

The Stephan Co.
Third Quarter Report
September 30, 2017

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Financial results are unaudited unless otherwise indicated.

The Stephan Co
CONSOLIDATED BALANCE SHEETS
At September 30, 2017 and December 31, 2016
(In thousands, except share and per share amounts)

	2017 (Unaudited)	2016 (Audited)
<u>ASSETS</u>		
Current Assets		
Cash and cash equivalents	\$ 260	\$ 784
Accounts receivable, net	219	181
Inventories, net	1,061	974
Prepaid expenses and other current assets	<u>95</u>	<u>75</u>
Total Current Assets	1,635	2,014
Other assets, net	27	13
Property and equipment, net	200	250
Deferred tax assets	297	297
Intangibles	645	---
Goodwill, net	<u>1,395</u>	<u>1,395</u>
TOTAL ASSETS	<u>\$ 4,199</u>	<u>\$ 3,969</u>
<u>LIABILITIES & STOCKHOLDERS' EQUITY</u>		
Current Liabilities		
Accounts payable and accrued expenses	\$ 394	\$ 529
Loans payable	<u>70</u>	<u>---</u>
Total Current Liabilities	464	529
Deferred tax liability	<u>182</u>	<u>182</u>
TOTAL LIABILITIES	646	711
COMMITMENTS AND CONTINGENCIES		
STOCKHOLDERS' EQUITY		
At September 30, 2017 and December 31, 2016:		
Preferred stock, \$.01 par value; 1,000,000 shares authorized; none issued or outstanding	---	---
Common stock, \$.01 par value; 25,000,000 shares authorized; 4,599,611 shares issued (3,993,020 shares outstanding at September 30, 2017 and 3,807,027 shares outstanding at December 31, 2016)	46	44
Additional paid-in capital	18,583	18,178
Accumulated deficit	(13,882)	(13,814)
Treasury stock (606,591 shares at September 30, 2017 and 582,584 shares at December 31, 2016), at cost	<u>(1,194)</u>	<u>(1,150)</u>
TOTAL STOCKHOLDERS' EQUITY	<u>3,553</u>	<u>3,258</u>
TOTAL LIABILITIES & STOCKHOLDERS' EQUITY	<u>\$ 4,199</u>	<u>\$ 3,969</u>

The Stephan Co
CONSOLIDATED STATEMENTS OF OPERATIONS
Three Months Ended September 30, 2017 and September 30, 2016
(in thousands, except per share data)

	<u>2017</u> (Unaudited)	<u>2016</u> (Audited)
Revenue	\$ 1,953	\$ 1,933
Cost of revenue	<u>1,353</u>	<u>1,338</u>
Gross profit	600	595
Selling, general and administrative expenses	439	414
Depreciation and amortization	<u>20</u>	<u>13</u>
Operating income	141	169
Other expense, net	<u>(13)</u>	<u>---</u>
Income from continuing operations before income taxes	128	169
Provision for income taxes	<u>---</u>	<u>---</u>
Income from continuing operations	128	169
Income from discontinued operations, net of \$0 tax in 2017 and 2016	<u>---</u>	<u>---</u>
NET INCOME	<u>\$ 128</u>	<u>\$ 169</u>
Per common share:		
Income from continuing operations	\$ 0.03	\$ 0.04
Income from discontinued operations	<u>---</u>	<u>---</u>
Net income	<u>\$ 0.03</u>	<u>\$ 0.04</u>
Weighted average common shares outstanding	3,861,353	3,825,849

The Stephan Co
CONSOLIDATED STATEMENTS OF OPERATIONS
 Nine Months Ended September 30, 2017 and September 30, 2016
(in thousands, except per share data)

	<u>2017</u> (Unaudited)	<u>2016</u> (Audited)
Revenue	\$ 6,027	\$ 5,989
Cost of revenue	<u>4,137</u>	<u>4,140</u>
Gross profit	1,890	1,849
Selling, general and administrative expenses	1,302	1,272
Depreciation and amortization	<u>62</u>	<u>38</u>
Operating income	526	539
Other expense, net	<u>(9)</u>	<u>---</u>
Income from continuing operations before income taxes	517	539
Provision for income taxes	<u>---</u>	<u>---</u>
Income from continuing operations	517	539
Income from discontinued operations, net of \$0 tax in 2017 and 2016	<u>---</u>	<u>---</u>
NET INCOME	<u><u>\$ 517</u></u>	<u><u>\$ 539</u></u>
Per common share:		
Income from continuing operations	\$ 0.14	\$ 0.14
Income from discontinued operations	<u>---</u>	<u>---</u>
Net income	<u><u>\$ 0.14</u></u>	<u><u>\$ 0.14</u></u>
Weighted average common shares outstanding	3,820,524	3,928,582

The Stephan Co
CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY
 Nine Months Ended September 30, 2017
(in thousands, except share information)

	Shares <u>Issued</u>	<u>Par Value</u>	Additional <u>Paid-in Capital</u>	Accumulated <u>Deficit</u>	Treasury <u>Stock</u>	Stockholders' <u>Equity</u>
Balance at December 31, 2016 (Audited)	4,389,611	\$ 44	\$ 18,178	\$ (13,814)	\$ (1,150)	\$ 3,258
Stocks issued in business acquisition (200,000 shares at \$1.97 per share)	200,000	2	392	---	---	394
Options exercised	10,000	---	13	---	---	13
Stock buyback, 24,007 shares	---	---	---	---	(44)	(44)
Dividends paid	---	---	---	(585)	---	(585)
Net Income	---	---	---	517	---	517
Balance at September 30, 2017 (Unaudited)	<u>4,599,611</u>	<u>\$ 46</u>	<u>\$ 18,583</u>	<u>\$ (13,882)</u>	<u>\$ (1,194)</u>	<u>\$ 3,553</u>

The Stephan Co
CONSOLIDATED STATEMENTS OF CASH FLOWS
 Nine Months Ended September 30, 2017 and September 30, 2016
(in thousands)

	2017 (Unaudited)	2016 (Audited)
<u>CASH FLOWS FROM OPERATING ACTIVITIES</u>		
NET INCOME	\$ 517	\$ 539
Net cash flows provided by operating activities:		
Depreciation and amortization	62	38
Changes in operating assets & liabilities:		
(Increase) decrease in accounts receivable, net	(21)	25
(Increase) decrease in inventories, net	45	(59)
Increase in prepaid expenses and other assets	(34)	(102)
Increase (decrease) in accounts payable and accrued expenses	<u>(178)</u>	<u>177</u>
Net cash provided by operating activities - continuing operations	391	618
Net cash used in operating activities - discontinued operations	<u>---</u>	<u>(112)</u>
Net cash provided by operating activities	391	506
<u>CASH FLOWS FROM INVESTING ACTIVITIES</u>		
Cash paid for acquisition of MD Barber, net	(231)	---
Purchases of property and equipment	<u>(12)</u>	<u>---</u>
Net cash used in investing activities	(243)	---
<u>CASH FLOWS FROM FINANCING ACTIVITIES</u>		
Loan repayments	(56)	---
Stock options exercised	13	---
Stock repurchased	(44)	(266)
Dividends paid	<u>(585)</u>	<u>(591)</u>
Net cash used in financing activities	(672)	(857)
NET (DECREASE) IN CASH AND CASH EQUIVALENTS	(524)	(351)
CASH AND CASH EQUIVALENTS AT BEGINNING OF EACH PERIOD	<u>784</u>	<u>1,093</u>
CASH AND CASH EQUIVALENTS AT END OF EACH PERIOD	<u>\$ 260</u>	<u>\$ 742</u>

Management's Discussion and Analysis

The Stephan Co. acquired and integrated MD Barber Supply, LLC ("MD Barber") in the third quarter of 2017 (Q3 2017). Sales of MD Barber were insignificant in Q3 2017, as the acquisition closed in September 2017. Also, SPCO absorbed significant acquisition and integration expenses as well as MD Barber's expense structure in Q3 2017. In Q4 2017 to-date, sales of MD have picked up and organic sales (excluding MD Barber) at SPCO also improved markedly. Consolidated sales of SPCO in Q4 2017 are up approximately 20% through mid-December when compared to the same period one-year ago, and organic sales (excluding the acquired revenues) are up 9% in Q4 2017 on a year-over-year basis. The Company believes that it is taking market share due to more effective outbound sales efforts, an improved online sales presence and better merchandising. The Company continues to seek attractive acquisitions in the barber wholesale distribution and products space. SPCO is also continuing to reduce general and administrative expenses in 2018 and will provide more details in its Q4 2017 report on these cost savings expected in 2018. The Company has also recently been working on an agreement to monetize a portion of its trademark portfolio and will share the details if and when the deal is complete.

The Company's cash balance has built to \$569,700 as of December 15, 2017. The company is debt free as of this date.

Liquidity and Capital Resources

We had cash and cash equivalents of \$260,000 at September 30, 2017. Our cash was maintained in FDIC-insured bank accounts and collateralized short-term investments.

Our continuing operations provided cash flows of approximately \$391,000 for the nine months ended September 30, 2017. During the first nine months of the year, we distributed dividends amounting to \$585,000; net cash payment for the acquisition of MD Barber on September 7, 2017 for approximately \$231,000; and repurchased 24,007 shares of common stock for \$44,000 which is approximately 0.6% of outstanding shares. In addition, we assumed outstanding loans of approximately \$126,000 from the acquisition of MD Barber and have repaid \$56,000 as of September 30, 2017. The company issued 200,000 shares for the acquisition of MD Barber.

We have adequate liquidity and do not foresee the need for additional capital for day-to-day operations in the next year. At September 30, 2017, we have in excess of \$18.0 million in net operating loss ("NOL") carry forwards available to offset future taxable income, maintain approximately \$1.2 million in working capital and total net worth of \$3.5 million.

We have no off-balance sheet financing arrangements except for operating leases primarily related to our Distributor operations.

Statements of Cash Flows – Supplemental Schedule

The assets acquired and liabilities assumed and considerations paid in the acquisition of MD Barber are as follows:

Assets acquired:

Cash	\$ 38
Accounts receivable	21
Inventory	<u>132</u>
Total assets acquired	<u>191</u>

Liabilities assumed:

Accounts payable and accrued liabilities	50
Loans payable	<u>126</u>
Total liabilities assumed	<u>176</u>

Excess of assets acquired over liabilities assumed	<u>\$ 15</u>
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Cash and noncash considerations in business acquisition:	
Cash paid, net of \$8,800 owed to one of the shareholders	\$ 231
Stocks issued (200,000 shares at \$1.97 per share)	394
Purchase credit	<u>35</u>
Total considerations paid	<u>660</u>
Excess of considerations paid over net assets acquired	\$ <u>645</u>

The Company recorded all acquired assets and liabilities assumed at fair value, resulting in a new accounting basis for the assets and liabilities as well as the recording of \$645,000 of an intangible asset attributable to acquired trademark, customer relationship and online sales presence. This acquisition will also allow the Company to distribute its existing products via the online channel resulting from the acquisition of MD Barber.

The purchase credit for \$35,000 is available to one of the former shareholders of MD Barber. The purchase credit allows the former shareholder to purchase inventory, at discounted price, up to the available credit.

An additional \$10,000 consideration was held back by the Company for potential purchase price adjustments on inventory, debt and accounts payable balances 90 days after closing date as compared to the interim financial statements provided prior to the close. The net amount due under this provision is still being calculated as of the date of this report.

Total one-time expenses incurred in the acquisition of MD Barber amounted to approximately \$13,800 included under other expenses.

Results of Operations Three Months Ended September 30, 2017 vs. Three Months Ended September 30, 2016

Overall revenues for the three months ended September 30, 2017 were \$1,953,000 compared to \$1,933,000 for the three months ended September 30, 2016 or an increase in revenues of \$20,000, or 1.0%. The increase in revenues in Q3 2017 versus Q3 2016 is largely attributable to higher revenue of Barber Express and Williamsport. Gross profit margins were the same at 31% in Q3 2017 and Q3 2016.

Selling, general and administrative expenses for Q3 2017 increased by approximately \$25,000, or 6%. This is largely attributable to the selling, general and administrative expenses of the acquired business of MD Barber amounting to approximately \$19,000.

Results of Operations Nine Months Ended September 30, 2017 vs. Nine Months Ended September 30, 2016

The results of operations reported for the nine months ended September 30, 2017 mainly represent the Company's distribution business.

Overall revenues for the nine months ended September 30, 2017 were \$6,027,000 compared to \$5,989,000 for the nine months ended September 30, 2016. The net increase of \$38,000, or 0.6%, resulted mainly from increased organic sales of \$56,000 during Q2 2017 and Q3 2017 which offset the decline in revenue during the slow Q1 2017.

Selling, general and administrative expenses for the nine months increased by approximately \$30,000 or 2.4%. Of this amount \$19,000 is attributable to MD Barber. Also, included in Q3 2017 selling, general and administrative expenses were one-time acquisition expense amounting to \$13,800 classified under other expenses.

Nine Months Ended September 30, 2017 and September 30, 2016
(in thousands)

	<u>2017</u>	<u>2016</u>
Sales	6,027	5,989
% change	0.6%	---
Gross profit	1,890	1,849
% of sales	31.4%	30.9%
SG&A	1,302	1,272
% of sales	21.6%	21.2%
EBITDA	592	577
% of sales	9.8%	9.6%
Capex	12	0
 Working capital (1)	 816	 471
 Invested capital (2)	 1,208	 928
 LTM EBIT	 598	
LTM PRE-TAX ROIC	49.5%	

Note: (1) Working capital = Inventory plus AR less AP

(2) Invested capital = total tangible assets less cash and payables and accruals.

Please read our Audited 2016 Annual Report which can be found at www.otcm Markets.com (symbol: SPCO.PK) for further information about the Company's financial results and future plans.