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

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**FORM 10-Q**

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

For the quarterly period ended June 30, 2006

OR

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number 0-18050

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**PW EAGLE, INC.**

(Exact name of registrant as specified in its Charter)

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**MINNESOTA**  
(State of incorporation)

**41-1642846**  
(I.R.S. Employer Identification No.)

**1550 Valley River Drive**  
**Eugene, Oregon 97401**  
(Address of principal executive offices)

**Registrant's telephone number, including area code: (541) 343-0200**

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

Large accelerated filer

Accelerated filer

Non-accelerated filer

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes  No

The number of shares of the registrant's Common Stock, \$.01 par value per share, outstanding as of July 31, 2006 was:

Common Stock	12,369,066
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**PW EAGLE, INC.**

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**PART I. FINANCIAL INFORMATION**

**ITEM 1. CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**PW EAGLE, INC.**

Condensed Consolidated Statement of Operations – Three and Six- Months Ended June 30, 2006 and 2005  
(Unaudited)

(in thousands, except per share amounts)	Three Months Ended June 30,		Six Months Ended June 30,	
	<u>2006</u>	<u>2005</u>	<u>2006</u>	<u>2005</u>
Net sales	\$ 205,241	\$ 161,626	\$ 387,178	\$ 304,266
Cost of goods sold	157,001	137,321	284,973	256,822
Gross profit	48,240	24,305	102,205	47,444
Operating expenses:				
Freight expense	10,805	9,345	19,312	17,534
Selling expenses	5,244	4,346	9,188	8,326
General and administrative expenses	4,026	3,333	9,543	6,871
Other (income) expense, net	50	(1,210)	518	(1,764)
	20,125	15,814	38,561	30,967
Operating income	28,115	8,491	63,644	16,477
Interest expense	1,476	4,384	2,617	8,154
Income before income taxes and minority interest	26,639	4,107	61,027	8,323
Income tax expense	9,970	1,571	23,312	3,186
Minority interest in (income) of USPoly Company	--	(253)	--	(157)
Net income	\$ 16,669	\$ 2,283	\$ 37,715	\$ 4,980
Net income per share:				
Basic	\$ 1.39	\$ 0.27	\$ 3.22	\$ 0.61
Diluted	\$ 1.35	\$ 0.23	\$ 3.08	\$ 0.51
Cash dividends declared per common share	\$0.075	--	\$0.15	--
Weighted average number of common shares outstanding:				
Basic	12,025	8,561	11,716	8,152
Diluted	12,324	9,800	12,261	9,762

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

**PW EAGLE, INC.**

## Condensed Consolidated Balance Sheet – June 30, 2006 and December 31, 2005 (Unaudited)

(in thousands, except share and per share amounts)

	<u>June 30, 2006</u>	<u>December 31, 2005</u>
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$ 8,370	\$ 5,671
Accounts receivable, net	107,120	87,062
Inventories	62,104	64,239
Deferred income taxes	2,382	2,382
Other current assets	2,927	2,861
Total current assets	<u>182,903</u>	<u>162,215</u>
Property and equipment, net	52,060	56,301
Goodwill	6,441	6,441
Deferred tax asset	409	325
Intangible assets	3,542	4,020
Other assets	6,088	5,154
Total assets	<u>\$ 251,443</u>	<u>\$ 234,456</u>
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Current liabilities:		
Borrowings under revolving credit facilities	\$ --	\$ 7,184
Current maturities of long-term debt and capital leases	175	182
Accounts payable	68,981	68,675
Accrued liabilities	22,990	47,907
Total current liabilities	<u>92,146</u>	<u>123,948</u>
Capital lease obligations, less current maturities	19,447	19,525
Other long-term liabilities	4,626	4,944
Total liabilities	<u>116,219</u>	<u>148,417</u>
Commitments and contingencies		
Stockholders' equity:		
Stock warrants	4,259	5,844
Common stock & class B common stock	124	112
Additional paid-in capital	75,976	61,439
Unearned compensation	--	(326)
Accumulated other comprehensive income	364	372
Accumulated earnings	54,501	18,598
Total stockholders' equity	<u>135,224</u>	<u>86,039</u>
Total liabilities and stockholders' equity	<u>\$ 251,443</u>	<u>\$ 234,456</u>

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

**PW EAGLE, INC.**

## Condensed Consolidated Statement of Cash Flows – Six Months Ended June 30, 2006 and 2005 (Unaudited)

(in thousands)

	<b>Six Months Ended</b>	
	<b>June 30, 2006</b>	<b>June 30, 2005</b>
Cash flows from operating activities:		
Net income	\$ 37,715	\$ 4,980
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
(Gain) loss on disposal of long-lived assets	9	(500)
(Gain) on sale of metals parts business	--	(1,256)
Depreciation and amortization and asset write-down	6,789	6,529
Royalty accretion	643	292
Warrant fair value adjustment	--	715
Amortization of debt issue costs, discounts and premiums	181	551
Receivable provisions	164	167
Deferred income taxes	(176)	3,145
Issuance of subordinated debt for interest payment	--	891
Non-cash minority interest	--	157
Stock-based compensation	1,849	139
Changes in operating assets and liabilities	(42,973)	511
Net cash provided by (used in) operating activities	<u>4,201</u>	<u>16,321</u>
Cash flows from investing activities:		
Purchases of property and equipment	(3,746)	(1,592)
Proceeds from sale of metals parts business	--	2,534
Proceeds from disposal of long-lived assets	10	870
Net cash provided by (used in) investing activities	<u>(3,736)</u>	<u>1,812</u>
Cash flows from financing activities:		
Change in book overdraft	(192)	(1,075)
Net borrowings (payments) under revolving credit facilities	(7,184)	(14,162)
Dividends paid	(1,725)	--
Payments on capital lease obligation	(97)	(95)
Proceeds from exercise of stock options	4,032	--
Proceeds from exercise of stock warrants	743	--
Repayment of long-term debt	--	(2,411)
Incremental tax benefits from stock options exercised	6,657	--
Payment of debt issuance/financing costs	--	(101)
Net cash provided by (used in) financing activities	<u>2,234</u>	<u>(17,844)</u>
Net change in cash and cash equivalents	2,699	289
Cash and cash equivalents, beginning of period	5,671	986
Cash and cash equivalents, end of period	<u>\$ 8,370</u>	<u>\$ 1,275</u>

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

**Notes to Condensed Consolidated Financial Statements (Unaudited)****1. Presentation**

In the opinion of management, the accompanying unaudited condensed consolidated financial statements contain all adjustments (consisting of only normal recurring adjustments) necessary to state fairly the financial position of PW Eagle, Inc. (the "Company") at June 30, 2006 and the results of its operations and cash flows for the six month periods ended June 30, 2006 and 2005. Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted pursuant to the rules and regulations of the Securities and Exchange Commission. The balance sheet information as of December 31, 2005 is derived from the Company's December 31, 2005 audited financial statements and condensed. Although the Company's management believes that the disclosures are adequate to make the information presented not misleading, it is suggested that these condensed consolidated financial statements be read in conjunction with the financial statements of the Company included with its Annual Report on Form 10-K for the year ended December 31, 2005.

**2. Other Financial Statement Data**

The following provides additional information concerning inventory (in thousands):

	<u>June 30, 2006</u>	<u>December 31, 2005</u>
Raw materials	\$ 16,564	\$ 14,083
Finished goods	45,540	50,156
	<u>\$ 62,104</u>	<u>\$ 64,239</u>

There are no significant non-cash investing and financing activities for the six months ended June 30, 2006. For the six months ended June 30, 2005 the significant non-cash investing and financing activities related to notes receivable settled in exchange for stock for \$78 thousand.

**3. Assets Held For Sale**

In February 2006, the Company announced that its wholly owned subsidiary, USPoly Company LLC (Polyethylene products), would combine all of its Oklahoma-based operations into a single location. This involved relocating all production equipment, warehousing and other support services from Shawnee, OK into existing space at USPoly's Tulsa, OK location. This relocation was completed in May 2006, and the Shawnee land and buildings were listed for sale. A write-down to fair value of the expected sales proceeds less selling costs amounted to \$682 thousand, \$557 thousand in the first quarter and \$125 thousand in the second quarter, which is included in Operating expenses (other expense). The resulting fair value of the assets of \$884 thousand was reclassified to Assets Held for Sale, included with Other assets on the Condensed Consolidated Balance Sheet.

**4. Financing Arrangements**

Current and long-term obligations at June 30, 2006 and December 31, 2005 consisted of the following (in thousands):

	<u>June 30, 2006</u>	<u>December 31, 2005</u>
Borrowings under revolving credit facilities	\$ --	\$ 7,184
Long-term debt		
PW Eagle capital lease obligations	16,284	16,353
USPoly capital lease obligations	3,338	3,354
Total current and long-term obligations	<u>19,622</u>	<u>19,707</u>
Less current maturities	<u>(175)</u>	<u>(182)</u>
Total long-term obligations	<u>\$ 19,447</u>	<u>\$ 19,525</u>

On April 27, 2006, the Company entered into a \$100 million Amended Restated Senior Credit Facility with its lenders, replacing the previous facility of the same amount. The new agreement, which includes PW Eagle and USPoly as co-borrowers, generally contains lower interest rates and unused line of credit fees. It also provides greater flexibility in covenant requirements, acquisitions and shareholder distributions.

Under current financing agreements, the Company is required to comply with certain restrictive financial ratios and covenants. At June 30, 2006, the Company was in full compliance with these covenants.

**5. Comprehensive Income and Accumulated Other Comprehensive Income**

Comprehensive income for the Company includes net income, changes in fair market value of financial instruments designated as hedges of interest rate exposure and changes in fair market value of securities held for the non-qualified deferred compensation plans. Comprehensive income for the three and six months ended June 30, 2006 and 2005 was as follows (in thousands):

	Three months ended June 30,		Six months ended June 30,	
	2006	2005	2006	2005
Net income	\$16,669	\$2,283	\$37,715	\$4,980
Other comprehensive income:				
Changes in fair market value of financial instrument designated as a hedge of interest rate exposure, net of taxes	--	(39)	--	63
Unrealized gain (loss) on available for sale securities from non-qualified deferred compensation plans, net of taxes	(34)	19	(8)	(180)
Total comprehensive income	<u>\$16,635</u>	<u>\$2,263</u>	<u>\$37,707</u>	<u>\$4,863</u>

The components of accumulated other comprehensive income are as follows:

	June 30, 2006	December 31, 2005
Unrealized gain on available for sale securities from non-qualified deferred compensation plans, net of taxes	\$ 364	\$ 372
Total accumulated other comprehensive income	<u>\$ 364</u>	<u>\$ 372</u>

## 6. Share-Based Payments (amounts in thousands, except per share data)

In December 2004, the Financial Accounting Standards Board ("FASB") issued SFAS 123(R), "Share-Based Payment (as amended)." SFAS No. 123(R) eliminates the alternative to use the intrinsic value method of accounting that was provided in SFAS No. 123, which generally resulted in no compensation expense recorded in the financial statements related to the issuance of equity awards to employees and directors. SFAS No. 123(R) requires that the cost resulting from all share-based payment transactions be recognized in the financial statements. SFAS No. 123(R) establishes fair value as the measurement objective in accounting for share-based payment arrangements and requires all companies to apply a fair-value-based measurement method in accounting generally for all share-based payment transactions with employees. In accordance with the new rule, the Company adopted SFAS No. 123(R) using a modified prospective method for the recognition of share-based compensation expense on January 1, 2006.

On November 10, 2005, the FASB issued FASB Staff Position No. FAS 123(R)-3, "Transition Election Related to Accounting for Tax Effects of Share-Based Payment Awards." The Company has elected to adopt the alternative transition method provided in this FASB Staff Position for calculating the tax effects of share-based compensation pursuant to FAS 123(R). The alternative transition method includes a simplified method to establish the beginning balance of the additional paid-in capital pool (APIC pool) related to the tax effects of employee share-based compensation, which is available to absorb tax deficiencies recognized subsequent to the adoption of FAS 123(R).

Under FAS 123(R), share-based compensation cost is measured at the grant date, based on the estimated fair value of the award and is recognized as expense over the stated vesting period. The Company continues to use the Black-Scholes option-pricing model as its method for valuing stock options. The key assumptions for this valuation method include the expected term of the option, stock price volatility, risk-free interest rate, dividend yield, exercise price and forfeiture rate. Many of these assumptions are judgmental and highly sensitive in the determination of compensation expense. The following is a discussion of our methodology for developing each of the assumptions used in the valuation model when share-based awards are granted:

*Term* - This is the period of time over which the options granted are expected to remain outstanding. Options granted have a maximum term of ten years.

*Volatility* - This is a measure of the amount by which a price has fluctuated or is expected to fluctuate. Volatilities are based on historical volatility of PW Eagle's shares and other factors, such as expected changes in volatility arising from planned changes in PW Eagle's business operations. An increase in the expected volatility will increase compensation expense.

*Risk-Free Interest Rate* - This is the U.S. Treasury rate for the date of the grant having a term equal to the expected term of the option. An increase in the risk-free interest rate will increase compensation expense.

*Dividend Yield* - We did not make any dividend payments during the last five fiscal years. With stock based awards granted after January 1, 2006, we have incorporated a dividend yield. An increase in the dividend yield will decrease compensation expense.

*Forfeiture Rate* - This is the estimated percentage of options granted that are expected to be forfeited or canceled before becoming fully vested. An increase in the forfeiture rate will decrease compensation expense. Based on historical forfeitures of share-based

awards, the Company has estimated a 4% forfeiture rate. The Company will annually evaluate this assumption as future forfeitures occur.

The weighted-average estimated fair value of share-based awards granted during the six months ended June 30, 2006 was \$19.57 using the Black-Scholes model, with the following weighted-average assumptions for the six months ended June 30, 2006:

Volatility	80.19%
Risk-free interest rate	4.88%
Dividend yield	1.08%
Forfeiture rate	4.00%

The share-based compensation expense, related to all of the Company's share-based awards, recognized for the three and six months ended June 30, 2006, in selling, general and administrative expense was comprised as follows (in thousands, except per share data):

	Three months ended June 30, 2006	Six months ended June 30, 2006
Share-based compensation expense before taxes	\$ 1,351	\$ 1,859
Related income tax benefits	(359)	(412)
Share-based compensation expense, net of taxes	<u>\$ 992</u>	<u>\$ 1,447</u>
Net share-based compensation expense, per common share:		
Basic	\$ 0.08	\$ 0.12
Diluted	\$ 0.08	\$ 0.12

As of June 30, 2006, there was approximately \$2.9 million of total unrecognized compensation cost related to non-vested share-based compensation arrangements granted under our share-based compensation plan. This unrecognized compensation cost is expected to be recognized over the remaining vesting periods through May 26, 2009.

Prior to adopting the provisions of FAS 123(R), we applied Accounting Principles Board ("APB") Opinion No. 25, "Accounting for Stock Issued to Employees," and related interpretations in accounting for our share-based awards. The following table details the effect on net earnings and earnings per share had compensation expense for the employee-based awards been recorded in the three and six months ended June 30, 2005 based on the fair value method under SFAS No. 123.

	Three Months ended June 30, 2005	Six Months ended June 30, 2005
Net Income, as reported	\$ 2,283	\$ 4,980
Share-based employee compensation expense included in reported net income, Net of related tax benefits	34	67
Deduct: Total share-based compensation expense determined under fair value based method, net of related tax effects	(75)	(149)
Pro-forma net income	<u>\$ 2,242</u>	<u>\$ 4,898</u>
Earnings per share:		
Basic – as reported	\$0.27	\$0.61
Basic – pro forma	\$0.26	\$0.60
Diluted – as reported	\$0.23	\$0.51
Diluted – pro forma	\$0.23	\$0.50

#### *Share-based Compensation Plan*

As of January 1, 2006, we have one active share-based compensation plan, described below.

The PW Eagle, Inc. 1997 Stock Option Plan (the "Plan") permits the granting of nonqualified and incentive stock options to purchase shares of common stock up to a total of 2,700,000 shares. The exercise price of an incentive or nonqualified stock option may not be less than 100% of the fair market value of the Company's common stock on the date of grant. These options generally vest over a period of time set by the Board of Directors.

The term of an incentive stock option may not exceed ten years from the date of grant. All employees of the Company or any subsidiary are eligible to receive incentive stock options. All employees, directors and officers of, and consultants and advisors to, the Company or any subsidiary are eligible to receive nonqualified stock options. The Board of Directors may terminate or amend the Plan but may not amend the Plan to materially increase the benefits accruing to any individual or materially modify the requirements for eligibility to participate in the Plan without the approval of the Company's shareholders. The shareholders approved an increase in the number of shares available for the granting of options under the Plan from 2,200,000 to 2,700,000 on May 26, 2006.

A summary of the share option activity for the six month period ended June 30, 2006 is presented below (shares in thousands):

	Outstanding Shares	Weighted Average Exercise Price
Balance at January 1, 2006	1,136	\$ 7.84
Granted	90	27.85
Exercised	(798)	5.05
Forfeited or expired	(8)	5.64
Balance at June 30, 2006	<u>420</u>	<u>\$ 8.21</u>
Options vested at June 30, 2006	<u>104</u>	<u>\$ 16.05</u>

The following table summarizes information about stock options outstanding and exercisable at June 30, 2006 (shares in thousands):

Range of Exercise Prices	Options Outstanding			Options Exercisable	
	Number Outstanding	Weighted Average Remaining Contractual Life	Weighted Average Exercise Price	Number Exercisable	Weighted Average Exercise Price
\$4.04 to 4.51	46	6.74	\$ 4.05	9	\$ 4.04
\$5.15 to 5.82	110	6.84	5.39	36	5.22
\$16.00	4	3.45	16.00	4	16.00
\$23.47 to 27.85	260	9.11	24.99	55	25.28
	<u>420</u>	<u>8.21</u>	<u>\$17.48</u>	<u>104</u>	<u>\$16.05</u>

## 7. Earnings per Common Share

Basic earnings per common share is computed by dividing net income by the weighted average number of common shares outstanding during the reporting period. Diluted earnings per common share is computed by dividing net income by the combination of shares issuable under the Company's share-based compensation plan and warrant issuances, if dilutive, using the treasury stock method and the weighted average number of common shares outstanding during the reporting period. Both basic and diluted earnings per share are calculated in accordance with Statement of Financial Accounting Standards ("SFAS") No. 128, "Earnings Per Share". The following tables reflect the calculation of basic and diluted earnings per share (in thousands, except per share amounts):

	<u>Three months ended</u>		<u>Six months ended</u>	
	<u>June 30, 2006</u>	<u>June 30, 2005</u>	<u>June 30, 2006</u>	<u>June 30, 2005</u>
Net income	\$ 16,669	\$ 2,283	\$ 37,715	\$ 4,980
Basic weighted average shares outstanding	12,025	8,561	11,716	8,152
Dilutive effect of stock options, warrants and restricted shares	299	1,239	545	1,610
Diluted weighted average shares outstanding	<u>12,324</u>	<u>9,800</u>	<u>12,261</u>	<u>9,762</u>
Net income per share – basic	\$ 1.39	\$ 0.27	\$ 3.22	\$ 0.61
Net income per share – diluted	\$ 1.35	\$ 0.23	\$ 3.08	\$ 0.51

The following table summarizes outstanding securities which are excluded from the computation of diluted earnings per share because inclusion of these shares would be anti-dilutive (in thousands):

	<u>Three months ended</u>		<u>Six months ended</u>	
	<u>June 30, 2006</u>	<u>June 30, 2005</u>	<u>June 30, 2006</u>	<u>June 30, 2005</u>
Stock options	--	147	90	230
Stock warrants	--	278	227	396

## 8. Guarantees

*Product warranties:* The Company's products are generally guaranteed against defects in material and workmanship for one year. The product warranty liability is reviewed regularly by management to ensure the Company's warranty allowance is adequate based on frequency and average cost of historical warranty claims activity. Management studies trends of warranty claim activity to improve pipe quality and pipe installation techniques to minimize future claims activity.

(in thousands)

Three months ended

Six months ended

	<u>June 30, 2006</u>	<u>June 30, 2005</u>	<u>June 30, 2006</u>	<u>June 30, 2005</u>
Accrual for product warranties – beginning of period	\$ 356	\$ 305	\$ 305	\$ 325
Accruals for warranties issued during the period	172	100	287	109
Settlements made during the period	(172)	(125)	(236)	(154)
Accrual for product warranties – end of period	<u>\$ 356</u>	<u>\$ 280</u>	<u>\$ 356</u>	<u>\$ 280</u>

*Standby letters of credit:* The Company is required to maintain standby letters of credit totaling \$2.8 million. These letters of credit guarantee payment to third parties in the event the Company is unable to pay in a timely manner. Standby letters of credit reduce the funds available under the revolving credit facilities by \$2.8 million. No amounts were drawn on these letters of credit as of June 30, 2006.

## 9. Litigation

We are from time to time a party to various claims and litigation matters incidental to our normal course of business. We are not a party to any material litigation and are not aware of any threatened litigation that would have a material adverse effect on our business.

## 10. Segments of Business

The Company manufactures and distributes polyvinyl chloride (PVC) and polyethylene (PE) pipe and fittings used for potable water and sewage transmission, turf and agricultural irrigation, natural gas transmission, water wells, fiber optic lines, electronic and telephone lines, and commercial and industrial plumbing. The PE segment operates under the name USPoly. We distribute our products throughout the United States, including Hawaii and Alaska, with a minimal amount of shipments to certain foreign countries. While there are similarities in technology and manufacturing processes utilized between the segments, differences exist in products and customer base, with the PVC segment focused on the water, irrigation and electrical products and customers, and the PE segment focused primarily on the natural gas distribution products and customers.

A summary of the Company's business activities reported by its two business segments follows:

	<u>Three Months Ended</u>		<u>Six Months Ended</u>	
	<u>June 30,</u>		<u>June 30,</u>	
	<u>2006</u>	<u>2005</u>	<u>2006</u>	<u>2005</u>
Business Segments (in millions)				
Net Sales:				
PVC products	\$ 183.3	\$ 139.8	\$ 343.6	\$ 263.4
PE products	21.9	21.8	43.6	40.8
Total net sales	<u>\$ 205.2</u>	<u>\$ 161.6</u>	<u>\$ 387.2</u>	<u>\$ 304.2</u>
Operating income				
PVC products	\$ 26.9	\$ 6.4	\$ 60.9	\$ 14.3
PE products	1.2	2.1	2.7	2.1
Total operating income	<u>28.1</u>	<u>8.5</u>	<u>63.6</u>	<u>16.5</u>
Interest expense	<u>1.5</u>	<u>4.4</u>	<u>2.6</u>	<u>8.1</u>
Income before income taxes and minority interest	<u>\$ 26.6</u>	<u>\$ 4.1</u>	<u>\$ 61.0</u>	<u>\$ 8.3</u>
Expenditures for property and equipment:				
PVC	\$ 1.4	\$ 0.9	\$ 3.0	\$ 1.3
PE	0.7	0.1	0.8	0.3
Total	<u>\$ 2.1</u>	<u>\$ 1.0</u>	<u>\$ 3.8</u>	<u>\$ 1.6</u>
Depreciation and amortization expense:				
PVC	\$ 2.4	\$ 2.6	\$ 4.8	\$ 5.2
PE	0.7	0.7	1.3	1.3
Total	<u>\$ 3.1</u>	<u>\$3.3</u>	<u>\$ 6.1</u>	<u>\$ 6.5</u>
Goodwill:			<u>June 30,</u>	<u>December 31,</u>
PVC			2006	2005
PE			\$ 3.6	\$ 3.6
Total			<u>2.8</u>	<u>2.8</u>
			<u>\$ 6.4</u>	<u>\$ 6.4</u>

Total Assets:		
PVC products	\$ 210.4	\$ 191.8
PE products	38.2	39.9
Corporate	2.8	2.7
Total assets	<u>\$ 251.4</u>	<u>\$ 234.4</u>

## 11. Stockholders' Equity Transactions

On January 5, 2006, Corporate Property Associates 14 Incorporated completed the cashless conversion of warrants to purchase 125,818 shares of the Company's common stock in exchange for 125,745 shares of common stock.

On January 5, 2006, JP Morgan Partners (23A SIBC), L.P. completed the cashless conversion of warrants to purchase 242,308 shares of the Company's common stock in exchange for 135,681 shares of common stock.

On February 8, 2006, Mass Mutual completed the cashless conversion of warrants to purchase 107,692 shares of the Company's common stock in exchange for 59,322 shares of common stock.

On April 3, 2006, a 2,500 share restricted stock grant was issued to an employee. This restricted stock award provides for 20% immediate vesting, an additional 30% on April 3, 2007, with the remaining 50% on April 7, 2008. The Black-Scholes value for this grant is \$28.7793 per share.

During May 2006, a cash conversion of warrants to purchase 39,500 shares of common stock was completed for \$742,620.

In May 2006, the Board of Directors approved the accelerated vesting of all unvested stock option grants issued to board members prior to January 1, 2006. As a result of this action, 60,000 stock options received accelerated vesting, effective May 26, 2006. Based on the terms of their grant, 144,578 shares of restricted stock vested immediately upon the election of the new Board of Directors on May 26, 2006. An additional cumulative non-cash compensation expense of \$304,597, net of tax, was recorded under SFAS 123(R) for the three months ended June 30, 2006.

On May 26, 2006, an aggregate of 90,000 non-qualified stock options were granted to six board members. The individual 15,000 stock option grants provided for 25% immediate vesting, with additional 25% vesting per year through May 26, 2009. The exercise price is \$27.85 and the options expire after 10 years, on May 26, 2016. The Black-Scholes value for these stock options is \$19.3164 per share.

For the three and six months ended June 30, 2006, 536,068 and 797,900 stock options were exercised, respectively, resulting in an increase to stockholders' equity of \$2.6 million and \$4 million, respectively.

### *Share Repurchase Program*

On June 16, 2006, the Board of Directors authorized the Company to repurchase up to \$40 million of the Company's common stock outstanding with an expiration date of June 30, 2008. Repurchases may be made in the open market and in privately negotiated transactions utilizing various hedge mechanisms including, among other things, the sale to third parties of put options for the Company's common shares, or otherwise. During the six months ended June 30, 2006, the Company did not repurchase any of the Company's common stock outstanding.

### *Dividends*

Cash dividends declared in the six months ended June 30, 2006 and June 30, 2005 were as follows (per share):

	June 30, 2006	June 30, 2005
First quarter	\$0.075	\$ --
Second quarter	\$0.075	--
	<u>\$0.150</u>	<u>\$ --</u>

## 12. Related Party Transactions

On March 30, 2006, the Company terminated its Management Services Agreement (the Agreement), dated January 1, 2004 with Spell Capital Partners, LLC (Spell Capital), pursuant to which Spell Capital provided the Company with supervisory and monitoring services, as well as advice and assistance with acquisitions, divestitures and financing activities. The Agreement was terminated based on a determination by the Company that the Company no longer required the services of Spell Capital. The terms of the Agreement permitted the Company to not renew the Agreement upon the conclusion of any quarterly term of the Agreement in exchange for a

payment to Spell Capital equal to the monthly management fee currently due and owing to Spell Capital along with a payment equal to twenty-four (24) times the current monthly management fee. The amount of the termination payment paid by the Company to Spell Capital was \$1,248,000. The Company's wholly-owned subsidiary, USPoly Company, LLC, also terminated its Management Services Agreement with Spell Capital. The amount of the termination payment paid by USPoly to Spell Capital was \$112,500.

### **13. Recent Accounting Pronouncements**

In July 2006, the Financial Accounting Standards Board ("FASB") issued Interpretation No. 48, "Accounting for Uncertainty in Income Taxes," which defines the threshold for recognizing the benefits of tax return positions in the financial statements as "more-likely-than-not" to be sustained by the taxing authority. Interpretation No. 48 applies to all tax positions accounted for under SFAS No. 109, "Accounting for Income Taxes." Interpretation No. 48 is effective as of the beginning of the first fiscal year beginning after December 15, 2006. Upon adoption, we will adjust our financial statements to reflect only those tax positions that are more-likely-than-not to be sustained as of the adoption date. Any adjustment will be recorded directly to our beginning retained earnings balance in the period of adoption and reported as a change in accounting principle. We are currently analyzing the effects of adopting Interpretation No. 48.

### **14. Subsequent Events**

Subsequent to the end of the second quarter of 2006 through August 10, 2006, the Company repurchased 75,027 shares of our outstanding common stock for approximately \$2.2 million in accordance with the provisions of the approved share repurchase program (see Note 11 of the Notes to the Condensed Consolidated Financial Statements). The Company may continue to purchase shares of common stock in the open market or in privately negotiated transactions utilizing various hedge mechanisms including, among other things, the sale to third parties of put options for the Company's common shares, in accordance with the approved share repurchase program up to a \$40 million amount.

**PW EAGLE, INC.****Consolidated Results of Operations – Comparison Between Three Months Ended June 30, 2006 and 2005**

(in millions)

	Three months ended		Increase (Decrease)	
	June 30,		\$	%
	2006	2005		
Net sales	\$ 205.2	\$ 161.6	\$ 43.6	27.0%
Cost of goods sold	157.0	137.3	19.7	14.3%
Gross profit	48.2	24.3	23.9	98.4%
Operating expenses	20.1	15.8	4.3	27.2%
Operating income	28.1	8.5	19.6	230.6%
Interest expense	1.5	4.4	(2.9)	-65.9%
Income before income taxes and minority interest	26.6	4.1	22.5	548.8%
Income tax expense	9.9	1.6	8.3	518.8%
Minority interest in loss of USPoly Company	--	(0.2 )	0.2	-100.0%
Net income	\$ 16.7	\$ 2.3	\$ 14.4	626.1%

The significant increase in sales in the second quarter of 2006, compared to the second quarter of 2005, is due to higher selling prices and a 3.6% increase in volumes shipped. While selling prices declined in the second quarter of 2006 compared to the first quarter of 2006, they remain well above the second quarter of 2005. The total volume and price increases resulted in an overall increase in net sales of 27%. Similarly, resin prices also moderated in the second quarter of 2006 as compared to the first quarter of 2006, but remain above the second quarter of 2005. Selling prices have increased more than resin costs compared to the second quarter of 2005, and the resulting higher margins yield a much improved gross profit level.

Operating expenses increased \$4.3 million in the second quarter of 2006, compared to the second quarter of 2005. This increase in operating expenses is primarily the result of three items. Freight costs increased \$1.5 million due to higher volume and higher transportation rates, non-cash costs related to FAS 123(R) stock based compensation expenses were \$1.3 million, and 2005 operating expenses were reduced by a non-recurring gain on sale of the metals parts business of \$1.3 million. In addition, non-cash costs of \$0.1 million and cash costs of \$0.3 million related to the previously announced relocation of USPoly's injection molding operations, were incurred in the second quarter of 2006.

Interest expense was significantly reduced in 2006 compared to 2005, as a result of payment of all subordinated and term loans in the fourth quarter of 2005 and lower borrowings under our revolving line of credit in the second quarter of 2006 as compared to the second quarter of 2005.

The income tax provisions for the quarters ending June 30, 2006 and 2005 were calculated on management's then-current estimates of the annual effective rate for the year, with an estimated effective tax rate of 38.2% for 2006, and 38.3% for 2005. The income tax provision for the second quarter of 2006 includes an adjustment to the estimated annualized tax rate of 38.2 % for 2006.

**Results of Operations by Segment – Comparison Between Three Months Ended June 30, 2006 and 2005**

(in millions)

	Three months ended		Increase (Decrease)	
	June 30,		\$	%
	2006	2005		
Net sales:				
PVC products	\$ 183.3	\$ 139.8	\$ 43.5	31.1%
PE products	21.9	21.8	0.1	0.5%
Consolidated net sales	\$ 205.2	161.6	\$ 43.6	27.0%
Operating income:				
PVC products	\$ 26.9	\$ 6.4	\$ 20.5	320.3%
<i>% of sales</i>	14.7%	4.6%		
PE products	1.2	2.1	(0.9)	-42.9%
<i>% of sales</i>	5.5%	9.6%		
Consolidated operating income	28.1	8.5	19.6	230.6%
<i>% of sales</i>	13.7%	5.3%		
Interest expense	1.5	4.4	(2.9)	-65.9%
Income before income taxes and minority interest	\$ 26.6	\$4.1	\$ 22.5	548.8%

## PVC Products

The significant increase in sales in the second quarter of 2006, compared to the second quarter of 2005, is due to higher selling prices and an increase of 5% in volumes shipped. While selling prices declined in the second quarter of 2006 compared to the first quarter of 2006, they remain well above the second quarter 2005, resulting in the overall increase in net sales of 31.1%. Similarly, resin prices also moderated in the second quarter of 2006 as compared to the first quarter of 2006, but remain above the second quarter 2005. Selling prices have increased more than resin costs compared to the second quarter of 2005, and the resulting higher margins yield a much improved gross profit level. Operating expenses increased by \$3.2 million in the second quarter of 2006 compared to second quarter of 2005. Freight costs increased by \$1.4 million due to the higher volume and higher rates, and selling, general and administrative costs increased \$1.9 million primarily due to the non-cash compensation costs resulting from FAS 123(R). The net result was an increase in operating income of \$20.5 million.

## PE Products

PE sales increased 0.5% in the second quarter of 2006, compared to the second quarter of 2005. Increases in selling prices more than offset a 10% reduction in volumes shipped. The increased sales resulted in a small increase in gross margins. Operating expenses, however, increased by \$1.1 million as 2005 had included a gain on sale of the metals business of \$1.3 million, and 2006 includes the costs for relocation of the injection molding operations, as noted above. Administrative costs declined by \$0.4 million as a result of the merger of USPoly with PW Eagle. The net result was a decrease in operating income of \$0.9 million.

## Consolidated Results of Operations – Comparison Between Six Months Ended June 30, 2006 and 2005

(in millions)

	Six months ended		Increase (Decrease)	
	June 30,		\$	%
	2006	2005		
Net sales	\$ 387.2	\$ 304.2	\$ 83.0	27.3%
Cost of goods sold	285.0	256.8	28.2	11.0%
Gross profit	102.2	47.4	54.8	115.6%
Operating expenses	38.6	30.9	7.7	24.9%
Operating income	63.6	16.5	47.1	285.5%
Interest expense	2.6	8.2	(5.6)	-68.3%
Income before income taxes and minority interest	61.0	8.3	52.7	634.9%
Income tax expense	23.3	3.2	20.1	628.1%
Minority interest in loss of USPoly Company	--	(0.1)	0.1	-100.0%
Net income	\$ 37.7	\$ 5.0	\$ 32.7	654.0%

The significant increase in sales in the first six months of 2006, compared to the first six months of 2005, is due to higher selling prices, which more than offset a 3.4% decrease in volumes shipped. While selling prices declined in the first six months of 2006 compared to the fourth quarter of 2005, they remain well above the first six months of 2005. The price increases resulted in an overall increase in net sales of 27.3%. Similarly, resin prices also moderated in the first six months of 2006 as compared to the fourth quarter of 2005, but remain above the first six months of 2005. Selling prices have increased more than resin costs compared to the first six months of 2005, and the resulting higher margins yield a much improved gross profit level.

Operating expenses increased \$7.7 million in the first six months of 2006 over the first six months of 2005. There were several contributing factors to this increase: freight costs are up \$1.8 million due to higher transportation rates; termination fees paid to Spell Capital Partners amounted to \$1.4 million; non-cash compensation costs are \$1.9 million (primarily from FAS 123(R) costs); non-cash costs of \$0.7 million and cash costs of \$0.3 million related to the previously announced relocation of USPoly's injection molding operations, which occurred in the second quarter; and 2005 included a gain on the sale of land of \$0.5 million and a gain on the sale of the metals parts business of \$1.3 million.

Interest expense was significantly reduced in 2006 compared to 2005, as a result of payment of all subordinated and term loans in the fourth quarter of 2005 and lower borrowings under our revolving line of credit in the first six months of 2006 as compared to the first six months of 2005.

The income tax provisions for the six months ending June 30, 2006 and 2005 were calculated based on management's then-current estimates of the annual effective rate for the year, with an estimated effective tax rate of 38.2% for 2006, and 38.3% for 2005.

## Results of Operations by Segment – Comparison Between Six Months Ended June 30, 2006 and 2005

	Six months ended		Increase (Decrease)	
	2006	2005	\$	%
Net sales:				
PVC products	\$ 343.6	\$ 263.4	\$ 80.2	30.4%
PE products	43.6	40.8	2.8	6.9%
Consolidated net sales	<u>\$ 387.2</u>	<u>304.2</u>	<u>\$ 83.0</u>	<u>27.3%</u>
Operating income:				
PVC products	\$ 60.9	\$ 14.3	\$ 46.6	325.9%
<i>% of sales</i>	17.7%	5.4%		
PE products	2.7	2.2	0.5	22.7%
<i>% of sales</i>	6.2%	5.4%		
Consolidated operating income	<u>63.6</u>	<u>16.5</u>	<u>47.1</u>	<u>285.5%</u>
<i>% of sales</i>	16.4%	5.4%		
Interest expense	2.6	8.2	(5.6)	-68.3%
Income before income taxes and minority interest	<u>\$ 61.0</u>	<u>\$8.3</u>	<u>\$ 52.7</u>	<u>-634.9%</u>

### PVC Products

The significant 30.4% increase in sales in the first six months of 2006, compared to the first six months of 2005, is due to higher selling prices which more than offset a decrease of 3% in volumes shipped. While selling prices declined in the first six months of 2006 compared to the fourth quarter of 2005, they remained well above the first six months of 2005, resulting in the overall increase in net sales of 30.4%. Similarly, resin prices also moderated in the first six months of 2006 as compared to the fourth quarter of 2005, but remain above the first six months of 2005. Selling prices have increased more than resin costs compared to the first six months of 2005, and the resulting higher margins yield a much improved gross profit level.

Operating expenses increased by \$6.2 million in the first six months of 2006 compared to the first six months of 2005. Freight costs increased by \$1.6 million due to the higher transportation rates, and selling, general and administrative costs increased \$4.1 million due to termination fees paid to Spell Capital Partners of \$1.4 million, non-cash compensation costs of \$1.9 million (primarily from FAS 123(R) costs). In addition, 2005 included a gain on sale of land of \$0.5 million. The net result was an increase in operating income of \$46.6 million.

### PE Products

PE sales increased 6.9% in the first six months of 2006, compared to the first six months of 2005. Increases in selling prices more than offset a 9% reduction in volumes shipped. The increased sales and moderating material costs resulted in substantial increase in gross margins. Operating expenses, however, increased by \$1.4 million as 2005 had included a gain on sale of the metals business of \$1.3 million, and 2006 includes the costs for relocation of the injection molding operations of \$1.0 million, as noted above. Freight costs increased by \$0.2 million due to the higher transportation rates, and administrative costs declined by \$0.6 million as a result of the merger of USPoly with PW Eagle. The net result was an increase in operating income of \$0.5 million.

### Liquidity and Capital Resources

Total assets of \$251.4 million at June 30, 2006 represented a \$16.9 million increase from \$234.5 million at December 31, 2005. This increase was from current assets, with the net increase in cash, accounts receivable and inventories amounting to \$20.6 million, offset by decreases in property and equipment of \$3.3 million (net of \$0.9 million reclassified to assets held for sale). Total capitalization at June 30, 2006 was \$160.4 million, consisting of \$25.2 million of debt and \$135.2 million of equity, with debt decreasing by \$7.9 million and equity increasing by \$49.2 million from December 31, 2005 amounts.

The increase in current assets was primarily due to increasing accounts receivable due to the overall sales increase, and increasing cash due to the positive cash from operations. The decrease in property and equipment was primarily due to depreciation in excess of capital expenditures.

We had working capital of \$90.8 million at June 30, 2006, which is an improvement of \$52.4 million from December 31, 2005. In addition to the improvement in working capital, we had additional availability on our \$100 million revolving credit facility of \$97.2 million at June 30, 2006.

Capital spending for property and equipment was \$3.7 million in the first six months of 2006, consistent with our capital spending plan for 2006, expected to be in the range of \$6 to \$10 million.

Management believes that, for the foreseeable future, the Company can fund cash requirements for working capital, capital expenditures and other obligations with cash generated from operations and borrowing from existing credit facilities. In addition, based upon the Company's improved working capital and revolving debt availability, in June 2006 the Board of Directors authorized a repurchase of up to \$40 million of the Company's outstanding shares.

Cash provided by operating activities was \$4.2 million in the first six months of 2006, compared to \$16.3 million in the first six months of 2005. This net change of \$12.1 million is primarily a result of an increase in net income of \$32.3 million, offset by a net change in operating assets and liabilities of \$42.5 million. The primary changes in operating assets and liabilities are the increase in current assets and a reduction in accrued liabilities due to tax payments totaling \$36.6 million in the first six months of 2006.

Investing activities used \$3.7 million in the first six months of 2006 compared to \$1.8 million provided by investing activities in the first six months of 2005. The 2006 amount used was for capital expenditures; and the cash provided in 2005 was from proceeds from asset disposals, partially offset by capital expenditures.

Financing activities provided \$2.2 million in the first six months of 2006. The net decrease in our revolving credit facility of \$7.2 million and \$1.7 million in dividend payments were more than offset by the proceeds and tax benefits from exercises of stock options and warrants which provided \$11.4 million. Financing activities used \$17.8 million during the first six months of 2005 for debt payments and net reductions of our revolving credit facility.

### **Critical Accounting Estimates**

Management's discussion and analysis of its financial condition and results of operations are based upon our financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of these financial statements requires management to make certain estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the financial statements and the reported revenues and expenses during the reporting period. Management bases these estimates on historical experience and various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the recorded values of certain assets and liabilities. Actual results could differ from these estimates.

A discussion of the Company's critical accounting policies and areas that require more significant judgments and estimates used in the preparation of its financial statements is included in the Annual Report on Form 10-K.

### **Future Outlook**

**INFORMATION IN THIS OUTLOOK SECTION AND OTHER STATEMENTS IN THIS FORM 10-Q ARE FORWARD-LOOKING INFORMATION – ACTUAL RESULTS MAY DIFFER**

The statements contained above in Management's Discussion and Analysis of Financial Condition and Results of Operations that are not strictly historical, the statements set forth in this Outlook section and the statements made in Item 1A. Risk Factors are forward-looking statements made under the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. These statements reflect our expectations and beliefs as of August 2, 2006 and are based on information known to us, and our assumptions as of that date. Forward-looking statements made in this Quarterly Report, which relate to our ability to fund cash requirements for the foreseeable future with cash from operations and from existing credit facilities, our expected sales volumes and margins in the third quarter of 2006, the expected demand for our products and PVC and PE pipe in general, seasonality and cyclicity, our financial performance correlation to GDP growth, and the availability of raw materials involve known and unknown risks and uncertainties, including those described in Item 1A. Risk Factors of this Quarterly Report, some of which are beyond our control, that may cause the actual results to differ materially from those expected and stated in this Quarterly Report. As a result, our statements may not come true and our operating results may differ materially from our stated expectations and beliefs.

Some of our current beliefs and expectations are discussed below along with risk factors that impact our business and industry.

#### *Forward-Looking Statements*

PVC and PE resin manufacturers were significantly impacted by Hurricanes Katrina and Rita during the third quarter of 2005. Manufacturing plants in both Louisiana and Texas ceased operating during the storms and curtailed production thereafter due to lack of utilities and/or raw material supply. The subsequent difficulties with the rail service made the situation worse. Also, one manufacturer experienced production disruptions as a result of an accident and fire at one of its facilities. All major suppliers declared *force majeure* and for a period of time supplied customers on some form of allocation. These interruptions in supply resulted in significant price increases in both PE and PVC resin.

In light of the potential supply disruptions, PVC and PE pipe buyers accelerated their purchasing patterns, resulting in a very strong demand surge in September and continuing into the fourth quarter. Faced with this strong demand, limited raw material supply and

rising costs, we and many other pipe manufacturers implemented multiple price increases. Because we were able to increase prices at a rate ahead of increasing resin costs, we improved gross margins as well, resulting in strong sales volumes and high gross margins in the fourth quarter of 2005.

Most of the disruption in supply of PVC and PE resin caused by Hurricanes Katrina and Rita was resolved by the end of 2005, resulting in increased availability of, and decreasing prices for, resin. Starting in December 2005, and continuing through the first few months of 2006, PVC resin prices decreased and then stabilized during the second quarter. Resin manufacturers have announced intentions to increase prices during the third quarter. However, these are still subject to final settlement. Prices for PVC pipe have declined somewhat in the first part of 2006, and stabilized during the second quarter as resin prices have stabilized. If the resin price increases are implemented as announced, we are optimistic about our ability to continue to deliver strong results for the third quarter. Historically, we have been able to maintain or increase margins during periods of rising raw material costs. If resin supplies remain at levels to adequately service demand, however, resin prices could decrease during the fourth quarter of 2006. During periods of decreasing resin prices, pipe selling prices have tended to decrease faster than raw material cost, resulting in lower margins. The short term expectations described above may be mitigated to some extent by the following broader trends in our business. We expect the demand for plastic pipe to grow as acceptance of plastic pipe over metal pipe continues and the overall economy continues to grow. We believe that the Gross Domestic Product (GDP) is closely correlated to the demand for PVC and PE pipe, and we recognize that our business is tied to economic cycles. GDP is estimated to have grown at an annual rate of 3.5% in 2005, 5.6% in the first quarter of 2006, and 2.5% in the second quarter of 2006. Industry growth projections call for annual sales growth rates for PVC pipe of 3% or greater in 2006. The actual growth rate may be less or greater than 3% based on short-term economic conditions. Our strategy has been, and continues to be, to concentrate growth initiatives in higher profit products and geographic regions.

We have a long-term contract with one supplier for PVC resin, our primary raw material, and are substantially dependent on that relationship. The terms of our long-term agreement with our PVC supplier provide, among other things, for the extension of the agreement at the supplier's option through 2013, certain termination rights exercisable by the supplier without corresponding rights for us, a right of first negotiation with the supplier on the sale of the assets of one or more of our facilities that utilize PVC resin, and the supplier's option to require a buyer of all or a substantial portion of our assets to assume the agreement. These provisions may have the effect of limiting our ability to replace the supplier, procure PVC resin under more favorable terms or divest of our assets.

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

We were not exposed to any market risks on variable rate debt obligations at June 30, 2006, as we had no such obligations outstanding. Market risk is the potential loss arising from adverse changes in market rates and prices, such as interest rates. Market risk is estimated as the potential increase in interest expense resulting from a hypothetical one percent increase in interest rates.

We do not enter into derivatives or other financial instruments for trading or speculative purposes. We only enter into financial instruments to manage and reduce the impact of changes in interest on our Senior Credit Facility. At June 30, 2006, we had no outstanding derivatives.

### **ITEM 4. CONTROLS AND PROCEDURES**

- (a) *Evaluation of disclosure controls and procedures.* After evaluating the effectiveness of the Company's disclosure controls and procedures pursuant to Rule 13a-15(b) of the Securities Exchange Act of 1934 ("the Exchange Act") as of the end of the period covered by this quarterly report, our Chief Executive Officer and Chief Financial Officer with the participation of the Company's management, have concluded that the Company's disclosure controls and procedures are effective to ensure that information that is required to be disclosed by the Company in reports that it files under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the rules of the Securities Exchange Commission. Our Chief Executive Officer and Chief Financial Officer with the participation of the Company's management, have also concluded that the Company's disclosure controls and procedures are effective to ensure that information required to be disclosed in reports filed or submitted under the Exchange Act is accumulated and communicated to management, including our principal executive officer and principal financial officer, to allow timely decisions regarding required disclosures.
- (b) *Changes in internal controls.* There were no changes in our internal control over financial reporting that occurred during the period covered by this quarterly report that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

## **PART II. OTHER INFORMATION**

### **ITEM 1. LEGAL PROCEEDINGS**

We are from time to time a party to various claims and litigation matters incidental to our normal course of business. We are not a party to any material litigation and are not aware of any threatened litigation that would have a material adverse effect on our business.

#### **ITEM 1 A. RISK FACTORS**

##### **The pipe industry and our business are heavily dependent on the price and trend of resin, our main raw material.**

Our gross margin percentage is sensitive to raw material resin prices and the demand for PVC and PE pipe. Historically, when resin prices are rising or stable, our margins and sales volume have been higher. Conversely, when resin prices are falling, our sales volumes and margins have been lower. In response to hurricane-related supply disruptions and increasing energy and raw material costs, PVC resin producers implemented increases in September and October 2005. Starting in December 2005, and continuing through the first few months of 2006, PVC resin prices decreased and then stabilized during the second quarter. Resin manufacturers have announced intentions to increase prices during the third quarter. However, these are still subject to final settlement.

Our gross margins decrease when the supply of resin and pipe is greater than demand. Conversely, our gross margins improve when resin and pipe are in short supply. In April 2001, a major producer of PVC resin filed for bankruptcy and, during the first quarter of 2002 ceased operations at two manufacturing facilities. This resulted in a reduction of approximately 1.0 billion pounds of production capacity, or 5% of the North American industry capacity. Although two PVC producers have subsequently purchased these two facilities, only one of them has re-started a portion of its capacity. In December 2004, a major PVC producer announced plans to build a PVC plant with annual capacity of 1.3 billion pounds together with integrated production of chlorine and vinyl chloride monomer (VCM), with completion expected by 2007 for the first phase and by 2008 for the second phase. During 2005, two other PVC producers announced smaller expansions of existing facilities which are expected to be completed in 2007. If these capacity increases result in industry capacity exceeding demand when they begin production, it could result in decreasing prices for PVC resin and negatively impact our gross margins. In addition, we believe the production of PVC resin may be limited by the availability of chlorine, a major raw material component.

##### **The demand for our products is directly affected by the growth and contraction of the Gross Domestic Product and economic conditions.**

Due to the commodity nature of resin, pipe and the dynamic supply and demand factors worldwide, the markets for both resin and pipe have historically been very cyclical with significant fluctuations in prices and gross margins. Generally, after a period of rising or stable resin prices, capacity has increased to exceed demand with a resulting decrease in prices and gross margins. Over the last ten years, there have been consolidations in both markets, particularly with respect to PVC resin manufacturers. During the same period, the capacity of PVC resin producers has increased from just over 9 billion pounds to over 18 billion pounds today. In the last ten years published PVC resin prices have fluctuated between approximately \$0.25 and \$0.70 per pound. Since peaking in October 2005, PVC resin prices have decreased \$0.065 per pound.

We believe the main drivers of industry performance are U.S. Gross Domestic Product (GDP) growth and supply and demand of PVC resin. Historically, our profitability has improved during periods of strong GDP growth and decreased during periods of slower growth or recession. GDP growth improved in the first nine months of 2005 compared to 2004, demand for PVC resin for use in pipe was strong, and our margins increased. Although GDP growth slowed somewhat in the fourth quarter of 2005, the effect of hurricanes Katrina and Rita contributed to a continuing increase in demand and selling prices. GDP growth is estimated to have increased in the first quarter of 2006, and declined again in the second quarter. Additionally, because our products are used in both new residential and commercial construction and replacement and upgrade projects, a significant or prolonged decrease in the level of construction activity in the U.S. could lead to decreased demand for PVC and PE pipe, and result in lower prices and margins.

While we expect the demand for PVC and PE pipe to continue to increase over the long term, we also expect that the industry will continue to be subject to cyclical fluctuations and times when supply will exceed demand, driving prices and margins down. These conditions could result from a general economic slowdown either domestically or elsewhere in the world or capacity increases in either the resin or pipe markets. General economic conditions both in the United States and abroad will continue to have a significant impact on our prices and gross margins.

##### **We are substantially dependent on one supplier of PVC resin, our primary raw material. Our business and operating results could be seriously harmed if this supplier were unable to timely meet our requirements on a cost effective basis. Additionally, certain terms of our agreement with this supplier limit our business and operating flexibility.**

Our key raw materials, PE and PVC resin, are procured primarily from three suppliers. The cost, quality and availability of these raw materials, chief among them PVC resin, are essential to the successful production and sale of our products. There are a limited number of suppliers of PVC resin. Alternative sources are not always available or may not be available on terms acceptable to us. For

example, there are currently only five suppliers of PVC resin in North America who are capable of providing us the material in an amount that would meet our requirements on terms acceptable to us. We have a long-term agreement in place with one PVC resin supplier and thus are substantially dependent upon our relationship with that supplier, which we believe to be good. However, if our supplier experienced a natural disaster, a serious incident at a major production facility that limited production of PVC resin, or experienced any other event that resulted in a significant and extended limitation on its ability to provide us with PVC resin or was unwilling to meet our demand for PVC resin on terms acceptable to us and if we are unable to obtain an alternative source or if the price for an alternative source is prohibitive, our ability to maintain timely and cost-effective production of our products will be seriously harmed.

In September and October of 2005, all five PVC resin suppliers in North America declared *force majeure* due to the effects of Hurricanes Katrina and Rita, and due to an accident at one resin manufacturing facility. Despite this situation, we were able to secure sufficient amounts of raw material to maintain our operations at reasonable levels, primarily because of our agreement with our PVC supplier. During late fourth quarter of 2005 and early first quarter of 2006, resin suppliers were able to increase production to levels such that there are no longer supply limitations. However, if similar disruptions in our raw material supply occur in the future, we may be unable to effectively utilize our manufacturing capacity.

The terms of our long-term agreement with our PVC supplier provide, among other things, for the extension of the agreement at the supplier's option through 2013, certain termination rights exercisable by the supplier without corresponding rights for us, a right of first negotiation with the supplier on the sale of the assets of one or more of our facilities that utilize PVC resin, and the supplier's option to require a buyer of all or a substantial portion of our assets to assume the agreement. These provisions may have the effect of limiting our ability to replace the supplier, procure PVC resin under more favorable terms or divest of our assets.

**A significant portion of our business and the demand for our products is seasonal in nature and any adverse weather conditions that result in a slowdown in the construction industry may adversely affect demand for our products.**

Our products are used in new residential and commercial construction. Because of this, the demand for these products tends to be seasonal to correspond with increased construction activity in the late spring, summer, and early fall. Any significant or prolonged adverse weather conditions that negatively affect the construction industry or slow the growth of new construction activity may negatively affect our operating results.

**Our operating results are dependent on the price of resin and any competitive pressure in the resin industry that increases supply or decreases the price of resin may negatively affect our profitability.**

The primary raw material used in most of our products is PVC resin. Generally, in periods of strong demand and limited supply of PVC resin, prices of resin tend to increase. Conversely, PVC resin prices tend to decrease when demand is weak and there is excess supply. Historically, in response to increasing resin prices, we have been able to increase the price of our products at a greater rate, resulting in better margins. During periods of decreasing resin prices, our selling prices have tended to decrease faster than our raw material costs, resulting in lower margins. In the event of a significant increase in PVC resin capacity or a significant decrease in the demand for PVC resin, resulting in a period where there is an excess supply of PVC resin, our margins and profitability could be negatively impacted.

## **ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES**

On May 15, 2006, the Company issued 10,000 shares of its common stock in connection with a cash conversion of 10,000 warrants with an exercise price of \$27 per share. The Company received \$270,000 which was used for general working capital. The above securities were issued in reliance on the exemption from registration provided by Section 3(a)(9) of the Securities Act of 1933.

On May 19, 2006, the Company issued 12,000 shares of its common stock in connection with a cash conversion of 12,000 warrants with an exercise price of \$.01 per share. The Company received \$120 which was used for general working capital. The above securities were issued in reliance on the exemption from registration provided by Section 3(a)(9) of the Securities Act of 1933.

On May 25, 2006, the Company issued 17,500 shares of its common stock in connection with a cash conversion of 17,500 warrants with an exercise price of \$27 per share. The Company received \$472,500 which was used for general working capital. The above securities were issued in reliance on the exemption from registration provided by Section 3(a)(9) of the Securities Act of 1933.

## **ITEM 3. DEFAULTS UPON SENIOR SECURITIES**

None.

## **ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS**

- (a) Our Annual Meeting was held on May 26, 2006.

- (b) Proxies for the Annual Meeting were solicited pursuant to Regulation 14A under the Securities Exchange Act of 1934. There was no solicitation in opposition to management's nominees as listed in the proxy statement and all of such nominees were elected.

- (i) The shareholders set the number of directors at seven with the following votes:

<u>Votes For</u>	<u>Votes Against</u>	<u>Votes Abstain</u>	<u>Broker Non-Votes</u>
6,675,528	35,758	13,239	0

- (ii) The shareholders approved an amendment to the Company's Bylaws that provides for the declassification of the Company's Board of Directors.

<u>Votes For</u>	<u>Votes Against</u>	<u>Votes Abstain</u>	<u>Broker Non-Votes</u>
6,616,732	80,673	27,120	0

- (iii) The shareholders approved an amendment to the Company's 1997 Stock Option Plan to increase the number of common stock shares reserved for issuance under the Plan to 2,700,000.

<u>Votes For</u>	<u>Votes Against</u>	<u>Votes Abstain</u>	<u>Broker Non-Votes</u>
6,101,694	594,634	28,197	0

- (iv) The shareholders approved the issuance of a total of 90,500 shares of restricted stock to the Company's officers, directors and employees.

<u>Votes For</u>	<u>Votes Against</u>	<u>Votes Abstain</u>	<u>Broker Non-Votes</u>
6,287,534	408,488	28,503	0

- (v) The following persons were elected to serve as Class I Directors on our Board until the next annual meeting of shareholders with the following votes:

<u>Nominees</u>	<u>Votes For</u>	<u>Votes Withheld</u>
Martin White	6,597,821	126,704
Lee D. Meyer	6,597,421	127,104
Jerry A. Dukes	6,582,290	142,235
Stephen Rathkopf	6,596,811	127,714
Thomas R. Hudson, Jr.	6,597,900	126,625
Zachary R. George	6,457,030	267,495
Todd Goodwin	6,596,731	127,794

- (vi) The shareholders ratified the appointment of Grant Thornton LLP as the Company's independent registered public accounting firm for the fiscal year ending December 31, 2006.

<u>Votes For</u>	<u>Votes Against</u>	<u>Votes Abstain</u>	<u>Broker Non-Votes</u>
6,708,493	3,507	12,525	0

## ITEM 5. OTHER INFORMATION

None.

## ITEM 6. EXHIBITS

**EXHIBIT INDEX TO FORM 10-Q**  
**For the Quarter Ended June 30, 2006**  
**PW EAGLE, INC.**

<u>Number</u>	<u>Description</u>
10.1	Agreement between the Company and Pirate Capital, LLC, Jolly Roger Fund, LP, Jolly Roger Offshore Fund Ltd. and Jolly Roger Activist Portfolio Company Ltd., dated April 21, 2006 (Incorporated by reference to the Company's Form 8-K filed April 26, 2006).
10.2	Agreement between the Company and Caxton International, Ltd. dated April 24, 2006 (Incorporated by reference to the Company's Form 8-K filed April 26, 2006).
10.3	Fifth Amended and Restated Loan and Security Agreement, dated April 27, 2006 between the Company, USPoly, LLC, and Bank of America, N.A. (Incorporated by reference to the Company's Form 8-K filed May 3, 2006).
10.4	Amendment to 1997 Stock Option Plan (Incorporated by reference to the Company's Form 8-K filed May 31, 2006).
10.5	PW Eagle Director Compensation Plan (Incorporated by reference to the Company's Form 8-K filed May 31, 2006).
31.1	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.*
31.2	Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.*
32.1	Certification by the Chief Executive Officer pursuant to section 906 of the Sarbanes-Oxley Act.*
32.2	Certification by the Chief Financial Officer pursuant to section 906 of the Sarbanes-Oxley Act.*

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\* Filed herewith.

**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 undersigned thereunto duly authorized.

**PW EAGLE, INC.**

By /s/ Jerry A. Dukes  
Jerry A. Dukes  
Chief Executive Officer

By /s/ Scott Long  
Scott Long  
Chief Financial Officer

Dated: August 14, 2006

## CERTIFICATION

I, Jerry A. Dukes, Chief Executive Officer of PW Eagle, Inc., certify that:

1. I have reviewed this report on Form 10-Q of PW Eagle, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and we have:
  - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - c) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting.
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Dated: August 14, 2006

Signature:

/s/ Jerry A. Dukes

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Jerry A. Dukes  
Chief Executive Officer

## CERTIFICATION

I, Scott Long, Chief Financial Officer of PW Eagle, Inc., certify that:

1. I have reviewed this report on Form 10-Q of PW Eagle, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and we have:
  - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - c) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting.
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Dated: August 14, 2006

Signature: /s/ Scott Long

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Scott Long  
Chief Financial Officer

CERTIFICATION PURSUANT TO  
18 U.S.C. SECTION 1350,  
AS ADOPTED PURSUANT TO  
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Quarterly Report of PW Eagle, Inc. (the "Company") on Form 10-Q for the quarter ended June 30, 2006 as filed with the Securities and Exchange Commission (the "Report"), I, Jerry A. Dukes, Chief Executive Officer, of the Company, certify, pursuant to 18 U.S.C. §1350, as adopted pursuant to §906 of the Sarbanes-Oxley Act of 2002, that:

- (1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Dated: August 14, 2006

/s/ Jerry A. Dukes

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Jerry A. Dukes  
Chief Executive Officer

**CERTIFICATION PURSUANT TO  
18 U.S.C. SECTION 1350,  
AS ADOPTED PURSUANT TO  
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report of PW Eagle, Inc. (the "Company") on Form 10-Q for the quarter ended June 30, 2006 as filed with the Securities and Exchange Commission (the "Report"), I, Scott Long, Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. §1350, as adopted pursuant to §906 of the Sarbanes-Oxley Act of 2002, that:

- (1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Dated: August 14, 2006

/s/ Scott Long

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Scott Long  
Chief Financial Officer