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 September 30, 2019

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 0-21513

DXP Enterprises, Inc.

(Exact name of registrant as specified in its charter)

Texas	**76-0509661**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)

5301 Hollister, Houston, Texas 77040

(Address of principal executive offices, including zip code)

(713) 996-4700

(Registrant's telephone number, including area code)

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

Title of Each Class	Trading Symbol	Name of Exchange on which Registered
Common Stock par value $0.01	DXPE	NASDAQ Global Select Market

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, 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 [X] No [ ]

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See 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 [ ] 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 [X]

Number of shares of registrant's Common Stock outstanding as of October 31, 2019: 17,603,267 par value $0.01 per share.

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PART I: FINANCIAL INFORMATION

ITEM 1: FINANCIAL STATEMENTS

DXP ENTERPRISES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME
(in thousands, except per share amounts) (unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2019	2018	2019	2018
Sales	$ 327,178	$ 308,028	$ 971,721	$ 905,191
Cost of sales	234,474	223,958	702,830	659,560
Gross profit	92,704	84,070	268,891	245,631
Selling, general and administrative expenses	70,987	67,257	209,511	197,609
Income from operations	21,717	16,813	59,380	48,022
Other (income) expense, net	(25)	120	127	(1,318)
Interest expense	4,986	4,781	14,911	15,959
Income before income taxes	16,756	11,912	44,342	33,381
Provision for income taxes	3,606	3,550	10,655	8,962
Net income	13,150	8,362	33,687	24,419
Net income (loss) attributable to noncontrolling interest	41	(35)	(172)	(91)
Net income attributable to DXP Enterprises, Inc.	13,109	8,397	33,859	24,510
Preferred stock dividend	23	23	68	68
Net income attributable to common shareholders	$ 13,086	$ 8,374	$ 33,791	$ 24,442
Net income	$ 13,150	$ 8,362	$ 33,687	$ 24,419
Currency translation adjustments	(1,281)	3,390	(718)	1,880
Comprehensive income	$ 11,869	$ 11,752	$ 32,969	$ 26,299
Earnings per share :				
Basic	$ 0.74	$ 0.48	$ 1.92	$ 1.39
Diluted	$ 0.71	$ 0.46	$ 1.84	$ 1.33
Weighted average common shares outstanding :				
Basic	17,602	17,564	17,588	17,547
Diluted	18,442	18,404	18,428	18,387

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

DXP ENTERPRISES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
(in thousands, except share and per share data) (unaudited)

	As of			
		September 30, 2019		**December 31, 2018**
ASSETS				
Current assets:				
Cash	**$**	**28,436**	$	40,304
Restricted cash		**124**		215
Accounts Receivable, net of allowance for doubtful accounts of **$9,657** and $10,126		**210,098**		191,829
Inventories		**131,916**		114,830
Costs and estimated profits in excess of billings		**33,898**		32,514
Prepaid expenses and other current assets		**6,328**		4,938
Federal income taxes receivable		**1,518**		960
Total current assets		**412,318**		**385,590**
Property and equipment, net		**58,516**		51,330
Goodwill		**194,052**		194,052
Other intangible assets, net		**56,072**		67,207
Operating lease ROU assets		**67,296**		—
Other long-term assets		**3,300**		1,783
Total assets	**$**	**791,554**	**$**	**699,962**
LIABILITIES AND EQUITY				
Current liabilities:				
Current maturities of long-term debt	**$**	**2,500**	$	3,407
Trade accounts payable		**83,174**		87,407
Accrued wages and benefits		**20,242**		21,275
Customer advances		**4,606**		3,223
Billings in excess of costs and estimated profits		**7,201**		10,696
Short-term operating lease liabilities		**17,711**		—
Other current liabilities		**16,544**		17,269
Total current liabilities		**151,978**		**143,277**
Long-term debt, net of current maturities and unamortized debt issuance costs		**235,576**		236,979
Long-term operating lease liabilities		**49,602**		—
Other long-term liabilities		**951**		2,819
Deferred income taxes		**11,056**		8,633
Total long-term liabilities		**297,185**		**248,431**
Total liabilities		**449,163**		**391,708**
Commitments and contingencies (Note 11)				
Shareholders' Equity:				
Series A and B preferred stock, $1.00 par value each; 1,000,000 shares authorized each		16		16
Common stock, $0.01 par value, 100,000,000 shares authorized; **17,603,267** and 17,401,297 outstanding		**174**		174
Additional paid-in capital		**157,426**		156,190
Retained earnings		**203,526**		169,735
Accumulated other comprehensive loss		(19,985)		(19,267)
Total DXP Enterprises, Inc. Equity		**341,157**		**306,848**
Noncontrolling interest		**1,234**		1,406
Total Equity		**342,391**		**308,254**
Total liabilities and Equity	**$**	**791,554**	**$**	**699,962**

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

DXP ENTERPRISES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(in thousands) (unaudited)

	Nine Months Ended September 30,	
	2019	2018
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income attributable to DXP Enterprises, Inc.	$ 33,859	$ 24,510
Less: net loss attributable to non-controlling interest	(172)	(91)
Net income	33,687	24,419
Reconciliation of net income to net cash provided by operating activities:		
Depreciation	7,270	7,135
Amortization of intangible assets	11,423	12,575
Write-off of debt issuance costs	—	60
Gain on sale of property and equipment	(9)	(1,318)
Bad debt expense	(75)	2,633
Payment of contingent consideration liability in excess of acquisition-date fair value	(106)	—
Fair value adjustment on contingent consideration	101	—
Amortization of debt issuance costs	1,406	1,337
Stock compensation expense	1,502	2,023
Deferred income taxes	2,337	240
Changes in operating assets and liabilities		
Trade accounts receivable	(17,581)	(13,225)
Costs and estimated profits in excess of billings	(1,371)	(11,541)
Inventories	(17,039)	(22,468)
Prepaid expenses and other assets	1,786	(250)
Trade accounts payable and accrued expenses	(6,301)	4,291
Billings in excess of costs and estimated profits	(3,524)	1,320
Other long-term liabilities	(6,021)	2,611
Net cash provided by operating activities	**$ 7,485**	**$ 9,842**
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchase of property and equipment	(14,247)	(7,705)
Proceeds from the sale of property and equipment	35	2,546
Acquisition of business, net of cash acquired	—	(10,812)
Net cash used in investing activities	**$ (14,212)**	**$ (15,971)**
CASH FLOWS FROM FINANCING ACTIVITIES:		
Principal debt payments	(3,716)	(2,534)
Debt issuance costs	—	(60)
Payment for contingent consideration liability	(1,394)	—
Dividends paid	(68)	(68)
Payment for employee taxes withheld from stock awards	(266)	(332)
Net cash used in financing activities	**$ (5,444)**	**$ (2,994)**
Effect of foreign currency on cash	213	(66)
Net change in cash and restricted cash	(11,958)	(9,189)
Cash and restricted cash at beginning of period	40,519	25,579
Cash and restricted cash at end of period	**$ 28,561**	**$ 16,390**

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

DXP ENTERPRISES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF EQUITY
(in thousands) (unaudited)

	Series A preferred stock	Series B preferred stock	Common stock	Paid-in capital	Retained earnings	Non controlling interest	Accum other comp loss	Total equity
Balances at June 30, 2018	$ 1	$ 15	$ 174	$ 155,341	$ 150,261	$ 512	$ (21,001)	$ 285,303
Preferred dividends paid	—	—	—	—	(23)	—	—	$ (23)
Compensation expense for restricted stock	—	—	—	526	—	—	—	$ 526
Tax related items for share based awards	—	—	—	(196)	—	—	—	$ (196)
Currency translation adjustment	—	—	—	—	—	—	3,390	$ 3,390
Net income	—	—	—	—	8,397	(35)	—	$ 8,362
Balances at September 30, 2018	**$ 1**	**$ 15**	**$ 174**	**$ 155,671**	**$ 158,635**	**$ 477**	**$ (17,611)**	**$ 297,362**

	Series A preferred stock	Series B preferred stock	Common stock	Paid-in capital	Retained earnings	Non controlling interest	Accum other comp loss	Total equity
Balances at December 31, 2017	$ 1	$ 15	$ 174	$ 153,086	$ 134,193	$ 568	$ (19,491)	$ 268,546
Preferred dividends paid	—	—	—	—	(68)	—	—	$ (68)
Compensation expense for restricted stock	—	—	—	2,023	—	—	—	$ 2,023
Tax related items for share based awards	—	—	—	(332)	—	—	—	$ (332)
Issuance of shares of common stock	—	—	—	894	—	—	—	$ 894
Currency translation adjustment	—	—	—	—	—	—	1,880	$ 1,880
Net income	—	—	—	—	24,510	(91)	—	$ 24,419
Balances at September 30, 2018	**$ 1**	**$ 15**	**$ 174**	**$ 155,671**	**$ 158,635**	**$ 477**	**$ (17,611)**	**$ 297,362**

	Series A preferred stock	Series B preferred stock	Common stock	Paid-in capital	Retained earnings	Non controlling interest	Accum other comp loss	Total equity
Balances at June 30, 2019	$ 1	$ 15	$ 174	$ 157,091	$ 190,440	$ 1,193	$ (18,704)	$ 330,210
Preferred dividends paid	—	—	—	—	(23)	—	—	$ (23)
Compensation expense for restricted stock	—	—	—	473	—	—	—	$ 473
Tax related items for share based awards	—	—	—	(138)	—	—	—	$ (138)
Issuance of shares of common stock	—	—	—	—	—	—	—	$ —
Currency translation adjustment	—	—	—	—	—	—	(1,281)	$ (1,281)
Net income	—	—	—	—	13,109	41	—	$ 13,150
Balances at September 30, 2019	**$ 1**	**$ 15**	**$ 174**	**$ 157,426**	**$ 203,526**	**$ 1,234**	**$ (19,985)**	**$ 342,391**

	Series A preferred stock	Series B preferred stock	Common stock	Paid-in capital	Retained earnings	Non controlling interest	Accum other comp loss	Total equity
Balances at December 31, 2018	$ 1	$ 15	$ 174	$ 156,190	$ 169,735	$ 1,406	$ (19,267)	$ 308,254
Preferred dividends paid	—	—	—	—	(68)	—	—	$ (68)
Compensation expense for restricted stock	—	—	—	1,502	—	—	—	$ 1,502
Tax related items for share based awards	—	—	—	(266)	—	—	—	$ (266)
Issuance of shares of common stock	—	—	—	—	—	—	—	$ —
Currency translation adjustment	—	—	—	—	—	—	(718)	$ (718)
Net income	—	—	—	—	33,859	(172)	—	$ 33,687
Balances at September 30, 2019	**$ 1**	**$ 15**	**$ 174**	**$ 157,426**	**$ 203,526**	**$ 1,234**	**$ (19,985)**	**$ 342,391**

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

NOTE 1 - THE COMPANY

DXP Enterprises, Inc. together with its subsidiaries (collectively "DXP," "Company," "us," "we," or "our") was incorporated in Texas on July 26, 1996. DXP Enterprises, Inc. and its subsidiaries are engaged in the business of distributing maintenance, repair and operating ("MRO") products, and service to energy and industrial customers. Additionally, DXP provides integrated, custom pump skid packages, pump remanufacturing and manufactures branded private label pumps to energy and industrial customers. The Company is organized into three business segments: Service Centers ("SC"), Supply Chain Services ("SCS") and Innovative Pumping Solutions ("IPS"). See Note 12 - Segment Reporting for discussion of the business segments.

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING AND BUSINESS POLICIES

Basis of Presentation

The Company's financial statements are prepared in accordance with generally accepted accounting principles in the United States of America ("US GAAP"). The accompanying condensed consolidated financial statements include the accounts of the Company, its wholly owned subsidiaries and its variable interest entity ("VIE"). The accompanying unaudited condensed consolidated financial statements have been prepared on substantially the same basis as our annual consolidated financial statements and should be read in conjunction with our annual report on Form 10-K for the year ended December 31, 2018. For a more complete discussion of our significant accounting policies and business practices, refer to the consolidated annual report on Form 10-K filed with the Securities and Exchange Commission on March 8, 2019. The results of operations for three and nine months ended September 30, 2019 are not necessarily indicative of results expected for the full fiscal year. In the opinion of management, these condensed consolidated financial statements contain all adjustments necessary to present fairly the Company's condensed consolidated statements of operations and comprehensive income for three and nine months ended September 30, 2019 and September 30, 2018, condensed consolidated balance sheets as of September 30, 2019 and December 31, 2018, condensed consolidated statements of cash flows for the nine months ended September 30, 2019 and September 30, 2018, and condensed consolidated statement of equity for three and nine months ended September 30, 2019 and September 30, 2018. All such adjustments represent normal recurring items.

All inter-company accounts and transactions have been eliminated upon consolidation.

NOTE 3 - RECENT ACCOUNTING PRONOUNCEMENTS

Recently Adopted Accounting Pronouncements

Leases. In February 2016, the Financial Accounting Standards Board's ("FASB") issued Accounting Standards Update ("ASU") No. 2016-02, *Leases (Topic 842)* as modified by subsequently issued ASUs 2018-01, 2018-10, 2018-11 and 2018-20. The Company adopted the standard effective January 1, 2019. We have elected to apply the current period transition approach as introduced by ASU 2018-11 for our transition at January 1, 2019 and we have elected to apply several of the practical expedients in conjunction with accounting policy elections. See Note 4 - Leases for further discussion.

Accounting Pronouncements Not Yet Adopted

Intangibles-Goodwill and Other. In August 2018, the FASB issued ASU No. 2018-15, *Internal-Use Software (Subtopic 350-40): Customer’s Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That Is a Service Contract* based on a consensus of the FASB’s Emerging Issues Task Force (EITF) that requires implementation costs incurred by customers in cloud computing arrangements (CCAs) to be deferred and recognized over the term of the arrangement, if those costs would be capitalized by the customer in a software licensing arrangement under the internal-use software guidance in ASC 350-40, “Intangibles-Goodwill and Other-Internal-Use Software”. The ASU does not affect the accounting by cloud service providers, other software vendors or customers’ accounting for software licensing arrangements. The ASU will require companies to recognize deferred implementation costs to expense over the ‘term of the hosting arrangement’. Under the ASU, the term of the hosting arrangement comprises the non-cancellable period of the CCA plus any optional renewal periods that are reasonably certain to be exercised by the customer or for which exercise of the option is controlled by the vendor. The guidance is effective for fiscal years beginning after December 15, 2019, and interim periods within those fiscal years. We will adopt the new standard beginning January 1, 2020. We do not anticipate that the new standard will have a material impact on our results of operations.

Fair Value Measurement. In August 2018, the FASB issued ASU 2018-13: *Fair Value Measurement: Disclosure Framework-Changes to the Disclosure Requirements for Fair Value Measurement* which eliminates, adds and modifies certain disclosure requirements for fair value measurements as part of its disclosure framework project. Entities will no longer be required to disclose the amount of and reasons for transfers between Level 1 and Level 2 of the fair value hierarchy, but public companies will be required to disclose the range and weighted average used to develop significant unobservable inputs for Level 3 fair value measurements. The guidance is effective for all entities for fiscal years beginning after December 15, 2019 and for interim periods within those fiscal years, but entities are permitted to early adopt either the entire standard or only the provisions that eliminate or modify the disclosure requirements. The new standard will not have an impact on our results of operations, but it will significantly modify our disclosures around fair value measurements.

Financial Instruments – Credit Losses. In June 2016, the FASB issued ASU 2016-13: *Financial Instruments – Credit Losses,* which replaces the incurred loss impairment methodology in current US GAAP with a methodology that reflects expected credit losses ("CECL"). The update is intended to provide financial statement users with more useful information about expected credit losses.

We do not currently hold most of the financial instruments contemplated by the new standard, with the exception of trade receivables. CECL will become the single model to measure impairment on financial assets measured at amortized cost, which include trade receivables. Therefore, consistent with other types of financial assets measured at amortized cost, estimates of expected credit losses on trade receivables over their contractual life will be required to be recorded at inception, based on historical information, current conditions, and reasonable and supportable forecasts.

Currently, our reserve methodology for trade receivables is based on matrices in which historical loss percentages are applied to respective aging categories. CECL will require us to use a forward-looking methodology that incorporates lifetime expected credit losses. While our current reserving matrices may still be used under CECL, historical loss data will need to be combined with reasonable and supportable forecasts of future losses to determine estimated credit losses. The most visible impact of CECL will therefore be that receivables that are either current or not yet due, which today do not generally have a reserve, will have an allowance for expected credit losses.

The CECL model does not prescribe a specific methodology for developing a reasonable and supportable forecast, nor the duration of the period that losses can be forecast, nor the precision required to support the estimate. As a result, the determination of the reasonable and supportable forecast period is a judgment to be made in estimating the overall expected credit loss. Although the CECL model requires entities to perform this new evaluation for trade receivables, we generally do not expect to see a significant change in the impairment losses recognized on our trade receivables given their short-term nature. The amended guidance is effective for fiscal years beginning after December 15, 2019, with early adoption permitted. We will adopt the new guidance beginning January 1, 2020.

NOTE 4 - LEASES

In February 2016, the FASB issued ASU No. 2016-02, Leases (Topic 842) which was modified by subsequently issued ASUs 2018-01, 2018-10, 2018-11 and 2018-20. The update requires organizations that lease assets ("lessees") to recognize the assets and liabilities of the rights and obligations created by leases with terms of more than 12 months. The recognition, measurement and presentation of expenses and cash flows arising from a lease by a lessee remains dependent on its classification as a finance or operating lease. The criteria for determining whether a lease is a finance or operating lease was not significantly changed by this ASU. The ASU also requires additional disclosure of the amount, timing, and uncertainty of cash flows arising from leases, including qualitative and quantitative requirements. This pronouncement was effective for financial statements issued for annual periods beginning after December 15, 2018, including interim periods within those fiscal years. Early adoption was permitted.

In July 2018, the FASB issued ASU No. 2018-11, Leases: Targeted Improvements (Topic 842). ASU 2018-11 provided additional relief in the comparative reporting requirements for initial adoption of ASC 842. Prior to ASU 2018-11, a modified retrospective transition was required for financing or operating leases existing at or entered into after the beginning of the earliest comparative period presented in the financial statements. ASU 2018-11 provided an additional transition method to the existing transition method by allowing entities to initially apply the new leases standard at the adoption date (such as January 1, 2019, for calendar year-end public business entities) and recognize a cumulative-effect adjustment to the opening balance of retained earnings in the period of adoption without adjustment to the financial statements for periods prior to adoption.

The Company adopted the standard effective January 1, 2019. We elected to apply the current period transition approach as introduced by ASU 2018-11 for our transition at January 1, 2019 and we elected to apply the following practical expedients and accounting policy decisions.

We elected a package of transition expedients that allowed us to forgo reassessing certain conclusions reached under ASC 840 which must be elected together. All expedients in this package were applied together for all leases that commenced before the effective date, January 1, 2019, of ASC 842. As a result, in transitioning to ASC 842, for existing leases as of January 1,2019, we continued to use judgments made under ASC 840 related to embedded leases, lease classification and accounting for initial direct costs. We generally have four classes of leased assets : Real Estate related properties (such as office space, warehouses, distribution centers and land), Automobiles, Office Equipment and Manufacturing Equipment and do not utilize finance leases.

In addition, we have chosen, as an accounting policy election by class of underlying asset, not to separate nonlease components from the associated lease for all of our leased asset classes, except for Real Estate related leases. As a result, for classes of Automobiles, Office Equipment and Manufacturing Equipment, we account for each separate lease component and the nonlease components associated with that lease as a single lease component.

For short-term leases as defined under ASC 842, we elected the short-term lease exception pursuant to ASC 842 to all classes of our leased assets. We do not recognize a lease liability or a right of use asset on our consolidated balance sheets for our leased assets with an original lease term of twelve months or less. Instead, we recognize the lease payments in profit or loss on a straight-line basis over the lease term and variable lease payments in the period in which the obligation for those payments is incurred and disclose in the notes to the consolidated financial statements our short-term lease expense.

The new standard did have a material impact on our consolidated balance sheets related to recording right-of-use (ROU) assets and the corresponding lease liabilities for our inventory of operating leases. In January 2019, we recorded a ROU Asset and total lease liability obligations of approximately $72 million each. The new standard did not have a material impact on our consolidated statements of operations and had no impact on cash flows.

We lease office space, warehouses, land, automobiles, and office and manufacturing equipment. All of our leases are classified as operating leases.

Our leases have remaining lease terms of 1 month to 12 years, some of which include options to extend the leases for up to 14 years. The exercise of lease renewal options is at our sole discretion. Our lease agreements do not include options to purchase the leased property.

The lease expenses were as follows *(in thousands)*:

		Three Months Ended September 30,	Nine Months Ended September 30,
Lease cost	**Classification**	**2019**	
Short-term lease expense	SG&A expenses(*)	309	870
Other operating lease cost	SG&A expenses(*)	6,081	17,957
Total operating lease cost		$ 6,390	$ 18,827

(*) Manufacturing equipment and some vehicle rental expenses are included in the cost of sales.

Supplemental cash flow information related to leases was as follows *(in thousands)*:

	Nine Months Ended September 30,
Lease	**2019**
Cash paid for amounts included in the measurement of lease liabilities:	
Operating cash flows from operating leases	13,941
Right-of-use assets obtained in exchange for lease liabilities	
Operating leases	8,889

Supplemental balance sheet information related to leases was as follows *(in thousand)*:

Lease	Classification	September 30, 2019	Impact of ASC 842 Transition
Assets			
Operating	Operating lease right-of-use assets	67,296	72,679
Liabilities			
Current operating	Short-term operating lease liabilities	17,711	18,762
Non-current operating	Long-term operating lease liabilities	49,602	53,654
Total operating lease liabilities		**$ 67,313**	**$ 72,416**

Note: As most of our leases do not provide an implicit rate, we use our incremental borrowing rate based on the information available at the commencement date in determining the present value of lease payments for lease commenced on or after January 1, 2019. We used our incremental borrowing rate as of the transition date of January 1, 2019 for operating leases that commenced prior to transition.

Maturities of lease liabilities were as follows *(in thousands)*:

Year Ending December 31,	Operating leases [*]
2019 (excluding 9 months ended 9/30/2019)	5,880
2020	20,841
2021	17,530
2022	13,315
2023	8,170
Thereafter	14,218
Total lease payments	$ 79,954
Less: imputed interest	12,641
Present value of lease liabilities	$ 67,313

[*] Operating lease payments exclude $1.2 million of legally binding minimum lease payments for leases signed but not yet commenced.

Contractual obligations related to operating leases as of December 31, 2018, under ASC 840 *(in thousands)*:

	Payments due by period (in thousands)				
	Less than 1 year	1-3 years	3-5 years	More than 5 years	Total
Operating lease obligations	$ 22,096	$ 33,825	$ 18,379	$ 11,022	$ 85,322

Lease term and discount rate	Nine Months Ended September 30, 2019
Weighted average remaining lease term (years)	
Operating lease	**4.8**
Weighted average discount rate	
Operating lease	**7.3%**

For the nine months ended September 30, 2019, the Company paid approximately $1.9 million in lease expenses to entities controlled by the Company's Chief Executive Officer, David Little and family.

NOTE 5 - FAIR VALUE OF FINANCIAL ASSETS AND LIABILITIES

Authoritative guidance for financial assets and liabilities measured on a recurring basis applies to all financial assets and financial liabilities that are being measured and reported on a fair value basis. Fair value, as defined in the authoritative guidance, is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The authoritative guidance affects the fair value measurement of an investment with quoted market prices in an active market for identical instruments, which must be classified in one of the following categories:

Level 1 Inputs

Level 1 inputs come from quoted prices (unadjusted) in active markets for identical assets or liabilities.

Level 2 Inputs

Level 2 inputs are other than quoted prices that are observable for an asset or liability. These inputs include: quoted prices for similar assets or liabilities in active markets; quoted prices for identical or similar assets or liabilities in markets that are not active; inputs other than quoted prices that are observable for the asset or liability; and inputs that are derived principally from, or corroborated by, observable market data by correlation or other means.

Level 3 Inputs

Level 3 inputs are unobservable inputs for the asset or liability which require the Company's own assumptions.

Financial assets and liabilities are classified based on the lowest level of input that is significant to the fair value measurement. Our assessment of the significance of a particular input to the fair value measurement requires judgment and may affect the valuation of the fair value of assets and liabilities and their placement within the fair value hierarchy levels.

Our acquisitions may include contingent consideration as part of the purchase price. The fair value of the contingent consideration is estimated as of the acquisition date based on the present value of the contingent payments to be made using a weighted probability of possible payments. The unobservable inputs used in the determination of the fair value of the contingent consideration include managements assumptions about the likelihood of payment based on the established benchmarks and discount rates based on an internal rate of return analysis. The fair value measurement includes inputs that are Level 3 classified as discussed above, as they are not observable in the market. Should actual results increase or decrease as compared to the assumption used in our analysis, the fair value of the contingent consideration obligations will increase or decrease, up to the contracted limit, as applicable. Changes in the fair value of the contingent earn-out consideration are measured each reporting period and reflected in our results of operations. As of September 30, 2019, we recorded a $2.9 million liability for contingent consideration associated with the acquisition of Application Specialties Inc. ("ASI") in other current and long-term liabilities.

For the Company's assets and liabilities measured at fair value on a recurring basis using significant unobservable inputs (Level 3), the following table provides a reconciliation of the beginning and ending balances for each category therein, and gains or losses recognized during the nine months ended September 30, 2019:

Fair Value Measurements Using Significant Unobservable Inputs (Level 3)

	Contingent Liability for Accrued Consideration
	(in thousands)
Beginning balance at December 31, 2018	$ 4,319
Acquisitions and settlements	
Acquisitions	—
Settlements	(1,500)
Total remeasurement adjustments:	
Changes in fair value recorded in other (income) expense, net	101
*Ending Balance at September 30, 2019	$ 2,920

The amount of total losses for the quarter included in earnings or changes to net assets, attributable to changes in unrealized losses relating to liabilities still held at September 30, 2019.	$ 101

* Included in other current and long-term liabilities

Quantitative Information about Level 3 Fair Value Measurements

The significant unobservable inputs used in the fair value measurement of the Company's contingent consideration liabilities designated as Level 3 are as follows:

(in thousands, unaudited)	Fair value at September 30, 2019	Valuation Technique	Significant Unobservable Inputs
Contingent consideration: (ASI acquisition)	$ 2,920	Discounted cash flow	Annualized EBITDA and probability of achievement

Sensitivity to Changes in Significant Unobservable Inputs

As presented in the table above, the significant unobservable inputs used in the fair value measurement of contingent consideration related to the acquisition of ASI are annualized earnings before interest, tax, deprecation and amortization ("EBITDA") forecasts developed by the Company's management and the probability of achievement of those EBITDA results. The discount rate used in the calculation was 7.3%. Significant increases (decreases) in these unobservable inputs in isolation would result in a significantly (lower) higher fair value measurement.

Other financial instruments not measured at fair value on the Company's unaudited condensed consolidated balance sheet at September 30, 2019 and December 31, 2018, but which require disclosure of their fair values include: cash and cash equivalents, trade accounts receivable, trade accounts payable and accrued expenses, accrued payroll and related benefits, and the revolving line of credit and term loan debt under our syndicated credit agreement facility. The Company believes that the estimated fair value of such instruments at September 30, 2019 and December 31, 2018 approximates their carrying value as reported on the unaudited condensed consolidated balance sheets.

NOTE 6 – INVENTORIES

The carrying values of inventories are as follows (*in thousands*):

	September 30, 2019	December 31, 2018
Finished goods	$ 122,102	$ 110,182
Work in process	22,509	17,344
Obsolescence reserve	(12,695)	(12,696)
Inventories	$ 131,916	$ 114,830

NOTE 7 – COSTS AND ESTIMATED PROFITS ON UNCOMPLETED CONTRACTS

Under our customized pump production contracts in our IPS segment, amounts are billed as work progresses in accordance with agreed-upon contractual terms, upon various measures of performance, including achievement of certain milestones, completion of specified units, or completion of a contract. Generally, billing occurs subsequent to revenue recognition, resulting in contract assets. Our contract assets are presented as "cost and estimated profits in excess of billings" on our Condensed Consolidated Balance Sheets. However, we sometimes receive advances or deposits from our customers before revenue is recognized, resulting in contract liabilities that are presented as "Billings in excess of costs and estimated profits" on our Condensed Consolidated Balance Sheets.

Costs and estimated profits on uncompleted contracts and related amounts billed were as follows (*in thousands*):

	September 30, 2019	December 31, 2018
Costs incurred on uncompleted contracts	$ 52,506	$ 53,595
Estimated profits, thereon	8,932	6,847
Total	61,438	60,442
Less: billings to date	34,743	38,662
Net	$ 26,695	$ 21,780

Such amounts were included in the accompanying Condensed Consolidated Balance Sheets for September 30, 2019 and December 31, 2018 under the following captions (*in thousands*):

	September 30, 2019	December 31, 2018
Costs and estimated profits in excess of billings	$ 33,898	$ 32,514
Billings in excess of costs and estimated profits	(7,201)	(10,696)
Translation adjustment	(2)	(38)
Net	$ 26,695	$ 21,780

During the nine months ended September 30, 2019, $10.5 million of the balances that were previously classified as contract liabilities at the beginning of the period shipped. Contract assets and liability changes were primarily due to normal activity and timing differences between our performance and customer payments.

NOTE 8 – INCOME TAXES

Our effective tax rate from continuing operations was a tax expense of 24.0% for the nine months ended September 30, 2019 compared to a tax expense of 26.9% for the nine months ended September 30, 2018. Compared to the U.S. statutory rate for the nine months ended September 30, 2019, the effective tax rate was increased by state taxes, foreign taxes and nondeductible expenses partially offset by research and development tax credits, other tax credits, and a favorable statutory tax rate change in a foreign jurisdiction. Compared to the U.S. statutory rate for the nine months ended September 30, 2018, the effective tax rate was increased by state taxes, foreign taxes and nondeductible expenses partially offset by research and development tax credits and other tax credits.

To the extent penalties and interest would be assessed on any underpayment of income tax, such accrued amounts would be classified as a component of income tax provision (benefit) in the financial statements consistent with the Company's policy.

NOTE 9 – LONG-TERM DEBT

The components of the Company's long-term debt consisted of the following (*in thousands*):

	September 30, 2019		December 31, 2018	
	Carrying Value [1]	Fair Value	Carrying Value [1]	Fair Value
ABL Revolver	$ —	$ —	$ —	$ —
Term Loan B	245,000	246,225	246,875	245,949
Promissory note payable [2]	—	—	1,841	1,841
Total long-term debt	245,000	246,225	248,716	247,790
Less: current portion	(2,500)	(2,513)	(3,407)	(3,398)
Long-term debt less current maturities	$ 242,500	$ 243,712	$ 245,309	$ 244,392

[1] Carrying value amounts do not include unamortized debt issuance costs of $6.9 million and $8.3 million for September 30, 2019 and December 31, 2018, respectively**.**
[2] Note payable in monthly installments at 2.9% through January 2021, collateralized by equipment. In August 2019, the Company made a cash payment of $1.3 million to repay the outstanding promissory note payable.

The fair value measurements used by the Company are considered Level 2 inputs, as defined in the fair value hierarchy. The fair value estimates were based on quoted prices for identical or similar securities.

The Company was in compliance with all financial covenants under the ABL Revolver and Term Loan B Agreements as of September 30, 2019.

NOTE 10 - EARNINGS PER SHARE DATA

Basic earnings per share is computed based on weighted average shares outstanding and excludes dilutive securities. Diluted earnings per share is computed including the impacts of all potentially dilutive securities.

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

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2019	2018	2019	2018
Basic:				
Weighted average shares outstanding	17,602	17,564	17,588	17,547
Net income attributable to DXP Enterprises, Inc.	$ 13,109	$ 8,397	$ 33,859	$ 24,510
Convertible preferred stock dividend	23	23	68	68
Net income attributable to common shareholders	$ 13,086	$ 8,374	$ 33,791	$ 24,442
Per share amount	$ 0.74	$ 0.48	$ 1.92	$ 1.39
Diluted:				
Weighted average shares outstanding	17,602	17,564	17,588	17,547
Assumed conversion of convertible preferred stock	840	840	840	840
Total dilutive shares	18,442	18,404	18,428	18,387
Net income attributable to common shareholders	$ 13,086	$ 8,374	$ 33,791	$ 24,442
Convertible preferred stock dividend	23	23	68	68
Net income attributable to DXP Enterprises, Inc.	$ 13,109	$ 8,397	$ 33,859	$ 24,510
Per share amount	$ 0.71	$ 0.46	$ 1.84	$ 1.33

NOTE 11 - COMMITMENTS AND CONTINGENCIES

From time to time, the Company is a party to various legal proceedings arising in the ordinary course of business. While DXP is unable to predict the outcome of these lawsuits, it believes that the ultimate resolution will not have, either individually or in the aggregate, a material adverse effect on DXP's consolidated financial position, cash flows, or results of operations.

NOTE 12 - SEGMENT REPORTING

The Company's reportable business segments are: Service Centers, Innovative Pumping Solutions and Supply Chain Services. The Service Centers segment is engaged in providing maintenance, MRO products, equipment and integrated services, including logistics capabilities, to industrial customers. The Service Centers segment provides a wide range of MRO products in the rotating equipment, bearing, power transmission, hose, fluid power, metal working, fastener, industrial supply, safety products and safety services categories. The Innovative Pumping Solutions segment fabricates and assembles custom-made pump packages, remanufactures pumps and manufactures branded private label pumps. The Supply Chain Services segment provides a wide range of MRO products and manages all or part of a customer's supply chain, including warehouse and inventory management.

The high degree of integration of the Company's operations necessitates the use of a substantial number of allocations and apportionments in the determination of business segment information. Sales are shown net of intersegment eliminations.

The following table sets out financial information related to the Company's segments excluding amortization (*in thousands*):

	Three Months Ended September 30,							
	2019				2018			
	SC	IPS	SCS	Total	SC	IPS	SCS	Total
Product sales (recognized at a point in time)	$ 178,841	$ —	$ 46,998	$ 225,839	$ 173,022	$ —	$ 40,210	$ 213,232
Inventory management services (recognized over contract life)	—	—	4,284	$ 4,284	—	—	3,393	$ 3,393
Staffing services (day-rate basis)	14,886	—	—	$ 14,886	14,741	—	—	$ 14,741
Customized pump production (recognized over time)	—	82,169	—	$ 82,169	—	76,662	—	$ 76,662
Total Revenue	$ 193,727	$ 82,169	$ 51,282	$ 327,178	$ 187,763	$ 76,662	$ 43,603	$ 308,028
Income from operations	$ 25,071	$ 10,097	$ 3,110	$ 38,278	$ 20,590	$ 8,773	$ 3,886	$ 33,249

	Nine Months Ended September 30,							
	2019				2018			
	SC	IPS	SCS	Total	SC	IPS	SCS	Total
Product sales (recognized at a point in time)	$ 534,953	$ —	$ 141,768	$ 676,721	$ 509,756	$ —	$ 120,040	$ 629,796
Inventory management services (recognized over contract life)	—	—	12,149	$ 12,149	—	—	9,890	$ 9,890
Staffing services (day-rate basis)	44,931	—	—	$ 44,931	46,944	—	—	$ 46,944
Customized pump production (recognized over time)	—	237,920	—	$ 237,920	—	218,561	—	$ 218,561
Total Revenue	$ 579,884	$ 237,920	$ 153,917	$ 971,721	$ 556,700	$ 218,561	$ 129,930	$ 905,191
Income from operations	$ 67,281	$ 28,924	$ 10,980	$ 107,185	58,353	24,109	12,196	$ 94,658

The following table presents reconciliations of operating income for reportable segments to the consolidated income before taxes (*in thousands*):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2019	2018	2019	2018
Operating income for reportable segments	$ 38,278	$ 33,249	$ 107,185	$ 94,658
Adjustment for:				
Amortization of intangible assets	3,806	4,098	11,424	12,575
Corporate expenses	12,755	12,338	36,381	34,061
Income from operations	$ 21,717	$ 16,813	59,380	48,022
Interest expense	4,986	4,781	14,911	15,959
Other income, net	(25)	120	127	(1,318)
Income before income taxes	$ 16,756	$ 11,912	$ 44,342	$ 33,381

The Company's identifiable assets by segments are as follows *(in thousands)*:

	As of September 30, 2019	As of December 31, 2018
Service Centers	$ 458,975	$ 402,944
Innovative Pumping Solutions	225,361	188,765
Supply Chain Services	60,342	53,517
Total Identifiable Assets	$ 744,678	$ 645,226

The Company had identifiable assets at Corporate of $46.9 million and $54.7 million, as of September 30, 2019 and December 31, 2018.

NOTE 13 - SUBSEQUENT EVENTS

We have evaluated subsequent events through the date the interim Condensed Consolidated Financial Statements were issued. There were no subsequent events that required recognition or disclosure unless elsewhere identified in this report.

ITEM 2: MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following management discussion and analysis ("MD&A") of the financial condition and results of operations of DXP Enterprises, Inc. together with its subsidiaries (collectively "DXP," "Company," "us," "we," or "our") for the three and nine months ended September 30, 2019 should be read in conjunction with our previous annual report on Form 10-K and our quarterly reports on Form 10-Q, and the consolidated financial statements and notes thereto included in our annual and quarterly reports. The Company's consolidated financial statements are prepared in accordance with accounting principles generally accepted in the United States of America ("US GAAP").

DISCLOSURE REGARDING FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q (this "Report") contains statements that constitute "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995, as amended. Such statements can be identified by the use of forward-looking terminology such as "believes", "expects", "may", "might", "estimates", "will", "should", "could", "would", "suspect", "potential", "current", "achieve", "plans" or "anticipates" or the negative thereof or other variations thereon or comparable terminology, or by discussions of strategy. Any such forward-looking statements are not guarantees of future performance and may involve significant risks and uncertainties, and actual results may vary materially from those discussed in the forward-looking statements or historical performance as a result of various factors. These factors include the effectiveness of management's strategies and decisions, our ability to implement our internal growth and acquisition growth strategies, general economic and business conditions specific to our primary customers, changes in government regulations, our ability to effectively integrate businesses we may acquire, our success in remediating our internal control weaknesses, new or modified statutory or regulatory requirements, availability of materials and labor, inability to obtain or delay in obtaining government or third-party approvals and permits, non-performance by third parties of their contractual obligations, unforeseen hazards such as weather conditions, acts or war or terrorist acts and the governmental or military response thereto, cyber-attacks adversely affecting our operations, other geological, operating and economic considerations and declining prices and market conditions, including reduced oil and gas prices and supply or demand for maintenance, repair and operating products, equipment and service, and our ability to obtain financing on favorable terms or amend our credit facilities as needed. This Report identifies other factors that could cause such differences. We cannot assure that these are all of the factors that could cause actual results to vary materially from the forward-looking statements. Factors that could cause or contribute to such differences include, but are not limited to, those discussed in "Risk Factors", included in our Annual Report on Form 10-K filed with the Securities and Exchange Commission on March 8, 2019. We assume no obligation and do not intend to update these forward-looking statements. Unless the context otherwise requires, references in this Report to the "Company", "DXP", "we" or "our" shall mean DXP Enterprises, Inc., a Texas corporation, together with its subsidiaries.

RESULTS OF OPERATIONS
(in thousands, except percentages and per share data)

DXP is organized into three business segments: Service Centers ("SC"), Supply Chain Services ("SCS") and Innovative Pumping Solutions ("IPS"). The Service Centers are engaged in providing maintenance, repair and operating ("MRO") products, equipment and integrated services, including technical expertise and logistics capabilities, to industrial customers with the ability to provide same day delivery. The Service Centers provide a wide range of MRO products and services in the rotating equipment, bearing, power transmission, hose, fluid power, metal working, industrial supply and safety product and service categories. The SCS segment provides a wide range of MRO products and manages all or part of our customer's supply chain function, and inventory management. The IPS segment fabricates and assembles integrated pump system packages custom made to customer specifications, remanufactures pumps and manufactures branded private label pumps. Over 90% of DXP's revenues represent sales of products.

	Three Months Ended September 30,			
	2019	%	2018	%
Sales	$ 327,178	100.0 %	$ 308,028	100.0%
Cost of sales	234,474	71.7 %	223,958	72.7%
Gross profit	$ 92,704	28.3 %	$ 84,070	27.3%
Selling, general and administrative expenses	70,987	21.7 %	67,257	21.8%
Income from operations	$ 21,717	6.6 %	$ 16,813	5.5%
Other (income) expense, net	(25)	— %	120	—%
Interest expense	4,986	1.5 %	4,781	1.6%
Income before income taxes	$ 16,756	5.1 %	$ 11,912	3.9%
Provision for income taxes (benefit)	3,606	1.1 %	3,550	1.2%
Net income	$ 13,150	4.0 %	$ 8,362	2.7%
Net (loss) income attributable to noncontrolling interest	41	—	(35)	—
Net income attributable to DXP Enterprises, Inc.	$ 13,109	4.0 %	$ 8,397	2.7%
Per share amounts attributable to DXP Enterprises, Inc.				
Basic earnings per share	0.74		$ 0.48	
Diluted earnings per share	0.71		$ 0.46	

Three Months Ended September 30, 2019 compared to Three Months Ended September 30, 2018

SALES. Sales for the three months ended September 30, 2019 increased $19.2 million, or 6.2%, to approximately $327.2 million from $308.0 million for the prior year's corresponding period. This sales increase is the result of an increase in our SCS, SC and IPS segments of $7.7 million, $6.0 million and $5.5 million, respectively. The fluctuations in sales is further explained in our business segment discussions below.

	Three Months Ended September 30,			
	2019	2018	Change	Change%
Sales by Business Segment	*(in thousands, except change%)*			
Service Centers	$ 193,727	$ 187,763	$ 5,964	3.2%
Innovative Pumping Solutions	82,169	76,662	5,507	7.2%
Supply Chain Services	51,282	43,603	7,679	17.6%
Total DXP Sales	$ 327,178	$ 308,028	$ 19,150	6.2%

Service Centers segment. Sales for the Service Centers segment increased by approximately $6.0 million, or 3.2% for the three months ended September 30, 2019 compared to the prior year's corresponding period. This sales increase is primarily the result of increased sales of rotating equipment and safety supply products to customers engaged in the late upstream, midstream or downstream oil and gas markets or manufacturing equipment for these markets in connection with increased capital spending by oil and gas producers. If the U.S. crude oil production remain at levels experienced during the first nine months of 2019, this level of sales to the oil and gas industry might continue, or improve, during the remainder of 2019.

Innovative Pumping Solutions segment. Sales for the IPS segment increased by $5.5 million, or 7.2% for the three months ended September 30, 2019 compared to the prior year's corresponding period. This increase was primarily the result of an increase in the capital spending by oil and gas producers and related businesses stemming from an increase in U.S. crude oil production. This level of IPS sales might continue, or improve, during the remainder of 2019, if the U.S. crude oil production remain at levels experienced during the first nine months of 2019.

Supply Chain Services segment. Sales for the SCS segment increased by $7.7 million, or 17.6%, for the three months ended September 30, 2019, compared to the prior year's corresponding period. The improved sales are primarily related to increased sales to customers in the medical device, aerospace, oil and gas and food and beverage industries as a result of new locations.

GROSS PROFIT. Gross profit as a percentage of sales for the three months ended September 30, 2019 increased by approximately 104 basis points from the prior year's corresponding period. The increase in the gross profit percentage is primarily the result of an approximate 304 basis point increase in the gross profit percentage in our IPS segment and 77 basis point increase in the gross profit percentage in our SC segment partially offset by a 37 basis point decrease in the gross profit percentage in our SCS segment. Gross profit for the IPS segment increased as a result of an increase in the capital spending by oil and gas producers and related businesses stemming from an increase in the U.S. crude oil production compared to the corresponding period in 2018.

Innovative Pumping Solutions segment. As a percentage of sales, the third quarter gross profit percentage for the IPS segment increased approximately 304 basis points from the prior year's corresponding period primarily as a result of an increase in utilization and capacity within IPS' engineered-to-order business and an overall improvement in the pricing environment driven by an increase in capital spending by oil and gas producers. Additionally, gross profit margins for individual orders have continued to improve because of the increase in sales of built to order customer specific products. Operating income for the IPS segment increased $1.3 million or 15.1%, primarily as a result of the above mentioned increase in sales.

Service Centers segment. As a percentage of sales, the third quarter gross profit percentage for the Service Centers increased approximately 77 basis points from the prior year's corresponding period. This was primarily as a result of sales mix and price increases from vendors. Operating income for the Service Centers segment increased $4.5 million, or 21.8%. The increase in operating income is primarily the result of the improved sales.

Supply Chain Services segment. Gross profit as a percentage of sales decreased approximately 37 basis points, compared to the prior year's corresponding period. This was primarily as a result of costs associated with new customer implementation. Operating income for the third quarter of 2019 decreased $0.8 million compared to the prior year's corresponding period mainly due to an increase in SG&A expense of $2.3 million primarily related to payroll and incentive compensation offset by an increase in gross profit of $1.5 million.

SELLING, GENERAL AND ADMINISTRATIVE ("SG&A"). Selling, general and administrative expense for the three months ended September 30, 2019 increased by approximately $3.7 million, or 5.5%, to $71.0 million from $67.3 million for the prior year's corresponding period. The overall increase in SG&A is the result of increased payroll, incentive compensation and related taxes and 401(k) expenses primarily due to increased headcount. The remaining increase in SG&A expense for the third quarter of 2019, is a result of the increase in sales. The third quarter 2019 expense decreased 14 basis points to 21.7% from 21.8% for the prior year's corresponding period primarily as a result of the fixed cost leverage nature of SG&A.

OPERATING INCOME. Operating income for the third quarter of 2019 increased by $4.9 million to $21.7 million, from $16.8 million in the prior year's corresponding period. This increase in operating income is primarily related to the increase in sales discussed above.

INTEREST EXPENSE. Interest expense for the third quarter of 2019 increased $0.2 million compared with the prior year's corresponding period .

INCOME TAXES. Our effective tax rate from continuing operations was a tax expense of 21.5% for the three months ended September 30, 2019 compared to a tax expense of 29.8% for the three months ended September 30, 2018. Compared to the U.S. statutory rate for the three months ended September 30, 2019, the effective tax rate was increased by state taxes, foreign taxes, and nondeductible expenses. The effective tax rate was decreased by research and development tax credits, other tax credits, and a favorable statutory rate change in a foreign jurisdiction.

Compared to the U.S. statutory rate for the three months ended September 30, 2018, the effective tax rate was increased by state taxes, foreign taxes and nondeductible expenses. The effective tax rate was decreased by research and development tax credits and other tax credits.

	Nine Months Ended September 30,			
	2019	%	2018	%
Sales	$ 971,721	100.0%	$ 905,191	100.0 %
Cost of sales	702,830	72.3%	659,560	72.9 %
Gross profit	$ 268,891	27.7%	$ 245,631	27.1 %
Selling, general and administrative expenses	209,511	21.6%	197,609	21.8 %
Income from operations	$ 59,380	6.1%	$ 48,022	5.3 %
Other (income) expense, net	127	—%	(1,318)	(0.1)%
Interest expense	14,911	1.5%	15,959	1.8 %
Income before income taxes	$ 44,342	4.6%	$ 33,381	3.7 %
Provision for income taxes (benefit)	10,655	1.1%	8,962	1.0 %
Net income	$ 33,687	3.5%	$ 24,419	2.7 %
Net loss attributable to noncontrolling interest	(172)	—	(91)	—
Net income attributable to DXP Enterprises, Inc.	$ 33,859	3.5%	$ 24,510	2.7 %
Per share amounts attributable to DXP Enterprises, Inc.				
Basic earnings per share	$ 1.92		$ 1.39	
Diluted earnings per share	$ 1.84		$ 1.33	

Nine Months Ended September 30, 2019 compared to Nine Months Ended September 30, 2018

SALES. Sales for the nine months ended September 30, 2019 increased $66.5 million, or 7.3%, to approximately $971.7 million from $905.2 million for the prior year's corresponding period. This sales increase is the result of an increase in our SCS, SC and IPS segments of $24.0 million, $23.2 million and $19.4 million, respectively. The fluctuations in sales is further explained in our business segment discussions below.

	Nine Months Ended September 30,			
	2019	2018	Change	Change%
Sales by Business Segment	*(in thousands, except change%)*			
Service Centers	579,884	556,700	$ 23,184	4.2%
Innovative Pumping Solutions	237,920	218,561	19,359	8.9%
Supply Chain Services	153,917	129,930	23,987	18.5%
Total DXP Sales	$ 971,721	$ 905,191	$ 66,530	7.3%

Service Centers segment. Sales for the Service Centers segment increased by $23.2 million, or 4.2% for the nine months ended September 30, 2019 compared to the prior year's corresponding period. This sales increase is primarily the result of increased sales of rotating equipment and metal working products to customers engaged in the late upstream, midstream or downstream oil and gas markets or manufacturing equipment for these markets in connection with increased capital spending by oil and gas producers. If the U.S. crude oil production remain at levels experienced during the first nine months of 2019, this level of sales to the oil and gas industry might continue, or improve, during the remainder of 2019.

Supply Chain Services segment. Sales for the SCS segment increased by $24.0 million, or 18.5%, for the nine months ended September 30, 2019, compared to the prior year's corresponding period. The improved sales are primarily related to increased sales to customers in the medical device, aerospace, oil and gas and food and beverage industries as a result of new locations.

Innovative Pumping Solutions segment. Sales for the IPS segment increased by $19.4 million, or 8.9% for the nine months ended September 30, 2019 compared to the prior year's corresponding period. This increase was primarily the result of an increase in the capital spending by oil and gas producers and related businesses stemming from an increase in U.S. crude oil production. This level of IPS sales might continue, or improve, during the remainder of 2019, if the U.S. crude oil production remains at levels experienced during the first nine months of 2019.

GROSS PROFIT. Gross profit as a percentage of sales for the nine months ended September 30, 2019 increased by approximately 54 basis points from the prior year's corresponding period. The increase in the gross profit percentage is primarily the result of an approximate 266 basis point increase in the gross profit percentage in our IPS segment and 17 basis point increase in the gross profit percentage in our SC segment partially offset by 65 basis point decrease in the gross profit percentage in our SCS segment. Gross profit for the IPS segment increased as a result of an increase in the capital spending by oil and gas producers and related businesses stemming from an increase in the U.S. crude oil production during the first nine months of 2019.

Innovative Pumping Solutions segment. As a percentage of sales, the nine month period gross profit percentage for the IPS segment increased approximately 266 basis points from the prior year's corresponding period primarily as a result of an increase in utilization and capacity within IPS' engineered-to-order business and an overall improvement in the pricing environment driven by an increase in capital spending by oil and gas producers. Additionally, gross profit margins for individual orders have continued to improve because of the increase in sales of built to order customer specific products. Operating income for the IPS segment increased $4.8 million or 20.0%, primarily as a result of the above mentioned increase in sales.

Service Centers segment. As a percentage of sales, the nine month period gross profit percentage for the Service Centers increased approximately 17 basis points from the prior year's corresponding period. This was primarily as a result of sales mix and price increases from vendors. Operating income for the Service Centers segment increased $8.9 million, or 15.3%. The increase in operating income is primarily the result of the improved sales.

Supply Chain Services segment. Gross profit as a percentage of sales decreased approximately 65 basis points, compared to the prior year's corresponding period. This was primarily as a result of costs associated with new customer implementation. Operating income for the nine month period of 2019 decreased $1.2 million compared to the prior year's corresponding period mainly due to an increase in SG&A expense of $5.7 million primarily related to payroll and incentive compensation offset by an increase in gross profit of $4.5 million.

SELLING, GENERAL AND ADMINISTRATIVE ("SG&A"). Selling, general and administrative expense for the nine months ended September 30, 2019 increased by approximately $11.9 million, or 6.0%, to $209.5 million from $197.6 million for the prior year's corresponding period. The overall increase in SG&A is the result of increased payroll, incentive compensation and related taxes and 401(k) expenses primarily due to increased headcount. The remaining increase in SG&A expense for the nine month period of 2019, is a result of the increase in sales. The nine month period 2019 expense decreased 27 basis points to 21.6% from 21.8% for the prior year's corresponding period primarily as a result of the fixed cost leverage nature of SG&A.

OPERATING INCOME. Operating income for the nine months ended September 30, 2019 increased by $11.4 million, or 23.7%, to $59.4 million, from $48.0 million in the prior year's corresponding period. This increase in operating income is primarily related to the increase in sales discussed above.

INTEREST EXPENSE. Interest expense for the nine months ended September 30, 2019 decreased $1.0 million mainly due to third party fees of $0.9 million and $60 thousand of accelerated deferred debt issuance cost in connection with the Repricing Amendment in June 2018.

INCOME TAXES. Our effective tax rate from continuing operations was a tax expense of 24.0% for the nine months ended September 30, 2019 compared to a tax expense of 26.9% for the nine months ended September 30, 2018. Compared to the U.S. statutory rate for the nine months ended September 30, 2019, the effective tax rate was increased by state taxes, foreign taxes and nondeductible expenses partially offset by research and development tax credits, other tax credits, and a favorable statutory tax rate change in a foreign jurisdiction.

Compared to the U.S. statutory rate for the nine months ended September 30, 2018, the effective tax rate was increased by state taxes, foreign taxes, and nondeductible expenses. The effective tax rate was decreased by research and development tax credits and other tax credits.

LIQUIDITY AND CAPITAL RESOURCES

General Overview

As of September 30, 2019, we had cash and cash equivalents of $28.6 million and bank and other borrowings of $238.1 million. We have an $85 million Asset-Based loan facility that is due to mature in August 2022, under which we had no borrowing outstanding as of September 30, 2019.

Our primary source of capital is cash flow from operations, supplemented as necessary by bank borrowings or other sources of financing. As a distributor of MRO products and services and fabricator of custom pumps and packages, working capital can fluctuate as a result of changes in inventory levels, accounts receivable and costs in excess of billings for project work. Additional cash is required for capital items for information technology, warehouse equipment, leasehold improvements, pump manufacturing equipment and safety services equipment. We also require cash to pay our lease obligations and to service our debt.

The following table summarizes our net cash flows used in operating activities, net cash used in investing activities and net cash used in financing activities for the periods presented *(in thousands)*:

	Nine Months Ended September 30,	
	2019	2018
Net Cash Provided by (Used in):		
Operating Activities	$ 7,485	$ 9,842
Investing Activities	(14,212)	(15,971)
Financing Activities	(5,444)	(2,994)
Effect of Foreign Currency	213	(66)
Net Change in Cash	$ (11,958)	$ (9,189)

Operating Activities

The Company generated $7.5 million of cash in operating activities during the nine months ended September 30, 2019 compared to generating $9.8 million of cash during the prior year's corresponding period. The $2.4 million decrease in the amount of cash generated between the two periods was primarily driven by the timing of payments associated with trade accounts payable and inventory purchases.

Investing Activities

For the nine months ended September 30, 2019, net cash used in investing activities was $14.2 million compared to $16.0 million in the corresponding period in 2018. This $1.7 million decrease was primarily driven by the purchase of ASI in 2018 partially offset by investing in capital equipment and leasehold improvements. For the nine months ended September 30, 2019, purchases of property and equipment was approximately $14.2 million.

Financing Activities

For the nine months ended September 30, 2019, net cash used in financing activities was $5.4 million, compared to net cash used in financing activities of $3.0 million for the corresponding period in 2018. The activity in the period was primarily attributed to the payment of contingent consideration of $1.4 million associated with the purchase of ASI and the payment of $1.3 million to repay an outstanding promissory note.

During the nine months ended September 30, 2019, the amount available to be borrowed under our credit facility increased to $81.0 million compared to $79.3 million at December 31, 2018. This was the result of $4.0 million in letters of credit outstanding as of September 30, 2019 compared to $5.7 million in letters of credit outstanding as of December 31, 2018.

We believe this is adequate funding to support working capital needs within the business.

Funding Commitments

We intend to pursue additional acquisition targets, but the timing, size or success of any acquisition effort and the related potential capital commitments cannot be determined with certainty. We continue to expect to fund future acquisitions primarily with cash flows from operations and borrowings, including the undrawn portion of the credit facility or new debt issuances, but may also issue additional equity either directly or in connection with acquisitions. There can be no assurance that additional financing for acquisitions will be available at terms acceptable to us.

We believe our cash generated from operations will meet our normal working capital needs during the next twelve months. However, we may require additional debt outside of our credit facilities or equity financing to fund potential acquisitions. Such additional financings may include additional bank debt or the public or private sale of debt or equity securities. In connection with any such financing, we may issue securities that substantially dilute the interests of our shareholders.

DISCUSSION OF SIGNIFICANT ACCOUNTING AND BUSINESS POLICIES

Critical accounting and business policies are those that are both most important to the portrayal of a company's financial position and results of operations, and require management's subjective or complex judgments. These policies have been discussed with the Audit Committee of the Board of Directors of DXP.

The Company's condensed financial statements are prepared in accordance with accounting principles generally accepted in the United States of America ("US GAAP"). The accompanying Condensed Consolidated Financial Statements include the accounts of the Company, its wholly owned subsidiaries and its variable interest entity ("VIE"). The accompanying unaudited Condensed Consolidated Financial Statements have been prepared on substantially the same basis as our annual Consolidated Financial Statements and should be read in conjunction with our annual report on Form 10-K for the year ended December 31, 2018. For a more complete discussion of our significant accounting policies and business practices, refer to the consolidated annual report on Form 10-K filed with the Securities and Exchange Commission on March 8, 2019. The results of operations for the three and nine months ended September 30, 2019 are not necessarily indicative of results expected for the full fiscal year.

RECENT ACCOUNTING PRONOUNCEMENTS

See Note 3 - Recent Accounting Pronouncements to the Condensed Consolidated Financial Statements for information regarding recent accounting pronouncements.

ITEM 3: QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.

For quantitative and qualitative disclosures about market risk, see Item 7A, 'Quantitative and Qualitative Disclosures About Market Risk,' of our annual report on Form 10-K for the year ended December 31, 2018. Our exposures to market risk have not changed materially since December 31, 2018.

ITEM 4: CONTROLS AND PROCEDURES.

Disclosure Controls and Procedures

We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed by us in reports we file or submit under the Securities Exchange Act of 1934 is reported, processed, and summarized within the time periods specified in the SEC’s rules and forms. As of September 30, 2019, our management, with the participation of our Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities and Exchange Act of 1934). Based upon that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that, as a result of the material weakness in internal control over financial reporting previously disclosed in our Annual Report on Form 10-K for the year ended December 31, 2018, and as described below, our disclosure controls and procedures were not effective as of September 30, 2019.

Previously Reported Material Weakness

As reported in Item 9A of our Annual Report on Form 10-K for the year ended December 31, 2018, our management concluded that our internal control over financial reporting was not effective as of that date because of a material weakness in our internal controls over financial reporting. We concluded that we had material weaknesses in our control environment and monitoring to support the financial reporting process. We specifically did not maintain effective management review controls over the monitoring and review of certain accounts; and management did not effectively design, document nor monitor (review, evaluate and assess) the key internal control activities that provide the accounting information contained in the Company's consolidated financial statements.

Remediation Plans

We are committed to remediating the material weaknesses and, as such, implemented changes to our internal control over financial reporting. We implemented additional procedures to address the underlying causes of the material weaknesses throughout 2018 and beyond, and continue to implement changes and improvements in our internal control over financial reporting to remediate the control deficiencies that caused the material weaknesses. We believe with full implementation and testing of the design and operating effectiveness of the newly implemented and revised controls, the actions previously described in Item 9A of our Annual Report on Form 10-K for the year ended December 31, 2018 will successfully remediate the material weaknesses in our internal control over financial reporting. Management continues to report regularly to the Audit Committee regarding the status of the implementation activities and progress.

Changes in Internal Control over Financial Reporting

Except as described above, there are no changes in our internal control over financial reporting that occurred during the three and nine months ended September 30, 2019 that materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Inherent Limitations of Internal Controls

Internal control over financial reporting cannot provide absolute assurance of achieving financial reporting objectives because of its inherent limitations. Internal control over financial reporting is a process that involves human diligence and compliance and is subject to lapses in judgment and breakdowns resulting from human failures. Internal control over financial reporting can also be circumvented by collusion or improper management override. Because of such limitations, there is a risk that material misstatements may not be prevented or detected on a timely basis by internal control over financial reporting. However, these inherent limitations are known features of the financial reporting process. Therefore, it is possible to design into the process safeguards to reduce, though not eliminate, this risk.

PART II: OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS.

From time to time, the Company is a party to various legal proceedings arising in the ordinary course of business. While DXP is unable to predict the outcome of these lawsuits, it believes that the ultimate resolution will not have, either individually or in the aggregate, a material adverse effect on DXP's consolidated financial position, cash flows, or results of operations.

ITEM 1A. RISK FACTORS.

No material changes have occurred from risk factors previously disclosed in the Company's Annual Report on Form 10-K for the year ended December 31, 2018.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS.

None.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES.

None

ITEM 4. MINE SAFETY DISCLOSURES.

None.

ITEM 5. OTHER INFORMATION.

None.

ITEM 6. EXHIBITS.

3.1	Restated Articles of Incorporation, as amended (incorporated by reference to Exhibit 4.1 to the Company's Registration Statement on Form S-8 (Reg. No. 333-61953), filed with the Commission on August 20, 1998).
3.2	Bylaws, as amended on July 27, 2011 (incorporated by reference to Exhibit 3.1 to the Company's Quarterly Report on Form 10-Q, filed with the Commission on May 10, 2018.
10.1	DXP Enterprises, Inc. 2016 Omnibus Incentive Plan (incorporated by reference to Exhibit 99.1 to the Company's Registration Statement on Form S-8 (File No. 333-213226), filed with the Commission on August 19, 2016).
10.2	Amendment to the DXP Enterprises, Inc. 2016 Omnibus Incentive Plan, as amended (incorporated by reference to Exhibit 99.2 to the Company's Registration Statement on Form S-8 (File No. 333-233420), filed with the Commission on August 22, 2019).
* 31.1	Certification of Chief Executive Officer pursuant to Rule 13a-14(a) and rule 15d-14(a) of the Securities Exchange Act, as amended.
* 31.2	Certification of Chief Financial Officer pursuant to Rule 13a-14(a) and rule 15d-14(a) of the Securities Exchange Act, as amended.
* 32.1	Certification of Chief Executive Officer pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
* 32.2	Certification of Chief Financial Officer pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101	Interactive Data Files

Exhibits designated by the symbol * are filed or furnished with this Quarterly Report on Form 10-Q. All exhibits not so designated are incorporated by reference to a prior filing with the Commission as indicated.

SIGNATURES

Pursuant to the requirements 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.

DXP ENTERPRISES, INC.
(Registrant)
By: /s/ Kent Yee
Kent Yee
Senior Vice President and Chief Financial Officer
(Duly Authorized Signatory and Principal Financial Officer)

Dated: November 7, 2019

Exhibit 31.1

CERTIFICATION

I, David R. Little, certify that:

1. I have reviewed this report on Form 10-Q of DXP Enterprises, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

    a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

    b. Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, 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;

    c. Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

    d. Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

    a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

    b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

November 7, 2019

/s/ David R. Little
David R. Little
President and Chief Executive Officer
(Principal Executive Officer)

Exhibit 31.2

CERTIFICATION

I, Kent Yee, certify that:

1. I have reviewed this report on Form 10-Q of DXP Enterprises, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

    a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

    b. Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, 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;

    c. Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

    d. Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

    a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

    b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

November 7, 2019

/s/ Kent Yee
Kent Yee
Senior Vice President and Chief Financial Officer
(Principal Financial Officer)

Exhibit 32.1

CERTIFICATION

Pursuant to 18 U.S.C. Section 1350, the undersigned officer of DXP Enterprises, Inc. (the "Company"), hereby certifies that, to my knowledge, the Company's Quarterly Report on Form 10-Q for the quarter ended September 30, 2019 (the "Report") fully complies with the requirements of Section 13(a) or 15(d), as applicable, of the Securities Exchange Act of 1934 and that the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ David R. Little
David R. Little
President and Chief Executive Officer
(Principal Executive Officer)

November 7, 2019

The foregoing certification is being furnished solely pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, and is not being filed as part of the Report or as a separate disclosure document.

Exhibit 32.2

CERTIFICATION

Pursuant to 18 U.S.C. Section 1350, the undersigned officer of DXP Enterprises, Inc. (the "Company"), hereby certifies that, to my knowledge, the Company's Quarterly Report on Form 10-Q for the quarter ended September 30, 2019 (the "Report") fully complies with the requirements of Section 13(a) or 15(d), as applicable, of the Securities Exchange Act of 1934 and that the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ Kent Yee
Kent Yee
Senior Vice President and Chief Financial Officer
(Principal Financial Officer)

November 7, 2019

The foregoing certification is being furnished solely pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, and is not being filed as part of the Report or as a separate disclosure document.