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KINARK CORP
Form 10-Q
August 14, 2001

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SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

QUARTERLY REPORT UNDER SECTION 13 OR 15 (D)
OF THE SECURITIES EXCHANGE ACT OF 1934

FOR QUARTER ENDED JUNE 30, 2001

COMMISSION FILE NO. 1-3920

KINARK CORPORATION

(Exact name of the registrant as specified in its charter)

DELAWARE

(State of Incorporation)

71-0268502

(I.R.S. Employer Identification No.)

2250 EAST 73RD STREET
TULSA, OKLAHOMA 74136-6832

(Address of principal executive offices)

Registrant's telephone number: (918) 494-0964

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 and 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 the number of shares outstanding of each of the issuer's classes of common stock, as of June 30, 2001.

Common Stock \$.10 Par Value 6,712,209

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KINARK CORPORATION AND SUBSIDIARY

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FORWARD LOOKING STATEMENTS OR INFORMATION

Certain statements in this Form 10-Q, including information set forth under the caption "Management's Discussion and Analysis of Financial Condition and Results of Operations", constitute "Forward-Looking Statements" within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. Such statements are typically punctuated by words or phrases such as "anticipates," "estimate," "should," "may," "management believes," and words or phrases of similar import. The Company cautions investors that such forward-looking statements included in this Form 10-Q, or hereafter included in other publicly available documents filed with the Securities and Exchange Commission, reports to the Company's stockholders and other publically available statements issued or released by the Company involve significant risks, uncertainties, and other factors which could cause the Company's actual results, performance (financial or operating) or achievements to differ materially from the future results, performance (financial or operating) or achievements expressed or implied by such forward-looking statements. Factors that could cause or contribute to such differences could include, but are not limited to, changes in demand, prices, and the raw materials cost of steel and zinc; changes in economic conditions of the various markets the Company serves, as well as the other risks detailed herein and in the Company's reports filed with the Securities and Exchange Commission. The Company believes that the important factors set forth in the Company's cautionary statements at Exhibit 99 to this Form 10-Q could cause such a material difference to occur and investors are referred to Exhibit 99 for such cautionary statements.

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INDEPENDENT ACCOUNTANTS' REVIEW REPORT

To the Board of Directors and Stockholders of
Kinark Corporation:

We have reviewed the accompanying condensed consolidated balance sheet of Kinark Corporation and subsidiary (the "Company") as of June 30, 2001, and the related condensed consolidated statements of operations and comprehensive income, and of cash flows for the three and six-month periods ended June 30, 2001 and 2000. These financial statements are the responsibility of the Company's management.

We conducted our reviews in accordance with standards established by the American Institute of Certified Public Accountants. A review of interim financial information consists principally of applying analytical procedures to financial data and of making inquiries of persons responsible for financial and accounting matters. It is substantially less in scope than an audit conducted in accordance with auditing standards generally accepted in the United States of America, the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, we do not express such an opinion.

Based on our reviews, we are not aware of any material modifications that should be made to such condensed consolidated financial statements for them to be in conformity with accounting principles generally accepted in the United States of America.

We have previously audited, in accordance with auditing standards generally accepted in the United States of America, the consolidated balance sheet of Kinark Corporation and subsidiaries as of December 31, 2000, and the related consolidated statements of earnings, stockholders' equity and comprehensive income, and cash flows for the year then ended (not presented herein); and in our report dated February 23, 2001, we expressed an unqualified opinion on those consolidated financial statements. In our opinion, the information set forth in the accompanying condensed consolidated balance sheet as of December 31, 2000 is fairly stated, in all material respects, in relation to the consolidated balance sheet from which it has been derived.

/s/Deloitte & Touche LLP

Tulsa, Oklahoma
August 3, 2001

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KINARK CORPORATION AND SUBSIDIARY
CONDENSED CONSOLIDATED BALANCE SHEETS

(DOLLARS IN THOUSANDS)	Unaudited June 30 2001	Dec 31 2000
	-----	-----
ASSETS		
Current Assets		
Cash and cash equivalents	\$ 889	\$ 57
Trade receivables, net	5,087	5,421
Inventories	5,665	5,953

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Prepaid expenses and other assets	481	200
Deferred tax asset, net	672	605
	-----	-----
TOTAL CURRENT ASSETS	12,794	12,236
	-----	-----
FUNDS HELD BY BOND TRUSTEE	--	1,219
PROPERTY, PLANT AND EQUIPMENT, AT COST		
Land	1,690	1,600
Galvanizing plants and equipment	35,200	25,968
Other	66	66
	-----	-----
	36,956	27,634
Less: Allowance for depreciation	(13,677)	(12,014)
Construction in progress	409	7,581
	-----	-----
TOTAL PROPERTY, PLANT & EQUIPMENT, NET	23,688	23,201
	-----	-----
GOODWILL, NET OF ACCUMULATED AMORTIZATION	3,483	3,577
OTHER ASSETS	501	443
	-----	-----
TOTAL ASSETS	\$ 40,466	\$ 40,676
	=====	=====
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current Liabilities		
Current maturities of long-term obligations	\$ 882	\$ 1,001
Current portion of bonds payable	572	563
Trade accounts payable	1,206	1,241
Accrued payroll and employee benefits	847	823
Other taxes	208	194
Other accrued liabilities	661	775
	-----	-----
TOTAL CURRENT LIABILITIES	4,376	4,597
	-----	-----
DEFERRED TAX LIABILITY, NET	733	732
PENSION AND RELATED LIABILITIES	115	127
LONG-TERM OBLIGATIONS	8,692	9,420
BONDS PAYABLE	8,200	8,487
SUBORDINATED NOTES PAYABLE	907	--
	-----	-----
TOTAL LIABILITIES	23,023	23,363
	-----	-----
COMMITMENTS AND CONTINGENCIES (NOTE 7)	--	--
STOCKHOLDERS' EQUITY		
Common stock	819	819
Additional paid-in capital	17,464	17,364
Accumulated other comprehensive loss	(19)	--
Retained earnings	5,159	5,110
Common shares in treasury at cost	(5,980)	(5,980)
	-----	-----
TOTAL STOCKHOLDERS' EQUITY	17,443	17,313
	-----	-----
TOTAL LIABILITIES & STOCKHOLDERS' EQUITY	\$ 40,466	\$ 40,676
	=====	=====

See notes to condensed consolidated financial statements

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KINARK CORPORATION AND SUBSIDIARY
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
AND COMPREHENSIVE INCOME (Unaudited)

	Three Months Ended June 30	
(DOLLARS IN THOUSANDS EXCEPT PER SHARE AMOUNTS)	2001	2000
	-----	-----
SALES	\$ 9,262	\$ 10,662
Cost of sales	6,627	7,543
Selling, general & administrative expenses	1,274	1,436
Depreciation and amortization	892	710
	-----	-----
TOTAL COSTS AND EXPENSES	8,793	9,689
	-----	-----
OPERATING INCOME BEFORE CASUALTY LOSS	469	973
Casualty loss	--	--
	-----	-----
OPERATING INCOME	469	973
Interest expense, net	347	249
Other expense	118	--
INCOME (LOSS) FROM CONTINUING OPERATIONS BEFORE INCOME TAXES	4	724
Income tax expense (benefit)	2	318
	-----	-----
INCOME (LOSS) FROM CONTINUING OPERATIONS	2	406
Loss from Discontinued Operations, net of income tax benefit	--	(398)
Loss on Disposal of Discontinued Operations	--	(1,663)
	-----	-----
NET INCOME (LOSS)	2	(1,655)
	-----	-----
OTHER COMPREHENSIVE INCOME (LOSS)		
Cash flow hedges:		
Cumulative effect, accounting for derivatives, net of related income taxes of \$48	--	--
Less: reclassification adjustment for derivative losses included in net income, net of related income taxes of \$32	23	--
	-----	-----
OTHER COMPREHENSIVE INCOME (LOSS)	23	--
	-----	-----
COMPREHENSIVE INCOME (LOSS)	25	(1,655)
	=====	=====
NET INCOME (LOSS) PER COMMON SHARE		
Continuing Operations:		
Basic and Diluted	\$ --	\$.06
Discontinued Operations:		
Basic and Diluted	\$ --	\$ (.31)
	-----	-----
Net income (Loss):		

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Basic and Diluted \$ -- \$ (.25)

See notes to condensed consolidated financial statements.

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KINARK CORPORATION AND SUBSIDIARY
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
Unaudited

(DOLLARS IN THOUSANDS)	Six Months Ended June 30	
	2001	2000
OPERATING ACTIVITIES		
Net income (loss)	\$ 49	\$ (1,815)
Loss from discontinued operations	--	2,107
Depreciation and amortization	1,764	1,418
Deferred income taxes	(67)	272
Gain on disposal of assets	(11)	(7)
Change in assets and liabilities:		
Accounts receivable, net	334	(1,604)
Inventories and other assets	30	496
Accounts payable, accrued liabilities and other	(141)	105
	1,958	972
Net cash provided by continuing operations	1,958	972
Net cash used in discontinued operations	--	(1,212)
	1,958	(240)
CASH PROVIDED BY (USED IN) OPERATING ACTIVITIES		
INVESTING ACTIVITIES		
Net proceeds from sale of discontinued operations	--	371
Capital expenditures	(2,149)	(3,531)
Proceeds from sale of assets	3	9
	(2,146)	(3,151)
Net cash used in continuing operations	(2,146)	(3,151)
Net cash used in discontinued operations	--	(254)
	(2,146)	(3,405)
CASH USED IN INVESTING ACTIVITIES		
FINANCING ACTIVITIES		
Proceeds from subordinated debt	900	--
Proceeds from stock warrants	100	--
Proceeds from tax exempt bonds	--	9,050
Tax exempt bond funds held by bond trustee	1,219	(5,945)
Deferred financing costs	(76)	--
Proceeds from long-term obligations	10,124	8,060
Payments on long-term obligations	(10,969)	(7,718)
Repayment on bonds	(278)	--
	1,020	3,447
Net cash provided by continuing operations	1,020	3,447
Net cash used in discontinued operations	--	(5)
	1,020	3,442
CASH PROVIDED BY FINANCING ACTIVITIES		
INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	832	(203)
CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD	57	253

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CASH AND CASH EQUIVALENTS AT END OF PERIOD	----- \$ 889 =====	----- \$ 50 =====
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See notes to condensed consolidated financial statements.

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KINARK CORPORATION AND SUBSIDIARY
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
FOR THE THREE AND SIX MONTHS ENDED JUNE 30, 2001 AND 2000
UNAUDITED

NOTE 1. BASIS OF PRESENTATION

The condensed consolidated financial statements included in this report have been prepared by Kinark Corporation (the "Company") pursuant to the rules and regulations of the Securities and Exchange Commission for interim reporting and include all normal and recurring adjustments which are, in the opinion of management, necessary for a fair presentation. These financial statements have not been audited by an independent accountant. The condensed consolidated financial statements include the accounts of the Company and its subsidiary.

Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted pursuant to such rules and regulations for interim reporting. The Company believes that the disclosures are adequate to make the information presented not misleading. However, these financial statements should be read in conjunction with the financial statements and notes thereto included in the Company's Annual Report on Form 10-K, for the year ended December 31, 2000. The financial data for the interim periods presented may not necessarily reflect the results to be anticipated for the complete year.

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the balance sheet dates and the reported amounts of revenues and expenses for each of the years. Actual results will be determined based on the outcome of future events and could differ from the estimates.

During the third quarter of 2000, the Company's galvanizing subsidiary, North American Galvanizing Company ("NAG"), negotiated a new galvanizing contract with its largest customer. Under terms of the new one-year contract, NAG no longer provides additional services that previously included procurement and fabrication of steel products prior to galvanizing. In the first half of 2001 and 2000, sales to this customer accounted for approximately 3.8% and 15.6% of NAG's total sales, respectively.

NOTE 2. CHANGE IN ACCOUNTING PRINCIPLE

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On January 1, 2001 the Company adopted Statement of Financial Accounting Standards No. 133, "Accounting for Derivative Instruments and Hedging Activities" ("SFAS No. 133"). The statement, as amended, establishes accounting and reporting standards for derivative instruments and for hedging activities. It requires that an entity recognize all derivatives, at fair value, as either assets or liabilities in the balance sheet with an offset either to shareholder's equity and comprehensive income or income depending upon the

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classification of the derivative. The derivative instruments identified at January 1, 2001, under the provisions of SFAS No. 133 had been previously designated in hedging relationships that addressed the variable cash flow exposure of forecasted purchases of zinc; under the transition provisions of SFAS No. 133, on January 1, 2001 the Company recorded an after-tax, cumulative-effect-type transition charge of \$65,000 to accumulated other comprehensive income related to these derivatives. The Company did not elect subsequent hedge accounting for the derivative existing at January 1, 2001. Accordingly, all changes in the fair value of that derivative are recorded in income.

NOTE 3. EARNINGS PER COMMON SHARE

Basic earnings per common share for the periods presented is computed based upon the weighted average number of shares outstanding. Diluted earnings per common share for the periods presented is based on the weighted average shares outstanding, adjusted for the assumed exercise of stock options and warrants using the treasury stock method.

	Number of Shares	
	2001	2000
Three Months Ended June 30		
Basic	6,712,209	6,712,211
Diluted	7,386,583	6,712,211
Six Months Ended June 30		
Basic	6,712,209	6,712,215
Diluted	7,378,875	6,715,215

Substantially all of the Company's outstanding stock options have no dilutive effect on the calculation of earnings due to the option price being higher than the share value. The number of options excluded from the calculation of diluted earnings per share are 339,625 and 380,500 at June 30, 2001 and 2000, respectively.

NOTE 4. INVENTORIES

Inventories consist primarily of raw zinc "pigs," molten zinc in

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galvanizing kettles and other chemicals and materials used in the hot dip galvanizing process. Inventories are stated at the lower of cost or market with market value based on ultimate realizable value from the galvanizing process. Zinc cost is determined on a last-in-first-out (LIFO) basis. Other inventories are valued primarily on an average cost basis.

NOTE 5.

BONDS PAYABLE

During the first quarter of 2000, the Company issued \$9,050,000 of Harris County Industrial Development Corporation Adjustable Rate Industrial Development Bonds, Series 2000 (the "Bonds"). The Bonds are senior to other debt of the Company. Bond proceeds were used by NAG for the purchase of land and construction of a hot dip

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galvanizing plant in Harris County, Texas, which became operational during the first quarter of 2001.

The Bonds bear interest at a variable rate (5.25% at June 30, 2001) that can be converted to a fixed rate upon certain conditions outlined in the bond agreement. The Bonds are subject to annual sinking fund redemption of \$230,000 commencing on June 15, 2001, which increases annually thereafter to a maximum redemption of \$960,000 on June 15, 2012. Beginning January 2001, the Company began making monthly amortization payments of principal and interest of \$86,000 into a sinking fund. The final maturity date of the Bonds is June 15, 2013. The Company has the option of early redemption of the Bonds at par unless the bonds are converted to a fixed interest rate, in which case they are redeemable at a premium during a period specified in the bond agreement. The Company's obligation under the bond agreement is secured through a letter of credit with a bank which must remain in effect as long as any Bonds are outstanding. The letter of credit is collateralized by substantially all the assets of the Company.

NOTE 6.

SUBORDINATED DEBT

In February 2001, the Company completed a \$1,000,000 Private Placement of subordinated debt with stock warrants to purchase 666,666 shares of common stock of the Company. \$100,000 of the proceeds has been allocated to the stock warrants. The Company plans to use these proceeds for general working capital and construction of a new galvanizing plant in St. Louis. Participation in the Private Placement was offered to the Company's directors and eligible stockholders holding a minimum of 100,000 shares of common stock. The notes mature February 17, 2006 and bear interest at 10% payable annually. Terms of the warrants, which expire February 17, 2008, permit the holder to purchase shares of the Company's common stock at any time prior to the Expiration Date, for cash at an Exercise Price of \$.856 per share (fair value at date of issuance) or by surrender of shares of the Company's common stock with a fair market value equal to the aggregate Exercise Price. As of June 30, 2001 no warrants had been exercised.

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NOTE 7.

LONG-TERM OBLIGATIONS

(Dollars in Thousands)	June 30 2001	December 31 2000
Revolving lines of credit	\$ 5,473	\$ 6,666
Term loan	4,052	3,407
10.0% note due 2001	---	289
9.5% note due 2015	22	23
Capital leases	27	36
	9,574	10,421
Less current portion	882	1,001
	\$ 8,692	\$ 9,420

Kinark has a credit agreement with a domestic bank which provides an original term loan of \$4,200,000 and a maximum line of credit of \$9,000,000 for working capital and

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general corporate purposes. The expiration date of this agreement is September 2002. Interest rates on borrowings are based upon current bank prime rate or, at the option of the Company, upon the London Interbank Offered Rate, subject to a rate margin adjustment determined by the Company's consolidated debt service ratio.

Substantially all of the Company's accounts receivable, inventories, fixed assets and the stock of its subsidiary, North American Galvanizing Company are pledged as collateral under the agreement, and the agreement is secured by a guaranty from this subsidiary. The credit agreement requires the Company to maintain compliance with covenant limits for current ratio, debt to tangible net worth ratio, debt service coverage ratio and capital expenditures ratio. The Company was in compliance with such covenants at June 30, 2001.

During the second quarter of 2001, the Company amended and increased the bank Term Loan \$1,016,000 to \$3,980,584. Proceeds were used to pay an existing promissory note of \$266,000 and to pay down the Company's revolving line of credit in the amount of \$750,000. Term loan payments are based on a three-year amortization schedule with equal monthly payments of principal and interest, and the loan may be prepaid without penalty. The revolving line of credit may be paid down without penalty, or additional funds may be borrowed up to the maximum line of credit.

At June 30, 2001, \$9,525,000 was outstanding under the agreement, and \$275,000 was reserved for outstanding irrevocable letters of credit for workers' compensation insurance coverage. At June 30, 2001, the Company had additional borrowing capacity of \$401,000, net of outstanding letters of credit, under its revolving line of credit that reflected the underlying value of its accounts receivables and inventories.

NOTE 8.

COMMITMENTS AND CONTINGENCIES

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The Company has commitments with domestic and foreign zinc producers to purchase zinc used in its hot dip galvanizing operations. The terms of the commitments do not exceed twelve months. Commitments for the future delivery of zinc reflect rates quoted on the London Metals Exchange and are not subject to price adjustment. At June 30, 2001, the aggregate commitments for the procurement of zinc at fixed prices were \$6,742,000 and unpriced commitments for the purchase of zinc represented approximately 334 tons.

The Company utilizes derivative instruments, from time-to-time, which are intended to offset the impact of potential fluctuations in the market price of zinc. At June 30, 2001, commodity collar contracts with a bank were in place for a notional quantity of 400,000 pounds of zinc per month, representing a nominal percentage of NAG's projected zinc usage for the balance of 2001. These contracts contain a cap and floor price for a notional quantity of zinc, and they are cash settled each month based on the average of the daily closing price of zinc on the London Metal Exchange. For each potential decrease of \$.01 per pound in the market price of zinc below the contractual floor price, the Company will incur a cash settlement cost of \$4,000 per month. The Company has elected not to account for these instruments as hedges and changes in their market value

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and the monthly cash settlement amounts are recorded in other expense. The contracts expire in August and September 2001. The fair value of the commodity collar contracts in place at June 30, 2001 was a loss of \$139,000. The Company expects to continue evaluating derivative instruments to minimize the impact of zinc price fluctuations, as part of its inventory management strategy.

NAG was notified in 1997 by the Illinois Environmental Protection Agency ("IEPA") that it was one of a number of potentially responsible parties under the Comprehensive Environmental Response, Compensation, and Liability Information System ("CERCLIS") in connection with cleanup of an abandoned site formerly owned by Sandoval Zinc Co. ("Sandoval"). NAG arranged for the treatment and disposal of hazardous substances at Sandoval in the ordinary course of its business. Based on current information and the stage of investigation, NAG's share of any probable future costs cannot be estimated at this time.

The Company expects it will continue to have environmental compliance costs in the future associated with operations in the galvanizing business. The Company is committed to complying with the environmental legislation and regulations affecting its operations. Due to the uncertainties associated with future environmental technologies, regulatory interpretations, and prospective legislative activity, management cannot quantify potential costs in this area.

The Company expenses or capitalizes, where appropriate, environmental expenditures that relate to current operations as they are incurred. Such expenditures are expensed when they are

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attributable to past operations and are not expected to contribute to current or future revenue generation. The Company records liabilities when remediation or other environmental assessment or clean-up efforts are probable and the cost can be reasonably estimated.

Various litigation arising in the ordinary course of business is pending against the Company.

Management believes that resolution of the Company's litigation and environmental matters should not materially affect the Company's consolidated financial position or liquidity. Should future developments cause the Company to record an additional liability for environmental matters, litigation or customer claims, the recording of such a liability could have a material impact on the results of operations for the period involved.

NOTE 9. LABOR AGREEMENT

On April 1, 2001, NAG concluded negotiations of a one-year labor agreement with the United Steel Workers Union covering approximately 70 production workers at its Tulsa galvanizing plants. The new agreement is not materially changed from the previous agreement which expired March 31, 2001.

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NOTE 10. DISCONTINUED OPERATIONS

In the second quarter of 2000, the Company sold its Lake River Corporation ("Lake River") and North American Warehousing Company ("NAW") subsidiaries, comprising the Company's bulk liquids terminal and public warehousing businesses. Accordingly, second quarter and six-month 2000 operating results for the Lake River and NAW segments were accounted for as discontinued operations, and amounts in the financial statements and related notes for all periods shown have been restated to reflect discontinued operations accounting.

NOTE 11. SEGMENT DISCLOSURES

Subsequent to the sale of Lake River and NAW, the Company's sole business is hot dip galvanizing and coatings which is conducted through its wholly owned subsidiary, North American Galvanizing Company.

NOTE 12. NEW ACCOUNTING STANDARDS

In July 2001, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards No. 141, Business Combinations ("SFAS No. 141") which addresses financial accounting and reporting for business combinations and requires that all business combinations initiated after June 30, 2001 be accounted for under the purchase method. Use of the pooling of interests method is no longer permitted.

In July 2001, the FASB issued Statement of Financial Accounting

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Standards No. 142, "Goodwill and Other Intangible Assets" ("SFAS No. 142") which is fully effective in fiscal years beginning after December 15, 2001, although certain provisions of SFAS No. 142 are applicable to goodwill and other intangible assets acquired in transactions completed after June 30, 2001. SFAS No. 142 addresses financial accounting and reporting for acquired goodwill and other intangible assets and requires that goodwill no longer be amortized but instead be periodically reviewed for impairment. This standard had no impact on second quarter 2001 results and the Company is in the process of evaluating the effect of this standard on its financial reporting.

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KINARK CORPORATION AND SUBSIDIARY MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Kinark Corporation's (the "Company") sole line of business is hot dip galvanizing and coatings, which is conducted through its wholly-owned subsidiary, North American Galvanizing Company.

In 2000, Kinark exited the chemical storage and warehousing business with the sale of its wholly-owned subsidiaries, Lake River Corporation ("Lake River") and North American Warehousing Company ("NAW"). As a result, these subsidiaries have been classified as discontinued operations for accounting purposes and their revenues and expenses are not included in the results of continuing operations analyzed below. These subsidiaries accounted for approximately 15% and 19% of the Company's consolidated sales in the second quarter and first six months of 2000, respectively.

During the third quarter of 2000, NAG discontinued steel fabrication which had been provided as a specialty service for its largest customer. Sales to this customer were 3.1% and 17.7% of NAG's total sales in the second quarter of 2001 and 2000 and 3.8% and 15.6% in the first six months of 2001 and 2000, respectively for both periods. The Company no longer provides steel fabrication services and has no plans to resume such services in the future.

During the second quarter ended June 30, 2001, the Company completed a reorganization of corporate structure and personnel in NAG that is expected to result in annual savings of approximately \$350,000.

RESULTS OF OPERATIONS

REVENUES

Quarter Ended June 30	2001		2000	
	----		----	
Galvanizing	\$ 9,262	100.0%	\$ 9,215	86.4%
Steel Fabrication	---	---	1,447	13.6%
	-----	-----	-----	-----
Total	\$ 9,262	100.0%	\$10,662	100.0%
Six Months Ended June 30	2001		2000	
	----		----	
Galvanizing	\$18,244	100.0%	\$17,454	87.9%
Steel Fabrication	---	---	2,410	12.1%
	-----	-----	-----	-----
Total	\$18,244	100.0%	\$19,864	100.0%

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Galvanizing sales for the second quarter of 2001 increased 3.1% to \$9,262,000 from sales of \$8,982,000 for the first quarter of 2001. Despite signs of slowing activity in a number of market sectors, NAG's galvanizing tonnage increased 1.4% in the second quarter of 2001 over the record level produced in the first quarter of this year. Significantly, NAG's average selling prices continued to strengthen during the second quarter of 2001, reflecting the Company's commitment to provide improved service and value to its customers: large and small end-users of galvanized structural steel fabrications.

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Operating income for the second quarter of 2001 was \$469,000 compared to \$450,000 for the first quarter of 2001. Gross profit margin on sales of 28.4% for the second quarter of 2001 included full absorption of startup costs associated with NAG's newest galvanizing facility commissioned in February 2001 and compared to a gross profit margin of 29.4% in the first quarter of 2001.

Galvanizing sales for the second quarter and first half of 2001 exceeded sales for the comparable periods in 2000, excluding revenues from steel fabrication. Galvanizing sales in the second quarter of 2001 increased approximately 1% to \$9,262,000, compared to sales of \$9,215,000 in the same period a year ago. For the six months ended June 30, 2001, galvanizing sales increased 4.5% to \$18,244,000 versus sales of \$17,454,000 a year ago. Operating income for the second quarter of 2001 was \$469,000 compared to \$973,000 for the second quarter of 2000. The decrease in operating income for the second quarter of 2001 compared to the second quarter of 2000 was due primarily to the NAG's decision to discontinue metal fabrication service, slightly lower average selling prices for galvanizing and increased depreciation for the new galvanizing plant. For the six-month period ended June 30, 2001, operating income was \$919,000 compared to \$981,000 for the first half of 2000. In the first quarter of 2000, NAG recorded a casualty loss of \$313,000 for the expenses associated with a kettle failure.

Depreciation and amortization of goodwill for the second quarter and first six months of 2001 was \$892,000 and \$1,764,000, respectively, compared to \$710,000 and \$1,419,000 for the respective periods of 2000. The increase is attributable to the addition of NAG's new galvanizing facility and capital expenditures and improvements made in 2000.

Selling, general and administrative expenses ("SG&A") were lower for all periods of 2001 compared to 2000, with reductions in this area reflecting the Company's restructuring programs and, in general, efforts to control expenses. SG&A for the second quarter of 2001 was \$1,274,000 compared to \$1,436,000 for the same quarter a year ago. For the six months ended June 30, 2001, SG&A decreased \$297,000, or 10.1% to \$2,589,000 from \$2,886,000 in the comparable period a year ago.

Net interest expense increased \$98,000 to \$347,000 for the second quarter of 2001 and increased \$154,000 to \$615,000 for the first six months of 2001, over the comparable periods of 2000 primarily due to the added interest expense of the Company's 5.25% industrial revenue bonds that was capitalized in 2000 during construction of the new galvanizing facility. The Company incurred other expense of \$219,000 for the six months ended June 30, 2001 due to changes in the fair value of derivative instruments intended to offset the impact of fluctuations in the market price of zinc used in the galvanizing process. The Company's effective income tax rate for the three and six-month periods ended June 30, 2001 was 42% compared to 43.9% for the same periods of 2000. These rates were higher than federal statutory rates primarily due to non-deductible amortization of goodwill and state income taxes.

Income from continuing operations before income taxes was \$4,000 for the

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second quarter of 2001 compared with income of \$724,000 in the second quarter of 2000. For the six months ended June 30, 2001, income from continuing operations before income taxes was \$85,000 compared with income of \$520,000 in the same period a year ago. For the second quarter of 2001, the Company reported net income from continuing operations of \$2,000, \$0.0 per share, compared to net income of \$406,000, or \$.06 per share, for the second quarter of 2000. Net income from continuing operations of \$49,000, or \$.01 per share, for the six-month period ended June 30, 2001 compared to net income of \$292,000, or \$.04 per share, for the same period in 2000.

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LIQUIDITY AND CAPITAL RESOURCES

For the first half of 2001, the Company's continuing operating activities generated cash of \$1,958,000 compared to cash generated of \$972,000 in the first half of 2000. The increase in cash generated by 2001 operating activities over the same period a year ago is due primarily to a reduction in inventory and improved collections of accounts receivable. During the first half of 2001, the Company improved turn-over of trade accounts and reduced accounts receivables \$334,000; inventories were reduced \$288,000 as zinc raw material stock was realigned to support current production. In addition, during the first half of 2001, accounts payable, accrued liabilities and current debt obligations payable within one year decreased \$221,000.

Capital expenditures in the first half of 2001 were \$2,149,000, of which \$1,546,000 was for the new galvanizing facility in Houston. The company's financing activities in the first half of 2001 included making payments of \$10,969,000 on long-term obligations, payments of \$278,000 on tax exempt bonds and receiving proceeds of \$10,124,000 from utilization of the line of credit, for a net decrease of \$1,123,000 in long-term obligations. In March 2000, the Company obtained \$9,050,000 from the issuance of tax-exempt industrial revenue bonds, the proceeds of which were used for the construction of a new galvanizing facility in Houston, Texas. In February 2001, the Company issued \$1,000,000 of subordinated debt, the proceeds of which are expected to be utilized for construction of a new galvanizing facility in St. Louis, Missouri. In June 2001, the Company increased the bank term loan \$1,016,000, the proceeds of which were used to pay down the line of credit and payoff a promissory note. The Company's current credit facility includes a maximum \$9,000,000 revolving line of credit under a credit agreement that expires September 2002. The Company's availability under the revolver was \$401,000 at June 30, 2001. The Company believes it has the ability to generate cash and/or available credit facilities to meet its foreseeable needs for working capital planned capital expenditures.

ENVIRONMENTAL MATTERS AND OTHER CONTINGENCIES

As previously reported, NAG was notified in 1997 by the Illinois Environmental Protection Agency ("IEPA") that it was a potentially responsible party under the Comprehensive Environmental Response, Compensation, and Liability Information System (CERCLIS) in connection with cleanup of an abandoned site formerly owned by Sandoval Zinc Co. The IEPA notice includes NAG as one of 59 organizations which arranged for the treatment and disposal of hazardous substances at Sandoval. Based on current information and the preliminary stage of investigation, NAG's share of any probable future costs cannot be estimated at this time.

During 2000, NAG resolved an insurance claim arising from the failure of a galvanizing kettle during 1999. A major part of the claim resulted from additional costs incurred to galvanize product at an alternate NAG location in order to meet delivery commitments. NAG recorded a casualty loss of \$313,000 during the first quarter of 2000, primarily representing costs incurred during

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that period to transport product to an alternative galvanizing location.

The Company's facilities are subject to extensive environmental legislation and regulations affecting their operations and the discharge of wastes. The cost of compliance with such regulations

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was approximately \$481,000 in the first six months of 2001 and \$524,000 for the same period in 2000, for the disposal and recycling of waste acids generated by the galvanizing operations.

The Company is committed to complying with all federal, state and local environmental laws and regulations and using its best management practices to anticipate and satisfy future requirements. As is typical in the galvanizing and chemicals businesses, the Company will have additional environmental compliance costs associated with past, present, and future operations. Management has committed resources to discovering and eliminating environmental issues as they arise. Because of the frequent changes in environmental technology, laws and regulations management cannot reasonably attempt to quantify the Company's potential costs in this area.

DISCONTINUED OPERATIONS

During the second quarter of 2000, the Company elected to sell its Lake River and NAW subsidiaries, comprising the Company's bulk liquids terminal and public warehousing businesses.

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QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Kinark's current operations include managing market risks related to changes in interest rates and zinc commodity prices.

INTEREST RATE RISK. Kinark is exposed to financial market risk related to changing interest rates. Changing interest rates will affect interest paid on Kinark's variable rate debt. At June 30, 2001, variable rate debt consisting of \$9,525,000 was outstanding under the credit agreement with an effective rate of 6.75% and \$8,772,000 was outstanding under the bond agreement with an effective rate of 5.25% (see Note 5 to Condensed Consolidated Financial Statements). In addition, the Company's fixed rate debt consisting of \$1,000,000 of 10% subordinated promissory notes was outstanding. The borrowings under these facilities are due as follows: \$709,000 in 2001, \$9,689,000 in 2002, \$617,000 in 2003 and \$8,282,000 in years 2004 through 2013. Each increase of 10 basis points in the effective interest rate would result in an annual increase in interest charges on variable rate debt of approximately \$18,300 based on June 30, 2001 outstanding borrowings. The actual effect of changes in interest rates is dependent on actual amounts outstanding which vary under the revolving credit facility. The Company monitors interest rates and has sufficient flexibility to renegotiate the loan agreement, without penalty, in the event market conditions and interest rates change.

ZINC PRICE RISK. NAG enters into purchase commitments with domestic and foreign zinc producers to purchase certain of its zinc requirements for its hot dip galvanizing operations. Commitments for the future delivery of zinc reflect rates quoted on the London Metals Exchange which are not subject to future price adjustment. At June 30, 2001, the aggregate commitments for the procurement of zinc were approximately \$6.7 million. Additional procurement

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commitments of approximately 334 tons were unpriced at June 30, 2001. During the third and fourth quarters of 2000, the Company entered into two one-year commodity collar contracts which are intended to offset the impact of potential fluctuations in the market price of zinc. The contracts are cash settled monthly based on a commodity reference price, determined by the average of the daily closing price of zinc on the London Metal Exchange. At June 30, 2001, the commodity collar contracts were in place on a notional quantity of 400,000 pounds of zinc per month through September 30, 2001. The fair value of the commodity collar contracts in place at this date was an unrealized loss of \$139,000. Depending on zinc price trends, and other factors, the Company may elect to increase its use of zinc derivative instruments from time-to-time. Management believes these procurement commitments and the use of derivative contracts ensure adequate supplies of zinc and may assist in stabilizing income from its galvanizing operations. With respect to the zinc purchase commitments, a potential decrease of 10% in the market price of zinc from the June 30, 2001 level would cause a lost gross margin opportunity of approximately \$670,000. With respect to the zinc commodity collar contract, for each potential decrease of \$.01 per pound in the market price of zinc below the contractual floor price the Company would incur an additional cash settlement of \$4,000 per month.

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PART II

OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

Not applicable.

ITEM 2. CHANGES IN SECURITIES

Not applicable.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

Not applicable.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

The 2001 Annual Meeting of the Company's stockholders was held on Monday, May 14, 2001 in New York City, NY. At the meeting, the stockholders elected eight directors.

The votes for the election of directors were as follows:

	For ---	Withheld -----
Linwood J. Bundy	6,080,127	58,827
Paul R. Chastain	6,075,457	63,497
Ronald J. Evans	6,077,706	61,248
Gilbert L. Klemann, II	6,071,067	67,887

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Patrick J. Lynch	6,070,067	68,887
Joseph J. Morrow	6,074,527	64,427
John H. Sununu	6,073,365	65,589
Mark E. Walker	6,078,527	60,538

ITEM 5. OTHER INFORMATION

Not applicable.

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ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

(a) Exhibits

- 3.1 The Company's Restated Certificate of Incorporation (incorporated by reference to Exhibit 3.1 to the Company's Pre-Effective Amendment No. 1 to Registration Statement on Form S-3 (Reg. No. 333-4937) filed on June 7, 1996).
- 3.2 The Company's Amended and Restated Bylaws (incorporated by reference to Exhibit 3.2 to the Company's Quarterly Report on Form 10-Q dated March 31, 1996).
- 27 Financial Data Schedule
- 99 Cautionary Statements by the Company Related to Forward-Looking Statements

(b) Reports on Form 8-K

The Company did not file a Form 8-K Current Report during the quarter ended June 30, 2001.

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SIGNATURES

Pursuant to the requirements of Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized:

KINARK CORPORATION

Registrant

/S/Paul R. Chastain

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Paul R. Chastain
Vice President and
Chief Financial Officer
(Principal Financial Officer)

Date: August 13, 2001

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