

TREX CO INC
Form 10-K
February 14, 2019
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

Form 10-K

(Mark One)

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

For the fiscal year ended December 31, 2018

**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: 001-14649

Trex Company, Inc.

(Exact name of registrant as specified in its charter)

| | |
|--|--|
| Delaware (State or other jurisdiction of incorporation or organization) 160 Exeter Drive, Winchester, Virginia (Address of principal executive offices) | 54-1910453 (I.R.S. Employer Identification No.) 22603-8605 (Zip Code) |
|--|--|

(540) 542-6300

Registrant's telephone number, including area code:

Securities registered pursuant to Section 12(b) of the Act:

| | |
|--|---|
| Title of each class: Common Stock, par value \$0.01 per share | Name of each exchange on which registered: New York Stock Exchange |
|--|---|

Securities registered pursuant to Section 12(g) of the Act:

None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Exchange Act. Yes No

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

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

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

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

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

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

The aggregate market value of the registrant's common equity held by non-affiliates of the registrant at June 30, 2018, which was the last business day of the registrant's most recently completed second fiscal quarter, was approximately \$3.6 billion based on the closing price of the common stock as reported on the New York Stock Exchange on such date and assuming, for purposes of this computation only, that the registrant's directors, executive officers and beneficial owners of 10% or more of the registrant's common stock are affiliates.

The number of shares of the registrant's common stock outstanding on February 6, 2019 was 58,508,808.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the following documents are incorporated by reference in this Form 10-K as indicated herein:

| Document | Part of 10-K into which incorporated |
|---|---|
| Proxy Statement relating to Registrant's 2018 Annual Meeting of Stockholders | Part III |

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NOTE ON FORWARD-LOOKING STATEMENTS

This report, including the information it incorporates by reference, contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. We intend our forward-looking statements to be covered by the safe harbor provisions for forward-looking statements in these sections. All statements regarding our expected financial position and operating results, our business strategy, our financing plans, forecasted demographic and economic trends relating to our industry and similar matters are forward-looking statements. These statements can sometimes be identified by our use of forward-looking words such as believe, may, will, anticipate, estimate, expect, intend or similar expressions. We cannot promise you that expectations in such forward-looking statements will turn out to be correct. Our actual results could be materially different from our expectations because of various factors, including the factors discussed under Item 1A. Risk Factors in this report.

EXPLANATORY NOTE: On May 2, 2018, the Board of Directors of the Company approved a two-for-one stock split of the Company's common stock, par value \$0.01. The stock split was in the form of a stock dividend distributed on June 18, 2018, to stockholders of record at the close of business on May 23, 2018. The stock split entitled each stockholder to receive one additional share of common stock, par value \$0.01, for each share they held as of the record date. All common stock share and per share data for all periods presented in the accompanying consolidated financial statements and notes thereto have been retroactively adjusted to reflect the stock split.

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PART I

Some of the information contained in this report concerning the markets and industry in which we operate is derived from publicly available information and from industry sources. Although we believe that this publicly available information and the information provided by these industry sources are reliable, we have not independently verified the accuracy of any of this information.

Item 1. Business
General

Trex Company, Inc. (Company, we, us or our), was incorporated as a Delaware corporation in 1998. The Company is the world's largest manufacturer of wood-alternative decking and railing products, which are marketed under the brand name Trex® and manufactured in the United States. In addition, Trex is a leading national provider of custom-engineered railing and staging, systems for the commercial and multi-family market, including sports stadiums and performing arts venues. Our principal executive offices are located at 160 Exeter Drive, Winchester, Virginia 22603, and our telephone number at that address is (540) 542-6300.

Products

Operations and Products: The Company currently operates in two reportable segments: Trex Residential Products (Trex Residential) and Trex Commercial Products (Trex Commercial).

Trex Residential is the world's largest manufacturer of high-performance composite decking and railing products, which are marketed under the brand name Trex® and manufactured in the United States. We offer a comprehensive set of aesthetically appealing and durable, low-maintenance product offerings in the decking, railing, fencing, steel deck framing, and outdoor lighting categories. A majority of the products are eco-friendly and made in a proprietary process that combines reclaimed wood fibers and recycled polyethylene film. Trex Residential products are sold to distributors and home centers for final resale primarily to the residential market.

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Trex offers the following products through Trex Residential:

| | |
|----------------------------------|--|
| <i>Decking</i> | Our principal decking products are Trex Transcend [®] , Trex Enhance [®] and Trex Select [®] . Our decking products are comprised of a blend of 95 percent recycled wood and recycled plastic film and feature a protective polymer shell for enhanced protection against fading, staining, mold and scratching. We also offer Trex Hideaway [®] , a hidden fastening system for grooved boards. |
| <i>Railing</i> | Our railing products are Trex Transcend Railing, Trex Select Railing, and Trex Signature [®] aluminum railing. Trex Transcend Railing, made from approximately 40 percent recycled content, is available in the colors of Trex Transcend decking and finishes that make it appropriate for use with Trex decking products as well as other decking materials, which we believe enhances the sales prospects of our railing products. Trex Select Railing, made from approximately 40 percent recycled content, is ideal for consumers who desire a simple clean finished look for their deck. Trex Signature aluminum railing, made from a minimum of 50 percent recycled content, is available in three colors and designed for consumers who want a sleek, contemporary look. |
| <i>Fencing</i> | Our Trex Seclusions [®] fencing product is offered through two specialty distributors. This product consists of structural posts, bottom rail, pickets, top rail and decorative post caps. |
| <i>Steel Deck Framing</i> | Our triple-coated steel deck framing system called Trex Elevations [®] leverages the strength and dimensional stability of steel to create a flat surface for our decking. Trex Elevations provides consistency and reliability that wood does not and is fire resistant. |
| <i>Outdoor Lighting</i> | Our outdoor lighting systems are Trex DeckLighting and Trex LandscapeLighting. Trex DeckLighting is a line of energy-efficient LED dimmable deck lighting, which is designed for use on posts, floors and steps. The line includes a post cap light, deck rail light, riser light and a recessed deck light. The Trex LandscapeLighting line includes an energy-efficient well light, path light, multifunction light and spotlight. |

Trex Residential products offer a number of significant aesthetic advantages over wood while eliminating many of wood's major functional disadvantages, which include warping, splitting and other damage from moisture. In addition to resisting fading and surface staining, Trex Residential products require no sanding, staining or sealing, resist moisture damage, provide a splinter-free surface and do not require chemical treatment against rot or insect infestation. Special characteristics (including resistance to splitting, the ability to bend, and ease and consistency of machining and finishing) facilitate installation, reduce contractor call-backs and afford consumers a wide range of design options. Combined, these aspects yield significant aesthetic advantages and lower maintenance than wood decking and railing and ultimately render Trex Residential products less costly than wood over the life of the deck. Trex decking products do not have the tensile strength of wood and, as a result, are not used as primary structural members in posts, beams or columns used in a deck's substructure. However, Trex does offer the Trex Elevations steel deck framing system.

We have received product building code listings from the major U.S. building code listing agencies for decking and railing and from the major Canadian building code listing agency for decking. The listings facilitate the acquisition of building permits by deck builders and promote consumer and industry acceptance of our products as an alternative to wood decking.

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We are a licensor in a number of licensing agreements with third parties to manufacture and sell products under the Trex trademark. Our licensed products are:

Trex Outdoor Furniture A line of outdoor furniture products manufactured and sold by PolyWood, Inc.

Trex RainEscape® An above joist deck drainage system manufactured and sold by DriDeck Enterprises, LLC.

Trex CustomCurve® A system manufactured and sold by Curvelt, LLC that allows contractors to heat and bend Trex Products while on the job site.

Trex Pergola Pergolas made from low maintenance cellular PVC product, manufactured by Home & Leisure, Inc. dba Structureworks Fabrication.

Trex Latticeworks Outdoor lattice boards manufactured and sold by Rhea Products, Inc. dba Acurio Latticeworks.

Trex Cornhole Boards Cornhole boards manufactured and sold by IPC Global Marketing LLC.

Diablo® Trex Blade A specialty saw blade for wood-plastic composite decking manufactured and sold by Freud America, Inc.

Trex SpiralStairs and Structural Steel Posts An ultimate staircase alternative and structural steel posts for use with all deck substructures manufactured and sold by M. Cohen and Sons, Inc. dba The Iron Shop.

Trex Outdoor Kitchens, Cabinetry and Storage Outdoor kitchens, cabinetry and storage manufactured and sold by NatureKast Products, LLC.

Trex Commercial is a leading national provider of custom-engineered railing and staging systems. Trex Commercial designs and engineers custom railing solutions, which are prevalent in professional and collegiate sports facilities, standardized architectural and aluminum railing systems, which target commercial and high-rise applications, and

portable staging equipment for the performing arts, sports, and event production and rental markets. With a team of devoted engineers, and an industry-leading reputation for quality and dedication to customer service, Trex Commercial markets to architects, specifiers, contractors, and building owners.

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Trex offers the following products through Trex Commercial:

Architectural Railing Systems Our architectural railing systems are pre-engineered guardrails with options to accommodate styles ranging from classic and elegant wood top rail combined with sleek stainless components and glass infill, to modern and minimalist stainless cable and rod infill choices.

Aluminum Railing Systems Our aluminum railings, made from approximately 70 percent recycled content, are a versatile, cost-effective and low-maintenance choice for a variety of interior and exterior applications that we believe blend form, function and style. They are often used in sports stadiums and arenas, office buildings, and high-rise condominium and resort projects and offer safety and durability to stairs, public walkways and balconies. They are available in picket or glass infills with a selection of top cap styles, color finishes and mounting capabilities.

Custom Railing Options Trex Commercial can design, engineer and manufacture custom railing systems tailored to the customer's specific material, style and finish. Many railing styles are achievable, including glass, mesh, perforated railing and cable railing.

Staging Equipment and Accessories Our advanced modular, lightweight custom staging systems include portable platforms, orchestral shells, guardrails, stair units, barricades, camera platforms, VIP viewing decks, ADA infills, DJ booths, pool covers, and other custom applications. Our systems provide superior staging product solutions for facilities and venues with custom needs. Our modular stage equipment is designed to appear seamless, feel permanent, and maximize the functionality of the space.

Customers and Distribution

Trex Residential: Wholesale Distributors/Retail Lumber Dealers. We generate most of our sales for our wood-alternative decking and railing products through our wholesale distribution network by selling Trex Residential products to wholesale distributors, who in turn, sell our products to retail lumber outlets. These retail dealers market to both homeowners and contractors, but they emphasize sales to professional contractors, remodelers and homebuilders. Contractor-installed decks generally are larger installations with professional craftsmanship. Our retail dealers generally provide sales personnel trained in Trex Residential products, contractor training, inventory commitment and point-of-sale display support. We believe that attracting wholesale distributors, who are committed to our products and marketing approach and can effectively sell higher value products to contractor-oriented lumber yards and other retail outlets, is important to our future growth. Our distributors are able to provide value-added service in marketing our products because they sell premium wood decking products and other innovative building materials that typically require product training and personal selling efforts. We typically appoint two distributors on a non-exclusive basis to distribute Trex residential products within a specified area. The distributor purchases our products at prices in effect at

the time we ship the product to the distributor. Sales to two of our distributors, Boise Cascade Company and U.S. Lumber Group, LLC, each exceeded 10% of gross sales in 2018.

Home Depot and Lowe's. We sell our products through Home Depot and Lowe's stores. Home Depot and Lowe's purchase products directly from us for stocking on their shelves. They also purchase product through our wholesale distributors for special orders placed by consumers. Home Depot and Lowe's serve both the contractor market and the do-it-yourself market. We believe that brand exposure through Home Depot and Lowe's distribution promotes consumer acceptance of our products.

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We are committed to conducting business activities with the highest standards of business ethics and in accordance with all applicable laws and regulations. Our Vendor and Customer Code of Conduct and Ethics (Code), available at www.trex.com/our-company, applies to all parties providing goods and services to the Company, and all of our channel partners who distribute, sell and/or install our products (collectively, Business Partners). We expect all of our Business Partners, and all of our employees, agents and subcontractors to follow our high ethical standards set forth in the Code while they are conducting business with us or on our behalf. In addition, we expect our Business Partners to understand and comply with the Trex Company Code of Conduct and Ethics, available at www.trex.com/our-company, to do business with Business Partners who share the same commitment to human rights that we have and as set forth in our Human Rights Policy, available at www.trex.com/our-company.

Trex Commercial: We sell our modular and architectural railing and staging systems to the commercial and multifamily market, including sports stadiums and performing arts venues, primarily to facility owners and general contractors throughout the country. We market these products through our direct sales staff, independent sales representatives, and bidding on projects.

Manufacturing Process

Trex Residential products manufactured at our Winchester, Virginia and Fernley, Nevada manufacturing facilities are primarily manufactured from reclaimed wood fiber and scrap polyethylene. Our primary manufacturing process for the products involves mixing wood particles with plastic, heating and then extruding, or forcing, the highly viscous and abrasive material through a profile die. We use many proprietary and skill-based advantages in our eco-friendly manufacturing process. Trex Commercial products manufactured at our Minnesota manufacturing facilities are primarily manufactured from aluminum and stainless steel. Our primary manufacturing process for these products involves cutting, machining, welding and finishing. We use Six Sigma and Lean Manufacturing methodologies throughout our Company within our plant operations and in the planning and execution of certain projects.

Our manufacturing processes require significant capital investment, expertise and time to develop. We have continuously invested the capital necessary to expand our manufacturing throughput and improve our manufacturing processes. We have also broadened the range of raw materials that we can use to produce a consistent and high-quality finished product. In connection with national building code listings, we maintain a quality control testing program.

Suppliers

We conduct supply chain assessments when considered necessary in relation to the significance of the purchase and business opportunity for the Company. Assessments include in-person reviews and tours of operating facilities. The Company is committed to conducting business activities with the highest standards of business ethics and in accordance with all applicable laws and regulations. As stated above, our Vendor and Customer Code of Conduct and Ethics, our Code of Conduct and Ethics, and our Human Rights Policy apply to all suppliers of the Company.

The production of most of our decking products requires a supply of reclaimed wood fiber and scrap polyethylene. We fulfill requirements for raw materials under both purchase orders and supply contracts. In the year ended December 31, 2018, we purchased substantially all of our reclaimed wood fiber requirements under purchase orders, which do not involve long-term supply commitments. All of our polyethylene purchases are under short-term supply contracts that generally have a term of approximately one to two years for which pricing is negotiated as needed, or under purchase orders that do not involve long-term supply commitments.

Reclaimed Wood Fiber: Cabinet and flooring manufacturers are our preferred suppliers of reclaimed wood fiber because the reclaimed wood fiber produced by these operations contains little contamination and is low in moisture. These facilities generate reclaimed wood fiber as a byproduct of

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their manufacturing operations. If the reclaimed wood fiber meets our specifications, our reclaimed wood fiber supply agreements generally require us to purchase at least a specified minimum and at most a specified maximum amount of reclaimed wood fiber each year. Depending on our needs, the amount of reclaimed wood fiber that we actually purchase within the specified range under any supply agreement may vary significantly from year to year.

Scrap Polyethylene: The polyethylene we consume is primarily composed of scrap plastic film and plastic bags. We will continue to seek to meet our future needs for scrap polyethylene from the expansion of our existing supply sources and the development of new sources. We believe our use of multiple sources provides us with a cost advantage and facilitates an environmentally responsible approach to our procurement of polyethylene. Our ability to source and use a wide variety of polyethylene from third party distribution and manufacturing operations is important to our cost strategy. We maintain this ability through the continued expansion of our plastic reprocessing operations in combination with the advancement of our proprietary material preparation and extrusion processes.

In addition, we outsource the production of certain products to third-party manufacturers.

The production of our commercial products requires a supply of aluminum, stainless steel and glass components. We use multiple sources for each material to ensure consistent availability of material and competitive pricing. We purchase substantially all of our aluminum, stainless steel and glass under purchase orders, which do not involve long-term supply commitments.

Training

During 2016, we launched Trex University, our state-of-the-art training facility located near our Winchester manufacturing plant. Trex University is designed to educate and train retailers, contractors and other partners on the benefits of Trex aesthetically pleasing, high performance and low maintenance outdoor living products.

Growth Strategies

Our long-term goals are to perpetuate our position as the leading producer of branded superior wood-alternative decking, railing and other outdoor living products, and to extend our position as a leading national provider of custom-engineered railing and staging systems for the commercial and multi-family market, including performing arts venues and sports stadiums. To achieve our long-term goals, we intend to increase our market share and expand into new product categories and geographic markets through the design, creation and marketing of high-performance outdoor living products that offer superior aesthetics and quality, and by expanding our sales to commercial building projects. We will continue to explore opportunities that leverage our manufacturing and extrusion expertise and are tied to our recycling heritage. We intend to employ the following long-term strategies to achieve our goals:

Innovation: Bring to the market new products that address unmet consumer and trade professional needs. Provide a compelling value proposition through ease of installation, low maintenance, long-term durability and superior aesthetics.

Brand: Expand preference and commitment for the Trex brand with both consumers and trade professionals. Deliver on the brand's promise of superior quality, functionality, pleasing aesthetics and overall performance

in outdoor living products and custom-engineered railing and staging systems. Leverage online efforts to extend the Trex brand digital presence, both nationally and globally.

Channels: Achieve comprehensive market segment and geographic coverage for Trex products by increasing the number of stocking dealers and retailers and expanding our international presence for our wood-alternative outdoor living products, thereby making our products available wherever our customers choose to purchase their decking, railing, steel deck framing and outdoor lighting products, and by continuing to develop our commercial market penetration for our railing and staging systems.

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Quality: Continuously advance the quality of all operational and business processes, with the goal of achieving superior product quality and service levels, thereby giving us a sustainable competitive advantage.

Cost: Through capital investments and process engineering, continuously seek to lower the cost to manufacture Trex products. Investments in plastic recycling capabilities will allow us to expand our ability to use a wider breadth of waste materials thereby lowering raw material costs of our outdoor living products. We plan to continue to achieve significant improvements in manufacturing productivity by reducing waste and improving our production process.

Customer Service: Through our commitment to superior customer service, continually deliver consistently outstanding, personalized service to all of our customers and prospects in all target segments.

Competition

Our primary competition for our wood-alternative decking and residential railing products consists of wood products, which constitutes a substantial majority of decking and railing sales, as measured by linear feet of lumber. Many of the conventional lumber suppliers with which we compete have established ties to the building and construction industry and have well-accepted products. A majority of the lumber used in wood decks is pressure-treated lumber. Southern yellow pine and fir have a porosity that readily allows the chemicals used in the pressure treating process to be absorbed. The same porosity makes southern yellow pine susceptible to absorbing moisture, which causes the lumber to warp, crack, splinter and expel fasteners. In addition to pine and fir, other segments of wood material for decking include redwood, cedar and tropical hardwoods, such as ipe, teak and mahogany. These products are often significantly more expensive than pressure-treated lumber, but do not eliminate many of the disadvantages of other wood products.

In addition to wood, we also compete with other manufacturers of wood-alternative products. Industry studies indicate that we have the leading market share of the wood-alternative segment of the decking and railing market. Our principal competitors include The Azek Building Products, Inc., and Fiberon (a division of Fortune Brands, Inc.).

Our ability to compete depends, in part, on a number of factors outside our control, including the ability of our competitors to develop new wood-alternative decking and railing products that are competitive with our products. We believe that the principal competitive factors in the decking and railing market include product quality, price, aesthetics, maintenance cost, and distribution and brand strength. We believe we compete favorably with respect to these factors. We believe that our products offer aesthetic and cost advantages over the life of a deck when compared to other types of decking and railing materials. Although a contractor-installed deck built with Trex products using a pressure-treated wood substructure generally costs more than a deck made entirely from pressure-treated wood, Trex products are low maintenance compared to the on-going maintenance required for a pressure-treated deck and are, therefore, less costly over the life of the deck. We believe that our manufacturing process and utilization of relatively low-cost raw material sources provide us with a competitive cost advantage relative to other manufacturers of wood-alternative decking and railing products. The scale of our operations also confers cost efficiencies in manufacturing, sales and marketing.

Our primary competition for our products in the commercial and multi-family market consists of companies that provide components to assemble guard rails, including C.R. Laurence Co., Inc., a CRH Group company, regional railing and metal fabricators, and Wenger Corporation. Our ability to compete depends on our product design advantages, relationships with architects and general contractors, and competitive manufacturing costs.

Seasonality

Our operating results for Trex Residential have historically varied from quarter to quarter. Seasonal, erratic or prolonged adverse weather conditions in certain geographic regions reduce the level of home improvement

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and construction activity and can shift demand for its products to a later period. As part of its normal business practice and consistent with industry practice, Trex Residential Products has historically offered incentive programs to its distributors and dealers to build inventory levels before the start of the prime deck-building season in order to ensure adequate availability of its product to meet anticipated seasonal consumer demand. The seasonal effects are often offset by the positive effect of the incentive programs. The operating results for Trex Commercial have not historically varied from quarter to quarter as a result of seasonality. However, they are driven by the timing of individual projects, which may vary each quarterly period.

Government Regulation

We are subject to federal, state and local environmental regulation. The emissions of particulates and other substances from our manufacturing facilities must meet federal and state air quality standards implemented through air permits issued to us by the Department of Environmental Quality of the Commonwealth of Virginia, and the Division of Environmental Protection of Nevada's Department of Conservation and Natural Resources. Our facilities are regulated by federal and state laws governing the disposal of solid waste and by state and local permits and requirements with respect to wastewater and storm water discharge. Compliance with environmental laws and regulations has not had a material adverse effect on our business, operating results or financial condition.

Our operations also are subject to work place safety regulation by the U.S. Occupational Safety and Health Administration, the Commonwealth of Virginia, and the States of Nevada, and Minnesota. Our compliance efforts include safety awareness and training programs for our production and maintenance employees.

Intellectual Property

Our success depends, in part, upon our intellectual property rights relating to our products, production processes and other operations. We rely upon a combination of trade secret, nondisclosure and other contractual arrangements, and patent, copyright and trademark laws, to protect our proprietary rights. We have made substantial investments in manufacturing process improvements that have enabled us to increase manufacturing line production rates, facilitate our development of new products, and produce improvements in our existing products' dimensional consistency, surface texture and color uniformity.

Intellectual property rights may be challenged by third parties and may not exclude competitors from using the same or similar technologies, brands or works. We seek to secure effective rights for our intellectual property, but cannot provide assurance that third parties will not successfully challenge, or avoid infringing, our intellectual property rights.

We consider our trademarks to be of material importance to our business plans. The U.S. Patent and Trademark Office has granted us federal registrations for many of our trademarks. Federal registration of trademarks is effective for as long as we continue to use the trademarks and renew their registrations. We do not generally register any of our copyrights with the U.S. Copyright Office, but rely on the protection afforded to such copyrights by the U.S. Copyright Act. This law provides protection to authors of original works, whether published or unpublished, and whether registered or unregistered.

We hold a number of U.S. Patents and U.S. Patent Applications for various technologies. We have two current U.S. Patent Applications for decking technology and five U.S. Patents, as well as one pending U.S. Patent Application, for various staging systems, accessories and related technologies. We intend to maintain our existing patents in effect until they expire as well as to seek additional patents as we consider appropriate.

We enter into confidentiality agreements with our employees and limit access to and distribution of our proprietary information. If it is necessary to disclose proprietary information to third parties for business reasons, we require that such third parties sign a confidentiality agreement prior to any disclosure.

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Employees and Corporate Governance

At December 31, 2018, we had approximately 1,214 full-time employees, approximately 837 of whom were employed in our manufacturing operations. Our employees are not covered by collective bargaining agreements. We believe that our relationships with our employees are favorable. The Company has internal standards related to hiring practices that encourage diversity, formal programs to provide skill development for our employees, and anti-discrimination standards. The Company has not had any serious complaints or claims over the last three years. We have adopted a Human Rights Policy across all of our operations that sets forth our values related to working conditions and human rights and underscores our philosophy about the way we conduct our business. The policy is available at www.trex.com/our-company.

Information related to the Company's governance and related activities and programs may be found in the Company's Proxy Statement filed on March 22, 2018 in Schedule 14A. Also, a copy of the Company's Code of Conduct and Ethics (Code) is maintained on the Company's web site at www.trex.com/our-company. The Company has a whistle-blowing policy included in its Code that encourages reporting by employees of activities the employee considers illegal or dishonest. Each employee is notified of the whistle-blowing policy and a toll-free hotline is provided for reporting issues directly to the Board of Directors and the Company's General Counsel.

Environmental and Occupational Safety

Environmental

The Company's commitment to managing environmental impact includes developing and offering more sustainable products to the market as well as reducing the environmental impact of its corporate activities. From continuous improvement in its manufacturing practices that reduce the use of energy to making products using industry leading high levels of recycled materials, the Company is able to improve its use of resources, its greenhouse gas emissions, and its waste streams. Our Environmental Policy, located on our web site at www.trex.com/our-company, outlines our foundational commitment to conducting business in an ethical and socially responsible manner that respects the environment. Environmental matters relevant to the Company's operations are the responsibility of members of the executive management team, including the President and Chief Executive Officer, the Executive Vice President and Chief Financial Officer, and the General Counsel.

Trex's eco-friendly composite decking products consist of a blend of 95 percent reclaimed wood and recycled plastic film. Trex uses locally sourced reclaimed wood that would otherwise end up in a landfill. An average 500-square foot composite Trex deck contains 140,000 recycled plastic bags, which makes Trex one of the largest plastic bag and polyethylene film recyclers in North America. In addition, Trex's proprietary, eco-friendly processing method minimizes greenhouse gas emissions and our bi-coastal factories reduce fuel consumption and CO₂ emissions. Almost 100 percent of our factory runoff and refuse are recycled back into the manufacturing line. Any product that does not meet quality specifications is reprocessed, which eliminates the need for landfill. In addition, it is Trex's goal to provide eco-friendly products for the architectural railing market and promote an effort for design innovation that decreases the environmental footprint.

The Company's primary resource usage consists of water, natural gas and electricity. The Company develops budgets and plans that improve shareholder return by ensuring the optimal use of each resource, which promotes resource efficiency and minimal waste of the resource. Water management is of critical importance to us and we prioritize energy savings as part of our ongoing evaluation and optimization of business operations and manufacturing processes. We ensure that all of our manufacturing facilities meet emission standards for the locality in which they operate, and certify to applicable authorities that our emissions are within the relevant locality's standards.

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Market Recognition of Trex Brand's Environmental Characteristics

The Company's internal standards for environmental stewardship and product integrity are recognized year-over-year in the marketplace. In 2016, Trex was honored as Environmental Vendor of the Year by The Home Depot. In 2018 for the eleventh year in a row, Trex secured the highest number of top spots in the Builder magazine Brand Use Study across numerous award categories. For the past 8 years, Trex has been an award recipient in the Green Builder trade magazine Readers' Choice for greenest decking brand.

Trex Residential decking products meet LEED requirements for builders and our commercial products have contributed to the LEED certifications of some high profile venues. LEED is a point-based system created in part by the U.S. Green Building Council and designed to reward points to building projects that incorporate efficient, and safe eco-friendly products, leading to a building's designation as LEED Silver, Gold or Platinum. LEED buildings attract higher demand, premium rates and longer occupancy leases, thereby supporting continued and growing demand for products that can facilitate LEED designations. As a U.S. Green Building Council member, Trex works along with council members to transform the way buildings and communities are designed, built and operated with the goal of creating environmentally and socially responsible spaces that improve the quality of life.

Trex Commercial railing products also typically contribute to LEED certification points in the Materials and Resources category based on recycled aluminum, steel, stainless steel and glass content.

Occupational Safety

The Company is committed to plan and perform all operations at all facilities in a manner that is safe for its employees, and has adopted an Occupational Health and Safety Policy, located on our web site at www.trex.com/our-company, that sets forth our commitment to sustaining a compliant and safety conscious work environment and keeping safety at the forefront of our business. The commitment is based on:

A comprehensive understanding of worker expectations and requirements;

Compliance to statutory, regulatory and other legal requirements;

Prevention considerations in all designs and redesigns of facilities, equipment, processes, work methods and products, and incorporation of safe design methods into all phases of hazard and risk mitigation;

Demonstrating employee safety leadership in all of our processes while striving for world class performance; and

Continual improvement by analyzing this commitment through the use of leading and lagging key performance indicators, such as safety observation audit completions, attendance at monthly safety training, safety work order completions, and targets related to recordable and lost time incident rates and days away or restricted time.

The Company applies industry best-practices for monitoring and reporting near misses, lost days and frequency of incidents and for implementing safety systems similar to OHSAS 18001 including:

Management leadership and employee involvement;

Worksite analysis;

Hazard prevention and control; and

Safety and health training.

The Company's Design for Safety program incorporates reviewing and building safety into every project from conception through completion, beginning with a Pre-startup Safety Review (PSSR) that ensures safety

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items are addressed. A fully empowered Plant Safety Committee performs safety audits and observations, reviews and trends all incidents, writes their own Safety Work Orders, and participates in all PSSRs. Each member is required to successfully complete an Occupational Safety and Health Training course in General Industry Safety and Health, which is sanctioned and accredited by the U.S. Department of Labor/Occupational Safety and Health Administration. In addition, each manufacturing operation has an Employee Health and Safety Manager who is a Certified Occupational Safety Specialist and Certified Occupational Safety Manager. The Company is a member of the Voluntary Protection Program Participants Association, the National Safety Council, and the National Fire Protection Association.

Web Sites and Additional Information

The U. S. Securities and Exchange Commission (SEC) maintains an Internet web site at www.sec.gov that contains reports, proxy statements, and other information regarding our Company. In addition, we maintain an Internet corporate web site at www.trex.com/our-company/investor-relations. We make available through our web site our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and all amendments to those reports, as soon as reasonably practicable after we electronically file with or furnish such material to the SEC. We do not charge any fees to view, print or access these reports on our web site. The contents of our web site are not a part of this report.

Item 1A. Risk Factors

Our business operates in two reportable segments, Trex Residential and Trex Commercial, and is subject to a number of risks, including the following:

We may not be able to grow unless we increase market acceptance of our products, compete effectively and develop new products and applications.

Our primary competition for Trex Residential products consists of wood products, which constitute a substantial majority of decking, railing, fencing, and deck framing sales. Since wood-alternative products were introduced to the market in the late 1980s, their market acceptance has increased. Our ability to grow depends, in part, on our success in continuing to convert demand for wood products into demand for wood-alternative Trex products. To increase our market share, we must overcome:

Lack of awareness of the enhanced value of wood-alternative products in general and Trex brand products in particular;

Resistance of many consumers and contractors to change from well-established wood products;

Consumer lack of awareness that the greater initial expense of Trex products compared to wood is a one-time cost that is reduced over time as Trex products have lower maintenance costs and a longer life span than wood;

Established relationships existing between suppliers of wood products and contractors and homebuilders;

Actual and perceived quality issues with first generation wood-alternative products; and

Competition from other wood-alternative manufacturers.

Our failure to compete successfully in such markets could have a material adverse effect on our ability to replace wood or increase our market share amongst wood-alternatives. Many of the conventional lumber suppliers with which we compete have established ties to the building and construction industry and have well-accepted products. Our ability to compete depends, in part, upon a number of factors outside our control, including the ability of competitors to develop new alternatives that are more competitive with Trex products.

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Our ability to identify and respond to emerging consumer demands and preferences depends, in part, on how successfully we develop, manufacture and market new products. If our products do not meet emerging demands and preferences, we could lose market share, which could have a material adverse effect on our business. In addition, substantially all of our revenues are derived from sales of our proprietary wood/polyethylene composite material. Although we have developed, and continue to develop, new products made from other materials, if we should experience significant problems, real or perceived, with acceptance of the Trex wood/polyethylene composite material, our lack of product diversification could have a significant adverse impact on our net sales levels.

Although Trex Commercial is a leading national provider of custom-engineered railing and staging systems for the commercial and multi-family market, including performing arts venues and sports stadiums, there is intense competition for projects. In order to effectively compete, we must continually produce and install high quality products and innovate with new products. If our products do not keep up with consumer trends, demands, and preferences we could lose market share, which could have a material adverse effect on our business.

We may not be able to fully maintain our wholesaler and dealer channels.

Our Trex Residential growth strategy depends on maintaining our network of wholesale and dealer channels, and on our ability to compete with other entities for these channels. In order to successfully compete for wholesaler distributors and dealers, we must accurately assess their customers' needs and preferences. If we fail to compete successfully, our business could experience material adverse effects.

Our prospects for sales growth and profitability may be adversely affected if we fail to maintain product quality and product performance at an acceptable cost.

In order to expand our net sales and sustain profitable operations we must maintain the quality and performance of our products. If we are unable to produce high-quality products at standard manufacturing rates and yields, unit costs may be higher. A lack of product performance could impede acceptance of our products in the marketplace and negatively affect our profitability. We continue to receive and settle claims and maintain a warranty reserve related to decking product produced at our Nevada facility prior to 2007 that exhibits surface flaking. We have limited our financial exposure by settling a nationwide class action lawsuit that provides that a consumer's remedy is limited to the replacement of product and a partial labor reimbursement. However, because the establishment of reserves is an inherently uncertain process involving estimates of the number of future claims and the average cost of claims, our ultimate losses may differ from our warranty reserve. Increases to the warranty reserve and payments for related claims have had a material adverse effect on our profitability and cash flows. Future increases to the warranty reserve could have a material adverse effect on our profitability and cash flows.

A number of class action lawsuits alleging defects in our products have been brought against us, all of which have been settled. In the event future lawsuits relating to alleged product quality issues are brought against us, such lawsuits may be costly and could cause adverse publicity, which in turn could result in a loss of consumer confidence in our products and reduce our sales. Product quality claims could increase our expenses, have a material adverse effect on demand for our products and decrease net sales, net income and liquidity.

Our business is subject to risks in obtaining the raw materials we use at acceptable prices.

The manufacture of our Trex Residential wood-alternative decking and railing products requires substantial amounts of wood fiber and scrap polyethylene. Our business strategy is to create a substantial cost advantage over our competitors by using scrap polyethylene. Our ability to obtain adequate supplies of wood fiber and scrap polyethylene depends on our success in developing new sources that meet our quality requirements, maintaining favorable

relationships with suppliers and managing the collection of supplies from geographically dispersed locations. In addition to wood fiber and scrap polyethylene, we also use a small percentage of other materials in

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making our products, which are sometimes subject to volatility in supply and pricing and could negatively affect our profitability. The manufacture of our Trex Commercial products requires substantial amounts of aluminum, steel, glass and wood. These materials are also sometimes subject to volatility in pricing, which could negatively affect our profitability.

Our business could suffer from the termination of significant sources of raw materials, the payment of higher prices for raw materials, the quality of available raw materials, or from the failure to obtain sufficient additional raw materials to meet planned increases in production.

Certain of our residential product customers account for a significant portion of our sales, and the loss of one or more of these customers could have an adverse effect on our business.

A limited number of our residential product customers account for a significant percentage of our sales. Specifically, sales through our 15 largest customers accounted for approximately 85.0% and 90.0% of gross sales during fiscal years 2018 and 2017, respectively.

We expect that a significant portion of our residential sales will continue to be sold through a small number of customers, and certain customers will continue to account for a significant portion of our sales. The loss of a significant customer could have a significant negative impact on our business, results of operations and financial condition.

We have limited ability to project inventory build-ups in our distribution channel that can negatively affect our sales in subsequent periods.

The seasonal nature of, and changing conditions in, our industry can result in substantial fluctuations in inventory levels of Trex Residential products carried in our two-step distribution channel. We have limited ability to precisely project inventory build-ups, which can adversely affect our net sales levels in subsequent periods. We sell to wholesale distributors, who, in turn, sell our products to local dealers. Because of the seasonal nature of the demand for our products, our distribution channel partners must forecast demand for our products, place orders for the products, and maintain Trex product inventories in advance of the prime deck-building season, which generally occurs in the latter part of the first calendar quarter through the third calendar quarter. Accordingly, our results for the second and third quarters are difficult to predict and past performance will not necessarily indicate future performance. Inventory levels respond to a number of changing conditions in our industry, including product price increases, increases in the number of competitive producers, the rapid pace of product introduction and innovation, changes in the levels of home-building and remodeling expenditures and the cost and availability of consumer credit.

The demand for our Trex Residential products is negatively affected by adverse weather conditions.

Our Trex Residential products are generally purchased shortly before installation and used in outdoor environments. As a result, there is a correlation between the amount of product we sell and weather conditions during the time they are to be installed. Adverse weather conditions may interfere with ordinary construction, delay projects or lead to cessation of construction involving our products. These interferences may shift sales to subsequent reporting periods or decrease overall sales, given the limited decking season in many locations. Prolonged adverse weather conditions could have a negative impact on our results of operations and liquidity.

We depend on third parties for transportation services and the lack of availability of transportation and/or increases in cost could materially adversely affect our business and operations.

Our business depends on the transportation of both finished goods to our distributors and the transportation of raw materials to us. We rely on third parties for transportation of these items. In particular, a significant portion of our finished goods are transported by flatbed trucks, which are occasionally in high demand (especially at the end of calendar quarters) and/or subject to price fluctuations based on market conditions and the price of fuel.

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If the required supply of transportation services is unavailable when needed, we may be unable to sell our products at full value, or at all. Similarly, if any of these providers were unavailable to deliver raw materials to us in a timely manner, we may be unable to manufacture our products in response to customer demand. This could harm our reputation, negatively impact our customer relationships and have a material adverse effect on our financial condition and results of operations. In addition, a material increase in transportation rates or fuel surcharges could have a material adverse effect on our profitability.

The demand for our products is influenced by general economic conditions and could be adversely affected by economic downturns.

The demand for Trex Residential wood-alternative decking and railing products is influenced by the general health of the economy, the level of home improvement activity and, to a much lesser extent, new home construction. These factors are affected by home equity values, credit availability and interest rates, consumer confidence, income and spending habits, employment, inflation and general economic conditions. Devaluation in home equity values can adversely affect the availability of home equity withdrawals and result in decreased home improvement spending. We cannot predict general economic conditions or the home remodeling and new home construction environment. Any economic downturn or adverse changes in any of these factors could reduce consumer income or equity capital available for spending on discretionary items, which could adversely affect the demand for our products.

The demand for Trex Commercial railing and staging system products is influenced by the general health of the economy and the level of commercial construction activity, building variances, funding availability for large public use facilities, including sports stadiums and arenas, and the construction schedules of our projects. We cannot predict general economic conditions or the commercial construction environment. Any economic downturn could negatively impact the availability of funding for commercial construction projects and the ability of our customers to engage in commercial construction activity, which could adversely affect the demand for our products.

We have significant capital invested in assets that may become obsolete or impaired and result in a charge to our earnings.

We have made and may continue to make significant capital investments to our property plant and equipment in order to improve or expand our manufacturing capabilities. These investments sometimes involve the implementation of new technology and replacement of existing equipment at our manufacturing facilities, which may result in charges to our earnings if the existing equipment is not fully depreciated. We have also made and may continue to make significant capital investments in order to acquire businesses or operations that allow us to diversify into new product markets. These investments have resulted in, and may in the future result in, the recognition of goodwill, which may result in an impairment charge to our earnings if circumstances change and reduce the fair value of the goodwill acquired below its carrying amount. Significant replacement of equipment or changes in the expected cash flows related to our assets could result in reduced earnings or cash flows in future periods.

Our ability to continue to obtain financing on favorable terms, and the level of any outstanding indebtedness, could adversely affect our financial health and ability to compete.

Our ability to continue to obtain financing on favorable terms may limit our discretion on some business matters, which could make it more difficult for us to expand, finance our operations and engage in other business activities that may be in our interest. In addition, our senior credit facility may impose operating and financial restrictions.

At certain periods during the year, we borrow significant amounts on our senior credit facility for working capital purposes. In addition, we may borrow on the senior credit facility to pursue strategic opportunities or other general

business matters. Accordingly, our future level of indebtedness could have important consequences.

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Our ability to make future principal and interest payments, borrow and repay amounts under our senior credit facility and continue to comply with our loan covenants will depend primarily on our ability to generate sufficient cash flow from operations. Our failure to comply with our loan covenants might cause our lenders to accelerate our repayment obligations under our senior credit facility, which may be declared payable immediately based on a default.

Cyberattacks and other security breaches could compromise our proprietary and confidential information which could harm our business and reputation.

In the ordinary course of our business, we generate, collect and store confidential and proprietary information, including intellectual property and business information. The secure storage, maintenance, and transmission of and access to this information is important to our operations and reputation. Computer hackers may attempt to penetrate our computer systems and, if successful, misappropriate our proprietary and confidential information including e-mails and other electronic communications. In addition, an employee, contractor, competitor, or other third party with whom we do business may attempt to obtain such information, and may purposefully or inadvertently cause a breach involving such information. While we have certain safeguards in place to reduce the risk of and detect cyber-attacks, our information technology networks and infrastructure may be vulnerable to unpermitted access by hackers or other breaches, or employee error or malfeasance. Any such compromise of our data security and access to, or public disclosure or loss of, confidential business or proprietary information could disrupt our operations, damage our reputation, provide our competitors with valuable information and subject us to additional costs, which could adversely affect our business. We also collect limited information on consumers. Although we do not collect any highly sensitive information, there is a risk that a cybersecurity attack could compromise consumer's names, addresses and other personal information.

Item 1B. Unresolved Staff Comments

None.

Item 2. Properties

We lease our corporate headquarters in Winchester, Virginia, which consists of approximately 36,000 square feet of office space, under a lease that expires in March 2025. In addition, we lease 55,047 square feet of office and storage space in Dulles, Virginia, that we do not occupy. We have sublet all of the office space in Dulles, Virginia, for the remainder of the term of the lease obligation, which expires in mid-2019.

We own approximately 92 acres of land in Winchester, Virginia and the buildings on this land. The site includes our research and development technical facility and manufacturing facility, which contains approximately 465,000 square feet of space, and outside open storage. We own approximately 37 acres of land in Fernley, Nevada and the buildings on this land. The site includes our manufacturing facility, which contains approximately 240,000 square feet of space, and outside open storage. These facilities provide adequate capacity for current and anticipated future consumer demand.

In September 2007, we suspended operations at our Olive Branch, Mississippi facility (Olive Branch facility) and consolidated all of our manufacturing operations into our Winchester and Fernley sites. In January 2016, we sold a portion of the Olive Branch facility that contained the buildings. As of the date of this report, we continue to own approximately 62 acres of undeveloped land at the Olive Branch facility.

We lease a total of approximately 1.7 million square feet of warehouse and facility space under leases with expiration dates ranging from 2019 to 2028. For information about these leases, see Note 14 to our Consolidated Financial Statements appearing elsewhere in this report. The equipment and machinery we use in our operations consist principally of plastic and wood conveying and processing equipment. We own all of our manufacturing equipment. We lease some equipment, primarily forklifts, at our facilities under operating leases.

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We regularly evaluate our various facilities and equipment and make capital investments where necessary. In 2018, we spent a total of \$33.8 million on capital expenditures, primarily related to general plant cost reduction initiatives, the purchase of certain domain names, and equipment and new product development. We estimate that our capital expenditures in 2019 will be approximately \$40 million to \$45 million. We expect to use these expenditures principally to support cost reduction initiatives, new product launches in current and adjacent categories and general business support.

Item 3. Legal Proceedings

The Company has lawsuits, as well as other claims, pending against it which are ordinary routine litigation and claims incidental to the business. Management has evaluated the merits of these lawsuits and claims, and believes that their ultimate resolution will not have a material effect on the Company's consolidated financial condition, results of operations, liquidity or competitive position.

Item 4. Mine Safety Disclosures.

Not applicable.

Table of Contents**PART II****Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities**
Market for Common Stock

Our common stock has been listed on the New York Stock Exchange (NYSE) since April 8, 1999. Between April 8, 1999 and November 22, 2009, it was listed under the symbol "TWP". Effective November 23, 2009, the symbol changed to "TREX".

Dividend Policy

We have never paid cash dividends on our common stock and our credit agreement places limitations on our ability to pay cash dividends. We intend to retain future earnings to finance the development and expansion of our business or the repurchase of our common shares and, therefore, have no current intention to pay cash dividends. However, we reconsider our dividend policy on a regular basis and may determine to pay dividends in the future.

Issuer Purchases of Equity Securities

The following table provides information relating to the purchases of our common stock during the three months ended December 31, 2018 in accordance with Item 703 of Regulation S-K:

| Period | (a) Total Number of Shares (or Units) Purchased (1) | (b) Average Price Paid per Share (or Unit) (\$) | (c) Total Number of Shares (or Units) Purchased as Part of Publicly Announced Plans or Programs (2) | (d) Maximum number of Shares (or Units) that May Yet Be Purchased Under the Plan or Program |
|--------------------------------------|--|--|--|--|
| October 1, 2018 – October 31, 2018 | 209,277 | \$ 59.07 | 209,277 | 5,340,679 |
| November 1, 2018 – November 30, 2018 | | | | 5,340,679 |
| December 1, 2018 – December 31, 2018 | | | | 5,340,649 |
| Quarter ended December 31, 2018 | 209,277 | | 209,277 | |

(1)

During the three months ended December 31, 2018, no shares were withheld by, or delivered to, the Company pursuant to provisions in agreements with recipients of restricted stock granted under the Company's 2014 Stock Incentive Plan allowing the Company to withhold, or the recipient to deliver to the Company, the number of shares having the fair value equal to tax withholding due.

- (2) On February 16, 2018, the Company's Board of Directors authorized a common stock repurchase program of up to 5.8 million shares of the Company's outstanding common stock (February 2018 Stock Repurchase Program). The February 2018 Stock Repurchase Program was publicly announced on February 21, 2018. During the three months ended December 31, 2018, the Company repurchased 209,277 shares under the February 2018 Stock Repurchase Program.

Table of Contents**Stockholder Return Performance Graph**

The following graph and table show the cumulative total stockholder return on the Company's common stock for the last five fiscal years compared to the Russell 2000 Index and the Standard and Poor's 600 Building Products Index (S&P 600 Building Products). The graph assumes \$100 was invested on December 31, 2013 in (1) the Company's common stock, (2) the Russell 2000 Index and (3) the S&P 600 Building Products, and assumes reinvestment of dividends and market capitalization weighting as of December 31, 2014, 2015, 2016, 2017 and 2018.

Comparison of Cumulative Total Return**Among Trex Company, Inc., Russell 2000 Index, and S&P 600 Building Products Index**

| | 12/31/2013 | 12/31/2014 | 12/31/2015 | 12/31/2016 | 12/31/2017 | 12/31/2018 |
|---------------------------|-------------------|-------------------|-------------------|-------------------|-------------------|-------------------|
| Trex Company, Inc. | \$ 100.00 | \$ 107.09 | \$ 95.67 | \$ 161.97 | \$ 272.59 | \$ 298.59 |
| Russell 2000 Index | \$ 100.00 | \$ 104.89 | \$ 100.26 | \$ 121.63 | \$ 139.45 | \$ 124.10 |
| S&P 600 Building Products | \$ 100.00 | \$ 99.76 | \$ 119.68 | \$ 155.32 | \$ 186.73 | \$ 147.91 |

Other Stockholder Matters

As of February 6, 2019, there were approximately 160 holders of record of our common stock, although we believe that there are a significantly larger number of beneficial owners of our common stock.

In 2018, we submitted to the NYSE in a timely manner the annual certification that our Executive Vice President and Chief Executive Officer was not aware of any violation by us of the NYSE corporate governance listing standards.

Table of Contents**Item 6. Selected Financial Data**

The following table presents selected financial data as of December 31, 2018, 2017, 2016, 2015, and 2014 for each year in the five-year period ended December 31, 2018.

The selected financial data should be read in conjunction with Management's Discussion and Analysis of Financial Condition and Results of Operations and our Consolidated Financial Statements and related notes thereto appearing elsewhere in this report.

| | Year Ended December 31, (1) | | | | |
|--|------------------------------------|-----------------|-----------------|-----------------|-------------|
| | 2018 | 2017 (2) | 2016 (3) | 2015 (4) | 2014 |
| (In thousands, except share and per share data) | | | | | |
| Statement of Comprehensive Income Data: | | | | | |
| Net sales | \$ 684,250 | \$ 565,153 | \$ 479,616 | \$ 440,804 | \$ 391,660 |
| Cost of sales | 389,356 | 321,780 | 292,521 | 285,935 | 251,464 |
| Gross profit | 294,894 | 243,373 | 187,095 | 154,869 | 140,196 |
| Selling, general and administrative expenses | 118,225 | 100,993 | 83,140 | 77,463 | 72,370 |
| Income from operations | 176,669 | 142,380 | 103,955 | 77,406 | 67,826 |
| Interest (income) expense, net | (192) | 461 | 1,125 | 619 | 878 |
| Income before income taxes | 176,861 | 141,919 | 102,830 | 76,787 | 66,948 |
| Provision (benefit) for income taxes | 42,289 | 46,791 | 34,983 | 28,689 | 25,427 |
| Net income | \$ 134,572 | \$ 95,128 | \$ 67,847 | \$ 48,098 | \$ 41,521 |
| Basic earnings per share | \$ 2.29 | \$ 1.62 | \$ 1.15 | \$ 0.77 | \$ 0.64 |
| Basic weighted average shares outstanding | 58,739,670 | 58,785,118 | 58,789,118 | 62,701,084 | 64,639,298 |
| Diluted earnings per share | \$ 2.28 | \$ 1.61 | \$ 1.15 | \$ 0.76 | \$ 0.63 |
| Diluted weighted average shares outstanding | 59,067,302 | 59,150,920 | 59,225,338 | 63,365,018 | 65,502,148 |
| Cash Flow Data: | | | | | |
| Cash provided by operating activities | \$ 138,121 | \$ 101,865 | \$ 85,293 | \$ 62,634 | \$ 58,642 |
| Cash used in investing activities | (33,733) | (86,789) | (10,202) | (23,329) | (12,873) |
| Cash used in financing activities | (29,203) | (3,226) | (62,422) | (42,854) | (39,997) |

Other Data (unaudited):

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| | | | | | |
|---|------------|------------|------------|------------|------------|
| EBITDA (non-GAAP) (5) | \$ 193,136 | \$ 159,110 | \$ 118,136 | \$ 91,701 | \$ 82,653 |
| Balance Sheet Data: | | | | | |
| Cash and cash equivalents and restricted cash | \$ 105,699 | \$ 30,514 | \$ 18,664 | \$ 5,995 | \$ 9,544 |
| Working capital | 177,450 | 86,289 | 54,264 | 38,581 | 35,787 |
| Total assets | 465,122 | 326,227 | 221,430 | 211,998 | 195,824 |
| Total debt | | | | 7,000 | |
| Total stockholder s equity | \$ 342,963 | \$ 231,250 | \$ 134,161 | \$ 116,463 | \$ 113,385 |

- 1) All common stock share and per share data in the above table are presented on a post-split basis to reflect the two-for-one stock split of our common stock in the form of a stock dividend distributed on June 18, 2018 to stockholders of record at the close of business on May 23, 2018.

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- 2) On July 31, 2017, the Company's newly-formed, wholly-owned subsidiary, Trex Commercial Products, Inc. acquired certain assets and assumed certain liabilities of Staging Concepts Acquisition, LLC. The Consolidated Financial Statements include the accounts of Trex Commercial Products, Inc. from the date of acquisition. Also, the tax legislation H.R.1, An Act to Provide for Reconciliation Pursuant to Titles II and V of the Concurrent Resolution on the Budget for Fiscal Year 2018, known as the Tax Cuts and Jobs Act (Act), was enacted on December 22, 2017. Accordingly, we have recognized the tax effects of the Act in our financial statements and related notes as of and for the year ended December 31, 2017. Deferred tax assets that existed as of the enactment date and that reversed after the Act's effective date of January 1, 2018 were adjusted to reflect the new Federal statutory tax rate of 21%. The effect of the change in tax rate on the deferred tax assets was allocated to continuing operations as a discrete item. We finalized our analysis of the Act in 2018, which did not give rise to new deferred tax amounts.
- 3) Year ended December 31, 2016 was materially affected by a pre-tax increase of \$9.8 million to the warranty reserve related to surface flaking. Also, during 2016, the Company adopted Financial Accounting Standards Board Accounting Standards Update (ASU) No. 2015-17, *Income Taxes (Topic 740): Balance Sheet Classification of Deferred Taxes*, and ASU No. 2016-09, *Compensation - Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting*. Because the Company applied ASU No. 2015-17 prospectively in the quarterly period ended December 31, 2016, prior periods have not been adjusted. As a result, in 2016 deferred tax assets are now reported net of deferred tax liabilities, included as either a non-current asset or liability, and are no longer a component of working capital. Deferred tax assets or liabilities of prior fiscal years that were previously included in current assets or current liabilities continue to be reported as a component of working capital. Adoption of ASU No. 2016-09 did not have a material impact on the Company's results of operations and financial condition or cash flows for prior periods.
- 4) Year ended December 31, 2015 was materially affected by a pre-tax increase of \$7.8 million to the warranty reserve, the majority of which related to surface flaking.
- 5) EBITDA represents net income before interest, income taxes, depreciation and amortization. EBITDA is not a measurement of financial performance under accounting principles generally accepted in the United States (GAAP). The Company has included data with respect to EBITDA because management evaluates and projects the performance of the Company's business using several measures, including EBITDA. Management considers EBITDA to be an important supplemental indicator of the Company's operating performance, particularly as compared to the operating performance of the Company's competitors, because this measure eliminates many differences among companies in capitalization and tax structures, capital investment cycles and ages of related assets, as well as some recurring non-cash and non-operating charges to net income or loss. For these reasons, management believes that EBITDA provides important supplemental information to investors regarding the operating performance of the Company and facilitates comparisons by investors between the operating performance of the Company and the operating performance of its competitors. Management believes that consideration of EBITDA should be supplemental, because EBITDA has limitations as an analytical financial measure. These limitations include the following:

EBITDA does not reflect the Company's cash expenditures, or future requirements for capital expenditures, or contractual commitments;

EBITDA does not reflect the interest expense, or the cash requirements necessary to service interest or principal payments, on the Company's indebtedness;

Although depreciation and amortization are non-cash charges, the assets being depreciated and amortized will often have to be replaced in the future, and EBITDA does not reflect any cash requirements for such replacements;

EBITDA does not reflect the effect of earnings or charges resulting from matters the Company considers not to be indicative of its ongoing operations; and

Not all entities in the Company's industry may calculate EBITDA in the same manner in which the Company calculates EBITDA, which limits its usefulness as a comparative measure.

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The Company compensates for these limitations by relying primarily on its GAAP results to evaluate its operating performance and by considering independently the economic effects of the foregoing items that are not reflected in EBITDA. As a result of these limitations, EBITDA should not be considered as an alternative to net income, as calculated in accordance with GAAP, as a measure of operating performance, nor should it be considered as an alternative to cash flows as a measure of liquidity. The following table sets forth, for the years indicated, a reconciliation of EBITDA to net income:

| | 2018 | Year Ended December 31, | | | 2014 |
|-------------------------------------|-------------------|--------------------------------|-------------------|------------------|------------------|
| | | 2017 | 2016 | 2015 | |
| | | (In thousands) | | | |
| Net income | \$ 134,572 | \$ 95,128 | \$ 67,847 | \$ 48,098 | \$ 41,521 |
| Plus interest (income) expense, net | (192) | 461 | 1,125 | 619 | 878 |
| Plus income tax provision | 42,289 | 46,791 | 34,983 | 28,689 | 25,427 |
| Plus depreciation and amortization | 16,467 | 16,730 | 14,181 | 14,295 | 14,827 |
| EBITDA (non-GAAP) | \$ 193,136 | \$ 159,110 | \$ 118,136 | \$ 91,701 | \$ 82,653 |

Table of Contents**Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations**

This management's discussion and analysis contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. All statements regarding our expected financial position and operating results, our business strategy, our financing plans, forecasted demographic and economic trends relating to our industry and similar matters are forward-looking statements. These statements can sometimes be identified by our use of forward-looking words such as may, will, anticipate, estimate, expect, intend or similar expressions. We cannot promise you that our expectations in such forward-looking statements will turn out to be correct. Our actual results could be materially different from our expectations because of various factors, including the factors discussed under Item 1A. Risk Factors. These statements are also subject to risks and uncertainties that could cause the Company's actual operating results to differ materially. Such risks and uncertainties include, but are not limited to, the extent of market acceptance of the Company's current and newly developed products; the costs associated with the development and launch of new products and the market acceptance of such new products; the sensitivity of the Company's business to general economic conditions; the impact of seasonal and weather-related demand fluctuations on inventory levels in the distribution channel and sales of the Company's products; the availability and cost of third-party transportation services for our products and raw materials; the Company's ability to obtain raw materials at acceptable prices; the Company's ability to maintain product quality and product performance at an acceptable cost; the level of expenses associated with product replacement and consumer relations expenses related to product quality; the highly competitive markets in which the Company operates; cyber-attacks, security breaches or other security vulnerabilities; and the impact of upcoming data privacy laws and the EU General Data Protection Regulation and the related actual or potential costs and consequences.

OVERVIEW

General. Trex Company, Inc. is the world's largest manufacturer of wood-alternative decking and railing products marketed under the brand name Trex® and manufactured in the United States. We offer a comprehensive set of aesthetically pleasing, high performance, low maintenance products in the decking, railing, fencing, steel deck framing and outdoor lighting categories. We believe that the range and variety of our products allow consumers to design much of their outdoor living space using Trex brand products.

We offer the following wood-alternative decking and railing products:

Decking

Trex Transcend®

Trex Enhance®

Trex Select®

Railing

Trex Transcend Railing

Trex Signature® aluminum railing

Trex Select Railing

| | |
|--|---|
| <i>Fencing</i> | Trex Seclusions® |
| <i>Steel Deck Framing System</i> | Trex Elevations® |
| <i>Outdoor Lighting Systems</i> | Trex DeckLighting Trex LandscapeLighting |
| <i>Hidden Fastening System for Specially Grooved Boards</i> | Trex Hideaway® |

In addition, we offer modular and architectural railing and staging systems and solutions for the commercial and multifamily market, including sports stadiums and performing arts venues.

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Highlights related to the twelve months ended December 31, 2018 include:

Increase in net sales of 21.1%, or \$119.1 million, to \$684.3 million in the twelve months ended December 31, 2018 compared to \$565.2 million in the twelve months ended December 31, 2017. Net sales in 2018 were the highest of any year in our history.

Increase in gross profit of 21.2%, or \$51.5 million, to \$294.9 million for the twelve months ended December 31, 2018 compared to \$243.4 million for the twelve months ended December 31, 2017. Gross profit in 2018 was the highest of any year in our history.

Net income of \$134.6 million also reflects the highest of any year in our history.

Cash flows from operating activities were \$138.1 million in the twelve months ended 2018 compared to \$101.9 million in the twelve months ended 2017 and were the highest of any year in our history.

Business Acquisition. On July 31, 2017, through our wholly-owned subsidiary, Trex Commercial Products, Inc., we entered into a definitive agreement with SC Company and on that date acquired certain assets and liabilities of SC Company for \$71.8 million in cash. We used cash on hand and \$30.0 million from our existing revolving credit facility to acquire the business. The acquisition provides us with the opportunity to offer full service railing systems in the growing commercial and multi-family markets, access to a complementary product category with a track record of substantial revenue growth, the ability to achieve economies of scale around raw material procurement, and an increase in the range of products the Company may offer its core customers. The Consolidated Financial Statements include the accounts of Trex Commercial Products, Inc. from the date of acquisition.

Net Sales. Net sales consist of sales and freight, net of returns and discounts. The level of net sales is principally affected by sales volume and the prices paid for Trex products. The operating results for Trex Residential have historically varied from quarter to quarter, often due to seasonal trends in the demand for outdoor living products. Seasonal, erratic or prolonged adverse weather conditions in certain geographic regions reduce the level of home improvement and construction activity and can shift demand for its products to a later period. As part of its normal business practice and consistent with industry practices, Trex Residential has historically offered incentive programs to its distributors and dealers to build inventory levels before the start of the prime deck-building season to ensure adequate availability of its product to meet anticipated seasonal consumer demand and to enable production planning. These incentives include prompt payment discounts and favorable payment terms. In addition, we offer price discounts or volume rebates on specified products and other incentives based on increases in purchases as part of specific promotional programs. The timing of sales incentive programs can significantly impact sales, receivables and inventory levels during the offering period. However, the timing and terms of the majority of our programs are generally consistent from year to year. In addition, the operating results for Trex Commercial have not historically varied from quarter to quarter as a result of seasonality, but are driven by the timing of individual projects, which may vary each quarterly period.

Gross Profit. Gross profit represents the difference between net sales and cost of sales. Cost of sales consists of raw materials costs, direct labor costs, manufacturing costs, warranty costs, and freight. Raw materials costs generally include the costs to purchase and transport reclaimed wood fiber, scrap polyethylene and pigmentation for coloring Trex products. Direct labor costs include wages and benefits of personnel engaged in the manufacturing process.

Manufacturing costs consist of costs of depreciation, utilities, maintenance supplies and repairs, indirect labor, including wages and benefits, and warehouse and equipment rental activities.

Selling, General and Administrative Expenses. The largest component of selling, general and administrative expenses is personnel related costs, which include salaries, commissions, incentive compensation, and benefits of personnel engaged in sales and marketing, accounting, information technology, corporate operations, research and development, and other business functions. Another component of selling, general and administrative expenses is branding and other sales and marketing costs, which are used to build brand awareness of Trex. These costs consist primarily of advertising, merchandising, and other promotional costs. Other general and

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administrative expenses include professional fees, office occupancy costs attributable to the business functions previously referenced, and consumer relations expenses. As a percentage of net sales, selling, general and administrative expenses have varied from quarter to quarter due, in part, to the seasonality of our business.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

Our significant accounting policies are described in Note 2 to our Consolidated Financial Statements appearing elsewhere in this report. Our critical accounting estimates include the areas where we have made what we consider to be particularly difficult, subjective or complex judgments in making estimates, and where these estimates can significantly affect our financial results under different assumptions and conditions. We prepare our financial statements in conformity with accounting principles generally accepted in the United States. As a result, we are required to make estimates, judgments and assumptions that we believe are reasonable based upon the information available. These estimates, judgments and assumptions affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the periods presented. Actual results could be different from these estimates.

Product Warranty. We warrant that our Trex Residential products will be free from material defects in workmanship and materials. Generally this warranty period is 25 years for residential use and 10 years for commercial use, excluding Trex Signature® Railing, which has a warranty period of 25 years for both residential and commercial use. We further warrant that Trex Transcend, Trex Enhance, Trex Select and Universal Fascia products will not fade in color more than a certain amount and will be resistant to permanent staining from food substances or mold, provided the stain is cleaned within seven days of appearance. This warranty extends for a period of 25 years for residential use and 10 years for commercial use. If there is a breach of such warranties, we have an obligation either to replace the defective product or refund the purchase price. The Company also warrants its Trex Commercial products for one to three years.

We continue to receive and settle claims for Trex Residential products manufactured at our Nevada facility prior to 2007 that exhibit surface flaking and maintain a warranty reserve to provide for the settlement of these claims. Estimating the warranty reserve for surface flaking claims requires management to estimate (1) the number of claims to be settled with payment and (2) the average cost to settle each claim.

To estimate the number of claims to be settled with payment, we utilize actuarial techniques to quantify both the expected number of claims to be received and the percentage of those claims that will ultimately require payment (collectively, elements). Estimates for these elements are quantified using a range of assumptions derived from claim count history and the identification of factors influencing the claim counts. The number of claims received has declined each year since peaking in 2009. The cost per claim varies due to a number of factors, including the size of affected decks, the availability and type of replacement material used, the cost of production of replacement material and the method of claim settlement.

We monitor surface flaking claims activity each quarter for indications that our estimates require revision. Typically, a majority of surface flaking claims received in a year are received during the summer outdoor season, which spans the second and third quarters. It has been our practice to utilize the actuarial techniques discussed above during the third quarter, after a significant portion of all claims has been received for the fiscal year and variances to annual claims expectations are more meaningful. The number of incoming claims received in the year ended December 31, 2018, was lower than the Company's expectations and considerably lower than the number of claims received in the year ended December 31, 2017, continuing the historical year-over-year decline in incoming claims. The favorable experience in incoming claims was offset, in part, by increased average settlement cost per claim experienced in the year ended December 31, 2018. The Company believes its reserve at December 31, 2018 is sufficient to cover future

surface flaking obligations and no adjustments were required in the current year.

Our analysis is based on currently known facts and a number of assumptions, as discussed above, and current expectations. Projecting future events such as the number of claims to be received, the number of claims

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that will require payment and the average cost of claims could cause the actual warranty liabilities to be higher or lower than those projected, which could materially affect our financial condition, results of operations or cash flows. We estimate that the annual number of claims received will continue to decline over time and that the average cost per claim will increase slightly, primarily due to inflation. If the level of claims received or average cost per claim differs materially from expectations, it could result in additional increases or decreases to the warranty reserve and a decrease or increase in earnings and cash flows in future periods. We estimate that a 10% change in the expected number of remaining claims to be settled with payment or the expected cost to settle claims may result in approximately a \$2.6 million change in the surface flaking warranty reserve.

The following table details surface flaking claims activity related to our residential product warranty:

| | Year Ended December 31, | | |
|---------------------------------------|--------------------------------|-------------|-------------|
| | 2018 | 2017 | 2016 |
| Claims unresolved beginning of period | 2,306 | 2,755 | 2,500 |
| Claims received (1) | 1,481 | 2,250 | 2,615 |
| Claims resolved (2) | (1,766) | (2,699) | (2,360) |
| Claims unresolved end of period | 2,021 | 2,306 | 2,755 |
| Average cost per claim (3) | \$ 2,631 | \$ 2,546 | \$ 2,639 |

- (1) Claims received include new claims received or identified during the period.
(2) Claims resolved include all claims settled with or without payment and closed during the period.
(3) Average cost per claim represents the average settlement cost of claims closed with payment during the period.
For additional information about product warranties, see Notes 2 and 19 to the Consolidated Financial Statements appearing elsewhere in this report.

Inventories. We account for inventories of our wood-alternative decking and railing products at the lower of cost (last-in, first-out, or LIFO) or market value. At December 31, 2018, the excess of the replacement cost of inventory over the LIFO value of inventory was approximately \$18.4 million. Inventories for our railing and staging products are accounted for at the lower of cost (first-in, first-out method) and net realizable value. We believe that our current inventory of finished goods will be saleable in the ordinary course of business and, accordingly, have not established significant reserves for estimated slow moving products or obsolescence.

Goodwill. The Company evaluates the recoverability of goodwill in accordance with Accounting Standard Codification Topic 350, *Intangibles Goodwill and Other*, annually or more frequently if an event occurs or circumstances change in the interim that would more likely than not reduce the fair value of the asset below its carrying amount. Goodwill is considered to be impaired when the net book value of the reporting unit exceeds its estimated fair value. The Company first assesses qualitative factors to determine if it is more likely than not that the fair value of the reporting unit is less than its carrying amount to determine if it should proceed with the evaluation of goodwill for impairment. If the Company proceeds with the two-step impairment test, the Company first compares the fair value of the reporting unit to its carrying value. If the carrying value of a reporting unit exceeds its fair value, the goodwill of that reporting unit is potentially impaired and step two of the impairment analysis is performed. In step two of the analysis, an impairment loss is recorded equal to the excess of the carrying value of the reporting unit's goodwill over its implied fair value should such a circumstance arise. The Company measures fair value of the

reporting unit based on a present value of future discounted cash flows and a market valuation approach.

Revenue Recognition

Effective January 1, 2018, we adopted the requirements of Financial Accounting Standards Board Accounting Standards Update 2014-09, *Revenue from Contracts with Customers* (Topic 606). We determined

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the appropriate revenue recognition for our contracts with customers by analyzing the type, terms and conditions of our contracts with our customers. Topic 606 provides a single, comprehensive model for revenue recognition arising from contracts with customers. A performance obligation is a promise in a contract to transfer a distinct good or service to the customer and is the unit of account in Topic 606. A contract's transaction price is allocated to each distinct performance obligation and revenue is recognized when or as the Company satisfies the performance obligation. Revenue is recognized at an amount that reflects the consideration to which the entity expects to be entitled in exchange for transferring control of the goods or services to a customer. Adoption of Topic 606 did not have an impact on the Company's financial condition or results of operations. The following provides additional information about our contracts with customers.

Trex Residential Products

Trex Residential principally generates revenue from the manufacture and sale of its high performance, low maintenance composite decking and railing products and accessories. Substantially all of its revenues are from contracts with customers, which are individual customer purchase orders of short-term duration of less than one year. Trex Residential satisfies its performance obligations at a point in time. The shipment of each product is a separate performance obligation as the customer is able to derive benefit from each product shipped and no performance obligation remains after shipment. Upon shipment of the product, the customer obtains control over the distinct product and Trex Residential satisfies its performance obligation. Any performance obligation that remains unsatisfied at the end of a reporting period is part of a contract that has an original expected duration of one year or less. Any variable consideration related to the unsatisfied performance obligation is allocated wholly to the unsatisfied performance obligation and recognized when the product ships and the performance obligation is satisfied.

Trex Commercial Products

Trex Commercial generates revenue from the manufacture and sale of its modular and architectural railing and staging systems. All of its revenues are from fixed-price contracts with customers. Trex Commercial contracts have a single performance obligation as the promise to transfer the individual goods or services is not separately identifiable from other promises in the contract and is, therefore, not distinct.

Trex Commercial satisfies its performance obligation over time as work progresses because control is transferred continuously to its customers. Revenue and estimated profit is recognized over time based on the proportion of actual costs incurred to date relative to total estimated costs at completion to measure progress toward satisfying the performance obligation. Incurred costs represent work performed, which corresponds with, and thereby best depicts, the transfer of control to the customer. Incurred costs include all direct material, labor, subcontract and certain indirect costs. The Company reviews and updates its estimates regularly and recognizes adjustments in estimated profit on contracts under the cumulative catch-up method. Under this method, the impact of the adjustment on revenue and estimated profit to date on a contract is recognized in the period the adjustment is identified. Revenues and profits in future periods are recognized using the adjusted estimate. If at any time the estimate of contract profitability indicates an anticipated loss on the contract, the Company recognizes the total loss in the period it is identified. During the year ended December 31, 2018, no adjustment to any one contract was material to the Company's Consolidated Financial Statements and no impairment loss on any contract was recorded.

Income Taxes. We recognize deferred tax assets and liabilities based on the difference between the financial statement basis and tax basis of assets and liabilities using enacted tax rates in effect during the year in which it is expected that the differences reverse. We assess the likelihood that our deferred tax assets will be realized. Deferred tax assets are reduced by a valuation allowance when, after considering all available positive and negative evidence, it is determined that it is more likely than not that some portion, or all, of the deferred tax asset will not be realized. On December 22,

2017, the tax legislation H.R.1, An Act to Provide for Reconciliation Pursuant to Titles II and V of the Concurrent Resolution on the Budget for Fiscal Year 2018,

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known as the Tax Cuts and Jobs Act (Act), was enacted. The Act reduces the corporate tax rate to 21 percent, effective January 1, 2018. Accordingly, we recognized the tax effects of the Act in our financial statements and related notes as of and for the year ended December 31, 2017. The Company has finalized its analysis of the Act, which did not give rise to new deferred tax amounts. As of December 31, 2018, we have a valuation allowance of \$3.0 million against the deferred tax assets related to state tax credits we estimate will expire before they are realized. We will analyze our position in subsequent reporting periods, considering all available positive and negative evidence, in determining the expected realization of our deferred tax assets.

RESULTS OF OPERATIONS

Below we have included a discussion of our operating results and material changes in our operating results for the years ended December 31, 2018 compared to December 31, 2017, and December 31, 2017 compared to December 31, 2016.

Year Ended December 31, 2018 Compared To Year Ended December 31, 2017**Net Sales**

| | Year Ended December 31, 2018 | 2017 (dollars in thousands) | \$ Change | % Change |
|----------------------------|---------------------------------|--------------------------------|--------------|----------|
| Total net sales | \$ 684,250 | \$ 565,153 | \$ 119,097 | 21.1% |
| Trex Residential net sales | \$ 613,229 | \$ 543,346 | \$ 69,883 | 12.9% |
| Trex Commercial net sales | \$ 71,021 | \$ 21,807 | \$ 49,214 | 225.7% |

The 21.1% increase in net sales in the year ended 2018 compared to the year ended 2017 was due primarily to volume growth reflecting strong consumer demand for Trex branded residential decking and railing products and favorable market conditions. The volume growth was positively impacted by continued strength in the remodeling sector, our marketing programs aimed at taking market share from wood, and the healthy demand across our full suite of outdoor living products. The increase in net sales was offset by a \$6 million charge in the third quarter related to the expansion of stocking positions in all residential sales channels beginning in 2019. Residential net sales growth excluding the \$6 million totaled 14%. The remaining increase in total net sales in the year ended 2018 was from a full year of operations of Trex Commercial that was acquired in July 2017.

Gross Profit

| | Year Ended December 31, 2018 | 2017 (dollars in thousands) | \$ Change | % Change |
|----------------------|---------------------------------|--------------------------------|--------------|----------|
| Cost of sales | \$ 389,356 | \$ 321,780 | \$ 67,576 | 21.0% |
| % of total net sales | 56.9% | 56.9% | | |
| Gross profit | \$ 294,894 | \$ 243,373 | \$ 51,521 | 21.2% |
| Gross margin | 43.1% | 43.1% | | |

Gross profit as a percentage of total net sales, gross margin, was unchanged in the year ended 2018 compared to the year ended 2017. Gross margin for Trex Residential and Trex Commercial totaled 45.6% and 21.8%, respectively.

Excluding the \$6 million charge discussed above in Net Sales, Trex Residential gross margin was 46.1% in the year ended 2018, an increase of 1.8%, over the year ended 2017, resulting from our ability to identify, qualify and procure new lower cost recycling product streams, manufacturing efficiencies that are part of ongoing programs, and higher capacity utilization. Trex Commercial gross margin increased 9.3% due to improved execution and cost reduction initiatives. During the three months ended December 31, 2018, cost of sales at Trex Residential products increased approximately \$0.7 million due to initial start-up manufacturing

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expenses related to new products introduced in the latter part of 2018. In addition, project completion costs at Trex Commercial increased approximately \$1.8 million primarily related to contracts executed prior to our acquisition of SC Company in July 2017.

Selling, General and Administrative Expenses

| | Year Ended December 31, | | | |
|--|--------------------------------|-------------|------------------|-----------------|
| | 2018 | 2017 | \$ Change | % Change |
| | (dollars in thousands) | | | |
| Selling, general and administrative expenses | \$ 118,225 | \$ 100,993 | \$ 17,232 | 17.1% |
| % of total net sales | 17.3% | 17.9% | | |

The \$17.2 million increase in selling, general and administrative expenses in the year ended 2018 compared to the year ended 2017 resulted primarily from a \$4.3 million increase in personnel related expenses at Trex Commercial due to a full year of operations, a \$4.0 million increase in branding and advertising spend in support of our market growth strategies, \$2.7 million increase in incentive and stock compensation due to higher net sales, \$2.6 million increase in medical insurance, and a \$1.1 million increase in amortization expense related to the intangible assets of our commercial operation that was acquired during 2017. In the latter part of 2018, the Company incurred \$1.5 million in research and development expense related to the development of new products. As a percentage of net sales, total selling, general and administrative expenses decreased 0.6% in the year ended 2018 compared to the year ended 2017.

Provision for Income Taxes

| | Year Ended December 31, | | | |
|----------------------------|--------------------------------|-------------|------------------|-----------------|
| | 2018 | 2017 | \$ Change | % Change |
| | (dollars in thousands) | | | |
| Provision for income taxes | \$ 42,289 | \$ 46,791 | \$ (4,502) | (9.6)% |
| Effective tax rate | 23.9% | 33.0% | | |

We have recognized the tax effects of the Tax Cuts and Jobs Act in our financial statements and related notes as of and for the year ended December 31, 2017. Deferred tax assets that existed as of the enactment date and that reversed after the Act's effective date of January 1, 2018 were adjusted to reflect the new Federal statutory tax rate of 21%. The effect of the change in tax rate on the deferred tax assets and deferred tax liabilities resulted in a tax benefit of \$1.9 million for the year ended December 31, 2017, which was allocated to continuing operations. We finalized our calculation, which did not give rise to new deferred tax amounts. The effective tax rate for the year ended 2018 decreased by 9.1% compared to the effective tax rate for the year ended 2017 primarily due to enactment of the Tax cuts and Jobs Act.

Net Income and Earnings Before Interest, Taxes, Depreciation and Amortization (EBITDA)¹ (in thousands)

Reconciliation of net income (GAAP) to EBITDA (non-GAAP):

Year Ended December 31

| | 2018 Trex Residential | 2018 Trex Commercial | 2018 Consolidated |
|--------------------------------|--------------------------------------|-------------------------------------|------------------------------|
| Net income | \$ 131,823 | \$ 2,749 | \$ 134,572 |
| Interest (income) expense, net | (192) | | (192) |
| Taxes | 41,421 | 868 | 42,289 |
| Depreciation and amortization | 13,216 | 3,251 | 16,467 |
| EBITDA | \$ 186,268 | \$ 6,868 | \$ 193,136 |

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| Year Ended December 31 | 2017 Trex Residential | 2017 Trex Commercial | 2017 Consolidated |
|-------------------------------|--------------------------------------|-------------------------------------|------------------------------|
| Net income | \$ 97,412 | \$ (2,284) | \$ 95,128 |
| Interest | 461 | | 461 |
| Taxes | 47,911 | (1,120) | 46,791 |
| Depreciation and amortization | 14,598 | 2,132 | 16,730 |
| EBITDA | \$ 160,382 | \$ (1,272) | \$ 159,110 |

| | Year Ended December 31, | | \$ | % Change |
|-------------------------|------------------------------------|-------------|---------------|-----------------|
| | 2018 | 2017 | Change | |
| | (dollars in thousands) | | | |
| Total EBITDA | \$ 193,136 | \$ 159,110 | \$ 34,026 | 21.4% |
| Trex Residential EBITDA | \$ 186,268 | \$ 160,382 | \$ 25,886 | 16.1% |
| Trex Commercial EBITDA | \$ 6,868 | \$ (1,272) | \$ 8,140 | N/A |

The Company uses EBITDA to assess performance as it believes EBITDA facilitates performance comparison between its reportable segments by eliminating interest, income taxes, and depreciation and amortization charges to net income. Total EBITDA improved by 21.4% to \$193.1 million in the year ended 2018 compared to \$159.1 million in the year ended 2017. The improvement was driven by a \$25.9 million increase in Trex Residential EBITDA resulting primarily from higher net sales, which were offset by a \$6 million charge to residential net sales related to the expansion of stocking positions in all residential sales channels beginning in 2019, and improved execution and cost reduction initiatives in Trex Commercial during the year ended 2018, coupled with a full year of operations in 2018.

Year Ended December 31, 2017 Compared To Year Ended December 31, 2016**Net Sales**

| | Year Ended December 31, | | \$ | % Change |
|----------------------------|--------------------------------|-------------|---------------|-----------------|
| | 2017 | 2016 | Change | |
| | (dollars in thousands) | | | |
| Total net sales | \$ 565,153 | \$ 479,616 | \$ 85,537 | 17.8% |
| Trex Residential net sales | \$ 543,346 | \$ 479,616 | \$ 63,730 | 13.3% |
| Trex Commercial net sales | \$ 21,807 | \$ | \$ 21,807 | |

The 17.8% increase in net sales in the year ended 2017 compared to the year ended 2016 was due primarily to the \$63.7 million increase in net sales of our Trex branded decking and railing products. This increase in Trex Residential net sales was positively impacted by continued strength in the remodeling sector, our marketing programs aimed at taking market share from wood, and the healthy demand across our full suite of outdoor living products with decking and railing products as the major growth contributors. The remaining increase resulted from the \$21.8 million in net sales contributed by our recently acquired Trex Commercial products operation for the period from the date of acquisition of July 31, 2017 through year end.

Gross Profit

| | Year Ended December 31, | | \$ | |
|----------------------|------------------------------------|-------------|---------------|-----------------|
| | 2017 | 2016 | Change | % Change |
| | (dollars in thousands) | | | |
| Cost of sales | \$ 321,780 | \$ 292,521 | \$ 29,259 | 10.0% |
| % of total net sales | 56.9% | 61.0% | | |
| Gross profit | \$ 243,373 | \$ 187,095 | \$ 56,278 | 30.1% |
| Gross margin | 43.1% | 39.0% | | |

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Gross profit as a percentage of total net sales, gross margin, increased to 43.1% in the year ended 2017 from 39.0% in the year ended 2016, an improvement of 4.1%. Gross profit in the year ended 2016 included a \$9.8 million increase to the warranty reserve related to surface flaking of our residential product. Excluding this charge, the gross margin for the year ended 2017 increased by 2.0%, reflecting cost reduction initiatives, lower cost raw materials, and increased capacity utilization at our Trex branded decking and railing plants.

Selling, General and Administrative Expenses

| | Year Ended December 31, | | | |
|--|--------------------------------|-------------|------------------|-----------------|
| | 2017 | 2016 | \$ Change | % Change |
| | (dollars in thousands) | | | |
| Selling, general and administrative expenses | \$ 100,993 | \$ 83,140 | \$ 17,853 | 21.5% |
| % of total net sales | 17.9% | 17.3% | | |

The \$17.9 million increase in selling, general and administrative expenses in the year ended 2017 compared to the year ended 2016 resulted primarily from a \$6.4 million increase in personnel related expenses resulting from the SC Company acquisition and an increase in incentive compensation, a \$6.2 million increase in branding and advertising spend in support of our market growth strategies, and a \$2.0 million increase in amortization expense related to the intangible assets of our commercial operation that was acquired during 2017. As a percentage of net sales, total selling, general and administrative expenses increased a minimal 0.6% in the year ended 2017 compared to the year ended 2016.

Provision for Income Taxes

| | Year Ended December 31, | | | |
|----------------------------|--------------------------------|-------------|------------------|-----------------|
| | 2017 | 2016 | \$ Change | % Change |
| | (dollars in thousands) | | | |
| Provision for income taxes | \$ 46,791 | \$ 34,983 | \$ 11,808 | 33.8% |
| Effective tax rate | 33.0% | 34.0% | | |

We have recognized the tax effects of the Tax Cuts and Jobs Act in our financial statements and related notes as of and for the year ended December 31, 2017. Deferred tax assets that existed as of the enactment date and that are expected to reverse after the Act's effective date of January 1, 2018 have been adjusted to reflect the new Federal statutory tax rate of 21%. The effect of the change in tax rate on the deferred tax assets and deferred tax liabilities resulted in a tax benefit of \$1.9 million for the year ended December 31, 2017, which was allocated to continuing operations. We continue to analyze certain aspects of the Act and refine our calculation, which could potentially affect the measurement of these balances or give rise to new deferred tax amounts. The effective tax rate for the year ended 2017 decreased by 1.0% compared to the effective tax rate for the year ended 2016 primarily due to enactment of the Tax cuts and Jobs Act and the resulting revaluation of deferred tax assets and liabilities. The Company expects its effective tax rate will decrease in future periods primarily due to the tax effects of the lower Federal statutory rate of 21%, which may be offset by and other changes in the Tax Cuts and Jobs Act, such as the elimination of the domestic manufacturing deduction.

Table of Contents**Net Income and Earnings Before Interest, Taxes, Depreciation and Amortization (EBITDA)¹ (in thousands)**

Reconciliation of net income (GAAP) to EBITDA (non-GAAP):

| Year Ended December 31 | 2017 Trex Residential | 2017 Trex Commercial | 2017 Consolidated | 2016 Consolidated |
|-------------------------------|--------------------------------------|-------------------------------------|------------------------------|------------------------------|
| Net income | \$ 97,412 | \$ (2,284) | \$ 95,128 | \$ 67,847 |
| Interest | 461 | | 461 | 1,125 |
| Taxes | 47,911 | (1,120) | 46,791 | 34,983 |
| Depreciation and amortization | 14,598 | 2,132 | 16,730 | 14,181 |
| EBITDA | \$ 160,382 | \$ (1,272) | \$ 159,110 | \$ 118,136 |

| | Year Ended December 31, | | \$ | % |
|-------------------------|--------------------------------|-------------|---------------|---------------|
| | 2017 | 2016 | Change | Change |
| | (dollars in thousands) | | | |
| Total EBITDA | \$ 159,110 | \$ 118,136 | \$ 40,974 | 34.7% |
| Trex Residential EBITDA | \$ 160,382 | \$ 118,136 | \$ 42,246 | 35.8% |
| Trex Commercial EBITDA | \$ (1,272) | \$ | \$ (1,272) | |

The Company uses EBITDA to assess performance as it believes EBITDA facilitates performance comparison between its reportable segments by eliminating interest, taxes, and depreciation and amortization charges to income. Total EBITDA increased 34.7% to \$159.1 million for the year ended 2017 compared to \$118.1 million for the year ended 2016. The increase in total EBITDA resulted primarily from the increase in Trex Residential EBITDA. The increase in Trex Residential EBITDA was driven by increased net sales resulting primarily from volume growth of our Trex branded decking and railing products. The slight decrease in total EBITDA resulted from Trex Commercial EBITDA, our recently acquired commercial products operation, for the period from the date of acquisition of July 31, 2017 through December 31, 2017, which resulted primarily from the effects of lower margins on certain legacy contracts and \$0.5 million in acquisition related expenses.

LIQUIDITY AND CAPITAL RESOURCES

We finance operations and growth primarily with cash flow from operations, borrowings, operating leases and normal trade credit terms from operating activities.

Sources and Uses of Cash. The following table summarizes our cash flows from operating, investing and financing activities for the years ended December 31, 2018, 2017, and 2016 (in thousands):

| | Year Ended December 31, | | |
|---|--------------------------------|-------------|-------------|
| | 2018 | 2017 | 2016 |
| Net cash provided by operating activities | \$ 138,121 | \$ 101,865 | \$ 85,293 |
| Net cash used in investing activities | (33,733) | (86,789) | (10,202) |

| | | | |
|---|-----------|-----------|-----------|
| Net cash used in financing activities | (29,203) | (3,226) | (62,422) |
| Net increase in cash and cash equivalents | \$ 75,185 | \$ 11,850 | \$ 12,669 |

Operating Activities

Net cash provided by operating activities increased by \$36.3 million in 2018 compared to 2017 primarily due to the \$51.5 million increase in gross margin resulting from the \$119.1 million increase in net sales, and the \$26.2 million increase in accounts payable and accrued expenses. The increase was offset primarily by the increase in accounts receivable and inventories at December 31, 2018 of \$24.3 million and \$23.3 million, respectively.

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Net cash provided by operating activities increased by \$16.6 million in 2017 compared to 2016 primarily due to the \$23.2 million, or 17.8%, increase in net sales during in 2017 coupled with the 4.1% increase in gross margin. The increase was primarily offset by the increase in accounts receivable at December 31, 2017 of \$10.5 million.

Investing Activities

Investing activities in 2018 consisted principally of capital expenditures directed to new product development and to quick return cost investments to capture manufacturing cost savings. These investments allow us to meet the market's increased demand and corresponding volume requirements resulting in greater profitability and cash flow. Capital expenditures in 2018 were \$33.8 million consisting primarily of \$19.2 million for general plant cost reduction initiatives, \$6.3 million for the purchase of certain domain names, and \$4.7 million for equipment and new product development.

On July 31, 2017, through its newly-formed, wholly-owned subsidiary, Trex Commercial Products, Inc., the Company acquired certain assets and assumed certain liabilities of SC Company for \$71.8 million in cash. The Company used cash on hand and \$30 million of funding from its existing revolving credit facility to acquire the assets. Capital expenditures in 2017 were \$15.0 million consisting primarily of \$10.8 million for general plant cost reduction initiatives and \$3.0 million for equipment and new product development.

Financing Activities

Net cash used in financing activities in 2018 increased \$26.0 million compared to 2017 primarily due to the \$30.1 million in stock repurchase activity in 2018.

Net cash used in financing activities in 2017 decreased \$59.2 million compared to 2016 primarily due to the \$55.2 million in stock repurchase activity in 2016.

Stock Repurchase Programs.

On October 22, 2015, our Board of Directors adopted a stock repurchase program of up to 3.15 million shares of our outstanding common stock (October 2015 Stock Repurchase Program). In 2016, we repurchased 1,578,952 shares for \$53.3 million under the October 2015 Stock Repurchase Program. This authorization terminated on December 31, 2016.

On February 16, 2017, the Board of Directors authorized a common stock repurchase program of up to 2.961 million shares of our outstanding common stock (February 2017 Stock Repurchase Program). The Company made no repurchases under the February 2017 Stock Repurchase Program. On February 16, 2018, the Board of Directors terminated the February 2017 Stock Repurchase Program and adopted a new stock repurchase program of up to 5.8 million shares of the Company's outstanding common stock (February 2018 Stock Repurchase Program). As of the date of this report, the Company has repurchased 459,321 shares under the February 2018 Stock Repurchase Program.

Inventory in Distribution Channels. We sell our decking and residential railing products through a tiered distribution system. We have over 50 distributors worldwide and two national retail merchandisers to which we sell our products. The distributors in turn sell the products to dealers and retail locations who in turn sell the products to end users. Significant increases in inventory levels in the distribution channel without a corresponding change in end-use demand could have an adverse effect on future sales. We cannot definitively determine the level of inventory in the distribution channels at any time. We are not aware of significant changes in the levels of inventory in the distribution channels at December 31, 2018 compared to inventory levels at December 31, 2017.

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Product Warranty. We continue to receive and settle claims related to Trex Residential products manufactured at our Nevada facility prior to 2007 that exhibit surface flaking, which has had a material adverse effect on cash flow from operations, and regularly monitor the adequacy of the warranty reserve. In 2018 and 2017 we paid \$4.2 million and \$5.7 million, respectively, to settle surface flaking claims. We estimate that the number of claims received will continue to decline over time and that the average settlement cost per claim will increase slightly, primarily due to inflation. If the level of claims received or average settlement cost per claim differs materially from our expectations, it could result in additional increases or decreases to the warranty reserve and a decrease or increase in earnings and cash flow in future periods.

Business Acquisition. On July 31, 2017, through our wholly-owned subsidiary, Trex Commercial Products, Inc., we entered into a definitive agreement with SC Company and on that date acquired certain assets and liabilities of SC Company for \$71.8 million in cash. We used cash on hand and \$30.0 million from our existing revolving credit facility to acquire the business.

Seasonality. The operating results for Trex Residential have historically varied from quarter to quarter. Seasonal, erratic or prolonged adverse weather conditions in certain geographic regions reduce the level of home improvement and construction activity and can shift demand for its products to a later period. As part of its normal business practice and consistent with industry practice, Trex Residential has historically offered incentive programs to its distributors and dealers to build inventory levels before the start of the prime deck-building season in order to ensure adequate availability of its product to meet anticipated seasonal consumer demand. The seasonal effects are often offset by the positive effect of the incentive programs. The operating results for Trex Commercial have not historically varied from quarter to quarter as a result of seasonality; however, they are driven by the timing of individual projects, which may vary each quarterly period.

Indebtedness. On January 12, 2016, the Company entered into a Third Amended and Restated Credit Agreement and also the First Amendment to the Third Amended and Restated Credit Agreement (together, the Third Amended Credit Agreement) with Bank of America, N.A. (BOA) as Lender, Administrative Agent, Swing Line Lender and Letter of Credit Issuer; and certain other lenders including Citibank, N.A., Capital One, N.A., and SunTrust Bank (collectively, Lenders) arranged by Bank of America Merrill Lynch as Sole Lead Arranger and Sole Bookrunner. The Third Amended Credit Agreement amended and restated the Second Amended Credit Agreement.

Under the Third Amended Credit Agreement, the Lenders agree to provide the Company with one or more revolving loans in a collective maximum principal amount of \$250 million from January 1 through June 30 of each year and a maximum principal amount of \$200 million from July 1 through December 31 of each year throughout the term, which ends January 12, 2021. Included within the revolving loan limit are sublimits for a letter of credit facility in an amount not to exceed \$15 million and swing line loans in an aggregate principal amount at any time outstanding not to exceed \$5 million. The revolving loans, the letter of credit facility and the swing line loans are for the purpose of funding working capital needs and supporting general business operations.

The Company has the option to select interest rates for each loan request at the Base Rate or Eurodollar Rate. Base rate loans under the revolving loans and the swing line loans accrue interest at the Base Rate plus the Applicable Rate. Eurodollar Rate Loans for the revolving loans and swing line loans accrue interest at the Adjusted London InterBank Offered Rate plus the Applicable Rate. The Base Rate for any day is a fluctuating rate per annum equal to the highest of (a) the Federal Funds Rate plus 0.50%, (b) the rate of interest in effect for such day as publicly announced from time to time by BOA as its prime rate, and (c) the Eurodollar Rate plus 1.0%.

Repayment of all then outstanding principal, interest, fees and costs is due on January 12, 2021.

The Company will reimburse BOA for all amounts payable, including interest, under a letter of credit at the earlier of (i) the date set forth in the application, or (ii) one business day after the payment under such letter of credit by BOA.

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The Third Amended Credit Agreement is secured by property with respect to which liens in favor of the Administrative Agent, for the benefit of itself and the other holders of the obligations, are purported to be granted pursuant to and in accordance with the terms of the collateral documents as referenced in the Third Amended Credit Agreement.

At December 31, 2018, the Company had no outstanding borrowings under the Third Amended Credit Agreement and \$200 million of available borrowing capacity.

Compliance with Debt Covenants and Restrictions. Our ability to make scheduled principal and interest payments, borrow and repay amounts under any outstanding revolving credit facility and continue to comply with any loan covenants depends primarily on our ability to generate sufficient cash flow from operations. To remain in compliance with financial covenants, we are required to maintain specified financial ratios based on levels of debt, fixed charges, and earnings (excluding extraordinary gains and extraordinary non-cash losses) before interest, taxes, depreciation and amortization, all of which are subject to the risks of the business, some of which are discussed in this report under Risk Factors. We were in compliance with all covenants contained in the Third Amended Credit Agreement at December 31, 2018. Failure to comply with the financial covenants could be considered a default of our repayment obligations and, among other remedies, could accelerate payment of any amounts outstanding.

Contractual Obligations. The following tables show, as of December 31, 2018, our contractual obligations and commercial commitments, which consist primarily of purchase commitments and operating leases (in thousands):

Contractual Obligations**Payments Due by Period**

| | Total | 1 year | 2-3 years | 4-5 years | After 5 years |
|---|------------------|------------------|------------------|------------------|--------------------------|
| Purchase commitments (1) | \$ 26,602 | \$ 18,971 | \$ 7,631 | \$ | \$ |
| Operating leases | 61,824 | 10,998 | 18,269 | 13,477 | 19,080 |
| Total contractual cash obligations | \$ 88,426 | \$ 29,969 | \$ 25,900 | \$ 13,477 | \$ 19,080 |

(1) Purchase commitments represent supply contracts with raw material vendors. Open purchase orders written in the normal course of business for goods or services that are provided on demand have been excluded as the timing of which is not certain.

Off-Balance Sheet Arrangements. We do not have off-balance sheet financing arrangements other than operating leases.

Capital and Other Cash Requirements. We currently estimate that capital expenditures in 2019 will be approximately \$40 million to \$45 million. Our capital allocation priorities include expenditures for internal growth opportunities, manufacturing cost reductions, acquisitions which fit our long-term outdoor products growth strategy as we continue to evaluate opportunities that would be a good strategic fit for Trex, and return of capital to shareholders.

We believe that cash on hand, cash flows from operations and borrowings expected to be available under our revolving credit facility will provide sufficient funds to enable us to fund planned capital expenditures, make scheduled principal and interest payments, fund the warranty reserve, meet other cash requirements and maintain compliance with terms of our debt agreements for at least the next 12 months. We currently expect to fund future capital expenditures from operations and borrowings under the revolving credit facility. The actual amount and timing of future capital requirements may differ materially from our estimate depending on the demand for Trex

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and new market developments and opportunities. Our ability to meet our cash needs during the next 12 months and thereafter could be adversely affected by various circumstances, including increases in raw materials and product replacement costs, quality control problems, higher than expected product warranty claims, service disruptions and lower than expected collections of accounts receivable. In addition, any failure to negotiate amendments to our existing debt agreements to resolve any future noncompliance with financial covenants could adversely affect our liquidity by reducing access to revolving credit borrowings needed primarily to fund seasonal borrowing needs. We may determine that it is necessary or desirable to obtain financing through bank borrowings or the issuance of debt or equity securities to address such contingencies or changes to our business plan. Debt financing would increase our level of indebtedness, while equity financing would dilute the ownership of our stockholders. There can be no assurance as to whether, or as to the terms on which, we would be able to obtain such financing, which would be restricted by covenants contained in our existing debt agreements.

NEW ACCOUNTING STANDARDS

In June 2018, the FASB issued ASU No. 2018-07, *Compensation – Stock Compensation (Topic 718)*. The ASU expands the scope of Topic 718, which currently only includes share-based payments issued to employees, to also include share-based payments issued to nonemployees for goods or services. The ASU supersedes Subtopic 505-50, *Equity – Equity-Based Payment to Non-Employees*. Consequently, the accounting for share-based payments to nonemployees and employees will be substantially aligned. The ASU is effective for fiscal years beginning after December 15, 2018, including interim periods within that fiscal year. Early adoption is permitted. The Company intends to adopt the guidance on January 1, 2019 and does not believe adoption will have a material impact on its financial condition or results of operations.

In January 2017, the FASB issued ASU No. 2017-04, *Intangibles – Goodwill and Other (Topic 350), Simplifying the Test for Goodwill Impairment*. The guidance removes Step 2 of the goodwill impairment test and eliminates the need to determine the fair value of individual assets and liabilities to measure goodwill impairment. A goodwill impairment will now be the amount by which a reporting unit's carrying value exceeds its fair value, not to exceed the carrying amount of goodwill. Entities will continue to have the option to perform a qualitative assessment to determine if a quantitative impairment test is necessary. The guidance will be applied prospectively, and is effective for annual and interim goodwill impairment tests in fiscal years beginning after December 15, 2019. Early adoption is permitted for any impairment tests performed on testing dates after January 1, 2017. The Company intends to adopt the guidance on January 1, 2020 and does not believe adoption will have a material impact on its financial condition or results of operations.

In February 2016, the FASB issued ASU No. 2016-02, *Leases (Topic 842)*, and issued subsequent amendments to the initial guidance in January 2018 within ASU No. 2018-01 and in July 2018 within ASU Nos. 2018-10 and 2018-11. The standard requires lessees to recognize leases on the balance sheet as a right-of-use asset and a lease liability, other than leases that meet the definition of a short-term lease. The liability will be equal to the present value of the lease payments. The asset will be based on the liability, subject to adjustment. Currently, under existing U.S. generally accepted accounting principles, the Company does not recognize on the balance sheet a right-of-use asset or lease liability related to its operating leases. For income statement purposes, the leases will continue to be classified as either operating or finance. Operating leases will result in straight-line expense (similar to current operating leases) and finance leases will result in a front-loaded expense pattern (similar to current capital leases). The standard is effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2018. Early adoption is permitted. The standard allows an entity to elect to have a date of initial application as of the beginning of the period of adoption. The standard provides for the option to elect a package of practical expedients upon adoption. The Company intends to adopt the standard on January 1, 2019, and is currently planning on electing the package of practical expedients to not reassess prior conclusions related to contracts containing leases, lease classification and

initial direct costs and is evaluating the other practical expedients available under the guidance. The Company expects expanded financial statement note disclosure in addition to recognizing a right-of-use asset and lease liability for its operating leases on the balance sheet. Based on leases outstanding at December 31, 2018, the Company estimates the operating lease right of use

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asset and lease liability would have been in the range of \$45 million to \$50 million. The Company continues to evaluate the impacts of the pending adoption. As such, the Company's preliminary assessments are subject to change.

Item 7A. Quantitative and Qualitative Disclosures About Market Risk

We are subject to market risks from changing interest rates associated with our borrowings. To meet our seasonal working capital needs, we borrow periodically on our variable rate revolving line of credit. At December 31, 2018, we had no debt outstanding under our revolving line of credit. While variable rate debt obligations expose us to the risk of rising interest rates, an increase of 1% in interest rates would not have a material adverse effect on our overall financial position, results of operations or liquidity.

In certain instances we may use interest rate swap agreements to modify fixed rate obligations to variable rate obligations, thereby adjusting the interest rates to current market rates and ensuring that the debt instruments are always reflected at fair value. We had no interest rate swap agreements outstanding as of December 31, 2018.

Item 8. Financial Statements and Supplementary Data

The financial statements listed in Item 15 and appearing on pages F-2 through F-33 are incorporated by reference in this Item 8 and are filed as part of this report.

Item 9. Changes in and Disagreements With Accountants on Accounting and Financial Disclosure

None.

Item 9A. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

The Company's management, with the participation of its President and Chief Executive Officer, who is the Company's principal executive officer, and its Vice President and Chief Financial Officer, who is the Company's principal financial officer, has evaluated the effectiveness of the Company's disclosure controls and procedures as of December 31, 2018. Based on this evaluation, the President and Chief Executive Officer and the Vice President and Chief Financial Officer have concluded that the Company's disclosure controls and procedures are effective.

Item 9B. Other Information

None.

Table of Contents**Management's Report on Internal Control Over Financial Reporting**

We, as members of management of Trex Company, Inc. (the Company), are responsible for establishing and maintaining adequate internal control over financial reporting. The Company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. Internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the Company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the Company are being made only in accordance with authorizations of management and directors of the Company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the Company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies and procedures may deteriorate.

We assessed the Company's internal control over financial reporting as of December 31, 2018, based on criteria for effective internal control over financial reporting established in Internal Control-Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission (the COSO Framework). Based on this assessment, we concluded that, as of December 31, 2018, our internal control over financial reporting was effective, based on the COSO Framework.

The effectiveness of our internal control over financial reporting as of December 31, 2018, has been audited by Ernst & Young LLP, an independent registered public accounting firm, as stated in their report, which follows hereafter.

TREX COMPANY, INC.

February 14, 2019

By: /s/ JAMES E. CLINE
James E. Cline
President and Chief Executive Officer
(Principal Executive Officer)

February 14, 2019

By: /s/ BRYAN H. FAIRBANKS
Bryan H. Fairbanks
Executive Vice President and Chief Financial Officer
(Principal Financial Officer)

Changes in Internal Control Over Financial Reporting

There have been no changes in the Company's internal control over financial reporting identified in connection with the evaluation described above in Management's Report on Internal Control Over Financial Reporting that occurred during the Company's fourth fiscal quarter that have materially affected, or are reasonably likely to materially affect,

the Company's internal control over financial reporting.

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Report of Independent Registered Public Accounting Firm

To the Stockholders and the Board of Directors of Trex Company, Inc.

Opinion on Internal Control over Financial Reporting

We have audited Trex Company, Inc.'s internal control over financial reporting as of December 31, 2018, based on criteria established in Internal Control – Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (2013 framework) (the COSO criteria). In our opinion, Trex Company, Inc., (the Company) maintained, in all material respects, effective internal control over financial reporting as of December 31, 2018, based on the COSO criteria.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States) (PCAOB), the consolidated balance sheets of the Company as of December 31, 2018 and 2017, and the related consolidated statements of comprehensive income, changes in stockholders' equity and cash flows for each of the three years in the period ended December 31, 2018, and the related notes and schedule and our report dated February 14, 2019 expressed an unqualified opinion thereon.

Basis for Opinion

The Company's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting included in the accompanying Management's Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit. We are a public accounting firm registered with the PCAOB and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audit in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects.

Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

Definition and Limitations of Internal Control Over Financial Reporting

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

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Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

/s/ Ernst & Young LLP

Richmond, Virginia

February 14, 2019

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PART III

Item 10. Directors, Executive Officers and Corporate Governance

Information responsive to this Item 10 is incorporated herein by reference to our definitive proxy statement for our 2019 annual meeting of stockholders, which we will file with the SEC on or before 120 days after our 2018 fiscal year-end.

We have adopted a Code of Conduct and Ethics, which is applicable to all of our directors, officers and employees, including our Chief Executive Officer and Chief Financial Officer. The code is available on our corporate web site and in print to any stockholder who requests a copy. We also make available on our web site, at www.trex.com/our-company/corporate-governance, and in print to any stockholder who requests them, copies of our corporate governance principles and the charters of each standing committee of our board of directors. Requests for copies of these documents should be directed to Corporate Secretary, Trex Company, Inc., 160 Exeter Drive, Winchester, Virginia 22603-8605. To the extent required by SEC rules, we intend to disclose any amendments to our code of conduct and ethics, and any waiver of a provision of the code with respect to our principal executive officer, principal financial officer, principal accounting officer or controller, or persons performing similar functions, on our web site referred to above within four business days following any such amendment or waiver, or within any other period that may be required under SEC rules from time to time.

Item 11. Executive Compensation

Information responsive to this Item 11 is incorporated herein by reference to our definitive proxy statement for our 2019 annual meeting of stockholders, which we will file with the SEC on or before 120 days after our 2018 fiscal year-end.

Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters

Information responsive to this Item 12 is incorporated herein by reference to our definitive proxy statement for our 2019 annual meeting of stockholders, which we will file with the SEC on or before 120 days after our 2018 fiscal year-end.

Item 13. Certain Relationships and Related Transactions, and Director Independence

Information responsive to this Item 13 is incorporated herein by reference to our definitive proxy statement for our 2019 annual meeting of stockholders, which we will file with the SEC on or before 120 days after our 2018 fiscal year-end.

Item 14. Principal Accounting Fees and Services

Information responsive to this Item 14 is incorporated herein by reference to our definitive proxy statement for our 2019 annual meeting of stockholders, which we will file with the SEC on or before 120 days after our 2018 fiscal year-end.

year-end.

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PART IV

Item 15. Exhibits and Financial Statement Schedules

(a)(1) The following Consolidated Financial Statements of the Company appear on pages F-2 through F-33 of this report and are incorporated by reference in Part II, Item 8:

| | |
|---|-----|
| <u>Report of Independent Registered Public Accounting Firm</u> | F-2 |
| Consolidated Financial Statements | |
| <u>Consolidated Statements of Comprehensive Income for the three years ended December 31, 2018</u> | F-3 |
| <u>Consolidated Balance Sheets as of December 31, 2018 and 2017</u> | F-4 |
| <u>Consolidated Statements of Changes in Stockholders' Equity for the three years ended December 31, 2018</u> | F-5 |
| <u>Consolidated Statements of Cash Flows for the three years ended December 31, 2018</u> | F-6 |
| <u>Notes to Consolidated Financial Statements</u> | F-7 |

(a)(2) The following financial statement schedule is filed as part of this report:

| | |
|---|------|
| <u>Schedule II Valuation and Qualifying Accounts and Reserves</u> | F-34 |
|---|------|

All other schedules for which provision is made in the applicable accounting regulations of the SEC are not required under the related instructions or are inapplicable or not material and, therefore, have been omitted.

(a)(3) See Exhibit Index at the end of the Annual Report on Form 10-K for the information required by this Item.

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TREX COMPANY, INC.

Index to Consolidated Financial Statements

| | Page |
|---|-------------|
| <u>Report of Independent Registered Public Accounting Firm</u> | F-2 |
| Consolidated Financial Statements | |
| <u>Consolidated Statements of Comprehensive Income for the three years ended December 31, 2018</u> | F-3 |
| <u>Consolidated Balance Sheets as of December 31, 2018 and 2017</u> | F-4 |
| <u>Consolidated Statements of Changes in Stockholders' Equity for the three years ended December 31, 2018</u> | F-5 |
| <u>Consolidated Statements of Cash Flows for the three years ended December 31, 2018</u> | F-6 |
| <u>Notes to Consolidated Financial Statements</u> | F-7 |

The following Consolidated Financial Statement Schedule of the Registrant is filed as part of this Report as required to be included in Item 15(a)(2):

| | Page |
|---|-------------|
| <u>Schedule II Valuation and Qualifying Accounts and Reserves</u> | F-34 |

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Report of Independent Registered Public Accounting Firm

To the Stockholders and the Board of Directors of Trex Company, Inc.

Opinion on the Financial Statements

We have audited the accompanying consolidated balance sheets of Trex Company, Inc. (the Company) as of December 31, 2018 and 2017, the related consolidated statements of comprehensive income, changes in stockholders equity and cash flows for each of the three years in the period ended December 31, 2018, and the related notes and financial statement schedule listed in the Index at Item 15(a)(2) (collectively referred to as the consolidated financial statements). In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of the Company at December 31, 2018 and 2017, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2018, in conformity with U.S. generally accepted accounting principles.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States) (PCAOB), the Company s internal control over financial reporting as of December 31, 2018, based on criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (2013 framework) and our report dated February 14, 2019 expressed an unqualified opinion thereon.

Basis for Opinion

These financial statements are the responsibility of the Company s management. Our responsibility is to express an opinion on the Company s financial statements based on our audits. We are a public accounting firm registered with the PCAOB and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud. Our audits included performing procedures to assess the risks of material misstatement of the financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statements. We believe that our audits provide a reasonable basis for our opinion.

/s/ Ernst & Young LLP

We have served as the Company s auditor since 1995.

Richmond, Virginia

February 14, 2019

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TREX COMPANY, INC.

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

| | Year Ended December 31, | | |
|--|--|------------|------------|
| | 2018 | 2017 | 2016 |
| | (In thousands, except share and per share data) | | |
| Net sales | \$ 684,250 | \$ 565,153 | \$ 479,616 |
| Cost of sales | 389,356 | 321,780 | 292,521 |
| Gross profit | 294,894 | 243,373 | 187,095 |
| Selling, general and administrative expenses | 118,225 | 100,993 | 83,140 |
| Income from operations | 176,669 | 142,380 | 103,955 |
| Interest (income) expense, net | (192) | 461 | 1,125 |
| Income before income taxes | 176,861 | 141,919 | 102,830 |
| Provision for income taxes | 42,289 | 46,791 | 34,983 |
| Net income | \$ 134,572 | \$ 95,128 | \$ 67,847 |
| Basic earnings per common share | \$ 2.29 | \$ 1.62 | \$ 1.16 |
| Basic weighted average common shares outstanding | 58,739,670 | 58,785,118 | 58,789,118 |
| Diluted earnings per common share | \$ 2.28 | \$ 1.61 | \$ 1.15 |
| Diluted weighted average common shares outstanding | 59,067,302 | 59,150,920 | 59,225,338 |
| Comprehensive income | \$ 134,572 | \$ 95,128 | \$ 67,847 |

See Notes to Consolidated Financial Statements.

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TREX COMPANY, INC.
CONSOLIDATED BALANCE SHEETS

| | December 31, | |
|---|-----------------------|-------------------|
| | 2018 | 2017 |
| | (In thousands) | |
| ASSETS | | |
| Current Assets: | | |
| Cash and cash equivalents | \$ 105,699 | \$ 30,514 |
| Accounts receivable, net | 91,163 | 66,882 |
| Inventories | 57,801 | 34,524 |
| Prepaid expenses and other assets | 15,562 | 16,878 |
| Total current assets | 270,225 | 148,798 |
| Property, plant and equipment, net | 117,144 | 103,110 |
| Goodwill and other intangibles | 74,503 | 71,319 |
| Other assets | 3,250 | 3,000 |
| Total Assets | \$ 465,122 | \$ 326,227 |
| LIABILITIES AND STOCKHOLDERS EQUITY | | |
| Current Liabilities: | | |
| Accounts payable | \$ 31,084 | \$ 9,953 |
| Accrued expenses and other liabilities | 56,291 | 46,266 |
| Accrued warranty | 5,400 | 6,290 |
| Total current liabilities | 92,775 | 62,509 |
| Deferred income taxes | 2,125 | 1,286 |
| Non-current accrued warranty | 25,354 | 28,709 |
| Other long-term liabilities | 1,905 | 2,473 |
| Total Liabilities | 122,159 | 94,977 |
| Commitments and contingencies | | |
| Stockholders Equity: | | |
| Preferred stock, \$0.01 par value, 3,000,000 shares authorized; none issued and outstanding | | |
| Common stock, \$0.01 par value, 120,000,000 shares authorized; 69,998,336 and 69,844,222 shares issued and 58,551,653 and 58,856,860 shares outstanding at December 31, 2018 and 2017, respectively | 700 | 698 |
| Additional paid-in capital | 124,224 | 121,694 |
| Retained earnings | 416,942 | 282,370 |
| Treasury stock, at cost, 11,446,683 and 10,987,362 shares at December 31, 2018 and 2017, respectively | (198,903) | (173,512) |

| | | |
|---|------------|------------|
| Total Stockholders Equity | 342,963 | 231,250 |
| Total Liabilities and Stockholders Equity | \$ 465,122 | \$ 326,227 |

See Notes to Consolidated Financial Statements.

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Table of Contents**TREX COMPANY, INC.****CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS EQUITY****(In thousands, except share data)**

| | Common Stock | | Additional | Retained | Treasury Stock | | Total |
|---|--------------|--------|-----------------|------------|----------------|--------------|------------|
| | Shares | Amount | Paid-In Capital | | Earnings | Shares | |
| Balance, December 31, 2015 | 61,809,060 | \$ 696 | \$ 116,598 | \$ 119,395 | 7,829,458 | \$ (120,227) | \$ 116,462 |
| Net income | | | | 67,847 | | | 67,847 |
| Employee stock purchase and option plans | 158,350 | 2 | 279 | | | | 281 |
| Shares withheld for taxes on share-based payment awards | (26,386) | (2) | (1,932) | | | | (1,934) |
| Stock-based compensation | 17,984 | 2 | 4,788 | | | | 4,790 |
| Shares repurchased under our publicly announced share repurchase programs | (3,157,904) | | | | 3,157,904 | (53,285) | (53,285) |
| Balance, December 31, 2016 | 58,801,104 | 698 | 119,733 | 187,242 | 10,987,362 | (173,512) | 134,161 |
| Net income | | | | 95,128 | | | 95,128 |
| Employee stock purchase and option plans | 33,228 | 2 | 391 | | | | 393 |
| Shares withheld for taxes on share-based payment awards | (58,470) | (2) | (3,617) | | | | (3,619) |
| Stock-based compensation | 80,998 | | 5,187 | | | | 5,187 |
| Balance, December 31, 2017 | 58,856,860 | 698 | 121,694 | 282,370 | 10,987,362 | (173,512) | 231,250 |
| Net income | | | | 134,572 | | | 134,572 |
| Employee stock purchase and option plans | 63,448 | 1 | 881 | | | | 882 |
| Shares withheld for taxes on share-based payment awards | (13,028) | | (4,695) | | | | (4,695) |
| Stock-based compensation | 103,694 | 1 | 6,344 | | | | 6,345 |
| Shares repurchased under our publicly announced share repurchase programs | (459,321) | | | | 459,321 | (25,391) | (25,391) |
| Balance, December 31, 2018 | 58,551,653 | \$ 700 | \$ 124,224 | \$ 416,942 | 11,446,683 | \$ (198,903) | \$ 342,963 |

See Notes to Consolidated Financial Statements.

Table of Contents**TREX COMPANY, INC.****CONSOLIDATED STATEMENTS OF CASH FLOWS**

| | Year Ended December 31, | | |
|---|-------------------------|-----------|-----------|
| | 2018 | 2017 | 2016 |
| | (In thousands) | | |
| Operating Activities | | | |
| Net income | \$ 134,572 | \$ 95,128 | \$ 67,847 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | | |
| Depreciation and amortization | 16,597 | 16,860 | 14,498 |
| Deferred income taxes | 1,037 | 194 | 5,433 |
| Stock-based compensation | 6,344 | 5,187 | 4,788 |
| Loss (Gain) on disposal of property, plant and equipment | 47 | 1,738 | (185) |
| Other non-cash adjustments | (406) | (406) | (284) |
| Changes in operating assets and liabilities: | | | |
| Accounts receivable | (24,281) | (10,486) | (653) |
| Inventories | (23,276) | (3,635) | (5,442) |
| Prepaid expenses and other assets | (613) | (2,194) | (4,256) |
| Accounts payable | 21,131 | (4,804) | (6,966) |
| Accrued expenses and other liabilities | 5,040 | 2,488 | 9,403 |
| Income taxes receivable/payable | 1,929 | 1,795 | 1,110 |
| Net cash provided by operating activities | 138,121 | 101,865 | 85,293 |
| Investing Activities | | | |
| Expenditures for property, plant and equipment and intangibles | (33,816) | (15,040) | (14,551) |
| Proceeds from sales of property, plant and equipment | 83 | 55 | 4,349 |
| Acquisition of business, net of cash acquired | | (71,804) | |
| Net cash used in investing activities | (33,733) | (86,789) | (10,202) |
| Financing Activities | | | |
| Financing costs | | | (485) |
| Borrowings under line of credit | 172,250 | 201,000 | 242,700 |
| Principal payments under line of credit | (172,250) | (201,000) | (249,700) |
| Repurchases of common stock | (30,085) | (3,617) | (55,216) |
| Proceeds from employee stock purchase and option plans | 882 | 391 | 279 |
| Net cash used in financing activities | (29,203) | (3,226) | (62,422) |
| Net increase in cash and cash equivalents | 75,185 | 11,850 | 12,669 |
| Cash and cash equivalents at beginning of year | 30,514 | 18,664 | 5,995 |
| Cash and cash equivalents at end of year | \$ 105,699 | \$ 30,514 | \$ 18,664 |

Supplemental disclosures of cash flow information:

| | | | |
|---------------------------------|-----------|-----------|-----------|
| Cash paid for interest | \$ 662 | \$ 418 | \$ 852 |
| Cash paid for income taxes, net | \$ 48,238 | \$ 44,802 | \$ 28,626 |

See Notes to Consolidated Financial Statements.

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TREX COMPANY, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. BUSINESS AND ORGANIZATION

Trex Company, Inc. (together with its subsidiaries, the Company), a Delaware corporation, was incorporated on September 4, 1998. The Company's principal business based on net sales is the manufacture and distribution of wood/plastic composite products, as well as related accessories, primarily for residential and commercial decking and railing applications. A majority of its products are manufactured in a proprietary process that combines reclaimed wood fibers and scrap polyethylene. On July 31, 2017, through its newly-formed, wholly-owned subsidiary, Trex Commercial Products, Inc., the Company acquired certain assets and assumed certain liabilities of Staging Concepts Acquisition, LLC (SC Company) and thus expanded its markets to include the design, engineering and marketing of modular and architectural railing and staging systems for the commercial and multi-family market, including sports stadiums and performing arts venues. Additional information on the acquisition of SC Company is presented in Note 3. The principal executive offices are located at 160 Exeter Drive, Winchester, Virginia 22603, and the telephone number at that address is (540) 542-6300. Subsequent to the acquisition, the Company operates in two reportable segments, Trex Residential Products (Trex Residential) and Trex Commercial Products (Trex Commercial).

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Accounting

The accompanying consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States. The consolidated financial statements include the accounts of the Company, its wholly-owned subsidiary, Trex Wood-Polymer Espana, S.L. (TWPE) for all years presented, and its wholly-owned subsidiary, Trex Commercial Products, Inc. (Trex Commercial Products), from date of acquisition of July 31, 2017. Intercompany accounts and transactions have been eliminated in consolidation.

TWPE was formed to hold the Company's 35% equity interest in Denplax, S.A. (Denplax), a venture with a Spanish company responsible for public environmental programs in southern Spain and with an Italian equipment manufacturer. The venture was formed to recycle polyethylene at a facility in El Ejido, Spain. The Company's investment in Denplax is accounted for using the equity method. During 2010, the Company determined that its investment in Denplax and a related note receivable were no longer recoverable and recorded a \$2.4 million charge to earnings to fully reserve the equity investment and note. Both the equity investment and note remain fully reserved as of December 31, 2018.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and the accompanying notes. Actual results could differ from those estimates.

Cash and Cash Equivalents

Cash equivalents consist of highly liquid investments purchased with original maturities of three months or less.

Concentrations and Credit Risk

The Company's financial instruments that are exposed to concentrations of credit risk consist primarily of cash and cash equivalents and trade accounts receivable. The Company from time to time may have bank

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deposits in excess of insurance limits of the Federal Deposit Insurance Corporation. As of December 31, 2018, substantially all deposits are maintained in one financial institution. The Company has not experienced any losses in such accounts and believes it is not exposed to any significant credit risk related to its cash and cash equivalents.

The Company routinely assesses the financial strength of its customers and believes that its trade receivables credit risk exposure is limited. Trade receivables are recognized at the amount of revenue recognized on each shipment for Trex Residential products and for satisfied performance obligations for Trex Commercial products as the Company has an unconditional right to consideration from the customer and payment is due based solely on the passage of time. A valuation allowance is provided for known and anticipated credit losses and disputed amounts, as determined by management in the course of regularly evaluating individual customer receivables. This evaluation takes into consideration a customer's financial condition and credit history, as well as current economic conditions. There was no material valuation allowance recorded as of December 31, 2018 and 2017.

In the years ended December 31, 2018, 2017 and 2016, sales to certain customers accounted for 10% or more of the Company's total net sales. For the year ended December 31, 2018, two customers of the Company represented approximately 42% of the Company's net sales. For the year ended December 31, 2017, two customers of the Company represented approximately 41% of the Company's net sales. For the year ended December 31, 2016, two customers of the Company represented approximately 39% of the Company's net sales. At December 31, 2018, four customers represented 31%, 19%, 13% and 12%, respectively, of the Company's accounts receivable balance.

For each year ended December 31, 2018, 2017 and 2016, approximately 33% of the Company's materials purchases were purchased from its four largest suppliers.

Inventories

Inventories for the Company's wood-alternative decking and railing products are stated at the lower of cost (last-in, first-out, or LIFO, method) and market. The Company periodically reviews its inventory for slow moving or obsolete items and writes down the related products to estimated realizable value. The Company's reserves for estimated slow moving products or obsolescence are not material. At December 31, 2018, the excess of the replacement cost of inventory over the LIFO value of inventory was approximately \$18.4 million. Due to the nature of the LIFO valuation methodology, liquidations of inventories will result in a portion of the Company's cost of sales being based on historical rather than current year costs.

A majority of the Company's products are made in a proprietary process that combines reclaimed wood fibers and scrap polyethylene. The Company grinds up scrap materials generated from its manufacturing process and inventories deemed no longer salable and reintroduces the reclaimed material into the manufacturing process as a substitute for raw materials. The reclaimed material is valued at the costs of the raw material components of the material.

Inventories for the Company's railing and staging products for the commercial and multi-family market are stated at the lower of cost (first-in, first-out or FIFO method), using actual cost, and net realizable value. Work-in process includes estimated production costs.

Table of Contents*Property, Plant and Equipment*

Property, plant and equipment are stated at historical cost. The costs of additions and improvements are capitalized, while maintenance and repairs are expensed as incurred. Depreciation is provided using the straight-line method over the following estimated useful lives:

| | |
|---------------------------------|------------|
| Buildings | 40 years |
| Machinery and equipment | 3-11 years |
| Furniture and equipment | 10 years |
| Forklifts and tractors | 5 years |
| Computer equipment and software | 5 years |

Leasehold improvements are amortized over the shorter of the lease term or the estimated useful life of the asset.

The Company reviews its long-lived assets, including property, plant and equipment, whenever events or changes in circumstances indicate that the carrying amount of the assets may not be fully recoverable. To determine the recoverability of its long-lived assets, the Company evaluates the probability that future estimated undiscounted net cash flows will be less than the carrying amount of the long-lived assets. If the estimated cash flows are less than the carrying amount of the long-lived assets, the assets are written down to their fair value. The Company's estimates of anticipated cash flows and the remaining estimated useful lives of long-lived assets could be reduced in the future. As a result, the carrying amount of long-lived assets could be reduced in the future. Long-lived assets held for sale are stated at the lower of cost or fair value less cost to sell.

Fair Value Measurement

Assets and liabilities measured at fair value are measured at the amount that would be received for selling an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date and classified into one of the following fair value hierarchy:

Level 1 Quoted prices for identical instruments in active markets.

Level 2 Quoted prices for similar instruments in active markets; quoted prices for identical or similar instruments in markets that are not active; and model derived valuations in which all significant inputs and significant value drivers are observable in active markets.

Level 3 Valuations derived from management's best estimate of what market participants would use in pricing the asset or liability at the measurement date. Consideration is given to the risk inherent in the valuation technique and the risk inherent in the inputs to the model.

Goodwill

Goodwill represents the excess of cost over net assets acquired resulting from the Company's 1996 purchase of the Mobil Composite Products Division, the 2011 purchase of the assets of the Iron Deck Corporation, and the 2017 purchase of certain assets and the assumption of certain liabilities of SC Company. The Company evaluates the

recoverability of goodwill in accordance with Accounting Standard Codification Topic 350, *Intangibles Goodwill and Other*, annually or more frequently if an event occurs or circumstances change in the interim that would more likely than not reduce the fair value of the asset below its carrying amount. Goodwill is considered to be impaired when the net book value of the reporting unit exceeds its estimated fair value.

The Company first assesses qualitative factors to determine if it is more likely than not that the fair value of the reporting units is less than the carrying amount to determine if it should proceed with the evaluation of goodwill for impairment. The Company identified its reporting units based on the way it manages its operating segments. Each reporting unit constitutes a business with discrete financial information and operating segment

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management, at a level below the Company's chief operating decision maker, regularly reviews the operating results of the reporting unit. The Company assigned goodwill to the reporting units based on the excess of the fair values acquired over the fair value of the sum of the individual assets acquired and liabilities assumed that were assigned to the reporting units. If the Company proceeds with the two-step impairment test, the Company first compares the fair value of the reporting unit to its carrying value. If the carrying value of a reporting unit exceeds its fair value, the goodwill of that reporting unit is potentially impaired and step two of the impairment analysis is performed. In step two of the analysis, an impairment loss is recorded equal to the excess of the carrying value of the reporting unit's goodwill over its implied fair value should such a circumstance arise.

The Company measures fair value of the reporting units based on a present value of future discounted cash flows and a market valuation approach. The discounted cash flows model indicates the fair value of the reporting unit based on the present value of the cash flows that the reporting unit is expected to generate in the future. Significant estimates in the discounted cash flows model include: the weighted average cost of capital; long-term rate of growth and profitability of the business; and working capital effects. The market valuation approach indicates the fair value of the business based on a comparison of the Company against certain market information. Significant estimates in the market approach model include identifying appropriate market multiples and assessing earnings before interest, income taxes, depreciation and amortization (EBITDA) in estimating the fair value of the reporting unit.

For the years ended December 31, 2018, 2017 and 2016, the Company completed its annual impairment test of goodwill utilizing the qualitative assessment and concluded it was not more likely than not that the fair value of the reporting units are less than the carrying amounts. The Company performs the annual impairment testing of its goodwill as of October 31 of each year. However, actual results could differ from the Company's estimates and projections, which would affect the assessment of impairment. As of December 31, 2018, the Company had goodwill of \$68.5 million that is reviewed annually for impairment.

Product Warranty

The Company warrants that its Trex Residential decking products will be free from material defects in workmanship and materials. This warranty generally extends for a period of 25 years for residential use and 10 years for commercial use. With respect to Trex Signature® Railing, the warranty period is 25 years for both residential and commercial use. With respect to the Company's Transcend®, Enhance®, Select® and Universal Fascia product, the Company further warrants that the product will not fade in color more than a certain amount and will be resistant to permanent staining from food substances or mold, provided the stain is cleaned within seven days of appearance. This warranty extends for a period of 25 years for residential use and 10 years for commercial use. If there is a breach of such warranties, the Company has an obligation either to replace the defective product or refund the purchase price. The Company also warrants its Trex Commercial products for one to three years. The Company establishes warranty reserves to provide for estimated future expenses as a result of product defects that result in claims. Reserve estimates are based on management's judgment, considering such factors as cost per claim, historical experience, anticipated rates of claims, and other available information. Management reviews and adjusts these estimates, if necessary, based on the differences between actual experience and historical estimates.

Treasury Stock

The Company records the repurchase of shares of its common stock at cost. These shares are considered treasury stock, which is a reduction to stockholders' equity. Treasury stock is included in authorized and issued shares but excluded from outstanding shares.

Revenue Recognition

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Effective January 1, 2018, the Company retrospectively adopted the requirements of Financial Accounting Standards Board Accounting Standards Update 2014-09, Revenue from Contracts with Customers (Topic 606).

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The Company determined the appropriate revenue recognition for its contracts with customers by analyzing the type, terms and conditions of the contracts with customers. Topic 606 provides a single, comprehensive model for revenue recognition arising from contracts with customers. A performance obligation is a promise in a contract to transfer a distinct good or service to the customer and is the unit of account in Topic 606. A contract's transaction price is allocated to each distinct performance obligation and revenue is recognized when or as the Company satisfies the performance obligation. Revenue is recognized at an amount that reflects the consideration to which the entity expects to be entitled in exchange for transferring control of the goods or services to a customer. Adoption of Topic 606 did not have an impact on the Company's financial condition or results of operations. The following provides additional information about the Company's contracts with customers.

Trex Residential Products

Trex Residential principally generates revenue from the manufacture and sale of its high performance, low maintenance composite decking and railing products and accessories. Substantially all of its revenues are from contracts with customers, which are individual customer purchase orders of short-term duration of less than one year. Trex Residential satisfies its performance obligations at a point in time. The shipment of each product is a separate performance obligation as the customer is able to derive benefit from each product shipped and no performance obligation remains after shipment. Upon shipment of the product, the customer obtains control over the distinct product and Trex Residential satisfies its performance obligation. Any performance obligation that remains unsatisfied at the end of a reporting period is part of a contract that has an original expected duration of one year or less. Any variable consideration related to the unsatisfied performance obligation is allocated wholly to the unsatisfied performance obligation and recognized when the product ships and the performance obligation is satisfied.

Trex Commercial Products

Trex Commercial generates revenue from the manufacture and sale of its modular and architectural railing and staging systems. All of its revenues are from fixed-price contracts with customers. Trex Commercial contracts have a single performance obligation as the promise to transfer the individual goods or services is not separately identifiable from other promises in the contract and is, therefore, not distinct.

Trex Commercial satisfies its performance obligation over time as work progresses because control is transferred continuously to its customers. Revenue and estimated profit is recognized over time based on the proportion of actual costs incurred to date relative to total estimated costs at completion to measure progress toward satisfying the performance obligation. Incurred costs represent work performed, which corresponds with, and thereby best depicts, the transfer of control to the customer. Incurred costs include all direct material, labor, subcontract and certain indirect costs. The Company reviews and updates its estimates regularly and recognizes adjustments in estimated profit on contracts under the cumulative catch-up method. Under this method, the impact of the adjustment on revenue and estimated profit to date on a contract is recognized in the period the adjustment is identified. Revenues and profits in future periods are recognized using the adjusted estimate. If at any time the estimate of contract profitability indicates an anticipated loss on the contract, the Company recognizes the total loss in the period it is identified. During the year ended December 31, 2018, no adjustment to any one contract was material to the Company's Consolidated Financial Statements and no material impairment loss on any contract was recorded.

Stock-Based Compensation

The Company measures stock-based compensation at the grant date of the award based on the fair value. For stock options, stock appreciation rights and time-based restricted stock and time-based restricted stock units, stock-based compensation is recognized on a straight line basis over the vesting periods of the award. The Company recognizes

forfeitures as they occur. For performance-based restricted stock and performance-based restricted stock units, expense is recognized ratably over the performance and vesting period of each tranche

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based on management's judgment of the ultimate award that is probable to be paid out based on the achievement of predetermined performance measures. Stock-based compensation expense is included in Selling, general and administrative expenses in the accompanying Consolidated Statements of Comprehensive Income.

Income Taxes

The Company recognizes deferred tax assets and liabilities based on the difference between the financial statement basis and tax basis of assets and liabilities using enacted rates expected to be in effect during the year in which the differences reverse. The Company assesses the likelihood that its deferred tax assets will be realized. Deferred tax assets are reduced by a valuation allowance when, after considering all available positive and negative evidence, it is determined that it is more likely than not that some portion, or all, of the deferred tax asset will not be realized. The tax legislation H.R.1, An Act to Provide for Reconciliation Pursuant to Titles II and V of the Concurrent Resolution on the Budget for Fiscal Year 2018, known as the Tax Cuts and Jobs Act (Act), was enacted on December 22, 2017. Accordingly, the Company recognized the tax effects of the Act in its financial statements and related notes. As of December 31, 2018, the Company has a valuation allowance of \$3.0 million against these deferred tax assets. The Company analyzes its position in subsequent reporting periods, considering all available positive and negative evidence, in determining the expected realization of its deferred tax assets.

Research and Development Costs

Research and development costs are expensed as incurred. For the years ended December 31, 2018, 2017 and 2016, research and development costs were \$4.2 million, \$3.8 million, and \$3.7 million, respectively, and have been included in Selling, general and administrative expenses in the accompanying Consolidated Statements of Comprehensive Income.

Advertising Costs

The Company expenses its branding and advertising communication costs as incurred. Significant production costs are deferred and recognized as expense in the period that the related advertisement is first used. At December 31, 2017 and 2016, \$3.8 million, and \$2.4 million, respectively, were included in prepaid expenses for production costs. At December 31, 2018 there were no production costs included in prepaid expenses.

For the years ended December 31, 2018, 2017 and 2016, branding expenses, including advertising expenses as described above, were \$35.0 million, \$31.0 million, and \$24.8 million, respectively.

Fair Value of Financial Instruments

The Company considers the recorded value of its financial assets and liabilities, consisting primarily of cash and cash equivalents, accounts receivable, accounts payable, accrued expenses and other current liabilities to approximate the fair value of the respective assets and liabilities on the Consolidated Balance Sheets at December 31, 2018 and 2017.

Recently Adopted Accounting Standards

In May 2017, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2017-09, Compensation - Stock Compensation (Topic 718), Scope Modification Accounting. The guidance clarified when to account for a change to the terms or conditions of a share-based payment award as a modification. Under the new guidance, modification accounting is required only if the fair value (or calculated intrinsic value, if those amounts are being used to measure the award under ASC 718), the vesting conditions, or the classification of the award (as

equity or liability) changes as a result of the change in terms or conditions. The guidance was effective prospectively for annual periods beginning on or after December 15, 2017. Adoption of the new standard did not have a material impact on the Company's financial condition or results of operations.

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In January 2017, the FASB issued ASU No. 2017-01, *Business Combinations (Topic 805), Clarifying the Definition of a Business*. The guidance requires an entity to evaluate if substantially all of the fair value of the gross assets acquired is concentrated in a single identifiable asset or group of similar identifiable assets: if so, the set of transferred assets and activities is not a business. The guidance was effective for fiscal years beginning after December 15, 2017, and interim periods within those fiscal years. Adoption of the new standard did not have a material impact on the Company's financial condition or results of operations.

In August 2016, the FASB issued ASU No. 2016-15, *Statement of Cash flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments*. The guidance is intended to reduce diversity in practice across all industries in how certain transactions are classified in the statement of cash flows. The guidance was effective for financial statements issued for fiscal years beginning after December 15, 2017, and interim periods within those fiscal years. Adoption of the new standard did not have a material impact on the Company's consolidated financial statements.

In May 2014, the FASB issued ASU No. 2014-09, *Revenue from Contracts with Customers (Topic 606)*, and issued subsequent amendments to the initial guidance in August 2015 within ASU No. 2015-14, in March 2016 within ASU No. 2016-08, in April 2016 within ASU No. 2016-10, in May 2016 within ASU No. 2016-12, and in December 2016 within ASU No. 2016-20 (collectively, *Topic 606*). The Company adopted *Topic 606* on January 1, 2018 and applied *Topic 606* under the full retrospective method. The Company determined the appropriate revenue recognition for its contracts with customers by analyzing the type, terms and conditions of its contracts with its customers. The Company has consistently applied the accounting policies to all periods presented in these Consolidated Financial Statements. Adoption of *Topic 606* did not have an impact on the Company's financial condition or results of operations other than increased disclosures. Refer to Note 12, *Revenue from Contracts with Customers*, for a discussion of the Company's accounting policy related to revenue from contracts with customers.

New Accounting Standards Not Yet Adopted

In June 2018, the FASB issued ASU No. 2018-07, *Compensation—Stock Compensation (Topic 718)*. The ASU expands the scope of *Topic 718*, which currently only includes share-based payments issued to employees, to also include share-based payments issued to nonemployees for goods or services. The ASU supersedes Subtopic 505-50, *Equity—Equity-Based Payment to Non-Employees*. Consequently, the accounting for share-based payments to nonemployees and employees will be substantially aligned. The ASU is effective for fiscal years beginning after December 15, 2018, including interim periods within that fiscal year. Early adoption is permitted. The Company intends to adopt the guidance on January 1, 2019 and does not believe adoption will have a material impact on its financial condition or results of operations.

In January 2017, the FASB issued ASU No. 2017-04, *Intangibles—Goodwill and Other (Topic 350), Simplifying the Test for Goodwill Impairment*. The guidance removes Step 2 of the goodwill impairment test and eliminates the need to determine the fair value of individual assets and liabilities to measure goodwill impairment. A goodwill impairment will now be the amount by which a reporting unit's carrying value exceeds its fair value, not to exceed the carrying amount of goodwill. Entities will continue to have the option to perform a qualitative assessment to determine if a quantitative impairment test is necessary. The guidance will be applied prospectively, and is effective for annual and interim goodwill impairment tests in fiscal years beginning after December 15, 2019. Early adoption is permitted for any impairment tests performed on testing dates after January 1, 2017. The Company intends to adopt the guidance on January 1, 2020 and does not believe adoption will have a material impact on its financial condition or results of operations.

In February 2016, the FASB issued ASU No. 2016-02, *Leases (Topic 842)*, and issued subsequent amendments to the initial guidance in January 2018 within ASU No. 2018-01 and in July 2018 within ASU Nos. 2018-10 and 2018-11.

The standard requires lessees to recognize leases on the balance sheet as a right-of-use asset and a lease liability, other than leases that meet the definition of a short-term lease. The liability will be

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equal to the present value of the lease payments. The asset will be based on the liability, subject to adjustment. Currently, under existing U.S. generally accepted accounting principles, the Company does not recognize on the balance sheet a right-of-use asset or lease liability related to its operating leases. For income statement purposes, the leases will continue to be classified as either operating or finance. Operating leases will result in straight-line expense (similar to current operating leases) and finance leases will result in a front-loaded expense pattern (similar to current capital leases). The standard is effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2018. Early adoption is permitted. The standard allows an entity to elect to have a date of initial application as of the beginning of the period of adoption. The standard provides for the option to elect a package of practical expedients upon adoption. The Company intends to adopt the standard on January 1, 2019 and is currently planning on electing the package of practical expedients to not reassess prior conclusions related to contracts containing leases, lease classification and initial direct costs and is evaluating the other practical expedients available under the guidance. The Company expects expanded financial statement note disclosure in addition to recognizing a right-of-use asset and lease liability for its operating leases on the balance sheet. Based on leases outstanding at December 31, 2018, the Company estimates the operating lease right of use asset and lease liability would have been in the range of \$45 million to \$50 million. The Company continues to evaluate the impacts of the pending adoption. As such, the Company's preliminary assessments are subject to change.

3. ACQUISITION

On July 31, 2017, through its newly-formed, wholly-owned subsidiary, Trex Commercial Products, Inc., the Company acquired certain assets and assumed certain liabilities of SC Company for \$71.8 million in cash. The Company used cash on hand and \$30.0 million of funding from its existing revolving credit facility, which was fully paid on August 17, 2017, to acquire the assets. The acquired business designs, engineers and markets modular architectural railing and staging systems for the commercial and multi-family market, including sports stadiums and performing arts venues. As a result of the purchase, the Company gained access to growing commercial markets, expanded its custom design and engineering capabilities, and added the contract architect and specifier communities as new channels for its products.

The acquisition was accounted for using the acquisition method of accounting under U.S. Generally Accepted Accounting Principles, which requires, among other things, that the assets acquired and liabilities assumed be recognized at their fair values as of the acquisition date. The fair values of consideration transferred and net assets acquired were determined using a combination of Level 2 and Level 3 inputs as specified in the fair value hierarchy in ASC 820, *Fair Value Measurements and Disclosures*. The Company believes that the fair values assigned to the assets acquired and liabilities assumed are based on reasonable assumptions. The Company's consolidated results of operations include the operating results of the acquired business from the date of acquisition. The Company's consolidated balance sheets at December 31, 2018 and December 31, 2017 includes the acquired assets and any liabilities assumed.

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Based on the Company's valuation, total consideration of \$71.8 million was allocated to the assets acquired and liabilities assumed, as follows (in thousands):

| | |
|--|------------------|
| Accounts receivable, net | \$ 8,357 |
| Contract retainage | 1,948 |
| Inventories, net | 2,344 |
| Prepaid expenses and other assets | 1,223 |
| Revenues in excess of billings | 3,463 |
| Fixed assets, net | 1,264 |
| Intangible assets | 4,900 |
| Goodwill | 57,938 |
| Accounts payable | (3,990) |
| Accrued liabilities and other expenses | (2,329) |
| Billings in excess of revenues | (1,752) |
| Customer deposits | (1,562) |
| Total consideration | \$ 71,804 |

Goodwill of \$57.9 million is primarily attributable to the potential opportunity for the Company to offer full service railing systems in the growing commercial and multi-family markets, access to a complementary product category with a track record of substantial revenue growth, the ability to achieve economies of scale around raw material procurement, an increase in the range of products the Company may offer its core customers, and intangible assets that do not qualify for separable or legal criterion, such as an assembled workforce. The amount of goodwill that was amortized and deductible for tax purposes in 2018 and 2017 was \$3.9 million and \$1.6 million, respectively. Primarily all of the goodwill was recorded to Trex Commercial. The fair value attributed to intangible assets, which consists of production backlog and trade names and trademarks, is being amortized straight line over 12 months and is based on the estimated economics of the assets. The fair value attributed to the intangible assets acquired and goodwill was based on assumptions and other information compiled by management, including independent valuations that utilized established valuation techniques.

During the year ended December 31, 2018, Trex Commercial generated \$71.0 million of net sales and \$2.7 million of net income, which included amortization expense of \$2.9 million. From July 31, 2017, through December 31, 2017, Trex Commercial generated \$21.8 million in net sales and incurred a net loss of \$2.3 million, and which included \$0.5 million of acquisition-related expenses and \$2.0 million of amortization expense during the year ended December 31, 2017, which are included in selling, general and administrative expense.

4. INVENTORIES

Inventories (at LIFO value) consist of the following as of December 31 (in thousands):

| | 2018 | 2017 |
|----------------|-------------|-------------|
| Finished goods | \$ 46,638 | \$ 32,986 |
| Raw materials | 27,321 | 19,432 |

| | | |
|--|-----------|-----------|
| Total FIFO (first-in, first out) inventories | 73,959 | 52,418 |
| Reserve to adjust inventories to LIFO value | (18,442) | (20,070) |
| Total LIFO inventories | \$ 55,517 | \$ 32,348 |

Inventory related to the Company's wood-alternative decking and railing products is stated at the lower of LIFO cost or market. The Company periodically reviews its inventory for slow moving or obsolete items and writes down the related products to estimated market.

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Under the LIFO method, reductions in inventory cause a portion of the Company's cost of sales to be based on historical costs rather than current year costs. There was no inventory reduction during 2018 and 2017.

Inventories valued at lower of cost (FIFO method) and net realizable value as of December 31, 2018 and December 31, 2017, consist of \$2.3 million and \$2.2 million, respectively, of raw materials. The Company utilizes the FIFO method of accounting related to its commercial products.

5. PREPAID EXPENSES AND OTHER ASSETS

Prepaid expenses and other assets consist of the following as of December 31 (in thousands):

| | 2018 | 2017 |
|--|------------------|------------------|
| Revenues in excess of billings | \$ 7,987 | \$ 4,841 |
| Prepaid expenses | 3,390 | 7,494 |
| Contract retainage | 2,469 | 1,449 |
| Income tax receivable | 471 | 2,230 |
| Other | 1,245 | 864 |
| Total prepaid expenses and other assets | \$ 15,562 | \$ 16,878 |

6. GOODWILL AND OTHER INTANGIBLE ASSETS

The carrying amount of goodwill by reportable segment at December 31, 2018 and 2017 was \$14.2 million for Trex Residential and \$54.3 million for Trex Commercial.

Intangible assets consist of the following (in thousands):

| | December 31, 2018 | December 31, 2017 |
|---------------------------------------|------------------------------|------------------------------|
| Intangible assets: | | |
| Customer backlog | \$ 4,000 | \$ 4,000 |
| Trade names and trademarks | 900 | 900 |
| Domain names | 6,327 | |
| Total intangible assets | 11,227 | 4,900 |
| Accumulated amortization: | | |
| Customer backlog | (4,000) | (1,666) |
| Trade name and trademarks | (900) | (376) |
| Domain names | (285) | |
| Total accumulated amortization | (5,185) | (2,042) |

| | | | | |
|------------------------|----|-------|----|-------|
| Intangible assets, net | \$ | 6,042 | \$ | 2,858 |
|------------------------|----|-------|----|-------|

Intangible asset amounts were determined based on the estimated economics of the asset and are amortized over the estimated useful lives on a straight-line basis over 12 months for customer backlog and trade names and trademarks and 15 years for domain names, which approximates the pattern in which the economic benefits are expected to be received. In May 2018, the Company purchased certain domain names for \$6.3 million. We evaluate the recoverability of intangible assets periodically and consider events or circumstances that may warrant revised estimates of useful lives or that may indicate an impairment. Intangible asset amortization expense for the years ended December 31, 2018 and December 31, 2017, was \$3.1 million and \$2.0 million, respectively.

Table of Contents**7. PROPERTY, PLANT AND EQUIPMENT**

Property, plant and equipment consist of the following as of December 31 (in thousands):

| | 2018 | 2017 |
|--|-------------|-------------|
| Building and improvements | \$ 50,240 | \$ 49,403 |
| Machinery and equipment | 233,464 | 228,107 |
| Furniture and fixtures | 1,625 | 1,620 |
| Forklifts and tractors | 10,872 | 9,799 |
| Computer equipment | 10,142 | 9,680 |
| Construction in process | 16,392 | 5,954 |
| Land | 11,417 | 11,417 |
| | | |
| Total property, plant and equipment | 334,152 | 315,980 |
| Accumulated depreciation | (217,008) | (212,870) |
| | | |
| Total property, plant and equipment, net | \$ 117,144 | \$ 103,110 |

The Company had construction in process as of December 31, 2018 of approximately \$16.4 million. The Company expects that the construction in process will be completed and put into service in the year ending December 31, 2019.

Depreciation expense for the years ended December 31, 2018, 2017, and 2016 totaled \$13.4 million, \$14.7 million, and \$14.2 million, respectively.

8. ACCRUED EXPENSES AND OTHER LIABILITIES

Accrued expenses and other liabilities consist of the following as of December 31 (in thousands):

| | 2018 | 2017 |
|--------------------------------|-------------|-------------|
| Sales and marketing costs | \$ 25,379 | \$ 21,964 |
| Compensation and benefits | 19,124 | 14,818 |
| Manufacturing costs | 3,744 | 1,979 |
| Customer deposits | 2,058 | 1,230 |
| Rent obligations | 663 | 779 |
| Billings in excess of revenues | 512 | 1,842 |
| Other | 4,811 | 3,654 |
| | | |
| Total accrued expenses | \$ 56,291 | \$ 46,266 |

9. DEBT

The Company's debt consists of a revolving credit facility. At December 31, 2018 and 2017, the Company had no outstanding indebtedness. Available borrowing capacity at December 31, 2018, was \$200 million.

Revolving Credit Facility

On January 12, 2016, the Company entered into a Third Amended and Restated Credit Agreement and also the First Amendment to the Third Amended and Restated Credit Agreement (together, the Third Amended Credit Agreement) with Bank of America, N.A. (BOA) as Lender, Administrative Agent, Swing Line Lender and Letter of Credit Issuer; and certain other lenders including Citibank, N.A., Capital One, N.A., and SunTrust Bank (collectively, Lenders) arranged by Bank of America Merrill Lynch as Sole Lead Arranger and Sole Bookrunner. The Third Amended Credit Agreement amended and restated the Second Amended Credit Agreement.

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Under the Third Amended Credit Agreement, the Lenders agree to provide the Company with one or more revolving loans in a collective maximum principal amount of \$250 million from January 1 through June 30 of each year and a maximum principal amount of \$200 million from July 1 through December 31 of each year throughout the term, which ends January 12, 2021. Included within the revolving loan limit are sublimits for a letter of credit facility in an amount not to exceed \$15 million and swing line loans in an aggregate principal amount at any time outstanding not to exceed \$5 million. The revolving loans, the letter of credit facility and the swing line loans are for the purpose of funding working capital needs and supporting general business operations. Additionally, within the Revolving Loan Limit, the Company could borrow, repay, and reborrow, at any time or from time to time while the Third Amended Credit Agreement is in effect.

The Company has the option to select interest rates for each loan request at the Base Rate or Eurodollar Rate. Base rate loans under the revolving loans and the swing line loans accrue interest at the Base Rate plus the Applicable Rate. Eurodollar Rate Loans for the revolving loans and swing line loans accrue interest at the Adjusted London InterBank Offered Rate plus the Applicable Rate. The Base Rate for any day is a fluctuating rate per annum equal to the highest of (a) the Federal Funds Rate plus 0.50%, (b) the rate of interest in effect for such day as publicly announced from time to time by BOA as its prime rate, and (c) the Eurodollar Rate plus 1.0%. Repayment of all then outstanding principal, interest, fees and costs is due on January 12, 2021.

The Company shall reimburse BOA for all amounts payable, including interest, under a letter of credit at the earlier of (i) the date set forth in the application, or (ii) one business day after the payment under such letter of credit by BOA.

The Third Amended Credit Agreement is secured by property with respect to which liens in favor of the Administrative Agent, for the benefit of itself and the other holders of the obligations, are purported to be granted pursuant to and in accordance with the terms of the collateral documents as referenced in the Third Amended Credit Agreement.

Compliance with Debt Covenants and Restrictions

The Company's ability to make scheduled principal and interest payments, borrow and repay amounts under any outstanding revolving credit facility and continue to comply with any loan covenants depends primarily on its ability to generate sufficient cash flows from operations. To remain in compliance with financial covenants, the Company is required to maintain specified financial ratios based on levels of debt, fixed charges, and earnings (excluding extraordinary gains and extraordinary non-cash losses) before interest, taxes, depreciation and amortization, all of which are subject to the risks of the business, some of which are discussed in this report under Risk Factors. The material financial covenants and restrictions do not permit the Company's fixed charge coverage ratio to be less than 1.5 to 1.0 and do not permit the Company's consolidated debt to consolidated EBITDA ratio to exceed 3.0 to 1.0, measured as of the end of each fiscal quarter (and in the case of Consolidated EBITDA, for the four-quarter period ending on such date). The Company was in compliance with all covenants contained in the Third Amended Credit Agreement at December 31, 2018. Failure to comply with the financial covenants could be considered a default of repayment obligations and, among other remedies, could accelerate payment of any amounts outstanding.

10. FINANCIAL INSTRUMENTS

The Company considers the recorded value of its financial assets and liabilities, consisting primarily of cash and cash equivalents, accounts receivable, accounts payable, accrued expenses and other current liabilities to approximate the fair value of the respective assets and liabilities on the Consolidated Balance Sheets at December 31, 2018 and 2017.

Table of Contents**11. STOCKHOLDERS EQUITY***Amendment of Restated Certificate of Incorporation*

The Company's Board of Directors unanimously approved an amendment to the Company's Restated Certificate of Incorporation (Amendment) on February 14, 2018, subject to stockholder approval. At the annual meeting of stockholders of the Company held on May 2, 2018, the Company's stockholders approved the Amendment, effective as of May 2, 2018. The Amendment increased the number of shares of common stock, par value \$.01 per share, that the Company is authorized to issue from 80,000,000 shares to 120,000,000 shares. The Amendment was filed with the Delaware Secretary of State on May 2, 2018.

Stock Split

On May 2, 2018, the Board of Directors of the Company approved a two-for-one stock split of the Company's common stock, par value \$0.01. The stock split was in the form of a stock dividend distributed on June 18, 2018, to stockholders of record at the close of business on May 23, 2018. The stock split entitled each stockholder to receive one additional share of common stock, par value \$0.01, for each share they held as of the record date. All common stock share and per share data for all periods presented in the accompanying consolidated financial statements and notes thereto have been retroactively adjusted to reflect the stock split.

Earnings Per Share

The following table sets forth the computation of basic and diluted earnings per share (in thousands, except share and per share data):

| | Year Ended December 31, | | |
|---|--------------------------------|-------------|-------------|
| | 2018 | 2017 | 2016 |
| Numerator: | | | |
| Net income | \$ 134,572 | \$ 95,128 | \$ 67,847 |
| Denominator: | | | |
| Basic weighted average shares outstanding | 58,739,670 | 58,785,118 | 58,789,118 |
| Effect of dilutive securities: | | | |
| Stock appreciation rights | 176,700 | 198,642 | 250,238 |
| Restricted stock | 150,932 | 167,160 | 185,982 |
| Diluted weighted average shares outstanding | 59,067,302 | 59,150,920 | 59,225,338 |
| Basic earnings per share | \$ 2.29 | \$ 1.62 | \$ 1.16 |
| Diluted earnings per share | \$ 2.28 | \$ 1.61 | \$ 1.15 |

Diluted earnings per share is computed using the weighted average number of shares determined for the basic earnings per share computation plus the dilutive effect of common stock equivalents using the treasury stock method. The computation of diluted earnings per share excludes the following potentially dilutive securities because the effect would be anti-dilutive:

| | Year Ended December 31, | | |
|---------------------------|--------------------------------|-------------|-------------|
| | 2018 | 2017 | 2016 |
| Restricted stock | 214 | 166 | 24 |
| Stock appreciation rights | 13,347 | 21,234 | 9,262 |

Stock Repurchase Programs

On October 22, 2015, the Board of Directors adopted a stock repurchase program of up to 3.15 million shares of the Company's outstanding common stock (October 2015 Stock Repurchase Program). This authorization terminated on December 31, 2016. During 2016, the Company repurchased 1,578,952 shares for \$53.3 million under the October 2015 Stock Repurchase Program.

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On February 16, 2017, the Board of Directors authorized a common stock repurchase program of up to 2.961 million shares of the Company's outstanding common stock (February 2017 Stock Repurchase Program). The Company made no repurchases under the February 2017 Stock Repurchase Program.

On February 16, 2018, the Board of Directors terminated the February 2017 Stock Repurchase Program and adopted a new stock repurchase program of up to 5.8 million shares of the Company's outstanding common stock (February 2018 Stock Repurchase Program). As of the date of this report, the Company has repurchased 459,321 shares under the February 2018 Stock Repurchase Program.

12. REVENUE FROM CONTRACTS WITH CUSTOMERS

Topic 606 provides a single, comprehensive model for revenue recognition arising from contracts with customers. A performance obligation is a promise in a contract to transfer a distinct good or service to the customer and is the unit of account in Topic 606. A contract's transaction price is allocated to each distinct performance obligation and revenue is recognized when or as the Company satisfies the performance obligation. Revenue is recognized at an amount that reflects the consideration to which the entity expects to be entitled in exchange for transferring control of the goods or services to a customer.

Trex Residential Products

Trex Residential principally generates revenue from the manufacture and sale of its high performance, low maintenance composite decking and residential railing products and accessories. Substantially all of its revenues are from contracts with customers, which are purchase orders of short-term duration of less than one year. Its customers, in turn, sell primarily to the residential market, which includes replacement, remodeling and new construction related to outdoor living products. Trex Residential satisfies its performance obligations at a point in time. The shipment of each product is a separate performance obligation as the customer is able to derive benefit from each product shipped and no performance obligation remains after shipment. Upon shipment of the product, the customer obtains control over the distinct product and Trex Residential satisfies its performance obligation. Any performance obligation that remains unsatisfied at the end of a reporting period is part of a contract that has an original expected duration of one year or less. Any variable consideration related to the unsatisfied performance obligation is allocated wholly to the unsatisfied performance obligation and recognized when the product ships and the performance obligation is satisfied.

For each product shipped, the transaction price by product is specified in the purchase order. The Company recognizes revenue on the transaction price less any amount offered under a sales incentive program. The Company recognizes an account receivable (contract asset) for the amount of revenue recognized as it has an unconditional right to consideration at the time of shipment and payment from the customer is due based solely on the passage of time. The Company receives payments from its customers based on the payment terms applicable to each individual contract and the customer pays in accordance with the billing terms specified in the purchase order, which is less than one year. The related accounts receivables are included in Accounts receivable, net in the Consolidated Balance Sheets.

Trex Residential may offer various sales incentive programs throughout the year. It estimates the amount of sales incentive to allocate to each performance obligation, or product shipped, based on direct sales to the customer. The estimate is updated each reporting period and any changes are allocated to the performance obligations on the same basis as at inception. Changes in estimate allocated to a previously satisfied performance obligation are recognized as a reduction of revenue in the period in which the change occurs under the cumulative catch-up method. In addition to sales incentive programs, Trex Residential may offer a payment discount. It estimates the payment discount that it believes will be taken by the customer based on prior history.

Trex Residential pays commissions to certain employees. However, the sales commissions are not directly attributable to identifiable contracts, are discretionary in nature and are based on other factors not related to

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obtaining a contract, such as individual performance, profitability of the entity, annual sales targets, etc. These costs are included in selling, general and administrative expenses as incurred. Trex Residential does not grant contractual product return rights to customers other than pursuant to its assurance product warranty (see related disclosure on product warranties in Note 19, Commitments and Contingencies). Trex Residential accounts for all shipping and handling fees invoiced to the customer in net sales and the related costs in cost of sales.

Trex Commercial Products

Trex Commercial generates revenue from the manufacture and sale of its modular and architectural railing and staging systems. All of its revenues are from fixed-price contracts with customers. Trex Commercial contracts have a single performance obligation as the promise to transfer the individual goods or services is not separately identifiable from other promises in the contract and is, therefore, not distinct.

Trex Commercial satisfies its performance obligation over time as work progresses because control is transferred continuously to its customers. Revenue and estimated profit is recognized over time based on the proportion of actual costs incurred to date relative to total estimated costs at completion to measure progress toward satisfying the performance obligation. Incurred costs represent work performed, which corresponds with, and thereby best depicts, the transfer of control to the customer. Incurred costs include all direct material, labor, subcontract and certain indirect costs. The Company reviews and updates its estimates regularly and recognizes adjustments in estimated profit on contracts under the cumulative catch-up method. Under this method, the impact of the adjustment on revenue and estimated profit to date on a contract is recognized in the period the adjustment is identified. Revenues and profits in future periods are recognized using the adjusted estimate. If at any time the estimate of contract profitability indicates an anticipated loss on the contract, the Company recognizes the total loss in the period it is identified. During the year ended December 31, 2018, no adjustment to any one contract was material to the Company's Consolidated Financial Statements. In accordance with ASC 606-10-50-15, the Company discloses only the transaction price allocated to its remaining performance obligations on contracts with an original duration greater than one year, which was \$49.1 million as of December 31, 2018. The Company will recognize this revenue as performance obligations are satisfied, which is expected to occur within the next 18 months.

The Company recognizes an account receivable (contract asset) for satisfied performance obligations as it has an unconditional right to consideration and payment from the customer is due based solely on the passage of time. The Company receives payments from its customers on the accounts receivable based on the payment terms applicable to each individual contract and the customer pays in less than one year. Accounts receivables are included in Accounts receivable, net in the Consolidated Balance Sheets.

In addition, the timing of revenue recognition, billings and cash collections may result in revenues in excess of billings and contract retainage (contract assets), and billings in excess of revenues and customer deposits (contract liabilities). These assets and liabilities are reported on a contract-by-contract basis at the end of each reporting period in prepaid expenses and other assets (contract assets), and accrued expenses and other liabilities (contract liabilities). These assets and liabilities and changes in these assets and liabilities, respectively, were not material as of and for the year ended December 31, 2018.

Trex Commercial pays sales commissions that are directly attributable to identifiable contracts to certain of its employees. If the amortization period of the commission is one year or less then the Company recognizes the commission expense as incurred. Otherwise, the Company capitalizes the commission and amortizes it on a straight-line basis over the life of the contract. Trex Commercial does not grant contractual product return rights to customers other than pursuant to its assurance product warranty. All shipping and handling fees invoiced to the customer are included in net sales and the related costs are included in cost of sales.

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For the years ended December 31, 2018 and December 31, 2017, net sales were disaggregated in the following tables by (1) market (2) timing of revenue recognition, and (3) type of contract. The tables also include a reconciliation of the respective disaggregated net sales with the Company's reportable segments (in thousands).

| Year Ended December 31, 2018 | Reportable Segment | | |
|--|-----------------------------------|----------------------------------|--------------|
| | <i>Trex</i> <i>Residential</i> | <i>Trex</i> <i>Commercial</i> | <i>Total</i> |
| Timing of Revenue Recognition and Type of Contract | | | |
| Products transferred at a point in time and variable consideration contracts | \$ 613,229 | \$ | \$ 613,229 |
| Products transferred over time and fixed price contracts | | 71,021 | 71,021 |
| | \$ 613,229 | \$ 71,021 | \$ 684,250 |

| Year Ended December 31, 2017 | Reportable Segment | | |
|--|-----------------------------------|----------------------------------|--------------|
| | <i>Trex</i> <i>Residential</i> | <i>Trex</i> <i>Commercial</i> | <i>Total</i> |
| Timing of Revenue Recognition and Type of Contract | | | |
| Products transferred at a point in time and variable consideration contracts | \$ 543,346 | \$ | \$ 543,346 |
| Products transferred over time and fixed price contracts | | 21,807 | 21,807 |
| | \$ 543,346 | \$ 21,807 | \$ 565,153 |

13. STOCK-BASED COMPENSATION

On April 30, 2014, the Company's stockholders approved the Trex Company, Inc. 2014 Stock Incentive Plan (Plan), which was previously approved by the Board of Directors on February 19, 2014. The Plan amended and restated in its entirety the Trex Company, Inc. 2005 Stock Incentive Plan, as previously disclosed. The Plan is administered by the Compensation Committee of the Company's Board of Directors. Stock-based compensation is granted to officers, directors and certain key employees in accordance with the provisions of the Plan. The Plan provides for grants of stock options, restricted stock, restricted stock units, stock appreciation rights (SARs), and unrestricted stock. The total aggregate number of shares of the Company's common stock that may be issued under the Plan is 12,840,000.

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The Company recognizes stock-based compensation expense ratably over the period from grant date to the earlier of (1) the vesting date of the award, or (2) the date the grantee is eligible to retire without forfeiting the award. For performance-based restricted stock and performance-based restricted stock units, expense is recognized ratably over the performance and vesting period of each tranche based on management's judgment of the ultimate award that is probable to be paid out based on the achievement of the predetermined performance measures. For the employee stock purchase plan, compensation expense is recognized related to the discount on purchases. The following table summarizes the Company's stock-based compensation expense (in thousands):

| | Year Ended December 31, | | |
|---|--------------------------------|-----------------|-----------------|
| | 2018 | 2017 | 2016 |
| Time-based restricted stock and time-based restricted stock units | \$ 2,687 | \$ 1,992 | \$ 2,281 |
| Performance-based restricted stock and performance-based restricted stock units | 3,144 | 2,805 | 2,210 |
| Stock appreciation rights | 370 | 251 | 184 |
| Employee stock purchase plan | 143 | 139 | 113 |
| Total stock-based compensation | \$ 6,344 | \$ 5,187 | \$ 4,788 |

Stock-based compensation expense is included in Selling, general and administrative expenses in the accompanying Consolidated Statements of Comprehensive Income.

Time-Based Restricted Stock and Time-Based Restricted Stock Units

The fair value of time-based restricted stock and time-based restricted stock units is determined based on the closing price of the Company's shares on the grant date. Time-based restricted stock and time-based restricted stock units vest based on the terms of the awards. Unvested time-based restricted stock and unvested time-based restricted stock units are generally forfeitable upon the resignation of employment or termination of employment with cause. The total fair value of vested time-based restricted shares and vested time-based restricted stock units for the years ended December 31, 2018, 2017 and 2016 was \$5.1 million, \$5.5 million, and \$1.7 million, respectively. At December 31, 2018, there was \$4.2 million of total compensation expense related to unvested time-based restricted stock and unvested time-based restricted stock units remaining to be recognized over a weighted-average period of approximately 2.7 years.

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Time-based restricted stock and restricted stock unit activity under the Plan and all predecessor stock incentive plans is as follows:

| | Time-based Restricted Stock and Restricted Stock Unit | Weighted-Average Grant Price Per Share |
|--------------------------------|--|---|
| Nonvested at December 31, 2015 | 215,814 | \$ 14.72 |
| Granted | 115,748 | \$ 18.82 |
| Vested | (87,696) | \$ 21.17 |
| Forfeited | (266) | \$ 21.95 |
| Nonvested at December 31, 2016 | 243,600 | \$ 15.80 |
| Granted | 72,402 | \$ 36.27 |
| Vested | (162,372) | \$ 14.45 |
| Forfeited | (512) | \$ 18.68 |
| Nonvested at December 31, 2017 | 153,118 | \$ 26.90 |
| Granted | 87,264 | \$ 54.72 |
| Vested | (84,550) | \$ 26.65 |
| Forfeited | (284) | \$ 35.05 |
| Nonvested at December 31, 2018 | 155,548 | \$ 42.68 |

Performance-based Restricted Stock and Performance-Based Restricted Stock Units

The fair value of performance-based restricted stock and performance-based restricted stock units is determined based on the closing price of the Company's shares on the grant date. Unvested performance-based restricted stock and unvested performance-based restricted stock units are generally forfeitable upon the resignation of employment or termination of employment with cause. The performance-based restricted shares and performance-based restricted stock units have a three-year vesting period, vesting one-third each year based on target earnings before interest, taxes, depreciation and amortization (EBITDA) for 1 year, cumulative 2 years and cumulative 3 years, respectively. The number of shares that will vest, with respect to each vesting, will be between 0% and 200% of the target number of shares. At December 31, 2018, 2017, and 2016 there was \$1.6 million, \$1.8 million, and \$1.2 million, respectively, of total compensation expense related to unvested performance-based restricted stock and unvested performance-based restricted stock units remaining to be recognized over a weighted-average period of approximately 1.5 years.

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Performance-based restricted stock activity under the Plan is as follows:

| | Performance-based Restricted Stock and Performance-based Restricted Stock Units | Weighted-Average Grant Price Per Share |
|--------------------------------|--|---|
| Nonvested at December 31, 2015 | 58,194 | \$ 19.69 |
| Granted | 89,850 | \$ 17.92 |
| Vested | (29,898) | \$ 17.86 |
| Forfeited | (1,314) | \$ 16.85 |
| Nonvested at December 31, 2016 | 116,832 | \$ 18.32 |
| Granted | 86,614 | \$ 28.77 |
| Vested | (86,788) | \$ 18.64 |
| Forfeited | | \$ |
| Nonvested at December 31, 2017 | 116,658 | \$ 25.85 |
| Granted | 80,570 | \$ 35.26 |
| Vested | (106,022) | \$ 23.52 |
| Forfeited | | \$ |
| Nonvested at December 31, 2018 | 91,206 | \$ 36.86 |

Stock Appreciation Rights

SARs are granted with a grant price equal to the closing market price of the Company's common stock on the date of grant. These awards expire ten years after the date of grant and vest based on the terms of the individual awards. The SARs are generally forfeitable upon the resignation of employment or termination of employment with cause. The Company recognizes compensation cost on a straight-line basis over the vesting period for the award.

As of December 31, 2018, there was \$0.4 million of unrecognized compensation cost related to SARs. The fair value of each SAR is estimated on the date of grant using a Black-Scholes option-pricing model. There were no SARs issued in the year ended December 31, 2016. For SARs issued in the years ended December 31, 2018 and December 31, 2017, respectively, the assumptions shown in the following table were used:

| | December 31, 2018 | 2017 |
|---------------------------------|------------------------------|-------------|
| Dividend yield | 0% | 0% |
| Average risk-free interest rate | 2.7% | 2.0% |
| Expected term (years) | 5 | 5 |
| Expected volatility | 40.5% | 42.3% |

Dividend Yield. The Company has never paid cash dividends on its common stock.

Average Risk-Free Interest Rate. The Company uses the U.S. Treasury rate having a term that most closely resembles the expected term of the option.

Expected Term. The expected term is the period of time that the SARs granted are expected to remain unexercised. SARs granted during the years ended December 31, 2018 and 2017 had a maximum term of ten years. The Company used historical exercise behavior with further consideration given to the class of employees to whom the equity awards were granted to estimate the expected term of the SAR.

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Expected Volatility. Volatility is a measure of the amount by which a financial variable such as a share price has fluctuated (historical volatility) or is expected to fluctuate (expected volatility) during a period. The Company has used the historical volatility over the average expected term of the options granted as the expected volatility.

The Company recognizes forfeitures as they occur.

The weighted-average grant date fair value of SARs granted during the years ended December 31, 2018 and December 31, 2017 was \$22.09 and \$13.99, respectively.

SAR activity under the Plan and all predecessor stock incentive plans is as follows:

| | SARs | Weighted-Average Grant Price Per Share | Weighted- Average Remaining Contractual Life (Years) | Aggregate Intrinsic Value as of December 31, 2018 |
|-------------------------------------|-----------|--|---|---|
| Outstanding at December 31, 2015 | 524,154 | \$ 6.57 | | |
| Granted | | \$ | | |
| Exercised | (248,704) | \$ 5.55 | | |
| Canceled | | \$ | | |
| Outstanding at December 31, 2016 | 275,450 | \$ 9.79 | | |
| Granted | 37,478 | \$ 35.38 | | |
| Exercised | (34,812) | \$ 8.07 | | |
| Canceled | | \$ | | |
| Outstanding at December 31, 2017 | 278,116 | \$ 13.45 | | |
| Granted | 21,260 | \$ 56.59 | | |
| Exercised | (60,900) | \$ 5.27 | | |
| Canceled | | \$ | | |
| Outstanding at December 31, 2018 | 238,476 | \$ 19.26 | 5.3 | \$ 9,562,603 |
| Vested at December 31, 2018 | 192,232 | \$ 13.08 | 4.5 | \$ 8,896,335 |
| Exercisable at December 31, 2018 | 192,232 | \$ 13.08 | 4.5 | \$ 8,896,335 |

Employee Stock Purchase Plan

The Company has an employee stock purchase plan (ESPP) that permits eligible employees to purchase shares of common stock of the Company at a purchase price which is the lesser of 85% of the market price on either the first day of the calendar quarter or the last day of the calendar quarter. Eligible employees may elect to participate in the plan by authorizing payroll deductions of up to 15% of gross compensation for each payroll period. On the last day of each quarter, each participant's contribution account is used to purchase the maximum number of whole shares of

common stock determined by dividing the contribution account balance by the purchase price. The aggregate number of shares of common stock that may be purchased under the plan is 1,200,000. Through December 31, 2018, employees had purchased approximately 874,235 shares under the plan.

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The Company leases office space, storage warehouses and certain office and plant equipment under various operating leases. Minimum annual payments under these non-cancelable leases as of December 31, 2018 were as follows (in thousands):

| Year Ending December 31, | |
|-------------------------------------|------------------|
| 2019 | \$ 10,998 |
| 2020 | 9,317 |
| 2021 | 8,952 |
| 2022 | 6,901 |
| 2023 | 6,576 |
| Thereafter | 19,080 |
| Total minimum lease payments | \$ 61,824 |

For the years ended December 31, 2018, 2017 and 2016, the Company recognized rental expenses of approximately \$10.0 million, \$9.1 million, and \$9.9 million, respectively.

15. EMPLOYEE BENEFIT PLANS

The Company has two 401(k) Profit Sharing Plans for the benefit of its employees who meet certain eligibility requirements. The plans cover substantially all of the Company's full-time employees. One of the plans provides for the Company to match contributions equal to 100% of an employee's contribution to the plan up to 6% of base salary. The other plan provides for the Company to match \$0.25 in 2018 and \$0.50 beginning in 2019 for every \$1.00 contributed by an employee to the plan up to 6% of compensation.

The Company's contributions to the plans totaled \$4.2 million, \$3.0 million, and \$2.5 million, for the years ended December 31, 2018, 2017 and 2016, respectively.

16. INCOME TAXES

Income tax provision (benefit) consists of the following (in thousands):

| | Year Ended December 31, | | |
|---------------------------------------|--------------------------------|-------------|-------------|
| | 2018 | 2017 | 2016 |
| Current income tax provision: | | | |
| Federal | \$ 33,578 | \$ 41,177 | \$ 26,752 |
| State | 7,674 | 5,420 | 2,798 |
| | 41,252 | 46,597 | 29,550 |
| Deferred income tax provision: | | | |

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| | | | |
|----------------------------|-----------|-----------|-----------|
| Federal | 988 | 1,177 | 5,217 |
| State | 49 | (983) | 216 |
| | 1,037 | 194 | 5,433 |
| Total income tax provision | \$ 42,289 | \$ 46,791 | \$ 34,983 |

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The income tax provision differs from the amount of income tax determined by applying the U.S. Federal statutory rate to income before taxes as a result of the following (in thousands):

| | Year Ended December 31, | | |
|---|--------------------------------|---------------|---------------|
| | 2018 | 2017 | 2016 |
| U.S. Federal statutory taxes | \$ 37,141 | \$ 49,671 | \$ 35,990 |
| State and local taxes, net of U.S. Federal benefit | 7,716 | 5,110 | 3,747 |
| Permanent items | 470 | 576 | 396 |
| Excess tax benefits from vesting or settlement of stock compensation awards | (2,368) | (1,454) | (1,749) |
| Domestic production activities deduction | | (4,376) | (2,740) |
| Federal credits | (662) | (534) | (488) |
| Other | (8) | (2,202) | (173) |
| Total income tax provision | \$ 42,289 | \$ 46,791 | \$ 34,983 |

Deferred tax assets and liabilities consist of the following (in thousands):

| | As of December 31, | |
|---|---------------------------|----------------|
| | 2018 | 2017 |
| Deferred tax assets: | | |
| Net operating losses | \$ 79 | \$ 123 |
| Residential product warranty reserve | 7,804 | 8,876 |
| Stock-based compensation | 1,725 | 1,823 |
| Accruals not currently deductible and other | 3,928 | 1,838 |
| Inventories | 4,682 | 3,783 |
| State tax credit carryforwards | 3,400 | 3,619 |
| Gross deferred tax assets, before valuation allowance | 21,618 | 20,062 |
| Valuation allowance | (3,015) | (3,096) |
| Gross deferred tax assets, after valuation allowance | 18,603 | 16,966 |
| Deferred tax liabilities: | | |
| Depreciation | (13,893) | (12,046) |
| Goodwill amortization | (3,774) | (2,781) |
| Inventories and other | (3,061) | (3,228) |
| Gross deferred tax liabilities | (20,728) | (18,055) |
| Net deferred tax liability | \$ (2,125) | \$ (1,089) |

The Company recognizes deferred tax assets and liabilities based on the difference between the financial statement basis and tax basis of assets and liabilities using enacted rates expected to be in effect during the year in which the

differences reverse. In accordance with accounting standards, the Company assesses the likelihood that its deferred tax assets will be realized. Deferred tax assets are reduced by a valuation allowance when, after considering all available positive and negative evidence, it is determined that it is more likely than not that some portion, or all, of the deferred tax asset will not be realized.

The Company has recognized the tax effects of the Tax Cuts and Jobs Act (Act) in its consolidated financial statements and related notes as of and for the year ended December 31, 2017. Deferred tax assets and deferred tax liabilities that existed as of the enactment date and that reversed after the Act's effective date of January 1, 2018 were adjusted to reflect the new Federal statutory tax rate of 21%. The effect of the change in tax rate on the deferred tax assets and deferred tax liabilities resulted in a tax benefit of \$1.9 million for the year ended

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December 31, 2017, which is included in *Other* in the above tax rate reconciliation. The Company finalized its analysis of the Act and completed its calculation, which did not affect the measurement of these balances nor give rise to new deferred tax amounts. As of December 31, 2018, the Company had a valuation allowance of \$3.0 million against deferred tax assets it estimates will not be realized. The Company will analyze its position in subsequent reporting periods, considering all available positive and negative evidence, in determining the expected realization of its deferred tax assets.

The Company realized \$2.4 million and \$1.5 million of excess tax benefits during 2018 and 2017, respectively, related to share-based compensation awards.

The Company recognizes interest and penalties related to tax matters as a component of *Selling, general and administrative expenses* in the accompanying Consolidated Statements of Comprehensive Income. As of December 31, 2018, the Company has identified no uncertain tax position and, accordingly, has not recorded any unrecognized tax benefits or associated interest and penalties.

The Company operates in multiple tax jurisdictions and, in the normal course of business, its tax returns are subject to examination by various taxing authorities. Such examinations may result in future assessments by these taxing authorities, and the Company has accrued a liability when it believes that it is not more likely than not that it will realize the benefits of tax positions that it has taken or for the amount of any tax benefit that exceeds the cumulative probability threshold in accordance with accounting standards. As of December 31, 2018, Federal tax years 2015 through 2018 remain subject to examination. The Company believes that adequate provisions have been made for all tax returns subject to examination. Sales made to foreign distributors are not taxable in any foreign jurisdictions as the Company does not have a taxable presence.

17. SEGMENT INFORMATION

Prior to July 31, 2017, the Company operated in one reportable segment. Subsequent to the acquisition of certain assets and assumption of certain liabilities of SC Company on July 31, 2017, the Company operates in two reportable segments:

Trex Residential manufactures wood-alternative decking and railing and related products marketed under the brand name Trex®. The products are sold to its distributors and two national retailers who, in turn, sell primarily to the residential market, which includes replacement, remodeling and new construction related to outdoor living products. Trex Residential net sales were \$613.2 million, \$543.3 million, and \$479.6 million in the years ended December 31, 2018, 2017, and 2016, respectively.

Trex Commercial designs, engineers, and markets modular and architectural railing and staging systems for commercial and multi-family market, including sports stadiums and performing arts venues. The segment's products are sold through architects, specifiers, contractors, and others doing business within the segment's commercial market. Trex Commercial net sales were \$71.0 million in the year ended December 31, 2018, and \$21.8 million from the date of acquisition through December 31, 2017.

The Company's reportable segments have been determined in accordance with its internal management structure, which is organized based on residential and commercial operations. The Company evaluates performance of each segment primarily based on net sales and earnings before interest, taxes, depreciation and amortization (EBITDA).

The Company uses net sales to assess performance and allocate resources as this measure represents the amount of business the segment engaged in during a given period of time, is an indicator of market growth and acceptance of segment products, and represents the segment's customers' spending habits along with the amount of product the segment sells relative to its competitors. The Company uses EBITDA to assess performance and allocate resources because it believes that EBITDA facilitates performance comparison between the segments by eliminating interest, taxes, and depreciation and amortization charges to income. The

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below segment data includes data for Trex Residential for the years ended December 31, 2018 and December 31, 2017, and data for Trex Commercial for the year ended December 31, 2018, and for the year ended December 31, 2017 from the date of the acquisition of SC Company through December 31, 2017 (in thousands):

| | Year ended December 31, 2018 | | |
|-------------------------------|------------------------------|-----------------|------------|
| | Trex Residential | Trex Commercial | Total |
| Net sales | \$ 613,229 | \$ 71,021 | \$ 684,250 |
| Net income | \$ 131,823 | \$ 2,749 | \$ 134,572 |
| EBITDA | \$ 186,268 | \$ 6,868 | \$ 193,136 |
| Depreciation and amortization | \$ 13,216 | \$ 3,251 | \$ 16,467 |
| Income tax expense | \$ 41,421 | \$ 868 | \$ 42,289 |
| Capital expenditures | \$ 31,392 | \$ 2,424 | \$ 33,816 |
| Total assets | \$ 380,682 | \$ 84,440 | \$ 465,122 |

Reconciliation of net income to EBITDA:

| | Year Ended December 31, 2018 | | |
|--------------------------------|------------------------------|-----------------|------------|
| | Trex Residential | Trex Commercial | Total |
| Net income | \$ 131,823 | \$ 2,749 | \$ 134,572 |
| Interest (income) expense, net | (192) | | (192) |
| Taxes | 41,421 | 868 | 42,289 |
| Depreciation and amortization | 13,216 | 3,251 | 16,467 |
| EBITDA | \$ 186,268 | \$ 6,868 | \$ 193,136 |

| | Year ended December 31, 2017 | | |
|-------------------------------|------------------------------|-----------------|------------|
| | Trex Residential | Trex Commercial | Total |
| Net sales | \$ 543,346 | \$ 21,807 | \$ 565,153 |
| Net income (loss) | \$ 97,412 | \$ (2,284) | \$ 95,128 |
| EBITDA | \$ 160,382 | \$ (1,272) | \$ 159,110 |
| Depreciation and amortization | \$ 14,598 | \$ 2,132 | \$ 16,730 |
| Income tax expense (benefit) | \$ 47,911 | \$ (1,120) | \$ 46,791 |
| Capital expenditures | \$ 14,989 | \$ 51 | \$ 15,040 |
| Total assets | \$ 247,817 | \$ 78,410 | \$ 326,227 |

Reconciliation of net income to EBITDA:

| | Year Ended December 31, 2017 | | |
|-------------------|------------------------------|-----------------|-----------|
| | Trex Residential | Trex Commercial | Total |
| Net income (loss) | \$ 97,412 | \$ (2,284) | \$ 95,128 |
| Interest | 461 | | 461 |
| Taxes | 47,911 | (1,120) | 46,791 |

| | | | |
|-------------------------------|-------------------|-------------------|-------------------|
| Depreciation and amortization | 14,598 | 2,132 | 16,730 |
| EBITDA | \$ 160,382 | \$ (1,272) | \$ 159,110 |

18. SEASONALITY

The operating results for Trex Residential have historically varied from quarter to quarter. Seasonal, erratic or prolonged adverse weather conditions in certain geographic regions reduce the level of home improvement and construction activity and can shift demand for its products to a later period. As part of its normal business practice and consistent with industry practice, Trex Residential has historically offered incentive programs to its

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distributors and dealers to build inventory levels before the start of the prime deck-building season in order to ensure adequate availability of its product to meet anticipated seasonal consumer demand. The seasonal effects are often offset by the positive effect of the incentive programs. The operating results for Trex Commercial have not historically varied from quarter to quarter as a result of seasonality; however, they are driven by the timing of individual projects, which may vary each quarterly period.

19. COMMITMENTS AND CONTINGENCIES*Legal Matters*

The Company has lawsuits, as well as other claims, pending against it which are ordinary routine litigation and claims incidental to the business. Management has evaluated the merits of these lawsuits and claims, and believes that their ultimate resolution will not have a material effect on the Company's consolidated financial condition, results of operations, liquidity or competitive position.

Purchase Commitments

The Company fulfills requirements for raw materials under both purchase orders and supply contracts. In the year ended December 31, 2018, the Company purchased substantially all of its reclaimed wood fiber requirements under purchase orders which do not involve long-term supply commitments. All of the Company's scrap polyethylene, aluminum and stainless steel purchases are under short-term supply contracts that may average approximately one to two years, for which pricing is negotiated as needed, or under purchase orders that do not involve long-term supply commitments.

The wood and polyethylene supply contracts generally provide that the Company is obligated to purchase all of the wood or polyethylene a supplier provides, if the wood or polyethylene meets certain specifications. The amount of wood and polyethylene the Company is required to purchase under these contracts varies with the production of its suppliers and, accordingly, is not fixed or determinable. As of December 31, 2018, the Company has purchase commitments under material supply contracts of \$19.0 million, \$7.6 million, and \$0.03 million for the years ending December 31, 2019, 2020, and 2021, respectively.

Product Warranty

The Company warrants that its Trex Residential products will be free from material defects in workmanship and materials. This warranty generally extends for a period of 25 years for residential use and 10 years for commercial use, excluding Trex Signature® Railing, which has a warranty period of 25 years for both residential and commercial use. The Company further warrants that Trex Transcend®, Trex Enhance®, Trex Select® and Universal Fascia products will not fade in color more than a certain amount and will be resistant to permanent staining from food substances or mold, provided the stain is cleaned within seven days of appearance. This warranty extends for a period of 25 years for residential use and 10 years for commercial use. If there is a breach of such warranties, the Company has an obligation either to replace the defective product or refund the purchase price. The Company also warrants its Trex Commercial products for one to three years.

The Company continues to receive and settle claims for decking products manufactured at its Nevada facility prior to 2007 that exhibit surface flaking and maintains a warranty reserve to provide for the settlement of these claims. Estimating the warranty reserve for surface flaking claims requires management to estimate (1) the number of claims to be settled with payment and (2) the average cost to settle each claim.

To estimate the number of claims to be settled with payment, the Company utilizes actuarial techniques to determine a reasonable possible range of claims to be received and the percentage of those claims that will ultimately require payment. Management utilizes a range of assumptions derived from claim count history and the identification of factors influencing the claim counts to determine its best estimate of future claims for which

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to record a related liability. The number of claims received has declined each year since peaking in 2009, although the rate of decline has decelerated in recent years. The cost per claim varies due to a number of factors, including the size of affected decks, the availability and type of replacement material used, the cost of production of replacement material and the method of claim settlement.

The Company monitors surface flaking claims activity each quarter for indications that its estimates require revision. Typically, a majority of surface flaking claims received in a year are received during the summer outdoor season, which spans the second and third quarters. It has been the Company's practice to utilize the actuarial techniques discussed above during the third quarter, after a significant portion of all claims has been received for the fiscal year and variances to annual claims expectations are more meaningful. The number of incoming claims received in the year ended December 31, 2018, was lower than the Company's expectations and considerably lower than the number of claims received in the year ended December 31, 2017, continuing the historical year-over-year decline in incoming claims. The favorable experience in incoming claims was offset, in part, by increased average settlement cost per claim experienced in the year ended December 31, 2018. The Company believes its reserve at December 31, 2018 is sufficient to cover future surface flaking obligations and no adjustments were required in the current year.

The Company's analysis is based on currently known facts and a number of assumptions, as discussed above, and current expectations. Projecting future events such as the number of claims to be received, the number of claims that will require payment and the average cost of claims could cause the actual warranty liabilities to be higher or lower than those projected, which could materially affect the Company's financial condition, results of operations or cash flows. The Company estimates that the annual number of claims received will continue to decline over time and that the average cost per claim will increase slightly, primarily due to inflation. If the level of claims received or average cost per claim differs materially from expectations, it could result in additional increases or decreases to the warranty reserve and a decrease or increase in earnings and cash flows in future periods. The Company estimates that a 10% change in the expected number of remaining claims to be settled with payment or the expected cost to settle claims may result in approximately a \$2.6 million change in the surface flaking warranty reserve.

The Company also maintains a warranty reserve for the settlement of other residential product warranty claims and records the provision at the time of product sale.

The following is a reconciliation of the Company's residential product warranty reserve (in thousands):

| | Year Ended December 31, 2018 | | |
|-------------------------------------|-------------------------------------|------------------------------|--------------|
| | Surface Flaking | Other Residential | Total |
| Beginning balance, January 1 | \$ 28,158 | \$ 6,841 | \$ 34,999 |
| Provisions and changes in estimates | | 1,104 | 1,104 |
| Settlements made during the period | (4,207) | (1,142) | (5,349) |
| Ending balance, December 31 | \$ 23,951 | \$ 6,803 | \$ 30,754 |

| | Year Ended December 31, 2017 | | |
|--|-------------------------------------|------------------------------|--------------|
| | Surface Flaking | Other Residential | Total |

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| | | | |
|-------------------------------------|-----------|----------|-----------|
| Beginning balance, January 1 | \$ 33,847 | \$ 3,845 | \$ 37,692 |
| Provisions and changes in estimates | | 4,268 | 4,268 |
| Settlements made during the period | (5,689) | (1,272) | (6,961) |
| Ending balance, December 31 | \$ 28,158 | \$ 6,841 | \$ 34,999 |

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Three Months Ended

| | December 31, 2018 | September 30, 2018 | June 30, 2018 | March 31, 2018 | December 31, 2017 | September 30, 2017 | June 30, 2017 | March 31, 2017 |
|--|----------------------|-----------------------|------------------|-------------------|----------------------|-----------------------|------------------|-------------------|
|--|----------------------|-----------------------|------------------|-------------------|----------------------|-----------------------|------------------|-------------------|

(In thousands, except share and per share data)

| | | | | | | | | |
|--|------------|------------|------------|------------|------------|------------|------------|------------|
| Net sales | \$ 139,971 | \$ 166,380 | \$ 206,692 | \$ 171,207 | \$ 122,212 | \$ 140,194 | \$ 157,941 | \$ 144,806 |
| Gross profit | \$ 59,856 | \$ 67,210 | \$ 91,115 | \$ 76,713 | \$ 50,906 | \$ 55,284 | \$ 72,014 | \$ 65,169 |
| Net income | \$ 25,171 | \$ 29,471 | \$ 42,820 | \$ 37,110 | \$ 18,299 | \$ 20,098 | \$ 28,782 | \$ 27,949 |
| Basic net income per share | \$ 0.43 | \$ 0.50 | \$ 0.73 | \$ 0.63 | \$ 0.31 | \$ 0.34 | \$ 0.49 | \$ 0.48 |
| Basic weighted average common shares outstanding | 58,603,537 | 58,741,973 | 58,760,753 | 58,855,156 | 58,825,696 | 58,808,098 | 58,778,916 | 58,726,420 |
| Diluted net income per share | \$ 0.43 | \$ 0.50 | \$ 0.73 | \$ 0.63 | \$ 0.31 | \$ 0.34 | \$ 0.49 | \$ 0.48 |
| Diluted weighted average common shares outstanding | 58,936,795 | 59,084,117 | 59,051,413 | 59,199,622 | 59,222,258 | 59,156,432 | 59,100,836 | 59,122,812 |

The operating results for Trex Residential have historically varied from quarter to quarter. Seasonal, erratic or prolonged adverse weather conditions in certain geographic regions reduce the level of home improvement and construction activity and can shift demand for its products to a later period. The operating results for Trex Commercial have not historically varied from quarter to quarter as a result of seasonality; however, they are driven by the timing of individual projects, which may vary each quarterly period.

The Tax Cuts and Jobs Act (Act) was enacted on December 22, 2017. Accordingly, the Company has recognized the tax effects of the Act in its consolidated financial statements and related notes as of and for the year ended December 31, 2017. Deferred tax assets that existed as of the enactment date and that are expected to reverse after the Act's effective date of January 1, 2018 have been adjusted to reflect the new Federal statutory tax rate of 21%. The effect of the change in tax rate on the deferred tax assets and deferred tax liabilities resulted in a tax benefit of \$1.9 million for the year ended December 31, 2017.

On May 2, 2018, the Board of Directors of the Company approved a two-for-one stock split of the Company's common stock, par value \$0.01. The stock split was in the form of a stock dividend distributed on June 18, 2018, to stockholders of record at the close of business on May 23, 2018. The stock split entitled each stockholder to receive one additional share of common stock, par value \$0.01, for each share they held as of the record date. All common stock share and per share data for all periods presented have been retroactively adjusted to reflect the stock split.

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TREX COMPANY, INC.

SCHEDULE II VALUATION AND QUALIFYING ACCOUNTS AND RESERVES

(In thousands)

| Descriptions | Balance at Beginning of Period | Additions (Reductions) Charged to Cost and Expenses | Deductions | Balance at End of Period |
|---|--------------------------------------|---|------------|--------------------------------|
| Year ended December 31, 2018: | | | | |
| Trex Residential product warranty reserve | \$ 34,999 | \$ 1,104 | \$ (5,349) | \$ 30,754 |
| Income tax valuation allowance | \$ 3,096 | \$ | \$ (81) | \$ 3,015 |
| Year ended December 31, 2017: | | | | |
| Trex Residential product warranty reserve | \$ 37,692 | \$ 4,268 | \$ (6,961) | \$ 34,999 |
| Income tax valuation allowance | \$ 4,061 | \$ | \$ (965) | \$ 3,096 |
| Year ended December 31, 2016: | | | | |
| Trex Residential product warranty reserve | \$ 33,522 | \$ 10,852 | \$ (6,682) | \$ 37,692 |
| Income tax valuation allowance | \$ 4,582 | \$ | \$ (521) | \$ 4,061 |

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Table of Contents**SIGNATURES**

Pursuant to the requirements of Section 13 or 15(d) 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.

Trex Company, Inc.

Date: February 14, 2019

By: */s/ JAMES E. CLINE*
James E. Cline

President and Chief Executive Officer

(Duly Authorized Officer)

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed as of February 14, 2019 by the following persons on behalf of the registrant and in the capacities indicated.

| Signature | Title |
|--|---|
| <i>/s/ JAMES E. CLINE</i> James E. Cline | President and Chief Executive Officer (Principal Executive Officer); Director |
| <i>/s/ BRYAN H. FAIRBANKS</i> Bryan H. Fairbanks | Executive Vice President and Chief Financial Officer (Principal Financial Officer and Principal Accounting Officer) |
| <i>/s/ RONALD W. KAPLAN</i> Ronald W. Kaplan | Chairman |
| <i>/s/ MICHAEL F. GOLDEN</i> Michael F. Golden | Director |
| <i>/s/ JAY M. GRATZ</i> Jay M. Gratz | Director |
| <i>/s/ RICHARD E. POSEY</i> Richard E. Posey | Director |
| <i>/s/ PATRICIA B. ROBINSON</i> | Director |

Patricia B. Robinson

/s/ GERALD VOLAS

Director

Gerald Volas

Table of Contents**EXHIBIT INDEX**

| Exhibit | |
|----------------|---|
| Number | Exhibit Description |
| 2.1 | <u>Asset Purchase Agreement by and among Trex Commercial Products, Inc., Staging Concepts Acquisition, LLC and Stadium Consolidation, LLC. Filed as Exhibit 2.1 to the Company's Current Report on Form 8-K filed July 31, 2017 and incorporated herein by reference.</u> |
| 3.1 | <u>Restated Certificate of Incorporation of Trex Company, Inc. (the Company). Filed as Exhibit 3.1 to the Company's Registration Statement on Form S-1 (No. 333-63287) and incorporated herein by reference.</u> |
| 3.2 | <u>Certificate of Amendment to the Restated Certificate of Incorporation of Trex Company, Inc. dated April 30, 2014. Filed as Exhibit 3.2 to the Company's Quarterly Report on Form 10-Q for the quarterly period ended March 31, 2014 and incorporated herein by reference.</u> |
| 3.3 | <u>Second Certificate of Amendment to the Restated Certificate of Incorporation of Trex company, Inc. dated May 2, 2018. Filed as Exhibit 3.3 to the Company's Quarter Report on Form 10-Q for the quarterly period ended March 31, 2018 and incorporated herein by reference.</u> |
| 3.4 | <u>Amended and Restated By-Laws of the Company. Filed as Exhibit 3.2 to the Company's Current Report on Form 8-K filed May 7, 2008 and incorporated herein by reference.</u> |
| 4.1 | <u>Specimen certificate representing the Company's common stock. Filed as Exhibit 4.1 to the Company's Registration Statement on Form S-1 (No. 333-63287) and incorporated herein by reference.</u> |
| 4.2 | <u>Third Amended and Restated Credit Agreement dated as of January 12, 2016 between the Company, as borrower; the subsidiaries of the Company as guarantors; Bank of America, N.A., as a Lender, Administrative Agent, Swing Line Lender and Letter of Credit Issuer; and certain other lenders arranged by Bank of America Merrill Lynch as Sole Lead Arranger and Sole Bookrunner. Filed as Exhibit 4.1 to the Company's Current Report on Form 8-K filed on January 14, 2016 and incorporated herein by reference.</u> |
| 4.3 | <u>Revolver Note dated January 12, 2016 payable by the Company to Bank of America, N.A. in the amount of the lesser of \$110,000,000 or the outstanding revolver advances made by Bank of America, N.A. Filed as Exhibit 4.2 to the Company's Current Report on Form 8-K filed on January 14, 2016 and incorporated herein by reference.</u> |
| 4.4 | <u>Revolver Note dated January 12, 2016 payable by the Company to Citibank, N.A. in the amount of the lesser of \$75,000,000 or the outstanding revolver advances made by Citibank, N.A. Filed as Exhibit 4.3 to the Company's Current Report on Form 8-K filed on January 14, 2016 and incorporated herein by reference.</u> |
| 4.5 | <u>Revolver Note dated January 12, 2016 payable by the Company to Capital One, N.A. in the amount of the lesser of \$35,000,000 or the outstanding revolver advances made by Capital One, N.A. Filed as Exhibit 4.4 to the Company's Current Report on Form 8-K filed on January 14, 2016 and incorporated herein by reference.</u> |
| 4.6 | <u>Revolver Note dated January 12, 2016 payable by the Company to SunTrust Bank in the amount of the lesser of \$30,000,000 or the outstanding revolver advances made by SunTrust Bank. Filed as</u> |

Exhibit 4.5 to the Company's Current Report on Form 8-K filed on January 14, 2016 and incorporated herein by reference.

- 4.7 Third Amended and Restated Security and Pledge Agreement dated as of January 12, 2016 between the Company, as debtor, and Bank of America, N.A. as Administrative Agent (including Notices of Grant of Security Interest in Copyrights and Trademarks). Filed as Exhibit 4.6 to the Company's Current Report on Form 8-K filed on January 14, 2016 and incorporated herein by reference.

Table of Contents**Exhibit**

| Number | Exhibit Description |
|---------------|--|
| 4.8 | <u>Assignment of Amended and Restated Credit Line Deed of Trust, Substitution of Trustee and Amendment, dated as of January 12, 2016, by and among the Company as grantor, PRLAP, INC. as trustee, and Bank of America, N.A., as Administrative Agent for Bank of America, N.A., Citibank, N.A., Capital One, N.A., and SunTrust Bank, as Beneficiaries relating to real property partially located in the County of Frederick, Virginia and partially located in the City of Winchester, Virginia. Filed as Exhibit 4.7 to the Company's Current Report on Form 8-K filed on January 14, 2016 and incorporated herein by reference.</u> |
| 4.9 | <u>Amended and Restated Deed of Trust, dated as of January 12, 2016, by and among the Company as grantor, First American Title Insurance Company, as trustee, and Bank of America, N.A., Citibank, N.A., Capital One, N.A., and SunTrust Bank, as Beneficiaries relating to real property located in the County of Fernley, Nevada. Filed as Exhibit 4.8 to the Company's Current Report on Form 8-K filed on January 14, 2016 and incorporated herein by reference.</u> |
| 10.1 | <u>Description of Management Compensatory Plans and Arrangements. Filed herewith. **</u> |
| 10.2 | <u>Trex Company, Inc. Amended and Restated 2014 Stock Incentive Plan. Filed as Exhibit 10.1 to the Company's Quarterly Report on Form 10-Q for the quarterly period ended March 31, 2018 and incorporated herein by reference. **</u> |
| 10.3 | <u>Trex Company, Inc. Amended and Restated 1999 Incentive Plan for Outside Directors as amended on October 24, 2018. Filed as Exhibit 10.1 to the Company's Quarterly Report on Form 10-Q for the quarterly period ended September 30, 2018 and incorporated herein by reference. **</u> |
| 10.4 | <u>Form of Trex Company, Inc. 2014 Stock Incentive Plan Stock Appreciation Rights Agreement. Filed as Exhibit 10.1 to the Company's Quarterly Report on Form 10-Q for the quarterly period ended September 30, 2015 and incorporated herein by reference. **</u> |
| 10.5 | <u>Form of Trex Company, Inc. 2014 Stock Incentive Plan Time-Based Restricted Stock Unit Agreement. Filed as Exhibit 10.3 to the Company's Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2015 and incorporated herein by reference. **</u> |
| 10.6 | <u>Form of Trex Company, Inc. 2014 Stock Incentive Plan Performance-Based Restricted Stock Unit Agreement. Filed as Exhibit 10.4 to the Company's Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2015 and incorporated herein by reference. **</u> |
| 10.7 | <u>Form of Trex Company, Inc. Amended and Restated 1999 Incentive Plan for Outside Directors Restricted Stock Unit Agreement. Filed as Exhibit 10.2 to the Company's Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2015 and incorporated herein by reference. **</u> |
| 10.8 | <u>Change in Control Severance Agreement dated May 6, 2015 by and between Trex Company, Inc. and James E. Cline. Filed as Exhibit 10.1 to the Company's Current Report on Form 8-K filed May 8, 2015 and incorporated herein by reference. **</u> |
| 10.9 | <u>Severance Agreement dated May 6, 2015 by and between Trex Company, Inc. and James E. Cline. Filed as Exhibit 10.2 to the Company's Current Report on Form 8-K filed May 8, 2015 and incorporated herein by reference. **</u> |
| 10.10 | <u>Form of Change in Control Severance Agreement between Trex Company, Inc. and Officers other than the Chief Executive Officer. Filed as Exhibit 10.16 to the Company's Annual Report on Form 10-K for</u> |

the year ended December 31, 2016 and incorporated herein by reference. **

- 10.11 Form of Severance Agreement between Trex Company, Inc. and Officers other than the Chief Executive Officer. Filed as Exhibit 10.1 to the Company's Quarterly Report on Form 10-Q for the quarterly period ended March 31, 2015 and incorporated herein by reference. **
- 10.12 Retention Agreement, dated as of July 24, 2012, between Trex Company, Inc. and James E. Cline. Filed as Exhibit 10.4 to the Company's Quarterly Report on Form 10-Q for the quarterly period ended September 30, 2012 and incorporated herein by reference. **

Table of Contents**Exhibit**

| Number | Exhibit Description |
|---------------|--|
| 10.13 | <u>Form of Retention Agreement for Company Officers dated May 2, 2018. Filed as Exhibit 10.2 to the Company's Quarterly report on Form 10-Q for the quarterly period ended March 31, 2018 and incorporated herein by reference. **</u> |
| 10.14 | <u>Form of Indemnity Agreement for Directors. Filed as Exhibit 10.19 to the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2008 and incorporated herein by reference.</u> |
| 10.15 | <u>Form of Indemnity Agreement for Officers. Filed as Exhibit 10.20 to the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2008 and incorporated herein by reference.</u> |
| 10.16 | <u>Form of Indemnity Agreement for Director/Officers. Filed as Exhibit 10.21 to the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2008 and incorporated herein by reference.</u> |
| 10.17 | <u>Form of Distributor Agreement of Trex Company, Inc. Filed as Exhibit 10.23 to the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2008 and incorporated herein by reference.</u> |
| 10.18 | <u>Form of Trex Company, Inc. Fencing Agreement for Installers/Retailers. Filed as Exhibit 10.4 to the Company's Quarterly Report on Form 10-Q for the quarterly period ended September 30, 2006 and incorporated herein by reference.</u> |
| 21 | <u>Subsidiaries of the Company. Filed herewith.</u> |
| 23 | <u>Consent of Ernst & Young LLP, Independent Registered Public Accounting Firm. Filed herewith.</u> |
| 31.1 | <u>Certification of Chief Executive Officer of the Company pursuant to Rule 13a-14(a) under the Securities Exchange Act of 1934. Filed herewith.</u> |
| 31.2 | <u>Certification of Chief Financial Officer of the Company pursuant to Rule 13a-14(a) under the Securities Exchange Act of 1934. Filed herewith.</u> |
| 32 | <u>Certifications of Chief Executive Officer and Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (18 U.S.C. § 1350). Furnished herewith.</u> |
| 101.INS | XBRL Instance Document. Filed. |
| 101.SCH | XBRL Taxonomy Extension Schema Document. Filed. |
| 101.CAL | XBRL Taxonomy Extension Calculation Linkbase Document. Filed. |
| 101.DEF | XBRL Taxonomy Extension Definition Linkbase Document. Filed. |
| 101.LAB | XBRL Taxonomy Extension Label Linkbase Document. Filed. |
| 101.PRE | XBRL Taxonomy Extension Presentation Linkbase Document. Filed. |

** Management contract or compensatory plan or agreement.