BALCHEM CORP
Form 10-Q
November 09, 2005

FORM 10-Q

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

(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, 2005

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 1-13648

BALCHEM CORPORATION
(Exact name of registrant as specified in its charter)

Maryland	13-2578432
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)
P.O. Box 600 New Hampton, New York	10958
(Address of principal executive offices)	(Zip Code)

845-326-5600
Registrant's telephone number, including area code:

Indicate by a 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 filing requirements for the past 90 days.

Yes |X| No |_|

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act).

Yes |X| No |_|

Indicated by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes |_| No |X|

As of November 8, 2005 the registrant had 7,704,150 shares of its Common Stock, $.06 2/3 par value, outstanding.

Part 1 - Financial Information
Item 1. Financial Statements

BALCHEM CORPORATION
Condensed Consolidated Balance Sheets
(Dollars in thousands, except per share data)
Unaudited

Assets

Current assets:
Cash and cash equivalents
Accounts receivable
Inventories
Prepaid income taxes
Prepaid expenses
Deferred income taxes

Total current assets

Property, plant and equipment, net

Goodwill
Intangible assets with finite lives, net

Total assets

Liabilities and Stockholders' Equity

Current liabilities:
Trade accounts payable
Accrued expenses
Accrued compensation and other benefits
Customer deposits
Dividends payable
Income tax payable

Total current liabilities

Deferred income taxes
Other long-term obligations

Total liabilities

Stockholders' equity:
Preferred stock, $25 par value. Authorized 2,000,000 shares; none issued and outstanding
Common stock, $.0667 par value. Authorized 25,000,000 shares; 7,730,517 shares issued and 7,727,217 outstanding at September 30, 2005 and 7,621,158 shares issued and outstanding at December 31, 2004
Additional paid-in capital
Retained earnings
Treasury stock, at cost: 3,300 and 0 shares at September 30, 2005 and December 31, 2004, respectively

Total stockholders' equity

Total liabilities and stockholders' equity

See accompanying notes to condensed consolidated financial statements

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BALCHEM CORPORATION
Condensed Consolidated Statements of Earnings
(In thousands, except per share data)
(unaudited)

	Three Months Ended September 30, 2005	Three Months Ended September 30, 2004	Nine Month Septemb 2005
Net sales	$ 21,145	$ 17,356	$ 59,969
Cost of sales	13,496	11,137	38,026
Gross profit	7,649	6,219	21,943
Operating expenses:			
Selling expenses	1,200	1,252	3,511
Research and development expenses	492	383	1,537
General and administrative expenses	1,226	1,154	3,854
	2,918	2,789	8,902
Earnings from operations	4,731	3,430	13,041
Other expenses (income):			
Interest (income)	(46)	(22)	(155)
Interest expense	2	61	6
Other, net	(82)	--	(82)
Earnings before income tax expense	4,857	3,391	13,272
Income tax expense	1,833	1,231	4,950
Net earnings	$ 3,024	$ 2,160	$ 8,322
Net earnings per common share - basic	$ 0.39	$ 0.29	$ 1.08
Net earnings per common share - diluted	$ 0.37	$ 0.28	$ 1.04

See accompanying notes to condensed consolidated financial statements.

BALCHEM CORPORATION
Condensed Consolidated Statements of Cash Flows
(In thousands)

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Cash flows from operating activities:	
Net earnings	$
Adjustments to reconcile net earnings to net cash provided by operating activities:	
Depreciation and amortization	
Shares issued under employee benefit plans	
Deferred income taxes	
Provision for doubtful accounts	
Provision for income tax benefit of stock options	
Gain on sale of equipment	
Changes in assets and liabilities net of effects of acquisition of assets:	
Accounts receivable	(
Inventories	(
Prepaid expenses and other current assets	
Income taxes	
Customer deposits	
Accounts payable and accrued expenses	
Other long-term obligations	
Net cash provided by operating activities	
Cash flows from investing activities:	
Capital expenditures	(
Proceeds from sale of property, plant & equipment	
Cash paid for intangibles assets acquired	
Acquisition of assets	(1
Net cash used in investing activities	(1
Cash flows from financing activities:	
Principal payments on long-term debt	
Proceeds from stock options and warrants exercised	
Dividends paid	
Purchase of treasury stock	
Other financing activities	
Net cash provided by financing activities	

Increase in cash and cash equivalents	(
Cash and cash equivalents beginning of period	1
Cash and cash equivalents end of period	$ 1

See accompanying notes to condensed consolidated financial statements.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(All dollar amounts in thousands, except per share data)

NOTE 1 - CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

The condensed consolidated financial statements presented herein have been prepared by the Company in accordance with the accounting policies described in its December 31, 2004 consolidated financial statements, and should be read in conjunction with the consolidated financial statements and notes, which appear in our Annual Report on Form 10-K. References in this report to "the Company" mean Balchem and/or its subsidiary BCP Ingredients, Inc., as the context requires.

In the opinion of management, the unaudited condensed consolidated financial statements furnished in this Form 10-Q include all adjustments necessary for a fair presentation of the financial position, results of operations and cash flows for the interim periods presented. All such adjustments are of a normal recurring nature. The condensed consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles governing interim financial statements and the instructions to Form 10-Q and Article 10 of Regulation S-X and therefore do not include some information and notes necessary to conform to annual reporting requirements. The results of operations for the three and nine months ended September 30, 2005 are not necessarily indicative of the operating results expected for the full year.

NOTE 2 - ACQUISITION OF ASSETS

Effective June 30, 2005, pursuant to an asset purchase agreement of same date (the "Asset Purchase Agreement"), the Company acquired certain assets of Loders Croklaan USA, LLC ("Seller") relating to the encapsulation, agglomeration and granulation business for a purchase price including acquisition costs of $9,885 plus $725 for certain product inventories and $809 for certain accounts receivable. With the exception of $985, which was paid during the quarter ended June 30, 2005, all of such payment was made on July 1, 2005 from the Company's cash reserves.

The Asset Purchase Agreement also provides for the contingent payment by the Company of additional consideration to Seller based upon the volume of sales associated with one particular product acquired by the Company during the three year period following the acquisition. Such contingent consideration will be recorded as an additional cost of the acquired product lines.

The preliminary allocation of the purchase price of the acquisition has been assigned to the long-term net assets acquired as follows:

	Fair Value Recorded in Purchase Accounting
Equipment	$ 1,436
Customer List	1,350
Patent	140
Goodwill	6,959
Total	$ 9,885

The purchase price allocations have been made on the basis of estimates made by the Company. The financial statement items and amounts are subject to subsequent revision to give effect to reclassifications related to the allocation between identifiable assets, intangible assets and goodwill and for other pre-acquisition contingencies that may become resolved during subsequent periods.

The above acquisition has been accounted for using the purchase method of accounting and the purchase price of the acquisition has been assigned to the net assets acquired based on the fair value of such assets and liabilities at the date of acquisition. The consolidated financial statements include the results of operations of the acquired product lines from the date of purchase.

Pro Forma Summary of Operations

The following unaudited pro forma information has been prepared as if the aforementioned acquisition had occurred on January 1, 2004 and does not include cost savings expected from the transaction. In addition to including the results of operations, the pro forma information gives effect primarily to changes in depreciation and amortization of tangible and intangible assets resulting from the acquisition.

The pro forma information presented does not purport to be indicative of the results that actually would have been attained if the aforementioned acquisition had occurred at the beginning of the periods presented and is not intended to be a projection of future results.

	Pro-Forma Three Months Ended September 30, 2005	2004
Net sales	$ 21,145	$ 18,586
Net earnings	3,024	2,464
Basic EPS	.39	.33
Diluted EPS	.37	.32

	Pro-Forma Nine months ended September 30, 2005	2004
Net sales	$ 63,256	$ 53,190

Net earnings	8,894	6,975
Basic EPS	1.16	.93
Diluted EPS	1.11	.91

NOTE 3 - STOCK OPTION PLAN

At September 30, 2005, the Company has stock based employee compensation plans. The Company accounts for its stock option plans in accordance with the provisions of Accounting Principles Board (APB) Opinion No. 25, "Accounting for Stock Issued to Employees" and related interpretations. As such, compensation expense is recorded on

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the date of grant only if the current market price of the underlying stock exceeds the exercise price. No stock based employee compensation cost is reflected in net earnings, as all options granted under those plans had an exercise price equal to the market value of the underlying common stock on the date of grant. The Company has adopted the disclosure standards of Statement of Financial Accounting Standards (SFAS) No. 123, "Accounting for Stock-Based Compensation" and SFAS 148, "Accounting for Stock-Based Compensation - Transition and Disclosure an amendment of FASB Statement 123," which require the Company to provide pro forma net earnings and pro forma earnings per share disclosures for employee and director stock option grants made as if the fair-value based method of accounting for stock options as defined in SFAS No. 123 has been applied. The following table illustrates the effect on net earnings and per share amounts if the Company had applied the fair value recognition provisions of SFAS No. 123 to stock based employee compensation:

	Three Months Ended September 30, 2005	2004	Nine months Septembe 2005
Net Earnings			
Net earnings, as reported	$ 3,024	$ 2,160	$ 8,322
Deduct: Total stock-based employee compensation expense determined under fair value based method, net of related tax effects	(154)	(216)	(462)
Net earnings as adjusted	$ 2,870	$ 1,944	$ 7,860
Earnings per share:			
Basic EPS as reported	$ .39	$ .29	$ 1.08
Basic EPS as adjusted	$ .37	$ .26	$ 1.02
Diluted EPS as reported	$ .37	$ .28	$ 1.04
Diluted EPS as adjusted	$ .35	$ .25	$ .98

The fair value of each stock option granted during the nine months ended September 30, 2005 and 2004 is estimated on the date of grant using the Black-Scholes option pricing model with the following assumptions:

	2005	2004
Expected life (years)	4	6
Expected volatility	28%	27%
Expected dividend yield	.36%	.32%
Risk-free interest rate	3.83%	3.64%
Weighted average fair value of options granted	$7.78	$10.06

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NOTE 4 - INVENTORIES

Inventories at September 30, 2005 and December 31, 2004 consist of the following:

	September 30, 2005	December 31, 2004
Raw materials	$ 4,321	$ 2,305
Finished goods	4,440	4,014
Total inventories	$ 8,761	$ 6,319

NOTE 5 - PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment at September 30, 2005 and December 31, 2004 are summarized as follows:

	September 30, 2005	December 31, 2004
Land	$ 290	$ 290
Building	10,256	10,241
Equipment	30,154	28,619
Construction in Progress	1,044	387
	41,744	39,537
Less: Accumulated depreciation	17,245	15,349
Net property, plant and equipment	$ 24,499	$ 24,188

NOTE 6 - INTANGIBLE ASSETS

Goodwill represents the excess of costs over fair value of assets of businesses acquired. The Company adopted the provisions of SFAS No. 141, Business Combinations, and SFAS No. 142, Goodwill and Other Intangible Assets, as of

January 1, 2002. These standards require the use of the purchase method of business combination and define an intangible asset. Goodwill and intangible assets acquired in a purchase business combination and determined to have an indefinite useful life are not amortized, but instead tested for impairment at least annually in accordance with the provisions of SFAS No. 142. SFAS No. 142 also requires that intangible assets with estimable useful lives be amortized over their respective estimated useful lives to their estimated residual values, and reviewed for impairment in accordance with SFAS No. 144, Accounting for Impairment or Disposal of Long-Lived Assets.

As of December 31, 2004, the Company performed an impairment test of its goodwill balance. As of such date, the Company's reporting units' fair values exceeded their carrying amounts, and therefore there was no indication that goodwill was impaired. Accordingly, the Company was not required to perform any further impairment tests. The Company performs its impairment test each December 31.

The Company has goodwill in the amount of $13,327 and $6,368 at September 30, 2005 and December 31, 2004, respectively, subject to the provisions of SFAS Nos. 141 and 142. At September 30, 2005, the balance of goodwill includes the cost in excess of net

assets acquired of the acquired assets of the Loders Croklaan USA, LLC encapsulation, agglomeration and granulation business, described in note 2, of $6,959.

As of September 30, 2005 and December 31, 2004, the Company had identifiable intangible assets with finite lives with a gross carrying value of approximately $2,391 and $7,915, respectively, less accumulated amortization of $236 and $7,278, respectively. At September 30, 2005, the gross carrying amount included a customer list and patent acquired as part of the acquisition of certain assets of the Loders Croklaan USA, LLC encapsulation, agglomeration and granulation business, described in note 2. At December 31, 2004, the gross carrying amount and accumulated amortization included other customer lists and re-registration costs that were fully amortized during 2004. These fully amortized customer lists and re-registration costs were written-off on March 31, 2005 and, therefore, were not included in the gross carrying amount and accumulated amortization at September 30, 2005.

Identifiable intangible assets with finite lives at September 30, 2005 and December 31, 2004 are summarized as follows:

	Amortization Period (In years)	Gross Carrying Amount at 9/30/05	Accumulated Amortization at 9/30/05	Gross Carrying Amount at 12/31/04
Customer lists	10	$ 1,350	34	$ 6,760
Re-registration costs	10	11	--	356
Patents	15-17	746	131	538
Trademarks	17	209	46	207
Other	5	75	25	54
		$ 2,391	$ 236	$ 7,915

Amortization of identifiable intangible assets was approximately $74 for the first nine months of 2005. Assuming no change in the gross carrying value of identifiable intangible assets, the estimated amortization expense for the remainder of 2005 is $49 and approximately $195 per annum for 2006 through 2009. At September 30, 2005, there were no identifiable intangible assets with indefinite useful lives as defined by SFAS No. 142. Identifiable intangible assets are reflected in "Intangible assets with finite lives, net" in the Company's consolidated balance sheets. There were no changes to the useful lives of intangible assets subject to amortization during the nine months ended September 30, 2005.

NOTE 7 - NET EARNINGS PER SHARE

The following presents a reconciliation of the net earnings and shares used in calculating basic and diluted net earnings per share:

Three months ended September 30, 2005	Net Earnings (Numerator)	Number of Shares (Denominator)
Basic EPS - Net earnings and weighted average common shares outstanding	$3,024	7,727,868
Effect of dilutive securities - stock options		367,454
Diluted EPS - Net earnings and weighted average common shares outstanding and effect of stock options	$3,024	8,095,322

Three months ended September 30, 2004	Net Earnings (Numerator)	Number of Shares (Denominator)
Basic EPS - Net earnings and weighted average common shares outstanding	$2,160	7,534,202
Effect of dilutive securities - stock options		247,885
Diluted EPS - Net earnings and weighted average common shares outstanding and effect of stock options	$2,160	7,782,087

	Net	Number of

Nine months ended September 30, 2005	Earnings (Numerator)	Shares (Denominator)
Basic EPS - Net earnings and weighted average common shares outstanding	$8,322	7,699,352
Effect of dilutive securities - stock options		326,902
Diluted EPS - Net earnings and weighted average common shares outstanding and effect of stock options	$8,322	8,026,254

Nine months ended September 30, 2004	Net Earnings (Numerator)	Number of Shares (Denominator)
Basic EPS - Net earnings and weighted average common shares outstanding	$5,977	7,482,472
Effect of dilutive securities - stock options		196,259
Diluted EPS - Net earnings and weighted average common shares outstanding and effect of stock options	$5,977	7,678,731

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The Company had stock options covering 204,000 and 106,800 shares at September 30, 2005 and 2004, respectively, that could potentially dilute basic earnings per share in future periods that were not included in diluted earnings per share because their effect on the period presented was anti-dilutive.

NOTE 8 - SEGMENT INFORMATION

The Company's reportable segments are strategic businesses that offer products and services to different markets. Presently, the Company has three segments: specialty products, encapsulated / nutritional products (includes products relating to the the afforementioned June 30, 2005 acquisition of certain assets of the Loders Croklaan USA, LLC encapsulation, agglomeration and granulation business) and BCP Ingredients, its unencapsulated feed supplements segment.

Business Segment Net Sales:

	Three Months Ended September 30,		Nine mon Septem
	2005	2004	2005
Specialty Products	$ 7,352	$ 7,171	$ 22,088

Encapsulated/Nutritional Products	8,503	6,504	23,131
BCP Ingredients	5,290	3,681	14,750
Total	$ 21,145	$ 17,356	$ 59,969

Business Segment Earnings:

	Three Months Ended September 30, 2005	2004	Nine mo Sept 2005
Specialty Products	$ 2,846	$ 2,697	$ 8,377
Encapsulated/Nutritional Products	945	345	2,431
BCP Ingredients	940	388	2,233
Interest and other income (expense)	126	(39)	231
Earnings before income taxes	$ 4,857	$ 3,391	$ 13,272

NOTE 9- SUPPLEMENTAL CASH FLOW INFORMATION

Cash paid during the nine months ended September 30, 2005 and 2004 for income taxes and interest is as follows:

	Nine months ended September 30, 2005	2004
Income taxes	$ 3,846	$ 2,365
Interest	$ 6	$ 174

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NOTE 10 - COMMON STOCK

On December 16, 2004, the Board of Directors of the Company approved a three-for-two split of the Company's common stock to be distributed in the form of a stock dividend to shareholders of record on December 30, 2004. Such distribution was made on January 20, 2005. Accordingly, the stock split was recognized by reclassifying the par value of the additional shares resulting from the split, from additional paid-in capital to common stock. All references to number of common shares and per share amounts except shares authorized in the accompanying consolidated financial statements were retroactively adjusted to reflect the effect of the stock split.

In June 1999, the board of directors authorized the repurchase of shares of the Company's outstanding common stock over a two-year period commencing July 2, 1999. Under this program, which was subsequently extended, the Company had, as of December 31, 2004, repurchased a total 514,974 shares at an average cost of $6.17 per share, none of which remain in treasury. In June 2005, the board of directors authorized another extension to the stock repurchase program for up to an additional 600,000 shares, that is, over and above those 514,974 shares previously repurchased under the program. During the three months ended September 30, 2005, a total of 3,300 shares have been purchased at an average cost of $26.83 per share, all of which remain in treasury at September 30, 2005.

NOTE 11 - LONG TERM DEBT AND CREDIT AGREEMENTS

There was no debt outstanding at September 30, 2005. On June 1, 2001, the Company and its principal bank entered into a loan agreement (the "Loan Agreement") providing for a term loan of $13,500 (the "Term Loan"), the proceeds of which were used to fund the acquisition of certain assets of DCV, Inc. and its affiliate Ducoa L.P., (described in Note 4 of the Company's Form 10-K as of December 31, 2004). During the quarter ended December 31, 2004, the Company prepaid $7,839, the remaining balance of the Term Loan. Borrowings at September 30, 2004 included borrowings under the Term Loan bearing interest at LIBOR plus 1.25% (2.90% at September 30, 2004). Certain provisions of the Term Loan require maintenance of certain financial ratios, limit future borrowings, and impose certain other requirements as contained in the agreement. The Loan Agreement also provides for a short-term revolving credit facility of $3,000 (the "Revolving Facility"). Borrowings under the Revolving Facility bear interest at LIBOR plus 1.00%. No amounts have been drawn on the Revolving Facility as of September 30, 2005. The Revolving Facility was extended and now expires on May 31, 2006. Management believes that such facility will be renewed in the normal course of business.

Indebtedness under the Loan Agreement is secured by substantially all of the assets of the Company other than real properties.

NOTE 12 - EMPLOYEE BENEFIT PLANS

The Company sponsors a 401(k) savings and profit sharing plan for eligible employees. The plan allows participants to make pretax contributions and the Company matches certain percentages of those pretax contributions with shares of the Company's common stock. The profit sharing portion of the plan is discretionary and non-contributory. All

amounts contributed to the plan are deposited into a trust fund administered by independent trustees.

The Company also currently provides postretirement benefits in the form of an unfunded retirement medical plan under a collective bargaining agreement covering eligible retired employees of its Verona facility.

Net periodic benefit cost for such retirement medical plan for the nine months ended September 30 was as follows:

	2005	2004
Service Cost	$ 24	$ 23
Interest Cost	38	37
Expected return on plan assets	--	--
Amortization of transition obligation	--	--
Amortization of prior service cost	(11)	(8)
Amortization of (gain) or loss	--	--

Net periodic benefit cost	$ 51	$ 52

The plan is unfunded and approved claims are paid from Company funds. Historical cash payments made under such plan approximated $50 per year.

In December 2003, the Medicare Prescription Drug, Improvement and Modernization Act of 2003 ("the Act") was signed into law. The Act introduced a plan sponsor subsidy based on a percentage of a beneficiary's annual prescription drug benefits, within defined limits, and the opportunity for a retiree to obtain prescription drug benefits under Medicare. There is no impact of the subsidy on the postretirement benefit obligation and net periodic cost as Medicare eligible retirees are not covered under the Company's plan.

NOTE 13 - NEW ACCOUNTING PRONOUNCEMENTS

In December 2004, the FASB issued SFAS No. 123(R), "Share-Based Payment." SFAS No. 123(R) revises SFAS No. 123, Accounting for Stock-Based Compensation, and supersedes APB Opinion No. 25, Accounting for Stock Issued to Employees, and its related implementation guidance. SFAS No. 123(R) will require compensation costs related to share-based payment transactions to be recognized in the financial statements (with limited exceptions). The amount of compensation cost will be measured based on the grant-date fair value of the equity or liability instruments issued. Compensation cost will be recognized over the period that an employee provides service in exchange for the award. This statement was originally effective as of the beginning of the first interim or annual reporting period that begins after June 15, 2005. On April 14, 2005, the SEC adopted a new rule that amended the compliance dates of SFAS No. 123(R) to require implementation no later than the beginning of the first fiscal year after June 15, 2005 (the year beginning January 1, 2006 for the Company). The Company is currently evaluating the impact of this standard on its results of operations and financial position.

In November 2004, the Financial Accounting Standards Board issued Statement of Financial Accounting Standard No. 151, "Inventory Costs." The new statement amends Accounting Research Bulletin No. 43, Chapter 4, "Inventory Pricing," to clarify the

accounting for abnormal amounts of idle facility expense, freight, handling costs, and wasted material. This statement requires that those items be recognized as current period charges and requires that allocation of fixed production overheads to the cost of conversion be based on the normal capacity of the production facilities. This statement is effective for fiscal years beginning after June 15, 2005. The Company does not expect adoption of this statement to have a material impact on its financial condition or results of operations.

NOTE 14 - SUBSEQUENT EVENT

On November 2, 2005, the Company, through its wholly owned subsidiary Balchem Minerals Corporation, entered into a definitive stock purchase agreement with Chelated Minerals Corporation ("CMC"), a privately held Utah corporation, and its shareholders to acquire all of the outstanding capital stock of CMC for a purchase price of $17,350. CMC is a manufacturer and global marketer of mineral nutritional supplements for livestock, pet and poultry feeds. The purchase price is subject to adjustment based upon CMC's working capital as of the closing date. The parties anticipate closing the transaction during the fourth quarter of 2005. For further details of this transaction, please refer to the Company's Form 8-K filing submitted to the U.S. Securities and Exchange Commission on November 7, 2005.

Item 2 - Management's Discussion and Analysis of Financial Condition and Results of Operations (All dollar amounts in thousands)

This Report contains forward-looking statements, within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended, which reflect the Company's expectation or belief concerning future events that involve risks and uncertainties. The actions and performance of the Company could differ materially from what is contemplated by the forward-looking statements contained in this Report. Factors that might cause differences from the forward-looking statements include those referred to or identified in Item 1 of the Company's Annual Report on Form 10-K for the year ended December 31, 2004 and other factors that may be identified elsewhere in this Report. Reference should be made to such factors and all forward-looking statements are qualified in their entirety by the above cautionary statements.

Overview

The Company develops, manufactures and markets specialty performance ingredients and products for the food, feed and medical device sterilization industries. The Company's reportable segments are strategic businesses that offer products and services to different markets. The Company presently has three reportable segments: specialty products, encapsulated / nutritional products and BCP Ingredients.

Specialty Products

The specialty products segment repackages and distributes the following specialty gases: ethylene oxide, blends of ethylene oxide, propylene oxide and methyl chloride.

Ethylene oxide, at the 100% level, is sold as a sterilant gas, in returnable cylinders, primarily for use in the health care industry to sterilize medical devices. Contract sterilizers, medical device manufacturers and medical gas distributors are the Company's principal customers for this product. In addition, the Company sells 100% ethylene oxide in single use canisters to customers that sell medical device sterilization equipment commonly found in hospitals or doctor's offices. Blends of ethylene oxide are sold as fumigants and are highly effective in killing bacteria, fungi, and insects in spices and other seasoning materials. Propylene oxide and methyl chloride are sold principally to customers seeking smaller (as opposed to bulk) quantities.

Management believes that future success in this segment is highly dependent on the Company's ability to maintain its strong reputation for excellent quality, safety and customer service. The Company is also required to maintain an EPA regulatory permit.

Encapsulated / Nutritional Products

The encapsulated / nutritional products segment provides mircoencapsulation and agglomeration solutions to a variety of applications in food, pharmaceutical and nutritional ingredients to enhance performance of nutritional fortification, processing, mixing, packaging applications and shelf-life. Major end product applications are baked

goods, refrigerated and frozen dough systems, processed meats, seasoning blends, confections, nutritional supplementations and animal nutrition.

Management believes this segment's key strengths are its proprietary technology and end-product application capabilities. The success of the Company's efforts to increase revenue in this segment is highly dependent on the timing of marketing launches of new products in the U.S. and international food market by the Company's customers and prospects. The Company, through its proprietary technology and applications expertise, continues to develop new microencapsulation products designed to solve and respond to customer problems and needs. Sales of our REASHURE(TM) and NITROSHURE(TM) products for the animal nutrition and health industry are highly dependent on dairy industry economics as well as the ability of the Company to leverage the results of existing successful university research on the animal health benefits of these products.

BCP Ingredients

BCP Ingredients manufactures and supplies choline chloride, an essential nutrient for animal health, to the poultry and swine industries. In addition, certain derivatives of choline chloride are also marketed into industrial applications.

Management believes that success in this commodity-oriented marketplace is highly dependent on the Company's ability to maintain its strong reputation for excellent quality and customer service. In addition, the Company must continue to realize production efficiencies in order to maintain its low-cost position to effectively compete for market share in a highly competitive marketplace.

The Company sells products for all segments through its own sales force, independent distributors, and sales agents.

The following tables summarize consolidated net sales by segment and business segment earnings for the three and nine months ended September 30 (in thousands):

Business Segment Net Sales:

	Three Months Ended September 30, 2005	2004	Nine mont Septemb 2005
Specialty Products	$ 7,352	$ 7,171	$ 22,088
Encapsulated/Nutritional Products	8,503	6,504	23,131
BCP Ingredients	5,290	3,681	14,750
Total	$ 21,145	$ 17,356	$ 59,969

Business Segment Earnings:

	Three Months Ended September 30, 2005	2004	Nine mo Septe 2005
Specialty Products	$ 2,846	$ 2,697	$ 8,377
Encapsulated/Nutritional Products	945	345	2,431
BCP Ingredients	940	388	2,233
Interest and other income (expense)	126	(39)	231
Earnings before income taxes	$ 4,857	$ 3,391	$ 13,272

Share Repurchase Program

In June 1999, the board of directors authorized the repurchase of shares of the Company's outstanding common stock over a two-year period commencing July 2, 1999. Under this program, which was subsequently extended, the Company had, as of December 31, 2004, repurchased a total 514,974 shares at an average cost of $6.17 per share, none of which remain in treasury at December 31, 2004. In June 2005, the board of directors authorized another extension to the stock repurchase program for up to an additional 600,000 shares, that is, over and above those 514,974 shares previously repurchased under the program. During the three months ended September 30, 2005, a total of 3,300 shares have been purchased at an average cost of $26.83 per share, all of which remain in treasury at September 30, 2005. During the month of October 2005, the company purchased a total of 24,800 shares at an average cost of $ 26.92 per share. The Company intends to acquire shares from time to time at prevailing market prices if and to the extent it deems it advisable to do so based among other factors on its assessment of corporate cash flow and market conditions.

RESULTS OF OPERATIONS

Three months ended September 30, 2005 compared to three months ended September 30, 2004

Net Sales

Net sales for the three months ended September 30, 2005 were $21,145 compared with $17,356 for the three months ended September 30, 2004, an increase of $3,789 or 21.8%. Net sales for the specialty products segment were $7,352 for the three months ended September 30, 2005 compared with $7,171 for the three months ended September 30, 2004, an increase of $181 or 2.5%. This increase was principally due to an increase in sales volume of ethylene oxide for medical device sterilization and propylene oxide for starch modification as well as a modest price increase adopted early in 2005 to help offset rising raw material costs. Net sales for the encapsulated / nutritional products segment were $8,503 for the three months ended September 30, 2005 compared with $6,504 for the three months ended September 30, 2004, an increase of $1,999 or 30.7% This

increase was due principally to increased volumes sold in the domestic food market and approximately $1,800 associated with the Company's new pharmaceutical and food business lines resulting from the June 30, 2005 acquisition of certain assets of the Loders Croklaan USA, LLC encapsulation, agglomeration and granulation business, as described in Note 2. The Company also experienced volume improvements in the animal health industry relating to REASHURE(TM), NITROSHURE(TM) and NIASHURE(TM), our microencapsulated niacin product for dairy cows, and the human choline market. These increases were partially offset by a decline in volumes sold in the international food and the nutritional supplement product lines. Net sales of $5,290 were realized for the three months ended September 30, 2005 for the BCP Ingredients (unencapsulated feed supplements) segment, which markets choline additives for the poultry and swine industries as well as industrial choline derivative products, as compared with $3,681 for the three months ended September 30, 2004, an increase of $1,609 or 43.7%. This increase was due to increased volumes sold in the dry choline, aqueous choline, and specialty industrial product lines, along with modest price increases in all three product lines.

Gross Margin

Gross margin for the three months ended September 30, 2005 increased to $7,649 compared to $6,219 for the three months ended September 30, 2004. Gross margin percentage for the three months ended September 30, 2005 was 36.2% compared to 35.8% for the three months ended September 30, 2004. Margins for the specialty products segment increased slightly as increased sales volume, in addition to lower amortization expense, were partially offset by increases in raw material prices and distribution costs. Gross margin percentage in the encapsulated / nutritional products segment also increased slightly as margins were favorably affected by increased production, a result of greater sales volume as described above. Margins for BCP Ingredients increased 6.8% and were favorably affected by increased production volumes of choline chloride and specialty derivative products.

Operating Expenses

Operating expenses for the three months ended September 30, 2005 were $2,918 compared to $2,789 for the three months ended September 30, 2004, an increase of $129 or 4.6%. This increase was primarily a result of increased payroll costs, charges for search fees and relocation expenses associated with new hires. Total operating expenses as a percentage of sales were 13.8% for the three months ended September 30, 2005 compared to 16.1% for the three months ended September 30, 2004. During the three months ended September 30, 2005 and 2004, the Company spent $492 and $383, respectively, on Company-sponsored research and development programs, substantially all of which pertained to the Company's encapsulated / nutritional products segment for both food and animal feed applications.

Earnings From Operations

As a result of the foregoing, earnings from operations for the three months ended September 30, 2005 were $4,731 as compared to $3,430 for the three months ended September 30, 2004.

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Other expenses (income)

Interest income for the three months ended September 30, 2005 totaled $46 as compared to $22 for the three months ended September 30, 2004. This increase is attributable to the increase in the average total cash balance. Interest expense was $2 for the three months ended September 30, 2005 compared to $61 for the three months ended September 30, 2004. This decrease is the result of the prepayment of the Company's outstanding loan balance in December 2004. Other income of $82 for the three months ended September 30, 2005 represents the net gain on the sale of equipment.

Income Tax Expense

The Company's effective tax rate for the three months ended September 30, 2005 and 2004 was 37.7% and 36.3%, respectively.

Net earnings

As a result of the foregoing, net earnings were $3,024 for the three months ended September 30, 2005 as compared with $2,160 for the three months ended September 30, 2004, an increase of 40.0%.

Nine months ended September 30, 2005 compared to nine months ended September 30, 2004

Net Sales

Net sales for the nine months ended September 30, 2005 were $59,969 compared with $49,449 for the nine months ended September 30, 2004, an increase of $10,520 or 21.3%. Net sales for the specialty products segment were $22,088 for the nine months ended September 30, 2005 compared with $21,315 for the nine months ended September 30, 2004, an increase of $773 or 3.6%. This increase was due principally to greater sales volumes of ethylene oxide for medical device sterilization and propylene oxide for starch modification as well as a modest price increase adopted early in 2005 to help offset rising raw material costs. This increase was partially offset by a decline in volumes sold in the ethylene oxide blends product line and single use ethylene oxide canisters for use in sterilization equipment. Net sales for the encapsulated / nutritional products segment were $23,131 for the nine months ended September 30, 2005 compared with $18,527 for the nine months ended September 30, 2004, an increase of $4,604 or 24.9%. This increase was due principally to increased volumes sold in the domestic food market and approximately $1,800 associated with the Company's new pharmaceutical and food business lines resulting from the June 30, 2005 acquisition of certain assets of the Loders Croklaan USA, LLC encapsulation, agglomeration and granulation business, as described in Note 2. The Company also experienced volume improvements in the animal health industry relating to REASHURE(TM), NITROSHURE(TM) and NIASHURE(TM), our microencapsulated niacin product for dairy cows, and the human choline market. These increases were partially offset by a decline in volumes sold in the international food product lines and the nutritional supplement product line. Net sales of $14,750 were realized for the nine months ended September 30, 2005 in the BCP Ingredients segment compared with $9,607 for the nine months ended September 30, 2004, an increase of $5,143 or 53.5%. This increase was due to increased volumes sold in the dry choline, aqueous choline, and specialty industrial product lines, along with modest price increases in all three product lines.

Gross Margin

Gross margin for the nine months ended September 30, 2005 increased to $21,943 compared to $17,855 for the nine months ended September 30, 2004. Gross margin percentage for the nine months ended September 30, 2005 was 36.6% as compared to 36.1% for the nine months ended September 30, 2004. Gross margin percentage for the specialty products segment increased slightly as a result of increased sales volume and product mix in addition to lower amortization expense, partially offset by increases in raw material prices and distribution costs. Gross margin percentage in the encapsulated / nutritional products segment increased 2.9% as margins were favorably affected by increased production, a result of greater sales volume as described above. Gross margin percentage in BCP Ingredients increased 5.3% and was favorably affected by increased production volumes of choline chloride and specialty derivative products.

Operating Expenses

Operating expenses for the nine months ended September 30, 2005 increased to $8,902 from $8,308 for the nine months ended September 30, 2004, an increase of $594 or 7.1%. Total operating expenses as a percentage of sales were 14.8% for the nine months ended September 30, 2005 compared to 16.8% for the nine months ended September 30, 2004. The increase in operating expense for the nine months ended September 30, 2005 was principally a result of new hires, increased charges for search fees associated with new hires and associated relocation expenses. These increases were partially offset by a decrease in selling expenses. During the nine months ended September 30, 2005 and 2004, the Company spent $1,537 and $1,252, respectively, on Company-sponsored research and development programs, substantially all of which pertained to the Company's encapsulated / nutritional products segment for both food and animal feed applications.

Earnings From Operations

As a result of the foregoing, earnings from operations for the nine months ended September 30, 2005 were $13,041 as compared to $9,547 for the nine months ended September 30, 2004.

Other expenses (income)

Interest income for the nine months ended September 30, 2005 totaled $155 as compared to $74 for the nine months ended September 30, 2004. This increase is attributable to the increase in the average total cash balance. Interest expense was $6 for the nine months ended September 30, 2005 compared to $174 for the nine months ended September 30, 2004. This decrease is the result of the prepayment of the Company's outstanding loan balance in December 2004. Other income of $82 for the nine months ended September 30, 2005 represents the net gain on the sale of equipment.

Income Tax Expense

The Company's effective tax rate for the nine months ended September 30, 2005 and 2004 was 37.3% compared to a 36.8% rate for the nine months ended September 30, 2004

Net earnings

As a result of the foregoing, net earnings were $8,322 for the nine months ended September 30, 2005 as compared with $5,977 for the nine months ended September 30, 2004.

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FINANCIAL CONDITION

LIQUIDITY AND CAPITAL RESOURCES

Contractual Obligations

As part of the June 30, 2005 acquisition of certain assets relating to the encapsulation, agglomeration and granulation business of Loders Croklaan USA, LLC, the asset purchase agreement provides for the contingent payment by the Company of additional consideration based upon the volume of sales associated with one particular product acquired by the Company during the three year period following the acquisition. Such contingent consideration will be recorded as an additional cost of the acquired product lines. No such contingent consideration has been earned or paid as of September 30, 2005.

The Company's other contractual obligations and commitments principally include obligations associated with future minimum non-cancelable operating lease obligations (including for the headquarters office space entered into in 2002).

The Company knows of no current or pending demands on, or commitments for, its liquid assets that will materially affect its liquidity.

The Company expects its operations to continue generating sufficient cash flow to fund working capital requirements and necessary capital investments. The Company is actively pursuing additional acquisition candidates. As described in Note 14, the Company, on November 2, 2005, through its wholly owned subsidiary Balchem Minerals Corporation, entered into a definitive stock purchase agreement with Chelated Minerals Corporation ("CMC"), a privately held Utah corporation, and its shareholders to acquire all of the outstanding capital stock of CMC for a purchase price of $17,350. CMC is a manufacturer and global marketer of mineral nutritional supplements for livestock, pet and poultry feeds. The purchase price is subject to adjustment based upon CMC's working capital as of the closing date. The parties anticipate closing the transaction during the fourth quarter of 2005. The Company could seek bank loans or access to financial markets to fund such acquisitions, its operations, working capital, necessary capital investments or other cash requirements should it deem it necessary to do so.

Cash

Cash and cash equivalents decreased to $10,723 at September 30, 2005 from $12,734 at December 31, 2004. The $2,011 decrease resulted primarily from an increase in net cash provided by operating activities and financing activities of $9,827 and $480, respectively, offset by net cash used in investing activities of $12,318 principally for the acquisition of certain assets of the Loders Croklaan USA, LLC fluidized bed encapsulation and granulation business on June 30, 2005. Working capital amounted to $24,768 at September 30, 2005 as compared to $23,505 at December 31, 2004, an increase of $1,263.

Operating Activities

Cash flows from operating activities provided $9,827 for the nine months ended September 30, 2005 compared to $8,788 for the nine months ended September 30, 2004. The increase in cash flows from operating activities was primarily due to an increase in earnings and accounts payable and accrued expenses combined with a decrease in prepaid expenses and prepaid income taxes. This increase was partially offset by an increase in accounts receivable and inventories and a decrease in depreciation and amortization expense. The decrease in depreciation and amortization resulted from the completion of amortization of a customer list during the third quarter of 2004.

Investing Activities

Property and equipment expenditures were $1,186 for the nine months ended September 30, 2005 compared to $820 for the nine months ended September 30, 2004. Cash paid for the acquisition of assets relating to the Loders Croklaan USA, LLC fluidized bed encapsulation and granulation business, including acquisition costs, was $11,419. With the exception of $985, which was paid during the quarter ended June 30, 2005, all of such payment was made on July 1, 2005 from the Company's cash reserves.

Financing Activities

In June 1999, the board of directors authorized the repurchase of shares of the Company's outstanding common stock over a two-year period commencing July 2, 1999. Under this program, which was subsequently extended, the Company had, as of December 31, 2004, repurchased a total 514,974 shares at an average cost of $6.17 per share, none of which remain in treasury at December 31, 2004. In June 2005, the board of directors authorized another extension to the stock repurchase program for up to an additional 600,000 shares, that is, over and above those 514,974 shares previously repurchased under the program. During the three months ended September 30, 2005, a total of 3,300 shares have been purchased at an average cost of $26.83 per share, all of which remain in treasury at September 30, 2005. During the month of October 2005, the company purchased a total of 24,800 shares at an average cost of $ 26.92 per share. The Company intends to acquire shares from time to time at prevailing market prices if and to the extent it deems it advisable to do so based among other factors on its assessment of corporate cash flow and market conditions.

There was no debt outstanding at September 30, 2005. On June 1, 2001, the Company and its principal bank entered into a Loan Agreement (the "Loan Agreement") providing for a term loan of $13,500 (the "Term Loan"), the proceeds of which were used to fund the acquisition of certain assets of DCV, Inc. and its affiliate Ducoa L.P. During the quarter ended December 31, 2004, the Company prepaid $7,839, the remaining balance of the Term Loan. Borrowings at September 30, 2004 included borrowings under the Term Loan bearing interest at LIBOR plus 1.25% (2.90% at September 30, 2004). Certain provisions of the Term Loan require maintenance of certain financial ratios, limit future borrowings, and impose certain other requirements as contained in the agreement. The Loan Agreement also provides for a short-term revolving credit facility of $3,000

(the "Revolving Facility"). Borrowings under the Revolving Facility bear interest at LIBOR plus 1.00%. No amounts have been drawn on the Revolving Facility as of September 30, 2005 and 2004. The Revolving Facility was extended and now expires on May 31, 2006. Management believes that such facility will be renewed in the normal course of business.

Indebtedness under the Loan Agreement is secured by substantially all of the assets of the Company other than real properties.

Proceeds from stock options exercised totaled $1,263 and $1,814 for the nine months ended September 30, 2005 and 2004, respectively. Dividend payments were $685 and $389 for the nine months ended September 30, 2005 and 2004, respectively.

Other Matters Impacting Liquidity

The Company currently provides postretirement benefits in the form of a retirement medical plan under a collective bargaining agreement covering eligible retired employees of its Verona facility. The amount recorded on the Company's balance sheet as of September 30, 2005 for this obligation is $979. The postretirement plan is not funded. Historical cash payments made under such plan have approximated $50 per year.

Critical Accounting Policies

There were no changes to the Company's Critical Accounting Policies, as described in its December 31, 2004 Annual Report on Form 10-K, during the nine months ended September 30, 2005.

Related Party Transactions

The Company was not engaged in related party transactions during the three and nine months ended September 30, 2005 and all transactions of the Company during such period were at arms length.

Item 3. Quantitative and Qualitative Disclosures about Market Risk

Cash and cash equivalents are invested primarily in money market accounts. Accordingly, we believe we have limited exposure to market risk for changes in interest rates. The Company has no derivative financial instruments or derivative commodity instruments, nor does the Company have any financial instruments entered into for trading or hedging purposes. Foreign sales are generally billed in U.S. dollars. The Company believes that its business operations are not exposed in any material respect to market risk relating to foreign currency exchange risk or commodity price risk.

Item 4. Controls and Procedures

(a) Evaluation of Disclosure Controls and Procedures

Pursuant to the requirements of the Sarbanes-Oxley Act of 2002, the Company's management, under the supervision and with the participation of the Company's Chief Executive Officer and Chief Financial Officer, has evaluated, as of the end of the period covered by this Quarterly Report on Form 10-Q, the effectiveness of the Company's disclosure controls and procedures (including its internal controls and procedures), except for the disclosure controls and procedures of the Loders Croklaan encapsulation, agglomeration and granulation business, which were excluded from management's evaluation. We completed the acquisition of this business on June 30, 2005, and are currently conducting an assessment of the business' disclosure controls and procedures.

Based upon management's evaluation, the Chief Executive Officer and the Chief Financial Officer have concluded that, as of the end of such period, the Company's disclosure controls and procedures were effective in identifying the information required to be disclosed in the Company's periodic reports filed with the Securities and Exchange Commission ("SEC"), including this Quarterly Report on Form 10-Q, and ensuring that such information is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms.

(b) Changes in Internal Controls

During the most recent fiscal quarter, there has been no significant change in the Company's internal control over financial reporting that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

Part II. Other Information

Item 6. Exhibits

Exhibit 31.1	Certification of Chief Executive Officer pursuant to Rule 13a-14(a).
Exhibit 31.2	Certification of Chief Financial Officer pursuant to Rule 13a-14(a).
Exhibit 32.1	Certification of Chief Executive Officer pursuant to Rule 13a-14(b) and Section 1350 of Chapter 63 of Title 18 of the United States Code.
Exhibit 32.2	Certification of Chief Financial Officer pursuant to Rule 13a-14(b) and Section 1350 of Chapter 63 of Title 18 of the United States Code.

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.

BALCHEM CORPORATION

By: /s/ Dino A. Rossi

Dino A. Rossi, President and
Chief Executive Officer

Date: November 8, 2005

Exhibit Index

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