

Differential Brands Group Inc.
Form 10-Q
August 14, 2017
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 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: 0-18926

DIFFERENTIAL BRANDS GROUP INC.

(Exact name of registrant as specified in its charter)

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Delaware
(State or other jurisdiction of incorporation or organization)

11-2928178
(I.R.S. Employer Identification No.)

1231 South Gerhart Avenue, Commerce, California 90022
(Address of principal executive offices) (Zip Code)

(323) 890-1800

(Registrant's telephone number, including area code)

N/A

(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 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 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
Non-accelerated filer	Smaller reporting company
(Do not check if a 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 by Rule 12b-2 of the Exchange Act). Yes No

The number of shares of the registrant's common stock outstanding as of August 14, 2017 was 13,317,281.

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PART I — FINANCIAL INFORMATION

Item 1. Financial Statements

DIFFERENTIAL BRANDS GROUP INC.

CONDENSED CONSOLIDATED BALANCE SHEETS

(amounts in thousands, except share data)

	June 30, 2017 (unaudited)	December 31, 2016 (Note 1)	June 30, 2016 (unaudited)
ASSETS			
Current assets			
Cash and cash equivalents	\$ 6,305	\$ 6,476	\$ 8,368
Accounts receivable, net	16,982	20,225	14,339
Inventories, net	30,623	23,977	26,759
Prepaid expenses and other current assets	5,465	4,249	1,976
Total current assets	59,375	54,927	51,442
Property and equipment, net	9,651	10,620	13,003
Goodwill	8,340	8,271	6,524
Intangible assets, net	90,669	91,886	84,965
Other assets	514	467	477
Total assets	\$ 168,549	\$ 166,171	\$ 156,411
LIABILITIES AND EQUITY			
Current liabilities			
Accounts payable and accrued expenses	\$ 20,206	\$ 19,930	\$ 20,838
Short-term convertible notes	13,436	13,137	—
Current portion of long-term debt	1,875	1,250	875
Total current liabilities	35,517	34,317	21,713
Deferred rent	3,609	3,636	3,624
Line of credit	17,492	12,742	12,000
Convertible notes	13,242	12,660	12,251
Long-term debt, net of current portion	45,991	47,218	47,694
Deferred income taxes, net	13,416	11,074	9,723
Other liabilities	—	—	81
Total liabilities	129,267	121,647	107,086
Commitments and contingencies (Note 13)			
Equity	5	5	5

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Series A convertible preferred stock, \$0.10 par value: 50,000 shares authorized, issued and outstanding at June 30, 2017, December 31, 2016 and June 30, 2016

Common stock, \$0.10 par value: 100,000,000 shares authorized, 13,317,281, 13,239,125 and 12,379,000 shares issued and outstanding at June 30, 2017, December 31, 2016 and June 30, 2016, respectively

Additional paid-in capital	1,332	1,324	1,239
Accumulated other comprehensive income (loss)	59,962	59,154	56,093
Accumulated deficit	125	(221)	—
Total equity	(22,142)	(15,738)	(8,012)
Total liabilities and equity	39,282	44,524	49,325
	\$ 168,549	\$ 166,171	\$ 156,411

The accompanying notes are an integral part of these condensed consolidated financial statements.

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DIFFERENTIAL BRANDS GROUP INC.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS AND

COMPREHENSIVE INCOME (LOSS)

(in thousands, except per share data)

(unaudited)

	Three months ended		Six months ended	
	June 30, 2017	2016 (Note 2)	June 30, 2017	2016 (Note 2)
Net sales	\$ 36,453	\$ 32,373	\$ 76,555	\$ 66,088
Cost of goods sold	20,234	19,862	41,733	37,240
Gross profit	16,219	12,511	34,822	28,848
Operating expenses				
Selling, general and administrative	14,915	14,130	32,319	30,593
Depreciation and amortization	1,527	1,501	3,032	2,863
Retail store impairment	—	—	—	279
Total operating expenses	16,442	15,631	35,351	33,735
Operating loss from continuing operations	(223)	(3,120)	(529)	(4,887)
Interest expense	2,207	1,995	4,254	3,336
Other (income) expense, net	(12)	—	11	—
Loss from continuing operations before income taxes	(2,418)	(5,115)	(4,794)	(8,223)
Income tax provision (benefit)	1,636	(1,510)	1,610	577
Loss from continuing operations	(4,054)	(3,605)	(6,404)	(8,800)
Loss from discontinued operations, net of tax	—	—	—	(1,286)
Net loss	\$ (4,054)	\$ (3,605)	\$ (6,404)	\$ (10,086)
Net loss	\$ (4,054)	\$ (3,605)	\$ (6,404)	\$ (10,086)
Other comprehensive income, net of tax:				
Foreign currency translation adjustment	283	—	346	—
Other comprehensive income	283	—	346	—
Comprehensive loss	\$ (3,771)	\$ (3,605)	\$ (6,058)	\$ (10,086)
Loss per common share - basic				
Loss from continuing operations	\$ (0.30)	\$ (0.29)	\$ (0.48)	\$ (0.74)
Loss from discontinued operations	—	—	—	(0.11)
Loss per common share - basic	\$ (0.30)	\$ (0.29)	\$ (0.48)	\$ (0.85)
Loss per common share - diluted				
Loss from continuing operations	\$ (0.30)	\$ (0.29)	\$ (0.48)	\$ (0.74)
Loss from discontinued operations	—	—	—	(0.11)

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Loss per common share - diluted	\$ (0.30)	\$ (0.29)	\$ (0.48)	\$ (0.85)
Weighted average shares outstanding				
Basic	13,309	12,380	13,298	11,852
Diluted	13,309	12,380	13,298	11,852

The accompanying notes are an integral part of these condensed consolidated financial statements.

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DIFFERENTIAL BRANDS GROUP INC.

CONDENSED CONSOLIDATED STATEMENTS OF EQUITY

(in thousands, unaudited)

Common Stock		Preferred Series A		Additional Paid-In Capital	Accumulated Other Comprehensive Income (Loss)	Accumulated Deficit	Common Members		Preferred Members	
Shares	Par Value	Shares	Par Value				Units	Amount	Units	Amount
—	\$ —	—	\$ —	\$ —	\$ —	\$ —	4,900	\$ 22,743	5,100	\$ 24,798
—	—	—	—	—	—	—	—	(1,016)	—	(1,058)
—	—	—	—	—	—	—	—	(28,905)	—	(29,311)
8,825	883	—	—	(13,634)	—	—	(4,900)	7,178	(5,100)	5,573
3,509	351	—	—	19,649	—	—	—	—	—	—
—	—	50	5	49,064	—	—	—	—	—	—
—	—	—	—	516	—	—	—	—	—	—
45	5	—	—	498	—	—	—	—	—	—
—	—	—	—	—	—	(8,012)	—	—	—	—

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12,379	\$ 1,239	50	\$ 5	\$ 56,093	\$ —	\$ (8,012)	—	\$ —	—	\$ —
13,239	\$ 1,324	50	\$ 5	\$ 59,154	\$ (221)	\$ (15,738)	—	\$ —	—	\$ —
—	—	—	—	900	—	—	—	—	—	—
78	8	—	—	(92)	—	—	—	—	—	—
—	—	—	—	—	346	—	—	—	—	—
—	—	—	—	—	—	(6,404)	—	—	—	—
13,317	\$ 1,332	50	\$ 5	\$ 59,962	\$ 125	\$ (22,142)	—	\$ —	—	\$ —

The accompanying notes are an integral part of these condensed consolidated financial statements.

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DIFFERENTIAL BRANDS GROUP INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands, unaudited)

	Six months ended	
	June 30,	
	2017	2016
CASH FLOWS FROM OPERATING ACTIVITIES		
Loss from continuing operations	\$ (6,404)	\$ (8,800)
Adjustments to reconcile net loss from continuing operations to net cash used in operating activities:		
Depreciation and amortization	3,032	2,863
Retail store impairment	—	279
Amortization of deferred financing costs	215	162
Amortization of convertible notes discount	350	359
Paid-in-kind interest	770	92
Stock-based compensation	900	1,019
Provision for bad debts	194	31
Amortization of inventory step up	—	383
Deferred taxes	2,289	270
Changes in operating assets and liabilities:		
Accounts receivable	3,081	(1,339)
Inventories	(6,591)	(411)
Prepaid expenses and other assets	(1,253)	217
Accounts payable and accrued expenses	2,220	(8,264)
Deferred rent	(20)	56
Net cash used in continuing operating activities	(1,217)	(13,083)
Net cash used in discontinued operating activities	—	(1,384)
Net cash used in operating activities	(1,217)	(14,467)
CASH FLOWS FROM INVESTING ACTIVITIES		
Cash paid in reverse acquisition with Robert Graham, net of cash acquired	—	(6,538)
Refund of security deposit	7	—
Purchases of property and equipment	(601)	(1,125)
Net cash used in investing activities	(594)	(7,663)
CASH FLOWS FROM FINANCING ACTIVITIES		
Proceeds from issuance of Series A convertible preferred stock, net of offering costs	—	49,881
Proceeds from term debt	—	50,000
Repayment of long-term debt	(625)	(250)
Proceeds from line of credit, net	4,350	12,587
Repayment of terminated line of credit and loan payable	—	—