

SYNALLOY CORP
Form 10-Q
April 30, 2019

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

Form 10-Q

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

For the Quarterly Period Ended March 31, 2019

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 0-19687

Synalloy Corporation

(Exact name of registrant as specified in its charter)

Delaware

(State or other jurisdiction of incorporation or organization)

57-0426694

(I.R.S. Employer Identification No.)

4510 Cox Road, Suite 201, Richmond, Virginia

(Address of principal executive offices)

23060

(Zip Code)

(804) 822-3260

(Registrant's telephone number, including area code)

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

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit such files).

Yes x No "

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, smaller reporting company or emerging growth company. See definitions of "large accelerated filer," "accelerated filer," "smaller reporting company" and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated Filer " Accelerated filer x Non-accelerated filer "

Smaller reporting company x Emerging growth company "

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. Yes " No "

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

The number of shares outstanding of the registrant's common stock as of April 26, 2019 was 8,964,874.

Synalloy Corporation
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Part I - Financial Information

Item 1. Financial Statements

Synalloy Corporation

Condensed Consolidated Balance Sheets

| | March 31, 2019 (unaudited) | December 31, 2018 |
|-----------------------------------------------------------------------------------------------------------------|----------------------------------|----------------------|
| Assets | | |
| Current assets | | |
| Cash and cash equivalents | \$604,586 | \$2,220,272 |
| Accounts receivable, less allowance for doubtful accounts of \$211,125 and \$169,107, respectively | 46,858,362 | 41,065,251 |
| Inventories, net | 114,157,942 | 114,201,386 |
| Prepaid expenses and other current assets | 10,341,214 | 9,983,416 |
| Total current assets | 171,962,104 | 167,470,325 |
| Non-current assets | | |
| Property, plant and equipment, net of accumulated depreciation of \$59,177,813 and \$57,288,233 respectively | 42,792,288 | 40,924,455 |
| Right-of-use assets, operating leases, net of accumulated amortization | 36,759,065 | — |
| Goodwill | 16,843,526 | 9,799,992 |
| Intangible assets, net of accumulated amortization of \$13,849,639 and \$12,925,888 respectively | 18,772,361 | 9,696,112 |
| Deferred charges, net | 467,999 | 507,962 |
| Total assets | \$287,597,343 | \$228,398,846 |
| Liabilities and Shareholders' Equity | | |
| Current liabilities | | |
| Accounts payable | \$30,439,659 | \$25,073,698 |
| Accrued expenses and other current liabilities | 11,283,494 | 12,163,686 |
| Current portion of long-term debt | 4,000,000 | — |
| Current portion of operating lease liabilities | 3,473,925 | — |
| Current portion of finance lease liabilities | 235,685 | — |
| Total current liabilities | 49,432,763 | 37,237,384 |
| Long-term debt | 87,481,287 | 76,405,458 |
| Deferred income taxes | 1,508,084 | 252,988 |
| Long-term deferred gain, sale-leaseback | — | 5,599,077 |
| Long-term portion of earn-out liability | 7,408,647 | 4,702,562 |
| Long-term portion of operating lease liabilities | 34,366,152 | — |
| Long-term portion of finance lease liabilities | 539,073 | — |
| Other long-term liabilities | 65,535 | 1,717,291 |
| Total non-current liabilities | 131,368,778 | 88,677,376 |
| Commitments and contingencies – See Note 11 | | |
| Shareholders' equity | | |
| Common stock, par value \$1 per share; authorized 24,000,000 shares; issued 10,300,000 shares | 10,300,000 | 10,300,000 |
| Capital in excess of par value | 36,304,159 | 36,520,840 |
| Retained earnings | 72,661,388 | 68,965,410 |
| | 119,265,547 | 115,786,250 |

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| | | |
|-------------------------------------------------------------------------------------|---------------|---------------|
| Less cost of common stock in treasury: 1,335,125 and 1,424,279 shares, respectively | 12,469,745 | 13,302,164 |
| Total shareholders' equity | 106,795,802 | 102,484,086 |
| Total liabilities and shareholders' equity | \$287,597,343 | \$228,398,846 |

Note: The condensed consolidated balance sheet at December 31, 2018 has been derived from the audited consolidated financial

statements at that date. See accompanying notes to condensed consolidated financial statements.

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Synalloy Corporation
Condensed Consolidated Statements of Operations (Unaudited)

| | Three Months Ended | |
|-----------------------------------------------|--------------------|--------------|
| | March 31 | |
| | 2019 | 2018 |
| Net sales | \$84,803,832 | \$58,480,602 |
| Cost of sales | 76,120,178 | 47,247,183 |
| Gross profit | 8,683,654 | 11,233,419 |
| Selling, general and administrative expense | 8,895,128 | 5,856,120 |
| Acquisition related costs | 327,947 | — |
| Earn-out adjustments | 16,523 | 154,060 |
| Operating (loss) income | (555,944) | 5,223,239 |
| Other expense (income) | | |
| Interest expense | 1,023,941 | 313,984 |
| Change in fair value of interest rate swaps | 47,561 | (73,204) |
| Other, net | (294,667) | 88,296 |
| (Loss) income before income taxes | (1,332,779) | 4,894,163 |
| Income tax (benefit) provision | (406,257) | 1,059,000 |
| Net (loss) income | \$(926,522) | \$3,835,163 |
| Net (loss) income per common share: | | |
| Basic | \$(0.10) | \$0.44 |
| Diluted | \$(0.10) | \$0.44 |
| Weighted average shares outstanding: | | |
| Basic | 8,926,652 | 8,745,958 |
| Dilutive effect from stock options and grants | — | 60,131 |
| Diluted | 8,926,652 | 8,806,089 |

See accompanying notes to condensed consolidated financial statements

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Synalloy Corporation
Condensed Consolidated Statements of Cash Flows (Unaudited)

| | Three Months Ended March 31 | |
|----------------------------------------------------------------------------------------------------|--------------------------------|--------------|
| | 2019 | 2018 |
| Operating activities | | |
| Net (loss) income | \$(926,522) | \$3,835,163 |
| Adjustments to reconcile net (loss) income to net cash provided by (used in) operating activities: | | |
| Depreciation expense | 1,889,580 | 1,417,675 |
| Amortization expense | 923,752 | 576,723 |
| Amortization of debt issuance costs | 39,963 | 22,746 |
| Deferred income taxes | (55,755) | 158,720 |
| Earn-out adjustments | 16,523 | 154,060 |
| Payments of MUSA-Stainless earn-out liability in excess of acquisition date fair value | (370,289) | — |
| Provision for (reduction of) losses on accounts receivable | 134,193 | (14,105) |
| Provision for losses on inventories | 417,892 | 384,641 |
| Gain on disposal of property, plant and equipment | — | (14,462) |
| Amortization of deferred gain on sale-leaseback | — | (83,569) |
| Straight line lease cost | 137,079 | 93,043 |
| Change in fair value of interest rate swaps | 47,561 | (73,204) |
| Unrealized loss on equity securities | 53,125 | 88,296 |
| Realized gain on sale of equity securities | (325,811) | — |
| Employee stock option and grant compensation | 615,739 | 192,201 |
| Changes in operating assets and liabilities: | | |
| Accounts receivable | (2,393,383) | (6,069,663) |
| Inventories | 5,189,552 | (11,108,262) |
| Accounts payable | 3,965,952 | 5,160,092 |
| Accrued expenses | (3,540,419) | (996,420) |
| Accrued income taxes | (350,603) | 900,279 |
| Other assets and liabilities, net | 631,246 | (231,811) |
| Net cash provided by (used in) operating activities | 6,099,375 | (5,607,857) |
| Investing activities | | |
| Purchases of property, plant and equipment | (964,240) | (1,855,307) |
| Purchases of equity securities | (543,542) | (191,063) |
| Proceeds from sale of equity securities | 849,815 | — |
| Acquisition of the assets and operations of American Stainless Tubing, Inc. (see Note 9) | (21,895,409) | — |
| Net cash used in investing activities | (22,553,376) | (2,046,370) |
| Financing activities | | |
| Net (payments) borrowings (on) from line of credit | (4,257,504) | 8,360,577 |
| Borrowings from term loan | 20,000,000 | — |
| Payments on term loan | (666,667) | — |
| Principal payments on finance lease obligations | (47,041) | (21,366) |
| Payments on earn-out liabilities | (190,473) | (680,941) |
| Net cash provided by financing activities | 14,838,315 | 7,658,270 |
| (Decrease) increase in cash and cash equivalents | (1,615,686) | 4,043 |
| Cash and cash equivalents at beginning of period | 2,220,272 | 14,706 |
| Cash and cash equivalents at end of period | \$604,586 | \$18,749 |

Supplemental disclosure

Cash paid for:

Interest

\$878,035 \$289,848

Income taxes

\$— \$—

See accompanying notes to condensed consolidated financial statements

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Synalloy Corporation

Condensed Consolidated Statement of Shareholders' Equity (Unaudited)

Three Months Ended March 31, 2018

| | Common Stock | Capital in Excess of Par Value | Retained Earnings | Accumulated Other Comprehensive Income (Loss) | Cost of Common Stock in Treasury | Total |
|---------------------------------------------------------|-----------------|--------------------------------------|----------------------|--------------------------------------------------------|-------------------------------------------|---------------|
| Balance at December 31, 2017 | \$ 10,300,000 | \$ 35,193,152 | \$ 58,129,383 | \$ (10,864) | \$ (13,911,245) | \$ 89,700,426 |
| Net income | — | — | 3,835,163 | — | — | 3,835,163 |
| Cumulative adjustment due to adoption of ASU 2016-01 | — | — | (10,864) | 10,864 | — | — |
| Issuance of 24,204 shares of common stock from treasury | — | (214,909) | — | — | 214,909 | — |
| Employee stock option and grant compensation | — | 192,201 | — | — | — | 192,201 |
| Balance at March 31, 2018 | \$ 10,300,000 | \$ 35,170,444 | \$ 61,953,682 | \$ — | \$ (13,696,336) | \$ 93,727,790 |

Three Months Ended March 31, 2019

| | Common Stock | Capital in Excess of Par Value | Retained Earnings | Accumulated Other Comprehensive Income (Loss) | Cost of Common Stock in Treasury | Total |
|----------------------------------------------------------------|-----------------|--------------------------------------|----------------------|-----------------------------------------------------------|-------------------------------------------|----------------|
| Balance at December 31, 2018 | \$ 10,300,000 | \$ 36,520,840 | \$ 68,965,410 | \$ — | —\$(13,302,164) | \$ 102,484,086 |
| Net loss | — | — | (926,522) | — | — | (926,522) |
| Cumulative adjustment due to adoption of ASC 842 (see Note 12) | — | — | 4,622,500 | — | — | 4,622,500 |
| Issuance of 89,154 shares of common stock from treasury | — | (832,419) | — | — | 832,419 | — |
| Employee stock option and grant compensation | — | 615,739 | — | — | — | 615,739 |
| Balance at March 31, 2019 | \$ 10,300,000 | \$ 36,304,159 | \$ 72,661,388 | \$ — | —\$(12,469,745) | \$ 106,795,802 |

See accompanying notes to condensed consolidated financial statements.

Synalloy Corporation

Notes to Condensed Consolidated Financial Statements (unaudited)

Unless indicated otherwise, the terms "Company," "we," "us," and "our" refer to Synalloy Corporation and its consolidated subsidiaries.

1. Basis of Financial Statement Presentation

The accompanying unaudited condensed consolidated financial statements of the Company have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, they do not include all of the information and notes required by accounting principles generally accepted in the United States of America for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included as required by Regulation S-X, Rule 10-01. Operating results for the three-month period ended March 31, 2019 are not necessarily indicative of the results that may be expected for the year ending December 31, 2019. For further information, refer to the consolidated financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 2018.

Certain prior period amounts have been reclassified to conform to the current period presentation, including changes in the fair value of the Company's earn-out liabilities from "Other Expense (Income)" to "Operating Income (Loss)" on the accompanying Condensed Consolidated Statements of Operations.

2. Recently Issued Accounting Standards

Recently Issued Accounting Standards - Adopted

In February 2016, the FASB issued ASU No. 2016-02 "Leases (Topic 842)", as amended, which generally requires lessees to recognize operating and financing lease liabilities and corresponding right-of-use assets on the balance sheet and to provide enhanced disclosures surrounding the amount, timing and uncertainty of cash flows arising from leasing arrangements. The Company adopted the new standard as of January 1, 2019 on a modified retrospective basis, which does not require comparative periods to be restated. On adoption, we recognized additional operating lease liabilities of \$38,016,006 based on the present value of the remaining minimum rental payments as of January 1, 2019. We additionally recognized corresponding right-of-use assets for operating leases totaling \$37,072,072. On January 1, 2019, the Company also recorded cumulative-effect increases to equity and deferred tax assets totaling \$4,622,500 and \$1,310,850, respectively, related to a deferred gain for a sale leaseback transaction that occurred in 2016 and was being amortized into earnings under the prior accounting. The adoption of this standard did not have a material impact on the consolidated statement of operations or cash flows for the three months ended March 31, 2019. See Note 12.

Recently Issued Accounting Standards - Not Yet Adopted

In August 2018, the FASB issued ASU No. 2018-13 "Fair Value Measurement (Topic 820)". The updated guidance improves the disclosure requirements on fair value measurements. The updated guidance is effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2019. Early adoption is permitted for any removed or modified disclosures. The Company is currently assessing the timing and impact of adopting the updated provisions.

3. Revenues

Revenues are recognized when control of the promised goods or services is transferred to our customers upon shipment, in an amount that reflects the consideration we expect to be entitled to in exchange for those goods or services.

The following table presents the Company's revenues, disaggregated by product group. Substantially all of the Company's revenues are derived from contracts with customers where performance obligations are satisfied at a point-in-time.

Synalloy Corporation

Notes to Condensed Consolidated Financial Statements (unaudited)

| | Three Months Ended | |
|-------------------------------------|--------------------|-----------------|
| | Mar 31, 2019 | Mar 31, 2018 |
| Storage tank and vessel | \$9,828,955 | \$5,775,772 |
| Seamless carbon steel pipe and tube | 8,586,505 | 8,432,613 |
| Stainless steel pipe | 45,995,384 | 31,283,862 |
| Galvanized pipe | 6,692,235 | — |
| Specialty chemicals | 13,700,753 | 12,988,355 |
| Total revenues | \$84,803,832 | \$58,480,602 |

Arrangements with Multiple Performance Obligations

Our contracts with customers may include multiple performance obligations. For such arrangements, revenue for each performance obligation is based on its standalone selling price and revenue is recognized as each performance obligation is satisfied. The Company generally determines standalone selling prices based on the prices charged to customers using the adjusted market assessment approach or expected cost plus margin.

Deferred Revenues

Deferred revenues are recorded when cash payments are received in advance of satisfying the performance obligation, including amounts which are refundable. The deferred revenue balance increased \$43,344 during the first three months of 2019 to \$220,979 as of March 31, 2019 due to receiving \$838,069 in advance of satisfying our performance obligations during the period, offset by \$794,725 of revenue that was recognized during the period after satisfying the performance obligations that were included in the beginning deferred revenue balance or entered into during the current period. Deferred revenues are included in "Accrued expenses and other current liabilities" on the accompanying Condensed Consolidated Balance Sheets.

Our payment terms vary by the financial strength or location of our customer and the products offered. The length of time between invoicing and when payment is due is not significant. For certain customers, payment is required before the products or services are delivered to the customer.

4. Inventories

Inventories are stated at the lower of cost or net realizable value. Cost is determined by either specific identification or weighted average methods. The components of inventories are as follows:

| | Mar 31, 2019 | Dec 31, 2018 |
|-----------------|---------------|---------------|
| Raw materials | \$58,479,988 | \$59,778,767 |
| Work-in-process | 18,095,167 | 21,033,532 |
| Finished goods | 37,582,787 | 33,389,087 |
| | \$114,157,942 | \$114,201,386 |

5. Stock options and restricted stock

During the first three months of 2019 and 2018, no stock options were exercised by officers or employees of the Company. Stock compensation expense for the three-month periods ended March 31, 2019 and March 31, 2018 was \$615,739 and \$192,201, respectively.

In 2016, the Compensation & Long-Term Incentive Committee (the "Committee") of the Company's Board of Directors granted performance restricted stock awards ("2016 Performance Stock Award") to officers and certain key management-level employees. The 2016 Performance Stock Award vested three years from the grant date based on continuous service, with the number of shares earned (0% to 150% of the target award) depending on the extent to which the Company achieves certain financial performance targets measured over the period from January 1, 2016 to December 31, 2018. On February 8, 2019, the Committee approved the vesting of the 2016 Performance Stock Award

for a total of 46,477 restricted shares at a grant date market price of \$8.05.

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Synalloy Corporation

Notes to Condensed Consolidated Financial Statements (unaudited)

On February 8, 2019, the Committee approved grants under the Company's 2015 Stock Awards Plan to certain management employees of the Company where 44,949 shares with a market price of \$15.72 per share were granted under the Plan. These stock awards vest in either 20 percent or 33 percent increments annually, beginning one year after the date of grant. In order for the awards to vest, the employee must be in the continuous employment of the Company since the date of the award. Any portion of an award that has not vested is forfeited upon termination of employment. The Company may terminate any portion of the award that has not vested upon an employee's failure to comply with all conditions of the award or the 2015 Stock Awards Plan. An employee is not entitled to any voting rights with respect to any shares not yet vested, and the shares are not transferable.

The diluted earnings per share calculations exclude the effect of potentially dilutive shares when the inclusion of those shares in the calculation would have an anti-dilutive effect. For the three-month period ended March 31, 2019 there is no difference in the number of shares used to calculate basic and diluted shares outstanding because their effect would have been anti-dilutive due to the Company reporting a net loss. For the three-month period ended March 31, 2018, the Company had weighted average shares of common stock, in the form of stock grants and options of 117,879 which were not included in the diluted earnings per share calculation as their effect was anti-dilutive.

6. Income Taxes

The Company and its subsidiaries are subject to U.S. federal income tax as well as income tax of multiple state jurisdictions. The Company is no longer subject to U.S. federal examinations for years before 2014 or state income tax examinations for years before 2013. During the first three months of 2019, the Company did not identify nor reserve for any unrecognized tax benefits.

The effective tax rate was 30.5 percent and 21.6 percent for the three months ended March 31, 2019 and 2018, respectively. The March 31, 2019 effective tax rate is higher than the statutory rate of 21 percent due to state taxes, net of the federal benefit, and discrete tax benefits on our stock compensation plans. The March 31, 2018 effective tax rate was higher than the statutory rate of 21 percent due to state taxes, net of the federal benefit.

Synalloy Corporation
Notes to Condensed Consolidated Financial Statements (unaudited)

7. Segment Information

The following table summarizes certain information regarding segments of the Company's operations:

| | Three Months Ended | | |
|---------------------------------------------|--------------------|---------------|---|
| | Mar 31, 2019 | Mar 31, 2018 | |
| Net sales | | | |
| Metals Segment | \$71,103,079 | \$45,492,247 | |
| Specialty Chemicals Segment | 13,700,753 | 12,988,355 | |
| | \$84,803,832 | \$58,480,602 | |
| Operating income (loss) | | | |
| Metals Segment | \$1,436,642 | \$6,016,531 | |
| Specialty Chemicals Segment | 614,214 | 863,489 | |
| Unallocated corporate expenses | 2,308,423 | 1,502,721 | |
| Acquisition related costs | 281,854 | — | |
| Earn-out adjustments | 16,523 | 154,060 | |
| Operating (loss) income | (555,944 |) 5,223,239 | |
| Interest expense | 1,023,941 | 313,984 | |
| Change in fair value of interest rate swaps | 47,561 | (73,204 |) |
| Other (income) loss, net | (294,667 |) 88,296 | |
| (Loss) income before income taxes | \$(1,332,779 |) \$4,894,163 | |

| | As of | |
|-----------------------------|---------------|---------------|
| | Mar 31, 2019 | Dec 31, 2018 |
| Identifiable assets | | |
| Metals Segment | \$216,759,542 | \$192,195,733 |
| Specialty Chemicals Segment | 27,801,913 | 28,174,675 |
| Corporate ⁽¹⁾ | 43,035,888 | 8,028,438 |
| | \$287,597,343 | \$228,398,846 |
| Goodwill | | |
| Metals Segment | \$15,488,796 | \$8,445,262 |
| Specialty Chemicals Segment | 1,354,730 | 1,354,730 |
| | \$16,843,526 | \$9,799,992 |

(1) As of March 31, 2019, this amount included \$36,759,065 in right-of-use assets that were recorded with the adoption of ASC 842 ("Leases"). Refer to Note 12 for additional information.

8. Fair Value of Financial Instruments

The Company makes estimates of fair value in accounting for certain transactions, in testing and measuring impairment and in providing disclosures of fair value in its condensed consolidated financial statements. The Company determines the fair values of its financial instruments for disclosure purposes by maximizing the use of observable inputs and minimizing the use of unobservable inputs. Fair value disclosures for assets and liabilities are grouped into three levels. The levels prioritize the inputs used to measure the fair value of the assets or liabilities. These levels are:

Level 1 - Quoted prices (unadjusted) in active markets for identical assets or liabilities.

Level 2 - Inputs other than quoted prices that are observable for assets and liabilities, either directly or indirectly.

These inputs include quoted prices for similar assets or liabilities in active markets or quoted prices for identical or similar assets or liabilities in markets that are less active.

Synalloy Corporation

Notes to Condensed Consolidated Financial Statements (unaudited)

Level 3 - Unobservable inputs that are supported by little or no market activity for assets or liabilities and includes certain pricing models, discounted cash flow methodologies and similar techniques.

The Company's financial instruments include cash and cash equivalents, accounts receivable, derivative instruments, accounts payable, earn-out liabilities, revolving line of credit, term loan, and equity investments.

Level 1 Financial Instruments

For short-term instruments, other than those required to be reported at fair value on a recurring basis and for which additional disclosures are included below, management concluded the historical carrying value is a reasonable estimate of fair value because of the short period of time between the origination of such instruments and their expected realization. Therefore, as of March 31, 2019 and December 31, 2018, the carrying amounts for cash and cash equivalents, accounts receivable, accounts payable, the Company's revolving line of credit, which is based on a variable interest rate, and term loan approximate their fair value.

During the first quarter of 2019, the Company sold shares of its equity securities investments. Proceeds from the sale totaled \$849,815 which resulted in a realized gain of \$325,811 that is included in "Other expense (income)" on the accompanying Condensed Consolidated Statements of Operations.

During the first quarter of 2019, the Company also recorded a net unrealized loss of \$53,125 on the investments in equity securities held as of March 31, 2019, which is included in "Other expense (income)" on the accompanying Condensed Consolidated Statements of Operations.

The fair value of equity securities held by the Company as of March 31, 2019 and December 31, 2018 was \$2,901,423 and \$2,935,000, respectively, and is included in "Prepaid expenses and other current assets" on the accompanying Consolidated Balance Sheets.

Level 2 Financial Instruments

The Company has one interest rate swap contract, which is classified as a Level 2 financial instrument as it is not actively traded and is valued using pricing models that use observable market inputs. The fair value of the contract was an asset of \$99,904 and \$147,465 at March 31, 2019 and December 31, 2018, respectively. The interest rate swap was priced using discounted cash flow techniques. Changes in its fair value were recorded to other income (expense) with corresponding offsetting entries to current assets or liabilities, as appropriate. Significant inputs to the discounted cash flow model include projected future cash flows based on projected one-month LIBOR and the average margin for companies with similar credit ratings and similar maturities.

To manage the impact on earnings of fluctuating nickel prices, the Company occasionally enters into six-month forward option contracts, which are classified as Level 2. At March 31, 2019 and December 31, 2018, the Company did not have any such contracts in place.

Level 3 Financial Instruments

The fair value of contingent consideration ("earn-out") liabilities resulting from the 2017 MUSA-Stainless acquisition, 2018 MUSA-Galvanized acquisition, and 2019 American Stainless acquisition (see Note 9) are classified as Level 3. The fair value of the MUSA-Stainless earn-out was estimated by applying the Monte Carlo Simulation approach using management's projection of pounds to be shipped and future price per unit. The fair value of the MUSA-Galvanized earn-out and ASTI earn-out were estimated by applying the probability-weighted expected return method, using management's projection of pounds to be shipped and future price per unit. Each quarter-end, the Company re-evaluates its assumptions for all earn-out liabilities and adjusts to reflect the updated fair values. Changes in the estimated fair value of the earn-out liabilities are reflected in the results of operations in the periods in which they are identified. Changes in the fair value of the earn-out liabilities may materially impact and cause volatility in the Company's operating results.

Synalloy Corporation

Notes to Condensed Consolidated Financial Statements (unaudited)

The following table presents a summary of changes in fair value of the Company's earn-out liabilities during the period:

| | MUSA-Stainless | MUSA-Galvanized | ASTI | Total |
|-----------------------------------------------------------------------------------------|----------------|-----------------|-------------|--------------|
| Balance at December 31, 2018 | \$ 4,251,584 | \$ 3,357,800 | \$— | \$7,609,384 |
| Fair value of the earn-out liability associated with the American Stainless acquisition | — | — | 6,148,230 | 6,148,230 |
| Earn-out payments during the period | (370,289 |) (190,473 |) — | (560,762) |
| Changes in fair value during the period | 343,710 | (392,958 |) 65,771 | 16,523 |
| Balance at March 31, 2019 | \$ 4,225,005 | \$ 2,774,369 | \$6,214,001 | \$13,213,375 |

For the three-month period ended March 31, 2018, the Company recorded a \$154,060 charge related to changes in the fair value of the MUSA-Stainless earn-out liability.

There were no transfers of assets or liabilities between Level 1, Level 2 and Level 3 in the three-month period ended March 31, 2019 or year ended December 31, 2018. During the first three months of 2019, there have been no changes in the fair value methodologies used by the Company.

9. Acquisitions

Acquisition of the Assets and Operations of American Stainless Tubing, Inc.

On January 1, 2019, the Company's wholly-owned subsidiary, ASTI Acquisition, LLC, a North Carolina limited liability company ("ASTI"), completed the purchase of substantially all of the assets and operations of American Stainless Tubing, Inc., a North Carolina corporation ("American Stainless"), in Statesville and Troutman, North Carolina. The purchase price for the all-cash acquisition was \$21,895,409, subject to a post-closing working capital adjustment. The Company funded the acquisition with a new five-year \$20,000,000 term note and a draw against its recently increased \$100,000,000 asset-based line of credit (see Note 10).

The transaction is being accounted for using the acquisition method of accounting for business combinations. Under this method, the total consideration transferred to consummate the acquisition is allocated to the identifiable tangible and intangible assets acquired and liabilities assumed based on their respective fair values as of the closing date of the acquisition. The acquisition method of accounting requires extensive use of estimates and judgments to allocate the consideration transferred to the identifiable tangible and intangible assets acquired and liabilities assumed.

Accordingly, the allocation of the consideration transferred in the unaudited condensed consolidated financial statements is preliminary and will be adjusted upon completion of the final valuation of the assets acquired and liabilities assumed. Such adjustments could be significant. The final valuation is expected to be completed as soon as practicable but no later than twelve months after the closing date of the acquisition.

American Stainless will receive quarterly earn-out payments for a period of three years following closing. Pursuant to the asset purchase agreement between ASTI and American Stainless, earn-out payments will equate to six and one-half percent (6.5 percent) of ASTI's revenue over the three-year earn-out period. As of January 1, 2019, the Company forecasted earn out payments to be \$6,700,858, for which the Company established a fair value of \$6,148,230 using a probability-weighted expected return method and a discount rate of five percent. In determining the appropriate discount rate to apply to the contingent payments, the risk associated with the functional form of the earn-out, and the credit risk associated with the payment of the earn-out were all considered. The fair value of the contingent consideration was estimated by applying the Probability Weighted Expected Return method using management's estimates of pounds to be shipped and future price per unit. At March 31, 2019 the fair value of the earn-out totaled \$6,214,001 with \$2,713,830 of this liability classified as a current liability since the payments will be made quarterly.

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The fair value assigned to the customer list intangible will be amortized on an accelerated basis over 15 years. The excess of the consideration transferred over the fair value of the net tangible and identifiable intangible assets is reflected as goodwill. Goodwill consists of manufacturing cost synergies expected from combining American Stainless' production capabilities with the Metals Segment current operations. All of the goodwill recognized was assigned to the Company's Metals Segment and is expected to be deductible for income tax purposes. The preliminary allocation of the total consideration paid to the fair value of the assets acquired and liabilities assumed as of January 1, 2019 is as follows:

| | |
|------------------------------------------------------------|--------------|
| Inventories | \$5,564,000 |
| Accounts receivable | 3,533,921 |
| Other current assets - production and maintenance supplies | 605,613 |
| Property, plant and equipment | 2,793,173 |
| Customer list intangible | 10,000,000 |
| Goodwill | 7,043,534 |
| Contingent consideration (earn-out liability) | (6,148,230) |
| Accounts payable | (1,400,009) |
| Other liabilities | (96,593) |
| | \$21,895,409 |

ASTI's results of operations since acquisition are reflected in the Company's consolidated statements of operations as follows:

| | |
|----------------------------|---------------------------------------------|
| | Three Months Ended Mar 31, 2019 |
| Net sales | \$9,513,220 |
| Income before income taxes | 107,121 |

For the three-month period ended March 31, 2019, cost of sales included \$1,147,000 representing the fair value above predecessor cost associated with acquired inventory that was sold during the quarter.

The following unaudited pro-forma information is provided to present a summary of the combined results of the Company's operations with American Stainless as if the acquisition had occurred on January 1, 2018. The unaudited pro-forma financial information is for information purposes only and is not necessarily indicative of what the results would have been had the acquisition been completed on the date indicated above.

Pro-Forma

| | |
|-----------------------------|---------------------------------------------|
| | Three Months Ended Mar 31, 2018 |
| Pro-forma net sales | \$67,006,777 |
| Pro-forma net (loss) income | \$3,208,122 |
| (Loss) earnings per share: | |
| Basic | \$0.37 |
| Diluted | \$0.37 |

Pro-forma net income was reduced for the three-month period ended March 31, 2018 for the following:

- Amortization of American Stainless' customer list intangible of \$312,501;

Additional rent expense related to the Company's lease of American Stainless' real estate from Store Capital of \$121,449 ;

• An estimated amount of interest expense associated with the additional borrowings to fund the American Stainless acquisition of \$210,970;

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Notes to Condensed Consolidated Financial Statements (unaudited)

• Depreciation of \$41,252 related to the incremental fair value above historical cost for acquired property, plant and equipment; and

• An decrease in the provision for income taxes of \$173,144 related to the impact of the other pro-forma adjustments and American Stainless' previous status as a pass-through entity for income tax purposes prior to the acquisition.

Acquisition of the Galvanized Pipe and Tube Assets of Marcegaglia USA, Inc.

On July 1, 2018, Bristol Metals, LLC ("BRISMET"), a subsidiary of the Company's Metals Segment, acquired Marcegaglia USA, Inc.'s ("MUSA") galvanized tube assets and operations ("MUSA-Galvanized") located in Munhall, PA. The purchase price for the transaction totaled \$10,378,281. The assets purchased and liabilities assumed from MUSA include accounts receivable, inventory, equipment, and accounts payable.

Munhall-Galvanized's results of operations since acquisition are reflected in the Company's consolidated statements of operations as follows:

| | Three Months Ended Mar 31, 2019 |
|----------------------------|---------------------------------------------|
| Net sales | \$6,692,235 |
| Income before income taxes | 346,403 |

10. Long-term Debt

On December 20, 2018, the Company amended its Credit Agreement with its bank to refinance and increase its Line of Credit (the "Line") from \$80,000,000 to \$100,000,000 and to create a new 5-year term loan in the principal amount of \$20,000,000 (the "Term Loan"). The Term Loan was used to finance the purchase of substantially all of the assets of American Stainless (see Note 9). The Term Loan's maturity date is February 1, 2024, and shall be repaid in 60 consecutive monthly installments. Interest on the Term Loan is calculated using the One Month LIBOR Rate (as defined in the Credit Agreement), plus 1.90 percent. The Line will be used for working capital needs and as a source for funding future acquisitions. The maturity date of the Line has been extended to December 20, 2021. Interest on the Line remains unchanged and is calculated using the One Month LIBOR Rate, plus 1.65 percent. Borrowings under the Line are limited to an amount equal to a Borrowing Base calculation that includes eligible accounts receivable and inventory.

Pursuant to the Credit Agreement, the Company is subject to certain covenants including maintaining a minimum fixed charge coverage ratio, maintaining a minimum tangible net worth, and a limitation on the Company's maximum amount of capital expenditures per year, which is in line with currently projected needs. At March 31, 2019, the Company was in compliance with all debt covenants.

11. Contingencies

The Company is from time-to-time subject to various claims, possible legal actions for product liability and other damages, and other matters arising out of the normal conduct of the Company's business.

Management is not currently aware of any asserted or unasserted matters which could have a material effect on the financial condition or results of operations of the Company.

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Notes to Condensed Consolidated Financial Statements (unaudited)

12. Leases

Adoption of ASC Topic 842, "Leases"

On January 1, 2019, the Company adopted Topic 842 using the modified retrospective method applied to leases that were in place as of January 1, 2019. Results for reporting periods beginning after January 1, 2019 are presented under Topic 842, while prior period amounts are not adjusted and continue to be reported in accordance with our historic accounting under Topic 840. The Company's portfolio of leases contains both finance and operating leases that relate primarily to real estate agreements and manufacturing equipment agreements. Substantially all of the value of the Company's lease portfolio relates to a real estate master lease agreement with Store Master Funding XII, LLC, an affiliate of Store Capital Corporation ("Store") that was entered into in 2016, and amended with the 2018 MUSA-Galvanized and 2019 ASTI acquisitions. As of March 31, 2019, operating lease liabilities related to the master lease agreement with Store totaled \$37,192,255, or 96 percent of the total lease liabilities on the accompanying condensed consolidated balance sheet.

Practical Expedients and Elections

The Company elected the package of practical expedients permitted under the transition guidance, which allowed us to carryforward our historical lease classification, our assessment on whether a contract is or contains a lease, and our initial direct costs for any leases that exist prior to adoption of the new standard. We did not elect the hindsight practical expedient to determine the reasonably certain lease term for existing leases. We also elected to combine lease and non-lease components, and elected the short-term lease recognition exemption for all leases that qualify.

Deferred Gain on Sale Leaseback

On January 1, 2019, the Company recorded cumulative-effect adjustments to increase equity and deferred tax assets totaling \$4,622,500 and \$1,310,850, respectively, related to the derecognition of the deferred gain on its sale leaseback, consistent with transition guidance set forth in ASC 842-10-65-1.

Discount Rate

To determine the present value of minimum future lease payments for operating leases at January 1, 2019, the Company was required to estimate a rate of interest that we would have to pay to borrow on a collateralized basis over a similar term an amount equal to the lease payments in a similar economic environment (the "incremental borrowing rate" or "IBR"). The Company determined the appropriate IBR by identifying a reference rate and making adjustments that take into consideration financing options and certain lease-specific circumstances. For the reference rate, treasury rates for five years, 10 years, and 30 years were used as they cover the periods of the leases. The Company additionally used the Damodaran Credit Rating Model, which assesses a credit rating based on the interest coverage ratio and relates this to credit ratings of other large public manufacturers. Inputs required include EBIT, interest expense, future minimum lease payments, outstanding debt, and a reference rate. Based on this assessment of the aforementioned qualitative and quantitative factors, the Company determined that 7.32 percent was an appropriate incremental borrowing rate to apply to its portfolio of real-estate operating leases. The Company elected to utilize a single discount rate for its portfolio of operating leases because of similar lease characteristics; the resulting calculation does not differ materially from applying the standard to the individual leases.

Weighted average discount rates for operating and finance leases are as follows:

Operating Leases 7.32 %
Finance Leases 11.85 %

Balance Sheet Presentation

Operating and finance lease amounts included in the Consolidated Balance Sheet are as follows:

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Notes to Condensed Consolidated Financial Statements (unaudited)

| Financial Statement Line Item | Classification | March 31, 2019 |
|-------------------------------------------------|--------------------------------|-------------------|
| Right-of-use assets, operating leases | Assets | \$36,759,065 |
| Right-of-use assets, finance leases | Property, plant, and equipment | 532,062 |
| Current lease liabilities, operating leases | Current liabilities | 3,473,925 |
| Current lease liabilities, finance leases | Current liabilities | 235,685 |
| Non-current lease liabilities, operating leases | Non-current liabilities | 34,366,152 |
| Non-current lease liabilities, finance leases | Non-current liabilities | 539,073 |

Total Lease Cost

Individual components of the total lease cost incurred by the Company for the three month period ended March 31, 2019 is as follows:

| | Mar 31, 2019 |
|---------------------------------------|-----------------|
| Operating lease cost | \$ 1,005,191 |
| Finance lease cost | |
| Amortization of right-of-use assets | 43,714 |
| Interest on finance lease liabilities | 20,297 |
| Short-term lease cost | — |
| Total lease cost | \$ 1,069,202 |

Amortization of assets held under finance leases is included in depreciation expense. Minimum rental payments under operating leases are recognized on a straight-line basis over the term of the lease including any periods of free rent.

Maturity of Leases

The amount of undiscounted future minimum lease payments under operating leases are as follows:

| | |
|-----------------------------------------------------------------|--------------|
| Remainder of 2019 | \$2,622,191 |
| 2020 | 3,562,092 |
| 2021 | 3,635,376 |
| 2022 | 3,672,731 |
| 2023 | 3,563,383 |
| 2024 | 3,634,651 |
| Thereafter | 48,553,620 |
| Total undiscounted minimum future operating lease payments | 69,244,044 |
| Imputed Interest | 31,403,967 |
| Total operating lease liabilities recorded as of March 31, 2019 | \$37,840,077 |

The amount of undiscounted future minimum lease payments under finance leases are as follows:

| | |
|---------------------------------------------------------------|-----------|
| Remainder of 2019 | \$238,206 |
| 2020 | 329,534 |
| 2021 | 335,462 |
| 2022 | 11,998 |
| Total undiscounted minimum future finance lease payments | 915,200 |
| Imputed Interest | 140,442 |
| Total finance lease liabilities recorded as of March 31, 2019 | \$774,758 |

Additional Information

Weighted average remaining lease terms for operating and finance leases as of March 31, 2019 are as follows:

Synalloy Corporation
Notes to Condensed Consolidated Financial Statements (unaudited)

Operating Leases 207 months
Finance Leases 33 months

During the three-month period ended March 31, 2019, right-of-use assets obtained in exchange for new operating lease liabilities totaled \$4,900,243.

On January 1, 2019, the Company and Store Master Funding XII, LLC, entered into an Amended and Restated Master Lease Agreement (the "Master Lease"), pursuant to which the Company will lease the Statesville and Troutman, NC facilities, purchased by Store from American Stainless on January 1, 2019, for the remainder of the initial term of 20 years set forth in the Master Lease, with two renewal options of ten years each. Because the Company is reasonably certain to exercise these renewal options, the options are not considered in determining the lease term, and associated potential option payments are excluded from lease payments. The Master Lease includes a rent escalator equal to the lesser of 1.25 times the percentage increase in the Consumer Price Index since the previous increase or 2 percent.

Undiscounted future minimum lease payments under non-cancellable operating leases accounted for under ASC 840 "Leases" were as follows:

| | Dec 31, 2018 |
|------------|-----------------|
| 2019 | \$3,207,053 |
| 2020 | 3,243,694 |
| 2021 | 3,238,745 |
| 2022 | 3,224,810 |
| 2023 | 3,102,815 |
| Thereafter | 45,337,403 |

Undiscounted future minimum lease payments under non-cancellable capital leases accounted for under ASC 840 "Leases" were as follows:

| | Dec 31, 2018 |
|-----------------------------------------|-----------------|
| 2019 | \$ 354,299 |
| 2020 | 329,534 |
| 2021 | 335,462 |
| 2022 | 11,998 |
| 2023 | — |
| Total minimum lease payments | 1,031,293 |
| Less imputed interest costs | 164,826 |
| Present value of minimum lease payments | \$ 866,467 |

13. Goodwill and Intangible Assets

As a result of the January 1, 2019 American Stainless acquisition, the Company recognized \$7,043,534 in Goodwill for the excess of consideration transferred over the fair value of the acquired net tangible and identifiable intangible assets.

The Company also recorded a \$10,000,000 intangible asset on a preliminary basis for the fair value of the customer relationships that were acquired, to be amortized on an accelerated basis over 15 years.

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The balance of intangible assets subject to amortization at March 31, 2019 and December 31, 2018 is as follows:

| | March 31, 2019 | December 31, 2018 |
|-----------------------------------------------|-------------------|----------------------|
| Intangible assets, gross | \$32,622,000 | \$22,622,000 |
| Accumulated amortization of intangible assets | (13,849,639) | (12,925,888) |
| Intangible assets, net | \$18,772,361 | \$9,696,112 |

Estimated amortization expense related to intangible assets for the next five years is as follows:

| | |
|-------------------|-------------|
| Remainder of 2019 | \$2,660,675 |
| 2020 | 3,296,195 |
| 2021 | 3,104,819 |
| 2022 | 2,790,361 |
| 2023 | 1,245,083 |
| 2024 | 1,083,974 |
| Thereafter | 4,628,111 |

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Notes to Condensed Consolidated Financial Statements (unaudited)

14. Stock Repurchase Program

On February 21, 2019, the Board of Directors authorized a stock repurchase program for up to 850,000 shares of its outstanding common stock over twenty-four months. The shares will be purchased from time to time at prevailing market prices, through open market or privately negotiated transactions, depending on market conditions. Under the program, the purchases will be funded from available working capital, and the repurchased shares will be returned to the status of authorized, but unissued shares of common stock or held in treasury. There is no guarantee as to the exact number of shares that will be repurchased by the Company, and the Company may discontinue purchases at any time that management determines additional purchases are not warranted.

During the three-month period ended March 31, 2019 the Company did not purchase any shares under the stock repurchase program.

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

The following is management's discussion of certain significant factors that affected the Company during the three-month period ended March 31, 2019.

Consolidated net sales for the first quarter of 2019 totaled \$84,803,832, an increase of \$26,323,230 or 45 percent compared to net sales for the first quarter of 2018 of \$58,480,602. Excluding ASTI's and Munhall-Galvanized's net sales, consolidated net sales for the first quarter of 2019 increased \$10,283,081, or 17.6 percent compared to net sales for the first quarter of 2018.

The Company recorded a net loss of \$926,522, or \$0.10 diluted loss per share for the first quarter of 2019, compared to net income of \$3,835,163 or \$0.44 diluted earnings per share for the same quarter in the prior year. Excluding the financial results of ASTI and Munhall-Galvanized, net loss for the first quarter of 2019 decreased \$5,076,967, or 126 percent compared to net income for the first quarter of 2018.

Impact of 2019 and 2018 Acquisitions on Financial Results

The first quarter of 2019 includes financial results in the Company's Metals Segment related to the MUSA-Galvanized acquisition (which closed on July 1, 2018) as follows:

a. For the first quarter of 2019, net sales for Munhall-Galvanized totaled \$6,692,235 with pre-tax income of \$346,403.

The first quarter of 2019 include financial results in the Company's Metals Segment related to the American Stainless acquisition (which closed on January 1, 2019) as follows:

a. For the first quarter of 2019, net sales for ASTI totaled \$9,513,220, with pre-tax income of \$107,121.

Metals Segment

Metals Segment net sales for the first quarter of 2019 totaled \$71,103,079, an increase of \$25,610,832 or 56 percent from the first quarter of 2018. Excluding the net sales of ASTI and Munhall-Galvanized, Metals Segment net sales for the first quarter of 2019 increased \$9,405,377, or 21 percent, compared to net sales for the first quarter of 2018.

Sales for the first quarter of 2019 compared to the prior year are summarized as follows:

| | Sales Increase (decrease) from prior year period | | | Units shipped |
|-------------------------------------|--------------------------------------------------|-------|--------------------------------------|---------------|
| | \$ | % | Average selling price ⁽¹⁾ | |
| First quarter | | | | |
| Storage tank and vessel | \$4,053,183 | 70.2% | 66.6% | 3.6% |
| Seamless carbon steel pipe and tube | 153,892 | 1.8% | 11.0% | (9.2)% |
| Stainless steel pipe | 14,711,521 | 47% | 15.3% | 31.7% |
| Galvanized pipe | 6,692,236 | n/a | n/a | n/a |
| Total first quarter change | \$25,610,832 | | | |

⁽¹⁾ Average price increases for the first quarter of 2019 as compared to the first quarter of 2018 primarily relate to the following:

- Storage tank and vessels - product mix change to larger, more complex tanks;
- Seamless carbon steel pipe and tube - pass through of higher input material costs primarily related to the imposition of Section 232 Aluminum and Steel Import Tariffs;
- Stainless steel pipe - pass through of input and cost increases related to:
 - a. Alloy surcharges decrease of seven percent;
 - b. Increase of alloy mix with higher nickel content of seven percent; and
 - c. Base raw material input mill pricing, higher cost mix of roll and plate input materials, and import tariffs of approximately 15 percent.

For the overall Metals Segment, with the addition of the galvanized product line pricing (from the July 1, 2018 MUSA-Galvanized acquisition), pricing averages were impacted by the lower average selling prices of galvanized products as compared to other product lines in the Metals Segment. The inclusion of galvanized products lowered average pricing for the first quarter ended March 31, 2019 by 23 percent.

The Metals Segment's operating income decreased \$4,579,889 to \$1,436,642 for the first quarter of 2019 compared to operating income of \$6,016,531 for the first quarter of 2018.

Current year operating results were affected by the following factors:

Nickel prices and resulting surcharges for 304 and 316 alloys ended the first quarter of 2019 lower than the previous two quarters, with surcharges decreasing by \$0.05 and \$0.06 per pound, respectively from December 2018 and \$0.16 and \$0.19 per pound, respectively, from September 2018. That combined reduction in the nickel indices a. resulted in substantially lower pricing in the first quarter, generating a net unfavorable operating impact of \$3,375,470 related to metal pricing. Compared to a period of rising nickel pricing in the first quarter of 2018, which generated metal pricing gains of \$2,453,633, the first quarter of 2019 was unfavorable \$5,829,103 compared to the first quarter of 2018;

The January 1, 2019 acquisition of ASTI lowered first quarter operating income by \$1,357,946, primarily from b. purchase price accounting that marks up purchased inventory to fair value selling price, thus eliminating all profits on inventory sold during the period;

Year-over-year improvements in welded pipe and tube, including organic growth as well as the addition of ASTI, c. and substantial improvement in Palmer tank sales, yielded volume and product mix related incremental operating profits totaling \$2,770,276; and

Seamless carbon pipe and tube showed an improvement of 1.8 percent in sales, however, the impact of higher priced tariff materials, lower pricing driven by increased distributor inventories and some lower margin first quarter project d. business, all resulted in compressed margins of approximately three percent, lowering operating profit by approximately \$212,637. Some of those impacts should moderate as the year progresses, resulting in more favorable margin performance.

Specialty Chemicals Segment

Net sales for the Specialty Chemicals Segment in the first quarter of 2019 totaled \$13,700,753, representing a \$712,398 or 5 percent increase from the first quarter of 2018.

Net sales continued to benefit during the first quarter of 2019 primarily from organically-driven demand in both Contract/Toll Manufacturing and Proprietary Products.

Operating income for the Specialty Chemicals Segment for the first quarter of 2019 was \$614,214, a total that met plan expectations for the seasonally low, first quarter of the year. The result represents a nine percent improvement over the first quarter of 2018, excluding a \$313,000 favorable gain booked in the first quarter of 2018 from a successful legal claim.

Other Items

Unallocated corporate expenses for the first quarter of 2019 increased \$805,702, or 54 percent, to \$2,308,423 (approximately three percent of sales) compared to \$1,502,721 (approximately three percent of sales) for the first quarter of 2018. The first quarter increase resulted primarily from higher professional fees (\$307,390), higher stock option/grant compensation (\$279,332), and higher employee benefits (\$93,516).

Acquisition related costs were \$1,639,800 for the first quarter of 2019 (\$1,357,946 recorded in Metals Segment Cost of Sales/SG&A and \$281,854 in unallocated SG&A) resulting from costs associated with the January 1, 2019 American Stainless acquisition. This compares to \$186,763 (mainly in Metals Segment Cost of Sales) during the first quarter of 2018.

Interest expense was \$1,023,941 and \$313,984 for the first quarters of 2019 and 2018, respectively. The increase was primarily related to higher average debt outstanding in the first quarter of 2019, as additional borrowings were required primarily related to acquisitions and to support working capital requirements associated with increased business activity.

During the first quarter of 2019, the Company recorded a realized gain of \$325,811 on the sale of equity securities, offset by a net unrealized loss of \$53,125 on the investments in equity securities held as of March 31, 2019, both of which are included in "Other expense (income)" on the accompanying Condensed Consolidated Statements of Operations.

The effective tax rate was 30.5 percent for the three-month period ended March 31, 2019. The March 31, 2019 effective tax rate is higher than the statutory rate of 21 percent due to state taxes, net of the federal benefit, and discrete tax benefits on our stock compensation plans. The effective tax rate was 21.6 percent for the three-month period ended March 31, 2018. The 2018 effective tax rate was higher than the federal statutory rate of 21 percent due to state tax expense, net of the federal benefit.

The Company's cash balance decreased \$1,615,686 to \$604,586 as of March 31, 2019 compared to \$2,220,272 at December 31, 2018. Fluctuations affecting cash flows during the period were comprised of the following:

a. Net inventories remained relatively consistent at March 31, 2019 when compared to December 31, 2018, mainly due to efforts to balance inventory with projected business levels. Excluding the impact of American Stainless' acquired inventory, the Company generated \$5,189,552 of operating cash flows from the relief of inventory during the three months ended March 31, 2019. Inventory turns increased from 1.81 turns at December 31, 2018, calculated on a three-month average basis, to 2.15 turns at March 31, 2019;

b. Accounts payable increased \$5,365,961 as of March 31, 2019 as compared to December 31, 2018. The majority of the increase is related to increased levels of purchasing activity across all sectors of the business, including late first quarter receipts of inventory that were still unpaid on normal terms at the end of the quarter. Accounts payable days outstanding were approximately 36 days at March 31, 2019 compared to 37 days at December 31, 2018;

c. Net accounts receivable increased \$5,793,111 at March 31, 2019 as compared to December 31, 2018, which primarily resulted from a 14 percent increase in sales for the last two months of the first quarter 2019 compared to the last two months of the fourth quarter of 2018. Days sales outstanding, calculated using a three-month average basis, decreased from 52 days outstanding at the end of December 2018, to 50 days at the end of the first quarter 2019;

d. On January 1, 2019, the Company paid \$21,895,409 to complete the American Stainless acquisition (refer to Note 9 for further details);

e. The Company purchased and sold equity securities during the three-month period ended March 31, 2019, which resulted in net cash proceeds of \$306,273;

f. Capital expenditures for the first three months of 2019 were \$964,240; and

g. The Company paid out \$560,762, during the first three months of 2019 related to the earn-out liability from the 2017 MUSA-Stainless and 2018 MUSA-Galvanized acquisitions.

The Company increased its overall debt balance by \$15,075,829 during the first three months of 2019 and had \$91,481,287 of total borrowings outstanding as of March 31, 2019 with its lender. Covenants under the Credit Agreement include maintaining a minimum fixed charge coverage ratio, maintaining a minimum tangible net worth, and a limitation on the Company's maximum amount of capital expenditures per year, which is in line with currently projected needs. As of March 31, 2019, the Company had \$25,198,137 of remaining available capacity under its Line.

The Company was in compliance with all covenants as of March 31, 2019.

Safe Harbor Statement Under the Private Securities Litigation Reform Act of 1995

This quarterly report includes and incorporates by reference "forward-looking statements" within the meaning of the federal securities laws. All statements that are not historical facts are "forward-looking statements." The words "estimate," "project," "intend," "expect," "believe," "should," "anticipate," "hope," "optimistic," "plan," "outlook," "should," "could," "may" and similar expressions identify forward-looking statements. The forward-looking statements are subject to certain risks and uncertainties, including without limitation those identified below, which could cause actual results to differ materially from historical results or those anticipated. Readers are cautioned not to place undue reliance on these forward-looking statements. The following factors could cause actual results to differ materially from historical results or those anticipated: adverse economic conditions; the impact of competitive products and pricing; product demand and acceptance risks; raw material and other increased costs; raw materials availability; employee relations; ability to maintain workforce by hiring trained employees; labor efficiencies; customer delays or difficulties in the production of products; new fracking regulations; a prolonged decrease in oil and nickel prices; unforeseen delays in completing the integrations of acquisitions; risks associated with mergers, acquisitions, dispositions and other expansion activities; financial stability of our customers; environmental issues; unavailability of debt financing on acceptable terms and exposure to increased market interest rate risk; inability to comply with covenants and ratios required by our debt financing arrangements; ability to weather an economic downturn; loss of consumer or investor confidence and other risks detailed from time-to-time in the Company's SEC filings. The Company assumes no obligation to update the information included in this report.

Item 3. Quantitative and Qualitative Disclosures about Market Risks

Information about the Company's exposure to market risk was disclosed in its Annual Report on Form 10-K for the year ended December 31, 2018, which was filed with the SEC on March 18, 2019. There have been no material quantitative or qualitative changes in market risk exposure since the date of that filing.

Item 4. Controls and Procedures

Based on the evaluation required by 17 C.F.R. Section 240.13a-15(b) or 240.15d-15(b) of the Company's disclosure controls and procedures (as defined in 17 C.F.R. Sections 240.13a-15(e) and 240.15d-15(e)), the Company's Chief Executive Officer and Chief Financial Officer concluded that that such controls and procedures, as of the end of the period covered by this quarterly report, were effective.

Changes in Internal Control over Financial Reporting

During the first quarter of 2019, the Company implemented controls to support the adoption of the new lease accounting standard ASU No. 2016- 02, "Leases (Topic 842)". The Company has not identified any other changes in internal control over financial reporting that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting

PART II

Item 1. Legal Proceedings

It is not unusual for us and our subsidiaries to be involved in various unresolved legal actions, administrative proceedings and claims in the ordinary course of business involving, among other things, product liability, commercial, employment, workers' compensation, and environmental matters. We establish reserves in a manner that is consistent with accounting principles generally accepted in the U.S. for costs associated with such matters when a liability is probable and those costs are capable of being reasonably estimated. We cannot predict with any certainty the outcome of these unresolved legal actions or the range of possible loss or recovery. Based on current information, however, we believe that the eventual outcome of these unresolved legal actions, either individually or in the aggregate, will not have a material adverse effect on our financial position, results of operations or cash flows. There were no material changes in our Legal Proceedings, as discussed in Part I, Item 3 in the Company's Annual Report on Form 10-K for the period ending December 31, 2018.

Item 1A. Risk Factors

There were no material changes in our assessment of risk factors as discussed in Part I, Item 1A in the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2018.

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

None.

Item 3. Defaults Upon Senior Securities

None.

Item 4. Mine Safety Disclosures

None.

Item 5. Other Information

None.

Item 6. Exhibits

Exhibit

| No. | Description |
|-------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <u>31.1</u> | <u>Rule 13a-14(a)/15d-14(a) Certifications of Chief Executive Officer</u> |
| <u>31.2</u> | <u>Rule 13a-14(a)/15d-14(a) Certification of the Chief Financial Officer</u> |
| <u>32</u> | <u>Certifications Pursuant to 18 U.S.C. Section 1350</u> |
| 101.INS* | XBRL Instance Document |
| 101.SCH* | XBRL Taxonomy Extension Schema |
| 101.CAL* | XBRL Taxonomy Extension Calculation Linkbase |
| 101.LAB* | XBRL Taxonomy Extension Label Linkbase |
| 101.PRE* | XBRL Taxonomy Extension Presentation Linkbase |
| 101.DEF* | XBRL Taxonomy Extension Definition Linkbase |
| * | In accordance with Regulation S-T, the XBRL-related information in Exhibit 101 to this Quarterly Report on Form 10-Q shall be deemed "furnished" and not "filed." |

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.

SYNALLOY CORPORATION
(Registrant)

Date: April 30, 2019 By: /s/ Craig C. Bram
Craig C. Bram
President and Chief Executive Officer
(principal executive officer)

Date: April 30, 2019 By: /s/ Dennis M. Loughran
Dennis M. Loughran
Senior Vice President and Chief Financial Officer
(principal accounting officer)