SUPERIOR UNIFORM GROUP INC
Form 10-Q
July 27, 2017

**UNITED STATES**

**SECURITIES AND EXCHANGE COMMISSION**

**WASHINGTON, D.C. 20549**

**FORM 10-Q**

(Mark One)

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

For the quarterly period ended June 30, 2017

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15 (d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from ________ to __________

Commission file number: 001-05869

Exact name of registrant as specified in its charter:

SUPERIOR UNIFORM GROUP, INC.

| State or other jurisdiction of incorporation or organization: | I.R.S. Employer Identification No.: |
|---|---|
| Florida | 11-1385670 |

Address of principal executive offices:

10055 Seminole Boulevard

Seminole, Florida 33772-2539

Registrant's telephone number, including area code:

727-397-9611

Former name, former address and former fiscal year, if changed since last report: ____________________

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15 (d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes [X]  No [_]

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted 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 and post such files).

Yes [X]  No [_]

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

| | | | |
|---|---|---|---|
| Large accelerated filer | [_] | Accelerated filer | [X] |
| Non-accelerated filer | [_] | (Do not check if a smaller reporting company) | |
| | | 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 Company is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes [_]  No [X]

As of July 24, 2017, the registrant had 14,772,352 shares of common stock outstanding, which is the registrant's only class of common stock.

**PART I - FINANCIAL INFORMATION**

ITEM 1. Financial Statements

SUPERIOR UNIFORM GROUP, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

**THREE MONTHS ENDED JUNE 30,**

**(Unaudited)**

| | 2017 | 2016 |
|---|---|---|
| Net sales | **$65,604,000** | $64,660,000 |
| Costs and expenses: | | |
| Cost of goods sold | **42,230,000** | 42,897,000 |
| Selling and administrative expenses | **17,478,000** | 16,956,000 |
| Interest expense | **195,000** | 192,000 |
| | **59,903,000** | 60,045,000 |
| Income before taxes on income | **5,701,000** | 4,615,000 |
| Income tax expense | **1,360,000** | 1,307,000 |
| Net income | **$4,341,000** | $3,308,000 |
| Weighted average number of shares outstanding during the period | | |
| (Basic) | **14,501,399** | 14,120,617 |
| (Diluted) | **15,040,431** | 14,957,469 |
| Per Share Data: | | |
| Basic | | |
| Net income | **$0.30** | $0.23 |
| Diluted | | |
| Net income | **$0.29** | $0.22 |
| Other comprehensive income, net of tax: | | |

| | | |
|---|---|---|
| Defined benefit pension plans: | | |
| Recognition of net losses included in net periodic pension costs | **147,000** | 171,000 |
| Recognition of settlement loss included in net periodic pension costs | **173,000** | 33,000 |
| Gain (loss) on cash flow hedging activities | **(52,000)** | 21,000 |
| Foreign currency translation adjustments | **(43,000)** | 173,000 |
| Other comprehensive income | **225,000** | 398,000 |
| Comprehensive income | **$4,566,000** | $3,706,000 |
| Cash dividends per common share | **$0.0875** | $0.0825 |

See accompanying notes to consolidated interim financial statements.

**PART I - FINANCIAL INFORMATION**

ITEM 1. Financial Statements

SUPERIOR UNIFORM GROUP, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

**SIX MONTHS ENDED JUNE 30,**

**(Continued)**

**(Unaudited)**

| | **2017** | 2016 |
|---|---|---|
| Net sales | **$126,591,000** | $122,628,000 |
| Costs and expenses: | | |
| Cost of goods sold | **81,003,000** | 80,844,000 |
| Selling and administrative expenses | **35,121,000** | 33,419,000 |
| Interest expense | **379,000** | 340,000 |
| | **116,503,000** | 114,603,000 |
| Gain on sale of property, plant and equipment | **1,018,000** | - |
| Income before taxes on income | **11,106,000** | 8,025,000 |
| Income tax expense | **2,930,000** | 2,275,000 |
| Net income | **$8,176,000** | $5,750,000 |
| Weighted average number of shares outstanding during the period | | |
| (Basic) | **14,426,060** | 14,023,840 |
| (Diluted) | **14,985,063** | 14,813,064 |
| Per Share Data: | | |
| Basic | | |
| Net income | **$0.57** | $0.41 |
| Diluted | | |
| Net income | **$0.55** | $0.39 |

| | | |
|---|---|---|
| Other comprehensive income, net of tax: | | |
| Defined benefit pension plans: | | |
| Recognition of net losses included in net periodic pension costs | **323,000** | 342,000 |
| Recognition of settlement loss included in net periodic pension costs | **173,000** | 198,000 |
| Gain (loss) on cash flow hedging activities | **(180,000)** | 6,000 |
| Foreign currency translation adjustments | **7,000** | 294,000 |
| Other comprehensive income | **323,000** | 840,000 |
| Comprehensive income | **$8,499,000** | $6,590,000 |
| Cash dividends per common share | **$0.175** | $0.165 |

See accompanying notes to consolidated interim financial statements.

SUPERIOR UNIFORM GROUP, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

| | **June 30, 2017 (Unaudited)** | December 31, 2016 |
|---|---|---|
| ASSETS | | |
| CURRENT ASSETS: | | |
| Cash and cash equivalents | **$7,583,000** | $3,649,000 |
| Accounts receivable, less allowance for doubtful accounts of $1,755,000 and $1,276,000, respectively | **40,620,000** | 41,823,000 |
| Accounts receivable - other | **2,412,000** | 3,085,000 |
| Inventories* | **67,596,000** | 69,240,000 |
| Prepaid expenses and other current assets | **8,567,000** | 7,214,000 |
| TOTAL CURRENT ASSETS | **126,778,000** | 125,011,000 |
| | | |
| PROPERTY, PLANT AND EQUIPMENT, NET | **26,173,000** | 27,533,000 |
| OTHER INTANGIBLE ASSETS, NET | **22,097,000** | 23,238,000 |
| GOODWILL | **11,265,000** | 11,269,000 |
| DEFERRED INCOME TAXES | **7,090,000** | 6,800,000 |
| OTHER ASSETS | **4,780,000** | 2,997,000 |
| | **$198,183,000** | $196,848,000 |
| | | |
| LIABILITIES AND SHAREHOLDERS' EQUITY | | |
| | | |
| CURRENT LIABILITIES: | | |
| Accounts payable | **$13,988,000** | $13,507,000 |
| Other current liabilities | **8,247,000** | 10,716,000 |
| Current portion of long-term debt | **6,000,000** | 5,893,000 |
| Current portion of acquisition-related contigent liabilities | **3,135,000** | 1,788,000 |
| TOTAL CURRENT LIABILITIES | **31,370,000** | 31,904,000 |
| | | |
| LONG-TERM DEBT | **34,454,000** | 36,227,000 |
| LONG-TERM PENSION LIABILITY | **7,780,000** | 9,467,000 |
| LONG-TERM ACQUISITION-RELATED CONTINGENT LIABILITY | **4,173,000** | 7,238,000 |
| OTHER LONG-TERM LIABILITIES | **2,292,000** | 1,462,000 |
| COMMITMENTS AND CONTINGENCIES (NOTE 5) | | |
| SHAREHOLDERS' EQUITY: | | |
| Preferred stock, $.001 par value - authorized 300,000 shares (none issued) | - | - |
| Common stock, $.001 par value - authorized 50,000,000 shares, issued and outstanding - 14,768,272 and 14,513,207, respectively. | **15,000** | 15,000 |
| Additional paid-in capital | **44,701,000** | 42,416,000 |
| Retained earnings | **79,239,000** | 74,283,000 |

| | | |
|---|---|---|
| Accumulated other comprehensive income (loss), net of tax: | | |
| Pensions | **(5,762,000 )** | (6,258,000 ) |
| Cash flow hedges | **(159,000 )** | 21,000 |
| Foreign currency translation adjustment | **80,000** | 73,000 |
| TOTAL SHAREHOLDERS' EQUITY | **118,114,000** | 110,550,000 |
| | **$198,183,000** | $196,848,000 |

* Inventories consist of the following:

| | **June 30, 2017 (Unaudited)** | December 31, 2016 |
|---|---|---|
| Finished goods | **$56,582,000** | $57,887,000 |
| Work in process | **566,000** | 853,000 |
| Raw materials | **10,448,000** | 10,500,000 |
| | **$67,596,000** | $69,240,000 |

See accompanying notes to consolidated interim financial statements.

SUPERIOR UNIFORM GROUP, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

**SIX MONTHS ENDED JUNE 30,**

**(Unaudited)**

| | **2017** | 2016 |
|---|---|---|
| CASH FLOWS FROM OPERATING ACTIVITIES | | |
| Net income | **$8,176,000** | $5,750,000 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Depreciation and amortization | **2,715,000** | 2,333,000 |
| Provision for bad debts - accounts receivable | **575,000** | 180,000 |
| Share-based compensation expense | **1,108,000** | 1,097,000 |
| Deferred income tax benefit | **(509,000)** | (69,000) |
| Gain on sale of property, plant and equipment | **(1,018,000)** | - |
| Accretion of acquisition-related contingent liability | **81,000** | 81,000 |
| Changes in assets and liabilities, net of acquisition of business: | | |
| Accounts receivable - trade | **552,000** | (2,181,000) |
| Accounts receivable - other | **674,000** | 1,125,000 |
| Inventories | **1,632,000** | 653,000 |
| Prepaid expenses and other current assets | **(1,353,000)** | (1,648,000) |
| Other assets | **(1,784,000)** | (353,000) |
| Accounts payable | **585,000** | 2,238,000 |
| Other current liabilities | **(2,808,000)** | (1,464,000) |
| Long-term pension liability | **(894,000)** | 259,000 |
| Other long-term liabilities | **829,000** | 40,000 |
| Net cash provided by operating activities | **8,561,000** | 8,041,000 |
| CASH FLOWS FROM INVESTING ACTIVITIES | | |
| Additions to property, plant and equipment | **(2,004,000)** | (5,527,000) |
| Proceeds from disposals of property, plant and equipment | **2,810,000** | - |
| Purchase of business net of acquired cash | **-** | (15,252,000) |
| Net cash provided by (used in) investing activities | **806,000** | (20,779,000) |
| CASH FLOWS FROM FINANCING ACTIVITIES | | |
| Proceeds from long-term debt | **72,422,000** | 90,514,000 |
| Repayment of long-term debt | **(74,088,000)** | (71,138,000) |
| Payment of cash dividends | **(2,490,000)** | (2,270,000) |
| Payment of contingent liability | **(1,800,000)** | (1,800,000) |
| Proceeds received on exercise of stock options | **798,000** | 781,000 |
| Tax benefit from vesting of acquisition related restricted stock | **70,000** | 535,000 |
| Tax withholding on exercise of stock rights | **(421,000)** | (267,000) |

| | | |
|---|---|---|
| Net cash (used in) provided by financing activities | **(5,509,000)** | 16,355,000 |
| Effect of currency exchange rates on cash | **76,000** | 82,000 |
| Net increase in cash and cash equivalents | **3,934,000** | 3,699,000 |
| Cash and cash equivalents balance, beginning of year | **3,649,000** | 1,036,000 |
| Cash and cash equivalents balance, end of period | **$7,583,000** | $4,735,000 |

See accompanying notes to consolidated interim financial statements.

**Superior Uniform Group, Inc. and Subsidiaries**

**Notes to Consolidated Financial Statements**

(Unaudited)

**NOTE 1 – Summary of Significant Interim Accounting Policies:**

a) Basis of presentation

The consolidated interim financial statements include the accounts of Superior Uniform Group, Inc. and its wholly-owned subsidiaries, The Office Gurus, LLC, SUG Holding, Fashion Seal Corporation, and BAMKO, LLC; The Office Gurus, Ltda., de C.V., The Office Masters, Ltda., de C.V. and The Office Gurus, Ltd., each a subsidiary of Fashion Seal Corporation and SUG Holding; Power Three Web, Ltda. and Superior Sourcing, each a wholly-owned subsidiary of SUG Holding; BAMKO Importação, Exportação e Comércio de Brindes Ltda., a subsidiary of BAMKO, LLC and SUG Holding; Guangzhou Ben Gao Trading Limited, Worldwide Sourcing Solutions Limited, and BAMKO UK, Limited, each a direct or indirect subsidiary of BAMKO, LLC; and BAMKO India Private Limited, a 99%-owned subsidiary of BAMKO, LLC.  All of these entities are referred to collectively as “the Company”. Intercompany items have been eliminated in consolidation.  The accompanying unaudited interim financial statements have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission. Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted pursuant to such rules and regulations. These consolidated financial statements should be read in conjunction with the audited financial statements and notes thereto included in the Company’s Annual Report on Form 10-K for the year ended December 31, 2016, and filed with the Securities and Exchange Commission.  The interim financial information contained herein is not certified or audited; it reflects all adjustments (consisting of only normal recurring accruals) which are, in the opinion of management, necessary for a fair statement of the operating results for the periods presented, stated on a basis consistent with that of the audited financial statements.  The results of operations for any interim period are not necessarily indicative of results to be expected for the full year.

b) Revenue recognition

The Company records revenue as products are shipped and title passes and as services are provided. A provision for estimated returns and allowances is recorded based on historical experience and current allowance programs.

c) Recognition of costs and expenses

Costs and expenses other than product costs are charged to income in interim periods as incurred, or allocated among interim periods based on an estimate of time expired, benefit received or activity associated with the periods. Procedures adopted for assigning specific cost and expense items to an interim period are consistent with the basis followed by the registrant in reporting results of operations at annual reporting dates. However, when a specific cost or expense item charged to expense for annual reporting purposes benefits more than one interim period, the cost or expense item is allocated to the interim periods.

d) Amortization of other intangible assets

The Company amortizes identifiable intangible assets on a straight line basis over their expected useful lives. Amortization expense for other intangible assets was $570,000 and $607,000 for the three-month periods ended June 30, 2017 and 2016, respectively. Amortization expense for other intangible assets was $1,141,000 and $1,154,000 for the six-month periods ended June 30, 2017 and 2016, respectively.

e) Advertising expenses

The Company expenses advertising costs as incurred. Advertising costs for the three-month periods ended June 30, 2017 and 2016 were $22,000 and $22,000, respectively. Advertising costs for the six-month periods ended June 30, 2017 and 2016 were $39,000 and $32,000, respectively.

f) Shipping and handling fees and costs

The Company includes shipping and handling fees billed to customers in net sales. Shipping and handling costs associated with in-bound and out-bound freight are generally recorded in cost of goods sold. Other shipping and handling costs such as labor and overhead are included in selling and administrative expenses and totaled $2,680,000 and $2,497,000 for the three-month periods ended June 30, 2017 and 2016, respectively. Other shipping and handling costs included in selling and administrative expenses totaled $5,441,000 and $5,152,000 for the six-month periods ended June 30, 2017 and 2016, respectively

g) Inventories

Inventories at interim dates are determined by using both perpetual records on a first-in, first-out basis and gross profit calculations.

h) Accounting for income taxes

The provision for income taxes is calculated by using the effective tax rate anticipated for the full year.

i) Employee benefit plan settlements

The Company recognizes settlement gains and losses in its financial statements when the cost of all settlements in a year is greater than the sum of the service cost and interest cost components of net periodic pension cost for the plan for the year.

j) Earnings per share

Historical basic per share data is based on the weighted average number of shares outstanding. Historical diluted per share data is reconciled by adding to weighted average shares outstanding the dilutive impact of the exercise of outstanding stock options, stock appreciation rights, unvested shares, and performance shares.

k) Derivative financial instruments

The Company uses certain financial derivatives to mitigate its exposure to volatility in interest rates and foreign currency. The Company records derivatives on the balance sheet at fair value and establishes criteria for designation and effectiveness of hedging relationships. On the date a derivative contract is entered into, the Company may elect to designate the derivative as a fair value hedge, a cash flow hedge, or the hedge of a net investment in a foreign operation. The Company also formally assesses, both at the hedge’s inception and on an ongoing basis, whether the derivative that is used in the hedging transaction is highly effective. For those instruments that are designated as a cash flow hedge and meet certain documentary and analytical requirements to qualify for hedge accounting treatment, changes in the fair value for the effective portion are reported in other comprehensive income (“OCI”), net of related income tax effects, and are reclassified to the income statement when the effects of the item being hedged are recognized in the income statement. The Company discontinues hedge accounting prospectively when it is determined that the derivative is no longer effective in offsetting changes in the cash flows of the hedged item, the derivative expires or is sold, terminated, or exercised, or management determines that designation of the derivative as a hedging instrument is no longer appropriate. In situations in which the Company does not elect hedge accounting or hedge accounting is discontinued and the derivative is retained, the Company carries or continues to carry the derivative at its fair value on the balance sheet and recognizes any subsequent changes in its fair value through earnings.

The nature of the Company’s business activities involves the management of various financial and market risks, including those related to changes in interest rates and foreign currency. The Company does not enter into derivative instruments for speculative purposes. The Company manages market and credit risks associated with its derivative instruments by establishing and monitoring limits as to the types and degree of risk that may be undertaken, and by entering into transactions with high-quality counterparties.

Effective March 3, 2017, in order to reduce the interest rate risk on its future debt, the Company entered into an interest rate swap agreement that was designed to effectively convert or hedge the variable interest rate on a portion of its future borrowings to achieve a net fixed rate beginning March 1, 2018 with a notional amount of $18,000,000. The previous swap agreement was terminated on February 24, 2017. (See Note 2.)

On January 3, 2017, the Company entered into a foreign exchange forward contract to lock in the exchange rate on the Brazilian real to limit the risk of changes in foreign currency on the expected payment of a customer receivable. The amount of the contract was $1,800,000 and settled on June 29, 2017. As of June 30, 2017, we recognized a loss of $92,000 on this contract which is included in selling and administrative expenses on our consolidated statement of comprehensive income.

l) Use of estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

m) Comprehensive income

Total comprehensive income represents the change in equity during a period from sources other than transactions with shareholders and, as such, includes net earnings. For the Company, the only other components of total comprehensive income are the change in pension costs, change in fair value of qualifying hedges, and foreign currency translation adjustments.

n) Operating segments

Accounting standards require disclosures of certain information about operating segments and about products and services, geographic areas in which the Company operates, and their major customers. The Company has evaluated its operations and has determined that it has three reportable segments - Uniforms and Related Products, Remote Staffing Solutions and Promotional Products. (See Note 8.)

o) Share-based compensation

The Company awards share-based compensation as an incentive for employees to contribute to the Company’s long-term success. Historically, the Company has granted options, stock-settled stock appreciation rights, and restricted stock. In 2016, the Company began issuing performance shares as well. At June 30, 2017, the Company had

3,766,362 shares of common stock available for grant of awards of share-based compensation under its 2013 Incentive Stock and Awards Plan.

The Company recognizes share-based compensation expense for all awards granted to employees, which is based on the fair value of the award on the date of grant. Determining the appropriate fair value model and calculating the fair value of stock compensation awards requires the input of certain highly complex and subjective assumptions, including the expected life of the stock compensation awards and the Company's common stock price volatility, risk free interest rate and dividend rate. The assumptions used in calculating the fair value of stock compensation awards represent management's best estimates, but these estimates involve inherent uncertainties and the application of judgment. As a result, if factors change and the Company deems it necessary to use different assumptions, stock compensation expense could be materially different from what has been recorded in the current period.

p) Recent Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2014-09, Revenue from Contracts with Customers (Topic 606) that will supersede most current revenue recognition guidance, including industry-specific guidance. The core principle of the new guidance is that an entity will recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The standard provides a five-step analysis of transactions to determine when and how revenue is recognized. Other major provisions include the capitalization and amortization of certain contract costs, ensuring the time value of money is considered in the transaction price, and allowing estimates of variable consideration to be recognized before contingencies are resolved in certain circumstances. Additionally, the guidance requires disaggregated disclosures related to the nature, amount, timing, and uncertainty of revenue that is recognized. The amendments are required to be adopted by the Company on January 1, 2018. Transition to the new guidance may be done using either a full or modified retrospective method. The Company is still evaluating the impact of this ASU on the Company's consolidated financial statements and expects to complete the assessment process by the end of the third quarter 2017 prior to the adoption of this ASU on January 1, 2018. Our assessment of the guidance is primarily focused on reviewing our performance obligations in our contract portfolio and related disclosures.

In February 2016, the FASB issued ASU 2016-02 that amends the accounting guidance on leases. The primary change in this ASU requires lessees to recognize, in the balance sheet, a liability to make lease payments and a right-of-use asset representing the right to use the underlying asset over the lease term. The amendments in this ASU are to be applied using a modified retrospective approach and are effective for fiscal years beginning after December 15, 2018. The Company is in the preliminary phases of assessing the effect of this ASU. We have not yet selected a transition date nor have we yet determined the effect of this ASU on our results of operations, financial condition, or cash flows.

In March 2016, the FASB issued ASU 2016-09, "Compensation – Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting". This update was issued as part of FASB's simplification initiative and affects all entities that issue share-based payment awards to their employees. The amendment requires that excess tax benefits for share-based payments be recorded as a reduction of income tax expense and reflected within operating cash flows rather than being recorded in paid-in-capital and reflected within financing cash flows. The standard also clarifies that all cash payments when directly withholding shares for tax-withholding purposes should be classified as a financing activity on the statement of cash flows and provides for an accounting policy election to account for forfeitures when they occur. The amendments in this update were effective for annual and interim periods beginning after December 15, 2016. Early adoption is permitted in any interim or annual period but must be reflected as of the beginning of the fiscal year. The Company elected to early adopt the standard in the fourth quarter of 2016 which required us to reflect the adjustments as of January 1, 2016. The recognition of excess tax benefits in our provision for income taxes rather than paid-in-capital resulted in an income tax benefit of $405,000 or $0.03 per share and $628,000 or $0.04 per share for the three-month period and six-month period ended June 30, 2017, respectively. Additionally, the adoption in the fourth quarter resulted in an income tax benefit of $233,000 or $0.01 per share and $415,000 or $0.03 per share for the three-month period and six-month period ended June 30, 2016, respectively, from the previously reported income tax provisions in the consolidated statements of comprehensive income for the second quarter of fiscal year 2016. Lastly, the company has made an accounting policy election to account for forfeitures in compensation cost when they occur. There was no material impact of this election in fiscal 2016 or 2017.

**NOTE 2 - Long-Term Debt:**

| | June 30, 2017 | December 31, 2016 |
|---|---|---|
| Term loan payable to Fifth Third Bank, paid February 28, 2017 | $- | $39,643,000 |
| Note payable to Fifth Third Bank, pursuant to revolving credit agreement, paid February 28, 2017 | - | 2,540,000 |
| Term loan payable to BB&T maturing February 26, 2024 | 40,500,000 | - |
| Note payable to BB&T, pursuant to revolving credit agreement, maturing February 25, 2022 | - | - |
| | $40,500,000 | $42,183,000 |
| Less: | | |
| Payments due within one year included in current liabilities | $6,000,000 | $5,893,000 |
| Debt issuance costs | 46,000 | 63,000 |
| Long-term debt less current maturities | $34,454,000 | $36,227,000 |

Effective July 1, 2013, the Company entered into an amended and restated 5-year credit agreement with Fifth Third Bank that made available to the Company up to $15,000,000 on a revolving credit basis in addition to a $30,000,000 term loan utilized to finance the acquisition of substantially all of the assets of HPI Direct, Inc.

Effective March 8, 2016, the Company entered into an amended and restated 5-year credit agreement with Fifth Third Bank (the "Amended Credit Agreement") that increased its revolving credit facility from $15,000,000 to $20,000,000 (the "Amended Credit Facility") and refinanced its then-existing term loan with a new $45,000,000 term loan to help finance the acquisition of substantially all of the assets of BAMKO, Inc. Both loans were based upon the one-month LIBOR rate for U.S. dollar based borrowings. Interest was payable on the term loan at LIBOR plus 0.85% and on the revolving credit facility at LIBOR (rounded up to the next 1/8$^{th}$ of 1%) plus 0.85%. The Company paid a commitment fee of 0.10% per annum on the average unused portion of the commitment under the Amended Credit Facility. This credit agreement was paid in full on February 28, 2017 with the proceeds from a new loan agreement with Branch Banking and Trust Company ("BB&T").

Effective February 28, 2017, the Company entered into a new 7-year credit agreement (maturing February 26, 2024) with BB&T (the "Credit Agreement") that provides a new revolving credit facility of $35,000,000 (the "Credit Facility") which terminates on February 25, 2022 and provides a new term loan of $42,000,000 (the "Term Loan"). Both loans were based upon the one-month LIBOR rate for U.S. dollar based borrowings. Interest is payable for each loan at

LIBOR (rounded up to the next 1/100$^{th}$ of 1%) plus 0.75% (1.92% at June 30, 2017). The Company pays a commitment fee of 0.10% per annum on the average unused portion of the commitment under the Credit Facility. The available balance under the Credit Facility is reduced by outstanding letters of credit. As of June 30, 2017, there were no amounts due under the Credit Facility and no outstanding letters of credit.

The remaining scheduled amortization for the Term Loan is as follows: 2017 - $3,000,000; 2018 through 2023 - $6,000,000 per year; and 2024 - $1,500,000. The Term Loan does not include a prepayment penalty. In connection with the Credit Agreement, the Company incurred approximately $48,000 of debt financing costs, which primarily consisted of legal fees. These costs are being amortized over the life of the Credit Agreement as additional interest expense.

The Company’s obligations under the Credit Agreement are secured by substantially all of the operating assets of Superior Uniform Group, Inc. and are guaranteed by all domestic subsidiaries of Superior Uniform Group, Inc. The agreement contains restrictive provisions concerning a maximum funded indebtedness to EBITDA ratio not to exceed (4.0:1) as defined in the agreement and a fixed charge coverage ratio of at least (1.25:1). The Company is in full compliance with all terms, conditions and covenants of the Credit Agreement.

Effective July 1, 2013, in order to reduce interest rate risk on its debt, the Company entered into an interest rate swap agreement with Fifth Third Bank, N.A. that was designed to effectively convert or hedge the variable interest rate on a portion of its borrowings to achieve a net fixed rate of 2.53% per annum, beginning July 1, 2014 with a notional amount of $14,250,000. The notional amount of the interest rate swap was reduced by the scheduled amortization of the principal balance of the original term loan of $187,500 per month through July 1, 2015 and $250,000 per month through June 1, 2018 with the remaining notional balance of $3,250,000 to be eliminated on July 1, 2018. Effective March 8, 2016, the fixed rate on the notional amount was reduced to 2.43%. Effective February 24, 2017, this interest rate swap agreement was terminated. On this date the swap agreement had $65,000 in cumulative gains in OCI which was reversed to earnings.

Effective March 3, 2017, in order to reduce the interest rate risk on its future debt, the Company entered into an interest rate swap agreement with BB&T that was designed to effectively convert or hedge the variable interest rate on a portion of its future borrowings to achieve a net fixed rate of 3.12% per annum, beginning March 1, 2018 with a notional amount of $18,000,000. The notional amount of the interest rate swap is reduced by $250,000 per month through February 26, 2024. Under the terms of the interest rate swap, the Company will receive variable interest rate payments and make fixed interest rate payments on an amount equal to the notional amount at that time. Changes in the fair value of the interest rate swap designated as the hedging instrument that effectively offset the variability of cash flows associated with the variable rate, long-term debt obligation are recorded in OCI, net of related income tax effects. As of June 30, 2017, the swap agreement had a negative fair value of $253,000 which is presented within other current liabilities on the consolidated balance sheet.

**NOTE 3 – Periodic Pension Expense:**

The following table details the net periodic pension expense under the Company's plans for the periods presented:

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|---|---|---|---|---|
| | 2017 | 2016 | 2017 | 2016 |
| Service cost - benefits earned during the period | $16,000 | $14,000 | $32,000 | $28,000 |
| Interest cost on projected benefit obligation | 242,000 | 247,000 | 483,000 | 494,000 |
| Expected return on plan assets | (305,000) | (297,000) | (609,000) | (594,000) |
| Recognized actuarial loss | 270,000 | 258,000 | 547,000 | 523,000 |
| Settlement loss | 277,000 | 52,000 | 277,000 | 307,000 |
| Net periodic pension cost | $500,000 | $274,000 | $730,000 | $758,000 |

Effective June 30, 2013, the Company no longer accrues additional benefits for future service or for future increases in compensation levels for the Company’s primary defined benefit pension plan.

Effective December 31, 2014, the Company no longer accrues additional benefits for future service for the Company’s hourly defined benefit plan.

There were $1,520,000 and $500,000 in contributions made to the Company’s defined benefit plans during the six-month periods ended June 30, 2017 and 2016, respectively.

**NOTE 4 - Supplemental Cash Flow Information:**

Cash paid for income taxes was $3,748,000 and $3,173,000, respectively, for the six-month periods ended June 30, 2017 and 2016. Cash paid for interest was $313,000 and $278,000, respectively for the six-month periods ended June 30, 2017 and 2016.

During the three months ended June 30, 2017 and 2016, respectively, the company received 27,341 and 10,434 shares of its common stock as payment of the exercise price in the exercise of stock options for 71,599 and 30,416 shares.

During the six months ended June 30, 2017 and 2016, respectively, the Company received 43,841 and 10,434 shares of its common stock as payment of the exercise price in the exercise of stock options for 113,143 and 30,416 shares.

**NOTE 5 – Contingencies:**

The Company is involved in various legal actions and claims arising from the normal course of business. In the opinion of management, the ultimate outcome of these matters will not have a material impact on the Company’s results of operations, cash flows, or financial position.

**NOTE 6 – Share-Based Compensation:**

In 2003, the stockholders of the Company approved the 2003 Incentive Stock and Awards Plan (the “2003 Plan”), authorizing the granting of incentive stock options, non-qualified stock options, stock appreciation rights (“SARS”), restricted stock, performance shares and other stock based compensation. This plan expired in May of 2013, at which time, the stockholders of the Company approved the 2013 Incentive Stock and Awards Plan (the “2013 Plan”), authorizing the granting of incentive stock options, non-qualified stock options, SARS, restricted stock, performance shares and other stock based compensation. A total of 5,000,000 shares of common stock (subject to adjustment for expirations and cancellations of options outstanding from the 2003 Plan subsequent to its termination) have been reserved for issuance under the 2013 Plan. All options and SARS under both plans have been or will be granted with exercise prices at least equal to the fair market value of the shares on the date of grant. At June 30, 2017, the Company had 3,766,362 shares of common stock available for grant of share-based compensation under the 2013 Plan.

Share-based compensation is recorded in selling and administrative expense in the consolidated statements of comprehensive income. The following table details the share-based compensation expense by plan and the total related tax benefit for the periods presented:

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|---|---|---|---|---|
| | 2017 | 2016 | 2017 | 2016 |
| Stock options and SARS | $82,000 | $81,000 | $747,000 | $833,000 |
| Restricted stock | 80,000 | 71,000 | 164,000 | 151,000 |
| Performance shares | 104,000 | 68,000 | 197,000 | 113,000 |
| Total share-based compensation expense | $266,000 | $220,000 | $1,108,000 | $1,097,000 |
| | | | | |
| Related income tax benefit | $58,000 | $53,000 | $168,000 | $172,000 |

*Stock options and SARS*

The Company grants stock options and stock settled SARS to employees that allow them to purchase shares of the Company's common stock. Options are also granted to outside members of the Board of Directors of the Company. The Company determines the fair value of stock options and SARS at the date of grant using the Black-Scholes valuation model.

All options and SARS vest immediately at the date of grant. Awards generally expire five years after the date of grant with the exception of options granted to outside directors, which expire ten years after the date of grant. The Company issues new shares upon the exercise of stock options and SARS.

A summary of stock option transactions during the six months ended June 30, 2017 follows:

| | No. of Shares | Weighted Average Exercise Price |
|---|---|---|
| Outstanding December 31, 2016 | 825,251 | $ 10.46 |
| Granted | 101,012 | $ 17.09 |
| Exercised | (205,330) | $ 8.08 |
| Lapsed | - | $ - |
| Cancelled | - | $ - |
| Outstanding June 30, 2017 | 720,933 | $ 12.06 |

At June 30, 2017, options outstanding, all of which were fully vested and exercisable, had an aggregate intrinsic value of $7,418,000. The weighted-average remaining contractual term was 43 months.

Options exercised during the three-month period ended June 30, 2017 and 2016 had intrinsic values of $1,677,000 and $595,000, respectively. Options exercised during the six-month period ended June 30, 2017 and 2016 had intrinsic values of $2,289,000 and $1,196,000, respectively.

The weighted average fair values of the Company's 11,000 and 11,000 options granted during each of the three-month periods ended June 30, 2017 and 2016 was $7.41 and $7.38, respectively. The weighted average fair values of the Company's 101,012 and 120,332 options granted during each of the six-month periods ending June 30, 2017 and 2016 was $5.11 and $4.75, respectively.

During the three-month periods ended June 30, 2017 and 2016, respectively, the Company received $693,000 and $459,000 in cash from stock option exercises. Additionally, during the three-month period ended June 30, 2017 and 2016, the Company received 27,341 and 10,434 shares of its common stock as payment of the exercise price in the exercise of stock options for 71,599 and 30,416 shares. During the six-month periods ended June 30, 2017 and 2016, respectively, the Company received $798,000 and $781,000 in cash from stock option exercises. Additionally, during the six-month period ended June 30, 2017 and 2016, the Company received 43,841 and 10,434 shares of its common stock as payment of the exercise price in the exercise of stock options for 113,143 and 30,416 shares. The tax benefit recognized for these exercises during each of the three-month periods ended June 30, 2017 and 2016 was $196,000 and $165,000, respectively. The tax benefit recognized for these exercises during the six-month period ended June 30, 2017 and 2016 was $209,000 and $190,000, respectively.

The following table summarizes information about stock options outstanding as of June 30, 2017.

| Range of Exercise Price | Shares | Weighted Average Remaining Contractual Life (Years) | Weighted Average Exercise Price |
|---|---|---|---|
| $3.82 - $5.55 | 66,000 | 2.61 | $ 4.79 |
| $5.65 - $7.36 | 231,566 | 1.93 | $ 6.55 |
| $7.96 - $10.38 | 54,400 | 4.53 | $ 9.13 |
| $16.35 - $18.66 | 368,967 | 4.65 | $ 17.25 |
| $3.82 - $18.66 | 720,933 | 3.58 | $ 12.06 |

A summary of stock-settled SARS transactions during the six months ended June 30, 2017 follows:

| | No. of Shares | Weighted Average Exercise Price |
|---|---|---|
| Outstanding December 31, 2016 | 325,506 | $ 10.26 |
| Granted | 43,988 | 16.97 |
| Exercised | (128,062) | 6.87 |
| Lapsed | - | - |
| Cancelled | - | - |
| Outstanding June 30, 2017 | 241,432 | $ 13.28 |

At June 30, 2017, SARS outstanding, all of which were fully vested and exercisable, had an aggregate intrinsic value of $2,191,000. The weighted-average remaining contractual term was 31 months.

The weighted average fair values of the Company's 43,988 and 58,108 SARS granted during each of the six-month periods ended June 30, 2017 and 2016 was $4.83 and $4.49, respectively.

There were 68,698 and 39,584 SARS exercised during the three-month periods ended June 30, 2017 and 2016, respectively. SARS exercised during the three-month periods ended June 30, 2017 and 2016 had intrinsic values of $806,000 and $485,000. The tax benefit recognized for these exercises during each of the three-month periods ended June 30, 2017 and 2016 was $302,000 and $146,000, respectively.

There were 128,062 and 75,792 SARS exercised during the six-month periods ended June 30, 2017 and 2016, respectively. SARS exercised during the six-month periods ended June 30, 2017 and 2016 had intrinsic values of $1,544,000 and $928,000. The tax benefit recognized for these exercises during each of the six-month periods ended June 30, 2017 and 2016 was $572,000 and $311,000, respectively.

The following table summarizes information about SARS outstanding as of June 30, 2017:

| Range of | Weighted Average Remaining | Weighted Average |
|---|---|---|

| Exercise Price | | Shares | Contractual Life (Years) | Exercise Price |
|---|---|---|---|---|
| $5.65 | -$7.36 | 94,928 | 1.34 | $ 6.95 |
| $16.35 | -$18.66 | 146,504 | 3.42 | $ 17.38 |
| $5.65 | -$18.66 | 241,432 | 2.60 | $ 13.28 |

At June 30, 2017 shares available for grant as awards under the plan were 3,766,362. Options and SARS have never been repriced by the Company in any year.

The following table summarizes significant assumptions utilized to determine the fair value of options and SARS.

| Three months ended June 30, | SARS | Options |
|---|---|---|
| Exercise price | | |
| 2017 | N/A | $ 18.05 |
| 2016 | N/A | $ 18.55 |
| Market price | | |
| 2017 | N/A | $ 18.05 |
| 2016 | N/A | $ 18.55 |
| Risk free interest rate[1] | | |
| 2017 | N/A | 2.4 % |
| 2016 | N/A | 1.8 % |
| Expected award life (years)[2] | N/A | 10 |
| Expected volatility[3] | | |
| 2017 | N/A | 41.4 % |
| 2016 | N/A | 40.3 % |
| Expected dividend yield[4] | | |
| 2017 | N/A | 1.9 % |
| 2016 | N/A | 1.8 % |

| Six months ended June 30, | SARS | Options |
|---|---|---|
| Exercise price | | |
| 2017 | $ 16.97 | $16.97 - $18.05 |
| 2016 | $ 16.35 | $16.35 - $18.55 |
| Market price | | |
| 2017 | $ 16.97 | $16.97 - $18.05 |
| 2016 | $ 16.35 | $16.35 - $18.55 |
| Risk free interest rate[1] | | |
| 2017 | 1.9 % | 1.9% - 2.4% |
| 2016 | 1.3 % | 1.3% - 1.8% |

| | | |
|---|---|---|
| Expected award life (years)[2] | 5 | 5 - 10 |
| Expected volatility[3] | | |
| 2017 | 36.6 % | 36.6% - 41.4% |
| 2016 | 36.5 % | 36.5% - 40.3% |
| Expected dividend yield[4] | | |
| 2017 | 2.1 % | 1.9% - 2.1% |
| 2016 | 2.0 % | 1.8% - 2.0% |

[1] The risk-free interest rate is based on the yield of a U.S. treasury bond with a similar maturity as the expected life of the awards.

[2] The expected life in years for awards granted was based on the historical exercise patterns experienced by the Company when the award is made.

[3] The determination of expected stock price volatility for awards granted in each of the periods ending June 30, 2017 and 2016 was based on historical prices of Superior's common stock over a period commensurate with the expected life.

[4] The dividend yield assumption is based on the history and expectation of the Company's dividend payouts.

*Restricted Stock*

The Company has granted restricted stock to directors and certain employees under the terms of the 2013 Plan which vest at a specified future date, generally after three years, or when certain conditions are met. The shares are subject to accelerated vesting under certain circumstances as outlined in the 2013 Plan. Expense for each of these grants is based on the fair value at the date of the grant and is being recognized on a straight-line basis over the respective service period. As of June 30, 2017, the Company had $704,000 of unrecognized compensation cost related to nonvested grants expected to be recognized over the weighted average service period of 2.2 years.

A summary of restricted stock transactions during the six months ended June 30, 2017 follows:

| | No. of Shares | Weighted Average Exercise Price |
|---|---|---|
| Outstanding December 31, 2016 | 123,688 | $ 8.94 |
| Granted | 34,619 | 16.97 |
| Vested | (100,000) | 7.36 |
| Forfeited | - | - |
| Outstanding June 30, 2017 | 58,307 | $ 16.42 |

*Performance Shares*

The Compensation Committee of the Board of Directors has approved grants of performance shares under the terms of the 2013 Plan. Under the terms of the grants, certain employees received service-based or service-based and performance-based shares. The service-based awards vest after the service period is met, which is generally three to five years. Expense for these grants is based on the fair value on the date of the grant and is being recognized on a straight-line basis over the respective service period. The performance-based shares generally vest after five years if the performance and service targets are met. The Company evaluates the performance conditions associated with these grants each reporting period to determine the expected number of shares to be issued. Based upon this evaluation, expected expenses for these grants are being recognized based on the fair value on the date of the grant on a straight-line basis over the respective service period. The shares are subject to accelerated vesting under certain circumstances as outlined in the 2013 Plan. As of June 30, 2017, the Company had $1,838,000 of unrecognized compensation cost related to nonvested grants expected to be recognized over the weighted average service period of 3.8 years.

A summary of performance share transactions during the six months ended June 30, 2017 follows:

| | No. of Shares | Weighted Average Exercise Price |
|---|---|---|
| Outstanding December 31, 2016 | 101,000 | $ 16.36 |
| Granted | 37,392 | 16.97 |
| Vested | - | - |
| Forfeited | - | - |
| Outstanding June 30, 2017 | 138,392 | $ 16.53 |

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**NOTE 7 – Earnings Per Share:**

Historical basic per share data is based on the weighted average number of shares outstanding. Historical diluted per share data is reconciled by adding to weighted average shares outstanding the dilutive impact of the exercise of outstanding stock options, stock appreciation rights, unvested shares, and performance shares.

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|---|---|---|---|---|
| | 2017 | 2016 | 2017 | 2016 |
| Net earnings used in the computation of basic and diluted earnings per share | $4,341,000 | $3,308,000 | $8,176,000 | |