General Nutrition Centers, Inc., et al., U.S. District Court, Northern District of Alabama, 11CV1458 (filed April 11, 2011);
- Alexander Torres and Jessica Lee Pizarro v. GNC Corporation, et al., Court of Common Pleas Philadelphia County, 11-0403330 (filed May 2, 2011);
- Matthew Williams v. GNC Corporation, et al., Circuit Court of St. Charles County, Missouri, 1111-CV-03893 (filed April 29, 2011);
- Brandy Addair v. GNC Corporation, et al., Supreme Court of New York, Bronx County, 304757-2011 (filed May 27, 2011);
- Timothy Bishop, et al. v. General Nutrition Centers, Inc., et al., Superior Court of California, County of Orange, 30-2011-00471939-CU-MT-CXC (filed May 2, 2011);
- Jonathan Botello, et al. v. GNC Corporation, et al., Superior Court of California, County of Los Angeles, No. BC460524 (filed April 27, 2011);
- Nancy Chapman, et al. v. GNC Corporation, et al., Superior Court of California, County of Orange, 00472214-CU-PL-CXC (filed May 5, 2011);
- Chris Dale, et al. v. General Nutrition Corporation, et al., Superior Court of California, County of Orange, 00472224-CXC (filed May 5, 2011);
- Noyola v. Iovate Health Sciences U.S.A., Inc., et al., U.S. District Court, Southern District of New York, 09CV6740 (Second Amended Complaint filed April 28, 2011);
- Jorge Delvalle v. GNC Corporation, et al., Superior Court of California, County of Orange, 30-2011-00471879-CU-PL-CXC (filed April 29, 2011);
- Michelle Kowalski, et al. v. GNC Corporation, et al., Superior Court of California, County of Los Angeles, BC-460552 (filed April 29, 2011);
- Jesse Lucero, et al. v. GNC Corporation, et al., Superior Court of California, County of Los Angeles, BC-460526 (filed April 29, 2011);

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- JT Sanders, et al. v. GNC Corporation, et al., Superior Court of California, County of Los Angeles, BC-460551 (filed April 29, 2011); and,
- Sean Sebastian Waters v. GNC, Inc., et al., Superior Court of New Jersey, Atlantic County, ATL-L- 00270510 (filed June 24, 2010 (GNC added to amended complaint on May 2, 2011)), and,
- Kerry and Nadia Donald v. Iovate Health Sciences Group, et al., Court of Common Pleas, Philadelphia County, 11-0502384 (filed May 20, 2011).

**Item 1A. Risk Factors.**

Risk factors that affect our business and financial results are discussed in our quarterly report on Form 10-Q for the quarter ended June 30, 2011 and are incorporated herein by reference.

**Item 2. Unregistered Sales of Equity Securities and Use of Proceeds.**

None.

**Item 3. Defaults Upon Senior Securities.**

None.

**Item 4. Removed and Reserved.**

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**Item 5. Other Information.**

None.

**Item 6. Exhibits.**

Exhibit

| <u>No.</u> | <u>Description</u>   |
|------------|--|
| 31.1       | Certification of Principal Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.                                |
| 31.2       | Certification of Principal Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.                                |
| 32.1       | Certification of CEO and CFO Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. |
| 101.INS    | XBRL Instance Document   |
| 101.SCH    | XBRL Taxonomy Extension Schema   |
| 101.CAL    | XBRL Taxonomy Extension Calculation Linkbase   |
| 101.LAB    | XBRL Taxonomy Extension Label Linkbase   |
| 101.PRE    | XBRL Taxonomy Extension Presentation Linkbase  |
| 101.DEF    | XBRL Taxonomy Extension Definition Linkbase  |

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**SIGNATURES**

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

GNC HOLDINGS, INC.  
(Registrant)

October 21, 2011

/s/ Joseph M. Fortunato  
Joseph M. Fortunato  
Chief Executive Officer  
(Principal Executive Officer)

October 21, 2011

/s/ Michael M. Nuzzo  
Michael M. Nuzzo  
Chief Financial Officer  
(Principal Financial Officer)