1221 Page Street
Kewanee, IL 61443
PH: 800.447.4581
F: 309.852.084

Boss Holdings, Inc.
2018 Fiscal Year End Report

Boss Holdings, Inc. and its subsidiaries (collectively, the "Company") operate in four primary business segments. Boss Manufacturing Company is a leading distributor of work gloves and protective wear, including CAT® branded work gloves and safety products. Galaxy Balloons, Incorporated is our industry award-winning custom imprinter and distributor of promotional and specialty products. Aries Manufacturing is a nationwide distributor of cell phone accessories and Boss Pet Products, Inc. ("Boss Pet") distributes a wide range of pet supplies.

Executive Summary

The Company's fiscal 2018 consolidated revenues were $77,060,000, up $14,748,000 over 2017. On April 30, 2018, Boss Pet acquired the operating assets of PetEdge, Inc., a leading supplier of wholesale pet grooming supplies and discount pet products. The PetEdge assets were acquired through a Delaware assignment for benefit of creditors proceeding. Accordingly, approximately $13,770,000 of the Company's increased 2018 revenues were due to the post-acquisition PetEdge operations.

Prior to acquisition of the PetEdge assets, secured lenders were in the process of liquidating its assets and PetEdge had laid off all but essential staff and warehouse personnel. As a result, suppliers had ceased shipping new product, inventory was severely depleted and operations were at a near standstill. Since the acquisition, we have shed excess warehouse space, relocated the PetEdge headquarters in Beverly, Massachusetts to smaller offices, replenished inventories, reorganized operations and reinvigorated the sales organization. The acquisition provides us dozens of well-known and industry-tested proprietary pet products under the Master Equipment™, Master Grooming Tools™, Top Performance®, Aria®, ProSelect®, Casual Canine®, and Zanies® brands, while also offering leading national and specialty brands like Oster®, Wahl®, BioGroom®, Tropiclean®, and Geib®.

The Company produced a consolidated loss of $2,083,000 in 2018, our first consolidated bottom-line annual loss in many years. Two primary components contributed to the net loss. One was an unrealized (non-cash) loss on available for sale securities of $1,185,000 (discussed below in "Earnings"). The other was the standalone net loss of approximately $2,500,000 for the PetEdge division. Of this amount, $980,000 reflected one-time acquisition, relocation or other non-recurring reorganization expenses. Included were approximately $287,000 of legal fees and costs, $326,000 in restructuring and relocation expenses and $366,000 of non-recurring administrative expense. Management believes the PetEdge acquisition brings significantly greater scale and expanded business opportunities to the pet supplies segment. While the turnaround and integration of PetEdge continues, substantially all non-recurring costs associated with the acquisition were incurred in 2018. Management expects 2019 revenues of the PetEdge division to exceed $25,000,000 and, with Boss Pet, total revenues for the pet supplies segment to exceed $34,000,000.

Revenue Trends

2018 net sales in the work gloves and protective wear segment increased $1,547,000 or 5.0% compared to fiscal 2017. All divisions of the work gloves and protective wear segment reported sales increases. Fiscal 2018 revenues for the cell phone accessory segment were down $3,225,000 from 2017, due primarily to reduced purchases by a significant customer. The pet supply segment experienced increased net sales of $15,851,000 compared with fiscal 2017, primarily due to the PetEdge acquisition noted above. In addition, however, our Boss Pet Products division realized a 33% increase in sales due largely to the addition of new customers and realizing a full year of revenue from our mid-2017 acquisition of Coast 2 Coast Wholesale Pet Supply. Our promotional and specialty products segment increased net sales $576,000 or 4.4% compared to fiscal 2017. During 2018, this segment acquired certain assets of a third-party distributor of novelty sunglasses and acquired a new line of drinkware products.

Operating Costs

Overall gross margin decreased to 25.1% in fiscal 2018 compared with 28.0% for fiscal 2017. Increases in freight and warehouse expenses, created by an increase in less than case pack fulfillment business, drove a portion of this margin reduction. Also, gross margins at the PetEdge division were slow to recover as it took time to reestablish supply, optimize product assortment and rationalize pricing. Overall 2018 operating expenses for the Company increased $6,124,000 compared to fiscal 2017 due in large part to the acquisition and turnaround of the PetEdge operations. Travel and trade show expenses also increased along with commissions and royalties, especially in the work gloves and protective wear segment, as the Company focused on increased revenues. Additional administrative staff in the work gloves and protective wear and pet segments further contributed to increased operating expenses, along with increased legal expenses due to the asset acquisitions completed during the year. As a result, the Company’s 2018 operating loss of $1,444,000 compares to operating income of $2,831,000 in fiscal 2017.

Earnings

2018 earnings before tax constituted a loss of $2,674,000, down from a profit of $3,284,000 in 2017. Much of this difference was due to the turnaround costs and negative operating results of the newly acquired PetEdge operations. Also, the Company recognized an unrealized (non-cash) loss of $1,185,000 at year-end on available for sale securities. As previously reported, such holdings are “marked-to-market” at the end of the period and unrealized gains or losses are reported although the underlying securities still are held by the Company. For comparison, during fiscal 2017 the Company recognized an unrealized gain of $527,000 on the same available for sale securities. During 2019, the share price of these holdings has recovered substantially, producing an unrealized gain of approximately $367,000 between December 30, 2018 and May 30, 2019.

Other 2018 Asset Acquisitions

In March 2018, the Company acquired certain assets of a third-party distributor of novelty sunglasses in connection with the promotional products business segment in exchange for cash consideration of approximately $159,000. In November 2018, the Company acquired certain assets of a third-party marketer and distributor of personalized drinkware for the advertising specialties segment for cash consideration of approximately $180,000.

Liquidity and Capital Resources

Due primarily to the business acquisitions noted above, the Company's liquidity decreased substantially in 2018 with cash decreasing $15,342,000 overall. Operating activities used $9,131,000 of cash in fiscal 2018. The Company's net loss and an overall $9,995,000 increase to inventories were primarily responsible for this cash usage. Restocking inventory for the PetEdge operations alone accounted for approximately $5,700,000 of increased inventory and the Company made opportunistic additions to inventory in response to increased U.S. tariffs on goods sourced from China. Investment activities utilized $7,382,000 of cash, primarily for business combinations discussed above. We also made machinery & equipment improvements in the promotional and specialty products segment and improved our Kewanee, Illinois warehouse facilities to provide a Midwest distribution point for PetEdge. Financing activities netted to a cash increase of $1,494,000, as the Company amended and restated its primary credit facility in September 2018, borrowing $4,0000,000 under a term loan and utilizing $2,506,000 of the term loan proceeds to pay off previously outstanding borrowings on its line of credit.

At December 29, 2018, the Company held $1,974,000 in cash. Effective September 14, 2018, the Company amended and restated its primary credit facility with a commercial bank. The revised Credit Agreement provides a revolving credit facility up to $7,500,000 that matures September 30, 2019 and a five-year term loan of $4,000,000 due September 14, 2023. As of December 29, 2018, availability under the revolving credit facility was $7,437,000, reduced by a letter of credit issued in favor of a supplier in the amount of $63,000. Management believes the Company's cash on hand and availability under the credit facility should provide ample liquidity for the Company's expected working capital and operating needs.

Effective April 30, 2015, the Company's Board of Directors authorized a stock buyback program (the "2015 Buyback Program") pursuant to which the Company may purchase shares of the Company's common stock in an amount up to $1,500,000, at such prices, and on such terms and conditions as are determined by appropriate officers of the Company from time to time. The Company's Board of Directors in its discretion may extend, curtail, amend or terminate the 2015 Buyback Program at any time. There were no stock buybacks by the Company during 2018.

Boss Holdings, Inc. and Subsidiaries

Consolidated Balance Sheets
(Dollars in Thousands, Except Per Share Data)

	December 29, 2018	December 30, 2017
Assets		
Current Assets:		
Cash and cash equivalents	$ 1,974	$ 17,316
Accounts receivable, net of allowance for doubtful accounts and returns 2018 $296; 2017 $139	13,839	9,892
Income Tax Receivable	873	859
Inventories	31,950	19,418
Prepaid expenses and other	1,166	678
Total current assets	49,802	48,163
Property and Equipment, net	4,220	2,647
Marketable Securities	240	1,425
Intangibles, net of amortization	1,304	881
Goodwill	2,853	2,853
Deferred tax asset	1,065	451
	$ 59,484	$ 56,420
Liabilities and Stockholders' Equity		
Current Liabilities:		
Current portion of long-term obligations	$ 202	$ 2,506
Accounts payable	6,338	3,332
Accrued payroll and related expenses	1,672	1,519
Accrued promotional expenses	1,281	968
Other accrued liabilities	951	589
Total current liabilities	10,444	8,914
Long-Term Obligations, net of current portion	3,801	3
Stockholders' Equity:		
Common stock, $.25 par value; authorized 10,000,000 shares; issued and outstanding 1,986,118 and 1,986,118 shares in 2018 and 2017, respectively	497	497
Additional paid-in capital	64,424	64,424
Accumulated (deficit)	(19,072)	(16,989)
Accumulated other comprehensive (loss)	(610)	(429)
Total stockholders' equity	45,239	47,503
	$ 59,484	$ 56,420

Boss Holdings, Inc. and Subsidiaries

Consolidated Statements of Comprehensive Income (Loss)
Periods Ended December 29, 2018 and December 30, 2017
(Dollars in Thousands, Except Per Share Data)

	Twelve Months Ended December 29, 2018	Twelve Months Ended December 30, 2017
Net sales	$ 77,060	$ 62,312
Cost of sales	57,756	44,857
Gross profit	19,304	17,455
Operating expenses	20,748	14,624
Operating income (loss)	(1,444)	2,831
Other income (expense):		
Interest income	147	-
Interest expense	(53)	(59)
Change in Unrealized Gain (Loss) On available for sale securities	(1,185)	527
Other	(139)	(15)
	(1,230)	453
Income (loss) before income tax	(2,674)	3,284
Income tax benefit	(591)	374
Change in deferred tax asset valuation	-	-
Net income (loss)	$ (2,083)	$ 2,910
Comprehensive income (loss)	$ (2,264)	$ 3,028
Weighted average shares outstanding	1,988,777	1,988,777
Basic earnings (loss) per common share	$ (1.05)	$ 1.46
Diluted earnings (loss) per common share	$ (1.05)	$ 1.46

Boss Holdings, Inc. and Subsidiaries

Consolidated Statements of Cash Flows
Periods Ended December 29, 2018 and December 30, 2017
(Dollars in Thousands)

	Twelve Months Ended December 29, 2018	Twelve Months Ended December 30, 2017
Cash Flows from Operating Activities:		
Net income (loss)	$ (2,083)	$ 2,910
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:		
Depreciation and amortization	1,327	659
Share-based compensation and related tax benefits	-	23
Deferred tax expense (benefit)	(614)	523
Changes in unrealized (gains) losses on available-for-sale securities	1,185	(527)
Changes in assets and liabilities net of acquisitions:		
(Increase) decrease in:		
Accounts receivable	(1,677)	211
Inventories	(9,995)	(456)
Prepaid expenses and other current assets	(667)	188
Other assets	(139)	(369)
Increase (decrease) in:		
Accounts payable	2,921	453
Accrued liabilities	611	(1,058)
Net cash provided by (used in) operating activities	(9,131)	2,557
Cash Flows from Investing Activities:		
Purchase of property and equipment	(629)	(520)
Purchase of available-for-sale securities	-	(898)
Payments for business combinations'	(6,753)	(504)
Net cash (used in) investing activities	(7,382)	(1,922)
Cash Flows from Financing Activities:		
Repurchase of common stock	-	(225)
Proceeds from long-term revolving line of credit	-	-
Repayment of long-term obligations'	(2,506)	(6)
Proceeds from long-term obligations	4,000	-
Proceeds from exercise of stock options	-	63
Net cash provided by (used in) financing activities	1,494	(168)
Effect of exchange rates on cash and cash equivalents	(323)	257
Increase (decrease) in cash and cash equivalents	(15,342)	724
Cash and cash equivalents:		
Beginning of period	17,316	16,592
End of period	$ 1,974	$ 17,316