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BALCHEM CORP

Form 10-Q

May 03, 2019

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**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549**

FORM 10-Q

(Mark One)

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF
1934

For the quarterly period ended March 31, 2019

OR
TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF
1934

For the transition period from _____ to _____

Commission file number: 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)

52 Sunrise

Park Road,

New

Hampton,

NY 10958

(Address

of

principal

executive

offices)

(Zip Code)

Registrant's

telephone

number,

including

area code:

(845)

326-5600

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes No

Indicate by check mark whether the Registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

(Check one): Large accelerated filer Accelerated filer

Non-accelerated filer Smaller reporting company Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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

Yes No

As of April 25, 2019, the registrant had 32,333,546 shares of its Common Stock, \$.06 2/3 par value, outstanding.

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 QUARTERLY REPORT ON FORM 10-Q
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Table of Contents**Part I. Financial Information****Item 1. Financial Statements****BALCHEM CORPORATION****Condensed Consolidated Balance Sheets***(Dollars in thousands, except share and per share data)*

<u>Assets</u>	March 31, 2019 (unaudited)	December 31, 2018
Current assets:		
Cash and cash equivalents	\$ 39,004	\$ 54,268
Accounts receivable, net of allowance for doubtful accounts of \$583 and \$610 at March 31, 2019 and December 31, 2018 respectively	99,834	99,545
Inventories	66,764	67,187
Prepaid expenses	3,510	3,830
Assets held for sale	11,748	—
Other current assets	806	1,484
Total current assets	221,666	226,314
Property, plant and equipment, net	188,036	194,339
Goodwill	446,453	447,995
Intangible assets with finite lives, net	100,088	105,985
Right of use assets	8,036	—
Other assets	7,609	6,722
Total assets	\$ 971,888	\$ 981,355
<u>Liabilities and Stockholders' Equity</u>		
Current liabilities:		
Trade accounts payable	\$ 26,342	\$ 33,345
Accrued expenses	20,922	22,025
Accrued compensation and other benefits	6,255	11,022
Dividends payable	78	15,220
Income tax payable	6,989	444
Lease liabilities - current	2,467	—
Liabilities held for sale	757	—
Total current liabilities	63,810	82,056
Revolving loan	140,000	156,000
Deferred income taxes	44,311	44,309
Lease liabilities - non-current	5,559	—
Other long-term obligations	7,699	7,372
Total liabilities	261,379	289,737
Commitments and contingencies (note 16)		
Stockholders' equity:		
Preferred stock, \$25 par value. Authorized 2,000,000 shares; none issued and outstanding	—	—
	2,156	2,151

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Common stock, \$.0667 par value. Authorized 120,000,000 shares; 32,336,228 shares issued and 32,330,032 outstanding at March 31, 2019 and 32,256,915 shares issued and 32,256,209 outstanding at December 31, 2018, respectively

Additional paid-in capital	166,762	165,098
Retained earnings	546,810	528,027
Accumulated other comprehensive loss	(4,686) (3,602
Treasury stock, at cost: 6,196 and 706 shares at March 31, 2019 and December 31, 2018	(533) (56
Total stockholders' equity	710,509	691,618

Total liabilities and stockholders' equity	\$ 971,888	\$ 981,355
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See accompanying notes to condensed consolidated financial statements.

Table of Contents**BALCHEM CORPORATION****Condensed Consolidated Statements of Earnings***(Dollars in thousands, except per share data)*

(unaudited)

	Three Months Ended March 31, 2019 2018	
Net sales	\$ 157,029	\$ 161,410
Cost of sales	107,934	109,951
Gross margin	49,095	51,459
Operating expenses:		
Selling expenses	14,126	14,059
Research and development expenses	2,895	2,569
General and administrative expenses	5,594	7,591
	22,615	24,219
Earnings from operations	26,480	27,240
Other expenses:		
Interest expense, net	1,589	1,874
Other, net	98	189
	1,687	2,063
Earnings before income tax expense	24,793	25,177
Income tax expense	6,010	5,831
Net earnings	\$ 18,783	\$ 19,346
Net earnings per common share - basic	\$ 0.58	\$ 0.60
Net earnings per common share - diluted	\$ 0.58	\$ 0.60

See accompanying notes to condensed consolidated financial statements.

Table of Contents**BALCHEM CORPORATION****Condensed Consolidated Statements of Comprehensive Income***(Dollars in thousands)*

(unaudited)

	Three Months Ended March 31, 2019 2018	
Net earnings	\$18,783	\$19,346
Other comprehensive (loss) income, net of tax:		
Net foreign currency translation adjustment	(1,089)	1,363
Net change in postretirement benefit plans, net of taxes of \$(2) and \$(4) for the three months ended March 31, 2019 and 2018	5	13
Other comprehensive (loss) income	(1,084)	1,376
Comprehensive income	\$17,699	\$20,722
<i>See accompanying notes to condensed consolidated financial statements.</i>		

Table of Contents**BALCHEM CORPORATION****Condensed Consolidated Statements of Changes in Stockholders' Equity****For the three months ended March 31, 2019 and 2018***(Dollars in thousands, except share and per share data)*

	Total Stockholders' Equity	Retained Earnings	Accumulated Other Comprehensive (Loss) Income	Common Stock Shares	Amount	Treasury Stock Shares	Amount	Additional Paid-in Capital
Balance - December 31, 2018	\$ 691,618	\$ 528,027	\$ (3,602)	32,256,209	\$ 2,151	(706)	\$ (56)	\$ 165,098
Net earnings	18,783	18,783	—	—	—	—	—	—
Other comprehensive (loss)	(1,084)	—	(1,084)	—	—	—	—	—
Treasury shares purchased	(727)	—	—	—	—	(8,496)	(727)	—
Shares and options issued under stock plans	1,919	—	—	73,823	5	3,006	250	1,664
Balance - March 31, 2019	\$ 710,509	\$ 546,810	\$ (4,686)	32,330,032	\$ 2,156	(6,196)	\$ (533)	\$ 166,762
Balance - December 31, 2017	\$ 616,881	\$ 464,639	\$ (1,642)	32,019,605	\$ 2,135	—	—	\$ 151,749
Net earnings	19,346	19,346	—	—	—	—	—	—
Other comprehensive income	1,376	—	1,376	—	—	—	—	—
Dividends	1	1	—	—	—	—	—	—
Treasury shares purchased	(786)	—	—	—	—	(10,454)	(786)	—
Shares and options issued under stock plans	3,072	—	—	80,505	5	10,454	786	2,281
Balance - March 31, 2018	\$ 639,890	\$ 483,986	\$ (266)	32,100,110	\$ 2,140	—	—	\$ 154,030

See accompanying notes to consolidated financial statements.

Table of Contents**BALCHEM CORPORATION****Condensed Consolidated Statements of Cash Flows***(Dollars in thousands)*

(unaudited)

	Three Months Ended March 31, 2019 2018	
Cash flows from operating activities:		
Net earnings	\$18,783	\$19,346
Adjustments to reconcile net earnings to net cash provided by operating activities:		
Depreciation and amortization	10,836	11,127
Stock compensation expense	1,631	1,793
Deferred income taxes	35	(38)
Provision for (recovery of) doubtful accounts	88	(69)
Foreign currency transaction loss	50	51
Asset impairment charge	114	71
Gain on disposal of assets	(2,719)	(1,093)
Changes in assets and liabilities		
Accounts receivable	(912)	(4,340)
Inventories	(139)	(5,442)
Prepaid expenses and other current assets	972	345
Accounts payable and accrued expenses	(12,389)	(2,273)
Income taxes	6,575	5,633
Other	(442)	368
Net cash provided by operating activities	22,483	25,479
Cash flows from investing activities:		
Capital expenditures	(8,488)	(3,735)
Proceeds from insurance	2,727	1,590
Intangible assets acquired	(19)	(119)
Net cash used in investing activities	(5,780)	(2,264)
Cash flows from financing activities:		
Principal payments on revolving loan	(16,000)	—
Principal payments on long-term debt	—	(8,750)
Proceeds from stock options exercised	288	1,261
Dividends paid	(15,135)	(13,421)
Purchase of treasury stock	(727)	(786)
Net cash used in financing activities	(31,574)	(21,696)
Effect of exchange rate changes on cash	(393)	744
(Decrease) increase in cash and cash equivalents	(15,264)	2,263
Cash and cash equivalents beginning of period	54,268	40,416
Cash and cash equivalents end of period	\$39,004	\$42,679
<i>See accompanying notes to condensed consolidated financial statements.</i>		

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

(All dollar amounts in thousands, except share and 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, 2018 consolidated financial statements, and should be read in conjunction with the consolidated financial statements and notes, which appear in the Annual Report on Form 10-K for the year ended December 31, 2018. References in this report to the “Company” mean either Balchem Corporation or Balchem Corporation and its subsidiaries, including SensoryEffects, Inc., SensoryEffects Cereal Systems, Inc., Albion Laboratories, Inc. (formerly known as Albion International, Inc.), BCP Ingredients, Inc., Aberco, Inc., Balchem BV, Balchem Italia Srl, Bioscreen Technologies Srl, Innovative Food Processors, Inc., and Balchem LTD, on a consolidated basis, 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 (“U.S. GAAP” or “GAAP”) governing interim financial statements and the instructions to Form 10-Q and Article 10 of Regulation S-X under the Securities Exchange Act of 1934 (the “Exchange Act”) and therefore do not include some information and notes necessary to conform to annual reporting requirements. The results of operations for the three months ended March 31, 2019 are not necessarily indicative of the operating results expected for the full year or any interim period.

Certain reclassifications have been made to prior period amounts to conform with the current period's presentation.

Recent Accounting Pronouncements

Recently Issued Accounting Standards

In March 2019, the FASB issued ASU 2019-01, “Leases (Topic 842): Codification Improvements,” which further clarifies the determination of fair value of leases and modifies transition disclosure requirements for changes in accounting principles. The effective date of the amendments is for fiscal years beginning after December 15, 2019, and interim periods within those fiscal years. The Company is currently evaluating the impact of this pronouncement on the Company’s consolidated financial statements and disclosures. As stated below, the Company adopted Accounting Standards Codification (“ASC”) 842 (“ASU 2016-02), Leases, as of January 1, 2019.

In August 2018, the FASB issued ASU 2018-15, “Customer’s Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement that is a Service Contract.” The guidance requires implementation costs incurred by customers in cloud computing arrangements to be deferred over the noncancelable term of the cloud computing arrangements plus any optional renewal periods (1) that are reasonably certain to be exercised by the customer or (2) for which exercise of the renewal option is controlled by the cloud service provider. The effective date of this pronouncement is for fiscal years beginning after December 15, 2019, and interim periods within those fiscal years. Early adoption is permitted and the standard may be adopted either using the prospective or retrospective transition approach. The Company is currently evaluating the impact of this pronouncement on the Company’s consolidated financial statements and disclosures.

In August 2018, the FASB issued ASU 2018-14, “Disclosure Framework-Changes to the Disclosure Requirements for Defined Benefit Plans,” which modifies the disclosure requirements for employers that sponsor defined benefit pension or other postretirement benefit plans. The guidance removes disclosures that are no longer considered cost beneficial, clarifies the specific requirements of disclosures and adds disclosure requirements identified as relevant. This update should be applied on a retrospective basis to all periods presented and is effective for fiscal years ending after December 31, 2020. Early adoption is permitted. The Company expects this new guidance will have minimal impact on its financial reporting.

In January 2017, the FASB issued ASU No. 2017-04, “Simplifying the Test for Goodwill Impairment” (ASU 2017-04), which addresses changes to the testing for goodwill impairment by eliminating Step 2 of the process. The guidance is effective for annual and interim goodwill impairment tests in fiscal years beginning after December 15, 2019. Early

adoption is permitted; however, the Company has elected not to adopt early as this ASU will not have a significant impact on the Company's consolidated financial statements.

Recently Adopted Accounting Standards

In February 2016, the FASB issued ASU No. 2016-02, "Leases" ("ASU 2016-02"), which was clarified by ASU 2018-11 and addresses the recognition of assets and liabilities that arise from all leases. The guidance requires lessees to recognize right-of-use assets

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("ROU") and lease liabilities for most leases in the Consolidated Balance Sheets. The guidance is effective for annual and interim periods beginning after December 15, 2018. The Company adopted the new standard on January 1, 2019 and has elected the optional transition method to account for the impact of the adoption with a cumulative-effect adjustment in the period of adoption. The new standard provides a number of optional practical expedients in transition. The Company has elected the "package of practical expedients", which permits it not to reassess under the new standard its prior conclusions about lease identification, lease classification and initial direct costs. The Company has not elected the use-of-hindsight or the practical expedient pertaining to land easements, the latter not being applicable to the Company. The new standard also provides practical expedients for an entity's ongoing accounting. The Company has elected the short-term lease recognition exemption for all leases that qualify, which means for those leases that qualify, the Company will not recognize ROU assets or lease liabilities. The Company has also elected the practical expedient to not separate lease and non-lease components for all of its leases. Refer to Note 19 "Leases."

NOTE 2 – SIGNIFICANT ACQUISITIONS AND DIVESTITURES

The Company did not complete any acquisitions during the three months ended March 31, 2019 or 2018. Total transaction and integration costs related to recent acquisitions, including the subsequent event identified below, are recorded in general and administrative expenses and amounted to \$485 and \$689 for the three months ended March 31, 2019 and 2018, respectively.

Potential Divestiture

As of March 31, 2019, the Company was in negotiations for the sale of an insignificant portion of the Company's business. The transaction is estimated to be completed during 2019 and no gain or loss has been recognized in the Company's condensed consolidated statements of earnings as of March 31, 2019. The related assets and liabilities have been reclassified as current assets held for sale and current liabilities held for sale within the Company's condensed consolidated balance sheets as of March 31, 2019 and include the following:

	March 31, 2019
Accounts receivable	\$353
Inventory	376
Property, plant, and equipment, net	9,314
Right of use assets	317
Goodwill	1,380
Other current assets	8
Assets held for sale	\$11,748
Trade accounts payable	\$126
Accrued expenses	260
Accrued compensation and other benefits	52
Lease liabilities	319
Liabilities held for sale	\$757

Subsequent Event

On May 2, 2019, the Company entered into a securities purchase agreement for the acquisition of Chemogas Holding NV and its Subsidiaries ("Chemogas"), a privately held specialty gases company headquartered in Grimbergen, Belgium, for a purchase price of €95,000, subject to certain adjustments as provided in the definitive agreement. The transaction is subject to customary conditions to closing and will be financed through the Company's Credit Agreement (as defined below) and cash on hand.

Chemogas has been a leader in the packaging and distribution of a wide variety of specialty gases, most notably ethylene oxide, primarily in the European and Asian markets, for medical device sterilization. Through its operational and logistical excellence, Chemogas supports its customers' needs across more than 70 countries. With this

acquisition, Balchem significantly expands its geographic presence in the packaged ethylene oxide market, enabling the Company to offer worldwide service and support to its medical device sterilization customers within the Specialty Products segment. The Chemogas sites in Europe and Asia will form a global network of facilities when combined with Balchem's sites in the United States.

In connection with this transaction, the Company incurred transaction costs of \$307 for the three months ended March 31, 2019, which are included in general and administrative expenses.

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The Company's results for the three months ended March 31, 2019 and 2018 reflected the following stock-based compensation cost, and such compensation cost had the following effects on net earnings:

	Increase/(Decrease) for the Three Months Ended March 31, 2019 2018	
Cost of sales	\$ 288	\$ 245
Operating expenses	1,343	1,548
Net earnings	(1,258)	(1,378)

As allowed by ASC 718, the Company has made an estimate of expected forfeitures based on its historical experience and is recognizing compensation cost only for those stock-based compensation awards expected to vest.

The Company's stock incentive plans allow for the granting of stock awards and options to purchase common stock. Both incentive stock options and nonqualified stock options can be awarded under the plans. No option will be exercisable for longer than ten years after the date of grant. The Company has approved and reserved a number of shares to be issued upon exercise of the outstanding options that is adequate to cover all exercises. As of March 31, 2019, the plans had 1,096,274 shares available for future awards. Compensation expense for stock options and stock awards is recognized on a straight-line basis over the vesting period, generally three years for stock options, three to four years for employee restricted stock awards, three years for employee performance share awards, and three to four years for non-employee director restricted stock awards. Certain awards provide for accelerated vesting if there is a change in control (as defined in the plans) or other qualifying events.

Option activity for the three months ended March 31, 2019 and 2018 is summarized below:

For the three months ended March 31, 2019	Shares (000s)	Weighted Average Exercise Price	Aggregate Intrinsic Value	Weighted Average Remaining Contractual Term
Outstanding as of December 31, 2018	887	\$ 61.59	\$ 16,192	
Granted	185	84.19		
Exercised	(7)	40.85		
Forfeited	—	—		
Canceled	—	—		
Outstanding as of March 31, 2019	1,065	\$ 65.64	\$ 28,924	6.7
Exercisable as of March 31, 2019	685	\$ 56.91	\$ 24,588	5.4
For the three months ended March 31, 2018	Shares (000s)	Weighted Average Exercise Price	Aggregate Intrinsic Value	Weighted Average Remaining Contractual Term
Outstanding as of December 31, 2017	946	\$ 55.44	\$ 24,714	
Granted	148	74.57		
Exercised	(39)	32.83		
Forfeited	(1)	73.49		