PROCTER & GAMBLE CO
Form 10-Q
November 02, 2005

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

FORM 10-Q

(Mark one)

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

For the Quarterly Period Ended September 30, 2005

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 1-434

THE PROCTER & GAMBLE COMPANY
(Exact name of registrant as specified in its charter)

Ohio	31-0411980
(State of incorporation)	(I.R.S. Employer Identification No.)

One Procter & Gamble Plaza, Cincinnati, Ohio	45202
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code (513) 983-1100

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

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act). Yes [X] No [ ]

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes [ ] No [X]

There were 2,377,658,052 shares of Common Stock outstanding as of September 30, 2005.

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

The Consolidated Statements of Earnings of The Procter & Gamble Company and subsidiaries (the "Company", "we" or "our") for the three months ended September 30, 2005 and 2004, the Consolidated Balance Sheets as of September 30, 2005 and June 30, 2005, and the Consolidated Statements of Cash Flows for the three

months ended September 30, 2005 and 2004 follow. In the opinion of management, these unaudited consolidated financial statements contain all adjustments necessary to present fairly the financial position, results of operations and cash flows for the interim periods reported. However, such financial statements may not be indicative necessarily of annual results.

THE PROCTER & GAMBLE COMPANY AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF EARNINGS

Amounts in millions except per share amounts

	Three Months Ended September 30	
	2005	2004
NET SALES	$ 14,793	$ 13,744
Cost of products sold	7,159	6,623
Selling, general and administrative expense	4,577	4,332
OPERATING INCOME	3,057	2,789
Interest expense	219	181
Other non-operating income, net	74	182
EARNINGS BEFORE INCOME TAXES	2,912	2,790
Income taxes	883	848
NET EARNINGS	$ 2,029	$ 1,942
PER COMMON SHARE:		
Basic net earnings	$ 0.82	$ 0.75
Diluted net earnings	$ 0.77	$ 0.70
Dividends	$ 0.28	$ 0.25
DILUTED WEIGHTED AVERAGE COMMON SHARES OUTSTANDING	2,649.7	2,766.1

See accompanying Notes to Consolidated Financial Statements

THE PROCTER & GAMBLE COMPANY AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS

Amounts in millions

ASSETS	September 30 2005	June 30 2005
CURRENT ASSETS		
Cash and cash equivalents	$ 6,310	$ 6,389
Investment securities	1,749	1,744
Accounts receivable	4,690	4,185
Inventories		
Materials and supplies	1,371	1,424
Work in process	384	350
Finished goods	3,406	3,232

Total inventories	5,161	5,006
Deferred income taxes	849	1,081
Prepaid expenses and other current assets	1,805	1,924
TOTAL CURRENT ASSETS	20,564	20,329
PROPERTY, PLANT AND EQUIPMENT		
Buildings	5,318	5,292
Machinery and equipment	20,631	20,397
Land	625	636
	26,574	26,325
Accumulated depreciation	(12,318)	(11,993)
NET PROPERTY, PLANT AND EQUIPMENT	14,256	14,332
GOODWILL AND OTHER INTANGIBLE ASSETS		
Goodwill	19,793	19,816
Trademarks and other intangible assets, net	4,435	4,347
NET GOODWILL AND OTHER INTANGIBLE ASSETS	24,228	24,163
OTHER NON-CURRENT ASSETS	2,858	2,703
TOTAL ASSETS	$ 61,906	$ 61,527
LIABILITIES AND SHAREHOLDERS' EQUITY		
CURRENT LIABILITIES		
Accounts payable	$ 3,423	$ 3,802
Accrued and other liabilities	6,247	7,531
Taxes payable	2,635	2,265
Debt due within one year	8,749	11,441
TOTAL CURRENT LIABILITIES	21,054	25,039
LONG-TERM DEBT	21,046	12,887
DEFERRED INCOME TAXES	2,007	1,896
OTHER NON-CURRENT LIABILITIES	3,266	3,230
TOTAL LIABILITIES	47,373	43,052
SHAREHOLDERS' EQUITY		
Preferred stock	1,477	1,483
Common stock - shares issued - Sept 30 2,976.6	2,977	
June 30 2,976.6		2,977
Additional paid-in capital	3,140	3,030
Reserve for ESOP debt retirement	(1,269)	(1,259)
Accumulated other comprehensive income	(1,485)	(1,566)
Treasury stock	(22,558)	(17,194)
Retained earnings	32,251	31,004
TOTAL SHAREHOLDERS' EQUITY	14,533	18,475
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	$ 61,906	$ 61,527

See accompanying Notes to Consolidated Financial Statements

THE PROCTER & GAMBLE COMPANY AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS

Amounts in millions	Three Months Ended September 30	
	2005	2004
CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD	$ 6,389	$ 4,232
OPERATING ACTIVITIES		
Net earnings	2,029	1,942
Depreciation and amortization	448	480
Share based compensation expense	95	122
Deferred income taxes	284	145
Changes in:		
Accounts receivable	(539)	(377)
Inventories	(149)	(326)
Accounts payable, accrued and other liabilities	(243)	57
Other operating assets & liabilities	175	(112)
Other	71	(19)
TOTAL OPERATING ACTIVITIES	2,171	1,912
INVESTING ACTIVITIES		
Capital expenditures	(401)	(413)
Proceeds from asset sales	26	366
Acquisitions	(1,178)	(335)
Change in investment securities	(17)	(216)
TOTAL INVESTING ACTIVITIES	(1,570)	(598)
FINANCING ACTIVITIES		
Dividends to shareholders	(727)	(685)
Change in short-term debt	(1,230)	(2,429)
Additions to long-term debt	8,612	2,996
Reductions of long-term debt	(1,858)	(130)
Impact of stock options and other	142	105
Treasury purchases	(5,555)	(622)
TOTAL FINANCING ACTIVITIES	(616)	(765)
EFFECT OF EXCHANGE RATE CHANGES ON CASH AND CASH EQUIVALENTS	(64)	59
CHANGE IN CASH AND CASH EQUIVALENTS	(79)	608
CASH AND CASH EQUIVALENTS, END OF PERIOD	$ 6,310	$ 4,840

See accompanying Notes to Consolidated Financial Statements

THE PROCTER & GAMBLE COMPANY AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. These statements should be read in conjunction with the Company's Annual Report on Form 10-K for the fiscal year ended June 30, 2005 and Form 8-Ks filed on September 23, 2005, and November 2, 2005 reflecting the Company's

historical results as conformed for the adoption of SFAS 123 (Revised 2004), "Share-Based Payment" (SFAS 123(R)) and the change in our method of accounting for Treasury Stock. The results of operations for the three-month period ended September 30, 2005 are not indicative necessarily of annual results.

2. Comprehensive Income - Total comprehensive income is composed primarily of net earnings, net currency translation gains and losses, impacts of net investment and cash flow hedges and net unrealized gains and losses on securities. Total comprehensive income for the three months ended September 30, 2005 and 2004 was $2,110 million and $2,159 million, respectively.

3. Segment Information - Following is a summary of segment results.

SEGMENT INFORMATION

Amounts in millions		Three Months Ended September 30		
		Net Sales	Earnings Before Income Taxes	Net Earnings
Beauty	2005	$ 4,989	$ 1,078	$ 783
	2004	4,655	983	674
Health Care	2005	2,083	501	336
	2004	1,844	360	245
Baby Care & Family Care	2005	2,999	510	320
	2004	2,850	501	309
Family Health	2005	5,082	1,011	656
	2004	4,694	861	554
Fabric Care & Home Care	2005	4,215	963	641
	2004	3,810	877	585
Snacks & Coffee	2005	706	108	73
	2004	740	120	78
Household Care	2005	4,921	1,071	714
	2004	4,550	997	663
Corporate	2005	(199)	(248)	(124)
	2004	(155)	(51)	51
Total	2005	$ 14,793	$ 2,912	$ 2,029
	2004	13,744	2,790	1,942

4. Goodwill and Other Intangible Assets - Goodwill as of September 30, 2005 is allocated by reportable segment and global business unit as follows (amounts in millions):

	Three Months Ended September 30, 2005
Total Beauty, beginning of year	$ 14,580
Acquistions & divestiture	(19)
Translation & other	8

Goodwill, September 30, 2005	14,569
Health Care, beginning of year	3,378
Acquistions & divestiture	--
Translation & other	(2)
Goodwill, September 30, 2005	3,376
Baby Care & Family Care, beginning of year	955
Acquistions & divestiture	(23)
Translation & other	12
Goodwill, September 30, 2005	944
Total Family Health, beginning of year	4,333
Acquistions & divestiture	(23)
Translation & other	10
Goodwill, September 30, 2005	4,320
Fabric Care & Home Care, beginning of year	644
Acquistions & divestiture	--
Translation & other	--
Goodwill, September 30, 2005	644
Snacks & Coffee, beginning of year	259
Acquistions & divestiture	--
Translation & other	1
Goodwill, September 30, 2005	260
Total Household Care, beginning of year	903
Acquistions & divestiture	--
Translation & other	1
Goodwill, September 30, 2005	904
Goodwill, Net, beginning of year	19,816
Acquistions & divestiture	(42)
Translation & other	19
Goodwill, September 30, 2005	$ 19,793

Identifiable intangible assets as of September 30, 2005 are comprised of (amounts in millions):

	Gross Carrying Amount	Accumulated Amortization
Amortizable intangible assets with determinable lives	$ 2,257	$ 755
Intangible assets with indefinite lives	2,933	-
Total identifiable intangible assets	$ 5,190	$ 755

Amortizable intangible assets consist principally of patents, technology and trademarks. The non-amortizable intangible assets consist primarily of certain trademarks.

The amortization of intangible assets for the three months ended September 30, 2005 was $49 million.

5. In December 2004, the Financial Accounting Standards Board (FASB) issued (SFAS 123(R)). This Statement revises SFAS No. 123 by eliminating the option to account for employee stock options under APB No. 25 and requires companies to recognize the cost of employee services received in exchange for awards of equity instruments based on the grant-date fair value of those awards (the "fair-value-based" method). We adopted SFAS 123(R) effective July 1, 2005 using the modified retrospective method. All prior periods were adjusted to give effect to the fair-value-based method of accounting for awards granted in fiscal years beginning on or after July 1,

1995. We provided revised Consolidated Financial Statements for the years ended June 30, 2005, 2004 and 2003 reflecting the adoption of SFAS 123(R) under the modified retrospective method in a Form 8-K dated November 2, 2005. The impact to the Company's net earnings of adopting SFAS 123(R) is consistent with the pro forma disclosures provided in previous financial statements. The impact of adopting SFAS 123(R) on Shareholders' Equity as of September 30, 2005, June 30, 2005 and June 30, 2004 is shown in Note 8.

For the three months ended September 30, 2005 and 2004, we recognized total share-based compensation of $95 million and $122 million, respectively, of which $73 million and $82 million relate to additional compensation recognized under SFAS 123(R) for stock options, and $22 million and $40 million relate to compensation for other share-based awards, primarily restricted stock and restricted stock units. These amounts are reflected in Cost of Products Sold and Selling, General and Administrative Expense and have been allocated to the reportable segments.

The fair value of each grant issued since January 1, 2005 was estimated using a binomial lattice-based model. The fair value of options granted prior to January 1, 2005 was estimated using the Black-Scholes option-pricing model. The utilization of the binomial lattice-based model did not have a significant impact on the valuation of stock options as compared to the Black-Scholes model. Assumptions utilized in the model are evaluated and revised, as necessary, to reflect market conditions and experience.

6. Postretirement Benefits - The Company offers various postretirement benefits to its employees. Additional information about these benefits is incorporated herein by reference to Note 8, Postretirement Benefits and Employee Stock Ownership Plan, which appears on page 54-58 of the Annual Report to Shareholders for the fiscal year ended June 30, 2005.

The components of net periodic benefit cost are as follows:

Amounts in millions	Pension Benefits		Other
	Three Months Ended September 30		Thr
	2005	2004	2005
Service Cost	$ 47	$ 38	$ 2
Interest Cost	61	58	3
Expected Return on Plan Assets	(47)	(43)	(9
Amortization of Prior Service Cost and Prior Transition Amount	2	1	(
Recognized Net Actuarial Loss	19	8	
Gross Benefit Cost	82	62	(3
Dividends on ESOP Preferred Stock	-	-	(1
Net Periodic Benefit Cost	$ 82	$ 62	$ (5

In 2005, the expected return on plan assets is 7.1% and 9.5% for defined benefit and other retiree benefit plans, respectively.

7. On October 1, 2005, we completed our acquisition of The Gillette Company. Pursuant to the acquisition agreement, we exchanged 0.975 shares of The Procter & Gamble Company common stock, on a tax-free basis, for each share of The Gillette Company. Under the purchase method of accounting, the total consideration was approximately $54 billion, determined using the average Company stock prices beginning two days before and ending two days after January 28, 2005, the date the acquisition was announced. The acquisition will be reflected in our consolidated financial statements beginning in the quarter ending December 31, 2005.

   The Gillette Company is a leader in several global product categories including blades and razors, oral care and batteries. Total sales for Gillette during its most recent year ended December 31, 2004 were $10.5 billion.

   In connection with this acquisition, we also announced a share buyback plan under which we will acquire $18 to $22 billion of Company common stock in the open market or from private transactions. Through September 30, 2005, we repurchased $8.6 billion under this plan. The repurchases were financed by borrowings under a $24 billion three-year credit facility with a syndicate of banks. The facility was entered into on July 27, 2005 and replaced a $3.4 billion bridge credit facility. Proceeds will be used for general corporate purposes with the expectation that the majority of the funds will be used as part of the share repurchase program. This facility is initially secured by a pledge of certain of the Company shares acquired under the share buyback plan. This credit facility carries a variable interest rate.

8. Change in Method of Accounting for Treasury Stock - On July 1, 2005, we elected to change our method of accounting for Treasury Stock. We previously accounted for share repurchases as if the Treasury Stock was constructively retired by reducing Common Stock and Retained Earnings within Shareholders' Equity. Reissuances of repurchased shares were accounted for by increasing Common Stock and Additional Paid-In Capital. Our new method of accounting will present Treasury Stock as a separate component of Shareholders' Equity. We believe that our new accounting method is preferable as it more closely depicts the underlying intent of the share repurchases in which the shares are not retired. In addition, we believe that our new presentation of Shareholders' Equity provides greater visibility of our share repurchase activity, including our share buyback plan announced in connection with the Gillette acquition.

   We adopted SFAS No. 154, "Accounting Changes and Error Corrections", on July 1, 2005. Accordingly, we reflected this new accounting method retrospectively by adjusting prior periods. This change is limited to reclassifications within Shareholders' Equity and has no effect on our net earnings, cash flows or total assets. The following tables summarize the changes within Shareholders' Equity as of September 30, 2005, June 30, 2005 and June 30, 2004 from the change in our method of accounting for Treasury Stock (the June 30, 2005 and 2004 tables also reflect changes to equity from the adoption of FAS 123(R)):

Amounts in millions As of September 30, 2005	As Computed Under Old Method	Effect of Treasury Stock Change	As Reported
Common Stock	$ 2,378	$ 599	$ 2,977
Preferred Stock	1,477	--	1,477
Additional Paid-In Capital	6,930	(3,790)	3,140
Reserve for ESOP Debt Retirement	(1,269)	--	(1,269)
Accumulated Other Comprehensive Income	(1,485)	--	(1,485)
Treasury Stock	--	(22,558)	(22,558)
Retained Earnings	6,502	25,749	32,251

Total Shareholders' Equity	$ 14,533	$ -	$ 14,533

Amounts in millions As of June 30, 2005	As Originally Reported	Effect of Treasury Stock Change	Effect of SFAS 123(R)	As
Common Stock	$ 2,473	$ 504	--	$
Preferred Stock	1,483	--	--	
Additional Paid-In Capital	3,142	(3,659)	3,547	
Reserve for ESOP Debt Retirement	(1,259)	--	--	
Accumulated Other Comprehensive Income	(1,566)	--	--	
Treasury Stock	--	(17,194)	--	
Retained Earnings	13,204	20,349	(2,549)	
Total Shareholders' Equity	$ 17,477	$ -	$ 998	$

Amounts in millions As of June 30, 2004	As Originally Reported	Effect of Treasury Stock Change	Effect of SFAS 123(R)	As
Common Stock	$ 2,544	$ 432	--	$
Preferred Stock	1,526	--	--	
Additional Paid-In Capital	2,425	(3,098)	3,127	
Reserve for ESOP Debt Retirement	(1,283)	--	--	
Accumulated Other Comprehensive Income	(1,545)	--	--	
Treasury Stock	--	(12,925)	--	
Retained Earnings	13,611	15,591	(2,215)	
Total Shareholders' Equity	$ 17,278	$ -	$ 912	$

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

Management's Discussion and Analysis of Financial Condition and Results of Operations (MD&A) is organized in the following sections:

Overview
Results of Operations - Three Months Ended September 30, 2005
Business Segment Discussion - Three Months Ended September 30, 2005
Financial Condition

Throughout MD&A, we refer to several measures used by management to evaluate performance including unit volume growth, net sales and after-tax profit. We also refer to organic sales growth (net sales excluding the impacts of acquisitions, divestitures and foreign exchange), free cash flow and free cash flow productivity, which are not defined under accounting principles generally accepted in the United States of America (U.S. GAAP). The explanation

of these measures at the end of MD&A provides more details.

Effective July 1, 2005, Procter & Gamble adopted SFAS 123 (R) which requires that all stock-based compensation, including grants of employee stock options, be accounted for using a fair value-based method. We have elected to adopt SFAS 123 (R) using the modified retrospective method. As a result, we have revised our historical results to include the effect of stock-based compensation. Therefore, all financial data provided in this Form 10-Q filing, including prior year data, have been revised to include the impact of stock option compensation expense.

OVERVIEW

Our business is focused on providing branded products of superior quality and value to improve the lives of the world's consumers. We believe this will lead to leadership sales, profits and value creation, allowing employees, shareholders and the communities in which we operate to prosper.

On October 1, 2005, we completed the acquisition of The Gillette Company ("Gillette"), a leading consumer products company that had $10.5 billion of sales in its most recent year ended December 31, 2004. The results of Gillette will be included in our results starting with the quarter ending on December 31, 2005; accordingly, results for the three months ended September 30, 2005 do not include any results related to Gillette.

Procter & Gamble markets approximately 300 consumer products in more than 160 countries. Our products are sold primarily through mass merchandisers, grocery stores, membership club stores and drug stores. We compete in multiple product categories and have three global business units: P&G Beauty, P&G Family Health and P&G Household Care. Under U.S. Generally Accepted Accounting Principles, we have five reportable segments: Beauty, Health Care, Baby Care & Family Care, Fabric Care & Home Care, and Snacks & Coffee. We have operations in over 80 countries through our Market Development Organization, which leads country business teams to build our brands in local markets and is organized along seven geographic areas: North America, Western Europe, Northeast Asia, Latin America, Central and Eastern Europe/Middle East/Africa, Greater China and ASEAN/Australasia/India.

The following table provides the percentage of net sales and net earnings by reportable business segment and global business unit for the three months ended September 30, 2005 (excludes net sales and net earnings in Corporate):

	NET SALES	NET EARNINGS
BEAUTY	33%	36%
FAMILY HEALTH:	34%	31%
Health Care	14%	16%
Baby Care and Family Care	20%	15%
HOUSEHOLD CARE:	33%	33%
Fabric Care and Home Care	28%	30%
Snacks and Coffee	5%	3%
TOTAL	100%	100%

SUMMARY OF RESULTS. The following are highlights of the results for the quarter ended September 30, 2005.

- Net sales increased eight percent and unit volume increased six percent. Growth was broad-based with all regions growing volume and sales during the period.

- Operating earnings increased 10 percent. Volume growth, pricing, and scale leverage on overhead expenses were partially offset by higher

commodity costs and the impact of Hurricane Katrina.

- Net earnings grew four percent. Net earnings growth trailed operating earnings growth as a result of the prior year impact of the sale of the juice business and higher interest expenses associated with the previously announced $18 to $22 billion share repurchase program related to the Gillette acquisition.

- Diluted net earnings per share were $0.77, an increase of 10%, in-line with operating earnings growth.

- Operating cash flow increased by 14 percent versus the comparable prior year period. Free cash productivity was 87%, ahead of the prior year period free cash productivity of 77%.

FORWARD LOOKING STATEMENTS. The markets in which the Company sells its products are highly competitive and comprised of both global and local competitors. Going forward, business and market uncertainties may affect results. Among the key factors that could impact results and must be managed by the Company are:

(1) the ability to achieve business plans, including with respect to lower income consumers and growing existing sales and volume profitably despite high levels of competitive activity, especially with respect to the product categories and geographical markets (including developing markets) in which the Company has chosen to focus;

(2) the ability to successfully execute, manage and integrate key acquisitions and mergers, including (i) the Domination and Profit Transfer Agreement with Wella, and (ii) the Company's merger with The Gillette Company, and to achieve the cost and growth synergies in accordance with the stated goals of the Gillette transaction;

(3) the ability to manage and maintain key customer relationships;

(4) the ability to maintain key manufacturing and supply sources (including sole supplier and plant manufacturing sources);

(5) the ability to successfully manage regulatory, tax and legal matters (including product liability, patent, and other intellectual property matters), and to resolve pending matters within current estimates;

(6) the ability to successfully implement, achieve and sustain cost improvement plans in manufacturing and overhead areas, including the Company's outsourcing projects;

(7) the ability to successfully manage currency (including currency issues in volatile countries), debt (including debt related to the Company's announced plan to repurchase shares of the Company's stock), interest rate and certain commodity cost exposures;

(8) the ability to manage the continued global political and/or economic uncertainty and disruptions, especially in the Company's significant geographical markets, as well as any political and/or economic uncertainty and disruptions due to terrorist activities;

(9) the ability to successfully manage competitive factors, including prices, promotional incentives and trade terms for products;

(10) the ability to obtain patents and respond to technological advances attained by competitors and patents granted to competitors;

(11) the ability to successfully manage increases in the prices of raw materials used to make the Company's products;

(12) the ability to stay close to consumers in an era of increased media fragmentation; and

(13) the ability to stay on the leading edge of innovation.

If the Company's assumptions and estimates are incorrect or do not come to fruition, or if the Company does not achieve all of these key factors, then the Company's actual results could vary materially from the forward-looking statements made herein, as that term is defined in the Private Securities Litigation Reform Act of 1995.

RESULTS OF OPERATIONS - THREE MONTHS ENDED SEPTEMBER 30, 2005

The following discussion provides a review of results for the three months ended September 30, 2005 versus the three months ended September 30, 2004.

THE PROCTER & GAMBLE COMPANY AND SUBSIDIARIES
(Amounts in Millions Except Per Share Amounts)
Consolidated Earnings Information

	Three Months Ended September 30		
	2005	2004	% CHG
NET SALES	$ 14,793	$ 13,744	8 %
COST OF PRODUCTS SOLD	7,159	6,623	8 %
GROSS MARGIN	7,634	7,121	7 %
SELLING, GENERAL & ADMINISTRATIVE EXPENSE	4,577	4,332	6 %
OPERATING INCOME	3,057	2,789	10 %
TOTAL INTEREST EXPENSE	219	181	
OTHER NON-OPERATING INCOME, NET	74	182	
EARNINGS BEFORE INCOME TAXES	2,912	2,790	4 %
INCOME TAXES	883	848	
NET EARNINGS	$ 2,029	$ 1,942	4 %
EFFECTIVE TAX RATE	30.3 %	30.4 %	
PER COMMON SHARE:			
BASIC NET EARNINGS	$ 0.82	$ 0.75	9 %
DILUTED NET EARNINGS	$ 0.77	$ 0.70	10 %
DIVIDENDS	$ 0.28	$ 0.25	
AVERAGE DILUTED SHARES OUTSTANDING	2,649.7	2,766.1	
COMPARISONS AS A % OF NET SALES			
GROSS MARGIN	51.6 %	51.8 %	(20)
SELLING, GENERAL & ADMINISTRATIVE EXPENSE	30.9 %	31.5 %	(60)
OPERATING MARGIN	20.7 %	20.3 %	40
EARNINGS BEFORE INCOME TAXES	19.7 %	20.3 %	(60)
NET EARNINGS	13.7 %	14.1 %	(40)

Unit volume for the July - September quarter grew six percent. Each of the Company's geographic regions grew volume during the period, led by developing markets with growth in the mid-teens. Beauty, family health, and household care each delivered volume growth of six percent or greater. This growth reflects progress on key brands and countries with all of the Company's top 10 brands and countries growing versus the prior year period. Growth came largely behind new product innovations across P&G's portfolio of brands such as Tide Coldwater, Tide with Febreze, Dawn Bleach Alternative, Naturella expansion in Central and

Eastern Europe, Pampers Feel and Learn, and Charmin Mega-Roll. Organic volume, which excludes the impacts of acquisitions and divestitures - primarily the divestiture of the juice business during the prior year period - increased seven percent.

Net sales for the quarter increased eight percent to $14.79 billion. Pricing contributed one percent to sales growth behind actions taken in various businesses and geographies that partially recovered the impact of higher commodity costs. Favorable foreign exchange rates also contributed one percent of sales growth. Organic sales, which exclude the impacts of acquisitions, divestitures, and foreign exchange, also increased eight percent.

	Volume						
	With Acquisitions & Divestitures	Without Acquisitions & Divestitures	FX	Price	Mix/ Other	Total Impact	T I E
BEAUTY	7%	7%	1%	0%	-1%	7%	
FAMILY HEALTH							
HEALTH CARE	11%	11%	1%	1%	0%	13%	
BABY CARE AND FAMILY CARE	5%	6%	1%	1%	-2%	5%	
HOUSEHOLD CARE							
FABRIC CARE AND HOME CARE	8%	8%	1%	2%	0%	11%	
SNACKS AND COFFEE	-7%	-7%	0%	5%	-3%	-5%	
TOTAL COMPANY	6%	7%	1%	1%	0%	8%	

NOTE: Sales percentage changes are approximations based on quantitative formulas that are consis

Gross margin decreased 20 basis points versus the prior year. Higher commodity costs reduced gross margins by over 100 basis points. Fixed cost leverage from volume growth, cost savings efforts and pricing did not fully offset the commodity cost impact.

Selling, general, and administrative expenses (SG&A) increased six percent for the quarter, but decreased as a percentage of net sales by 60 basis points. This was primarily due to sales growth that outpaced the increase in SG&A spending. The increase in spending was due primarily to higher marketing support spending and higher overhead expenses, although both decreased as a percentage of sales. Beauty increased marketing spending to support new product launches and initiatives such as Lacoste Essentials, Always Cottony Soft, Naturella expansion in Central and Eastern Europe, Pantene Color Expressions, and Olay Quench Hand & Body Lotion. Baby care increased marketing spending primarily in North America behind direct-to-consumer marketing investments.

Operating earnings increased 10 percent for the quarter to $3.06 billion. Operating earnings growth was due primarily to strong top-line growth, pricing, and scale leverage on overhead expenses. These benefits were partially offset by higher commodity prices and costs associated with Hurricane Katrina. Hurricane Katrina had a negative impact of approximately two percent on the Company's operating earnings growth due primarily to the disruption of the coffee business, write-offs of damaged inventory and physical assets, and clean-up and repair costs.

Net earnings increased four percent to $2.03 billion in the current period. Net earnings growth trailed operating earnings growth primarily due to the prior year impact of the sale of the juice business and higher interest expenses in

the current period. Interest expenses for the quarter increased $38 million versus the prior year period driven by the financing cost of the previously announced $18 to $22 billion share repurchase program associated with the Gillette acquisition. The Company repurchased $5.55 billion of P&G stock during the quarter under the share repurchase program, bringing cumulative repurchases under the program to $8.57 billion since January 2005. Interest expenses were partially offset by favorable currency mix on our total debt.

Diluted net earnings per share were $0.77, an increase of 10%, in-line with operating earnings growth. The impact of accelerated share repurchases, net of associated interest and Gillette acquisition expenses was neutral on earnings per share for the quarter.

BUSINESS SEGMENT DISCUSSION

The following discussion provides a review of results by business segment. An analysis of the results for the three months ended September 30, 2005 are compared to the same period ended September 30, 2004.

The table below provides supplemental information on net earnings by business segment for the three months ended September 30, 2005 versus the comparable prior year period:

	Three Months Ended September 30,			
	Net Sales	% Change Versus Year Ago	Earnings Before Income Taxes	% Change Versus Year Ago
BEAUTY	$ 4,989	7%	$ 1,078	10%
FAMILY HEALTH				
HEALTH CARE	2,083	13%	501	39%
BABY CARE AND FAMILY CARE	2,999	5%	510	2%
HOUSEHOLD CARE				
FABRIC CARE AND HOME CARE	4,215	11%	963	10%
SNACKS AND COFFEE	706	-5%	108	-10%
TOTAL BUSINESS SEGMENT	14,992	8%	3,160	11%
CORPORATE	(199)	n/a	(248)	n/a
TOTAL COMPANY	14,793	8%	2,912	4%

BEAUTY

Beauty unit volume increased seven percent, led by growth in developing markets. Growth was broad-based across hair care, skin care, and feminine care. The hair care business was led by double-digit volume growth in developing markets and globally on Pantene, Head & Shoulders and Rejoice. North America hair care volume declined versus the prior year period primarily due to the discontinuation of several minor brands. However, market share in US hair care was flat overall and up on Pantene, Herbal Essences, and Aussie. Skin care volume grew in upper single-digits led by double-digit growth on the Olay brand. Feminine care delivered volume growth in the upper single-digits behind double-digit growth on Always and Naturella. Net sales in beauty increased seven percent to $4.99 billion. Foreign exchange added one percent of sales growth. Mix reduced sales by one percent as a result of faster growth in developing

markets, where unit sales price is generally lower than the global business unit average. Net earnings increased 16 percent to $783 million. Earnings growth was driven by top-line growth, scale benefits, and savings from the Wella integration. These were partially offset with increased marketing spending behind new product launches such as Lacoste Essentials, Always Cottony Soft, Naturella expansion in Central and Eastern Europe, Pantene Color Expressions and Olay Quench Hand & Body lotion.

FAMILY HEALTH

Health care delivered double-digit volume, sales and earnings growth. Unit volume increased 11 percent behind double-digit growth in pharmaceuticals & personal health, and high single-digit growth in oral care. Pharmaceuticals & personal health grew primarily behind double-digit volume increase on Actonel and Prilosec OTC. Prilosec OTC volume more than doubled versus the prior year level, largely driven by accelerated sales ahead of a mid-September price increase as well as share growth versus the prior year. Given this advanced shipping effect, we expect shipment growth in the quarter ending December 31, 2005 to moderate versus shipment levels in the current quarter ended September 30, 2005. In addition, Prilosec OTC volume was suppressed in the base period by shipment allocation. Oral care volume grew in high single-digits led by double-digit growth in developing markets. Health care net sales increased 13 percent to $2.08 billion. Pricing actions in the prior fiscal year on pharmaceuticals & personal health and pet health & nutrition added one percent to sales growth. Foreign exchange also contributed one point of sales growth. Net earnings increased 37 percent to $336 million. The net earnings increase resulted from volume growth, product mix benefits, and a favorable base period comparison.

Baby care and family care unit volume increased five percent with balanced growth in both businesses. Volume growth was driven behind initiatives such as Pampers Feel and Learn and Charmin Mega-Roll. Net sales increased five percent to $3.00 billion including a positive foreign exchange impact of one percent. Pricing added one percent to sales growth behind the carryover impact of prior fiscal year increases in family care. Additionally, recent price increases in North America baby care more than offset competitive merchandising spending in Western Europe baby care. Mix reduced sales by two percent primarily due to growth in mid-tier products such as Bounty Basic and in developing markets, where unit sales price is generally lower than the global business unit average. Earnings increased four percent to $320 million driven primarily by volume growth. The benefits of cost savings efforts and pricing were largely offset by higher pulp and natural gas prices and increases in direct-to-consumer marketing investments in baby care.

HOUSEHOLD CARE

Fabric care and home care volume increased eight percent behind growth on Tide, Ariel, Downy, and Dawn. Growth was driven by new initiatives that began shipping this quarter, such as Tide with Febreze and Dawn Direct Foam, as well as the incremental benefit of prior year initiatives such as Tide Coldwater, Tide with a Touch of Downy, Ariel Ion Power Gel, Dawn Bleach Alternative, and Downy Simple Pleasures. Net sales increased 11 percent to $4.21 billion including a one percent increase from foreign exchange rates. The benefit of prior price increases, primarily in North America and Latin America, helped to offset higher commodity costs and increased sales by two percent. Net earnings increased 10 percent to $641 million behind the impacts of volume growth, pricing, ongoing savings programs, and foreign exchange gains from developing market currencies. These benefits were partially offset by rising commodity prices.

Snacks and coffee results were impacted by Hurricane Katrina. The business experienced business disruption and damages to our manufacturing facilities in New Orleans. Unit volume declined seven percent primarily due to reduced coffee shipments in September. Net sales declined by five percent to $706 million. Coffee price increases taken last fiscal year in response to higher bean costs

added five percent to sales growth. Mix effects reduced sales by three percent. Net earnings were $73 million, down six percent driven primarily by the business disruption and other damages associated with Hurricane Katrina.

CORPORATE

Corporate includes certain operating and non-operating activities not allocated to specific business units. These include incidental businesses managed at the corporate level, financing and investing activities, certain restructuring charges and other general corporate items. Eliminations to adjust management reporting principles to United States Generally Accepted Accounting Principles (U.S. GAAP) are held in Corporate. In addition, Corporate includes the historical results of divested businesses, including the juice business, which was divested in August of 2004.

For the quarter, net sales were impacted by the divestiture of the juice business, which recorded roughly one month of sales in the corporate segment during the base period. Net earnings in corporate were reduced primarily as a result of the base period gain on the sale of the juice business of $79 million and increased interest expenses. The increase in interest expenses was driven by the financing cost of the share repurchase program related to Gillette partially offset by favorable currency mix on our debt.

FINANCIAL CONDITION

OPERATING ACTIVITIES

Cash generated from operating activities for the three months ended September 30, 2005 was $2.17 billion compared to $1.91 billion in the prior year period, an increase of 14%. The increase in cash from operating activities was driven by earnings growth adjusted for non-cash items (depreciation, amortization, stock based compensation and deferred income taxes). Deferred income tax expense increased $139 million driven primarily by the settlement of deferred tax liabilities on foreign exchange movements related to bonds which matured during the quarter. These were partially offset by a net increase in working capital due primarily to business growth.

INVESTING ACTIVITIES

Investing activities in the current year used $1.57 billion compared to $598 million in the prior year. The increase was driven primarily by the settlement of a major portion of the Wella domination liability, which increased our total ownership in Wella to over 95%. Capital expenditures were $401 million, or three percent of net sales. Proceeds from asset sales decreased by $340 million due to the sale of the juice business, which was sold during the base period.

FINANCING ACTIVITIES

Financing activities used net cash of $616 million in the current year compared to a use of cash of $765 million in the base period. During the quarter, the Company repurchased $5.55 billion of P&G stock as part of the repurchase program associated with the Gillette acquisition. This brings cumulative share repurchases under the plan to $8.57 billion. The cash used for the repurchase program was funded by debt, which had a net increase of $5.52 billion in the quarter.

NON-GAAP MEASURES

Our discussion of financial results includes several measures not defined by U.S. GAAP. We believe these measures provide our investors with additional information about the underlying results and trends of the Company, as well as insight to some of the metrics used to evaluate management. When used in the MD&A, we have provided the comparable GAAP measure in the discussion.

ORGANIC SALES GROWTH. Organic sales growth is a non-GAAP measure of sales growth excluding the impacts of acquisitions, divestitures and foreign exchange from year-over-year comparisons. We believe this provides investors with a more complete understanding of underlying sales trends by providing sales growth on a consistent basis. The reconciliation of reported sales growth to organic sales growth:

Total Sales Growth	8%
Less: Foreign Exchange Impact	1%
Less: Acquisition/Divestiture Impact	-1%
Organic Sales Growth	8%

OTHER MEASURES

FREE CASH FLOW. Free cash flow is defined as operating cash flow less capital spending. We view free cash flow as an important measure because it is one factor in determining the amount of cash available for dividends and discretionary investment. Free cash flow is also one of the measures used to evaluate senior management and is a factor in determining their at-risk compensation.

FREE CASH FLOW PRODUCTIVITY. Free cash flow productivity is defined as the ratio of free cash flow to net earnings. The Company's long-term target is to generate free cash at or above 90 percent of net earnings. Free cash flow is also one of the measures used to evaluate senior management.

The reconciliation of free cash flow and free cash flow productivity is provided below:

($MM)	Operating Cash Flow	Capital Spending	Free Cash Flow	Net Earnings	Free Cash Flow Productivity
Jul-Sep'04	1,912	413	1,499	1,942	77%
Jul-Sep'05	2,171	401	1,770	2,029	87%

Item 3. Quantitative and Qualitative Disclosures about Market Risk

There have been no material changes in the Company's exposure to market risk since June 30, 2005. See Item 7A in the Company's Annual Report on Form 10-K for the year ended June 30, 2005.

Item 4. Controls and Procedures

The Company's Chairman of the Board, President and Chief Executive, A.G. Lafley, and the Company's Chief Financial Officer, Clayton C. Daley, Jr., have evaluated the Company's internal controls and disclosure controls systems as of the end of the period covered by this report.

Messrs. Lafley and Daley have concluded that the Company's disclosure controls systems are functioning effectively to provide reasonable assurance that the Company can meet its disclosure obligations. The Company's disclosure controls system is based upon a global chain of financial, staff and general business reporting lines that converge in the world-wide headquarters of the Company in Cincinnati, Ohio. The reporting process is designed to ensure that information required to be disclosed by the Company in the reports that it files or submits

with the Commission is recorded, processed, summarized and reported within the time periods specified in the Commission's rules and forms. Consistent with the SEC's suggestion, the Company has a Disclosure Committee consisting of key Company personnel designed to review the accuracy and completeness of all disclosures made by the Company.

In connection with the evaluation described above, no changes in the Company's internal control over financial reporting occurred during the Company's first fiscal quarter that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

In October 2005, The Procter & Gamble Paper Products Company, a subsidiary of the Company, received an offer of settlement from the Ventura County Air Pollution Control District to settle alleged non-compliance with air rules standards concerning the subsidiary's Oxnard, California plant. As a result of this offer, the Company anticipates negotiating a settlement to resolve these issues. No judicial proceeding is pending. The Company's liability is estimated not to exceed $406,000.

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

ISSUER PURCHASES OF EQUITY SECURITIES

Period	Total Number of Shares Purchased(1)	Average Price Paid per Share(2)	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs(3)	Approximate value of shar may yet be pu under our sh repurchase p ($ in Billio
7/1/05-7/31/05	16,266,380	$54.90	12,552,408	18.3
8/1/05-8/31/05	44,075,287	$54.56	44,039,700	15.9
9/1/05-9/30/05	43,851,798	$56.06	43,850,200	13.4

(1) All share repurchases were made in open-market transactions. The number of shares purchased other than through a publicly announced repurchase plan were 3,751,157 for the quarter, including those purchased by P&G's Profit Sharing Trust. This table excludes shares withheld from employees to satisfy minimum tax withholding requirements on option exercises and other equity-based transactions. The Company administers employee cashless exercises through an independent, third party broker and does not repurchase stock in connection with cashless exercises.

(2) Average price paid per share is calculated on a settlement basis and excludes commission.

(3) On January 28, 2005 the Company announced a share buyback plan in connection with its planned acquisition of The Gillette Company. Pursuant to the plan, the Board of Directors authorized the Company and its subsidiaries to acquire in open market and/or private transactions $18 to $22 billion of shares of Company common stock to be financed by issuing a combination of long-term and short-term debt. The share repurchases are expected to be largely completed by June 30, 2006.

Item 4. Submission of Matters to a Vote of Security Holders:

At the Company's 2005 Annual Meeting of Shareholders held on October 11, 2005, the following actions were taken:

The following Directors were elected for terms of office expiring in 2008:

	Votes For	Votes Withheld	Abstentions*	Broker Non-Votes*
BRUCE L. BYRNES	2,299,014,851	39,766,334	N/A	N/A
SCOTT D. COOK	2,307,794,743	30,986,442	N/A	N/A
CHARLES R. LEE	2,280,419,589	58,361,596	N/A	N/A
W. JAMES MCNERNEY, JR.	2,305,731,180	33,050,005	N/A	N/A
ERNESTO ZEDILLO	2,306,443,283	32,337,902	N/A	N/A

* Pursuant to the terms of the Notice of Annual Meeting and Proxy Statements, proxies received were voted, unless authority was withheld, in favor of the election of the five nominees named.

In addition, the following Directors continued to serve as Directors after the meeting:

Norman R. Augustine
R. Kerry Clark
Joseph T. Gorman
A. G. Lafley
Lynn M. Martin
Johnathan A. Rodgers
John F. Smith, Jr.
Ralph Snyderman
Robert D. Storey
Margaret C. Whitman

A proposal by the Board of Directors to ratify the appointment of Deloitte & Touche LLP as the Company's independent registered public accounting firm to conduct the annual audit of the financial statements of the Company and its subsidiaries for the fiscal year ending June 30, 2006, was approved by the shareholders. The shareholders cast 2,275,288,282 votes in favor of this proposal and 42,037,800 votes against. There were 21,455,103 abstentions.

A proposal by the Board of Directors to approve an amendment to the Amended Articles of Incorporation and Code of Regulations to eliminate the Executive Committee of the Board was approved by the shareholders. The shareholders cast 2,299,147,779 votes in favor of this proposal and 12,874,560 votes against. There were 26,758,846 abstentions.

A proposal by the Board of Directors to approve an amendment to the Code of Regulations to provide for the annual election of Directors was approved by the shareholders. The shareholders cast 2,277,105,529 votes in favor of this proposal and 37,632,055 votes against. There were 24,043,601 abstentions.

A shareholder resolution proposed by the People for the Ethical Treatment of Animals was defeated by the shareholders. The proposal requested that the Board report to shareholders on the Company's success and failure in achieving the objectives detailed in the Iams Company's Research Policy. The Board opposed the resolution. The shareholders cast 113,983,232 votes in favor of the resolution and 1,573,383,713 against. There were 182,422,692 abstentions and 468,991,548 broker non-votes.

A shareholder resolution proposed by Mark Klein, M.D. was defeated by the shareholders. The proposal requested that the Company hire an investment bank to explore the sale of the Company. The Board opposed the resolution. The shareholders cast 33,665,692 votes in favor of the resolution and 1,799,274,270 against. There were 36,858,496 abstentions and 468,982,727 broker non-votes.

A shareholder resolution proposed by the Laborers' Local Union and District Counsil Pension Fund was defeated by the shareholders. The proposal requested that the Company provide a report disclosing the Company's political contributions. The Board opposed the resolution. The shareholders cast 154,505,994 votes in favor of the resolution and 1,540,395,250 against. There were 174,878,842 abstentions and 469,001,099 broker non-votes.

Although these actions occurred following the first quarter, the Company is voluntarily including this information here.

Item 6. Exhibits

Exhibits

(3-1) Amended Articles of Incorporation.

(3-2) Regulations.

(11) Computation of Earnings per Share.

(12) Computation of Ratio of Earnings to Fixed Charges.

(18) Deloitte & Touche Preferability Letter.

(31) Rule 13a-14(a)/15d-14(a) Certifications.

(32) Section 1350 Certifications.

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.

THE PROCTER & GAMBLE COMPANY

/S/VALARIE L. SHEPPARD

(Valarie L. Sheppard)
Vice President and Comptroller

November 2, 2005

Date

EXHIBIT INDEX

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