MESA LABORATORIES INC /CO
Form 10-Q
November 06, 2017

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 SECURITES EXCHANGE ACT OF 1934

For the quarterly period ended September 30, 2017

TRANSITION REPORT PURSUANT TOSECTION 13 OR 15 (d) OF THE SECURITES EXCHANGE ACT OF 1934

For the transition period from ___ to ___

Commission File No: 0-11740

MESA LABORATORIES, INC.

(Exact name of registrant as specified in its charter)

Colorado	**84-0872291**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification number)

12100 West Sixth Avenue	
Lakewood, Colorado	**80228**
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code: **(303) 987-8000**

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934, during the preceding 12 months (or for such shorter period that the registrant was required to file such reports) and (2) has been subject to such filing requirements for the past 90 days.

Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (Section 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

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

Large accelerated filer	Accelerated filer	Non-accelerated filer (Do not check if a smaller reporting company)	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

Indicate the number of shares outstanding of each of the Issuer's classes of common stock, as of the latest practicable date:

There were 3,779,749 shares of the Issuer's common stock, no par value, outstanding as of October 27, 2017.

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Signatures

Certification of Chief Executive Officer Pursuant to Rule 13a-14(a)
Certification of Chief Financial Officer Pursuant to Rule 13a-14(a)
Certification of Chief Executive Officer Pursuant to Rule 13a-14(b) and 18 U.S.C. Section 1350
Certification of Chief Financial Officer Pursuant to Rule 13a-14(b) and 18 U.S.C. Section 1350

Part I. Financial Information

Item 1. ***Financial Statements***

Mesa Laboratories, Inc.

Condensed Consolidated Balance Sheets

(In thousands, except share amounts)

	September 30, 2017 (Unaudited)	**March 31, 2017**
ASSETS		
Current assets:		
Cash and cash equivalents	$ *10,268*	$*5,820*
Accounts receivable, less allowances of $245 and $252, respectively	*12,187*	*14,319*
Inventories, net	*12,913*	*13,873*
Prepaid income taxes	*2,039*	*587*
Prepaid expenses and other	*1,975*	*1,186*
Assets held for sale	*1,934*	*--*
Total current assets	*41,316*	*35,785*
Property, plant and equipment, net	*23,760*	*26,002*
Intangibles, net	*35,443*	*37,790*
Goodwill	*73,414*	*72,156*
Total assets	$ *173,933*	$*171,733*
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$ *2,036*	$*2,168*
Accrued salaries and payroll taxes	*3,420*	*4,350*
Unearned revenues	*3,805*	*4,117*
Current portion of contingent consideration	*1,165*	*1,294*
Other accrued expenses	*2,649*	*2,999*
Income taxes payable	*--*	*514*
Current portion of long-term debt	*1,375*	*1,125*
Total current liabilities	*14,450*	*16,567*

Deferred income taxes	*3,698*	*3,554*
Long-term debt, net of debt issuance costs and current portion	*50,455*	*53,675*
Contingent consideration	*92*	*116*
Total liabilities	*68,695*	*73,912*
Commitments and Contingencies (Note 8)		
Stockholders' equity:		
Common stock, no par value; authorized 25,000,000 shares; issued and outstanding, 3,779,717 and 3,727,704 shares, respectively	*28,974*	*25,925*
Retained earnings	*76,325*	*73,656*
Accumulated other comprehensive loss	*(61)*	*(1,760)*
Total stockholders' equity	*105,238*	*97,821*
Total liabilities and stockholders' equity	$ *173,933*	$ *171,733*

See accompanying notes to condensed consolidated financial statements.

Mesa Laboratories, Inc.

Condensed Consolidated Statements of Income

(Unaudited)

(In thousands except per share data)

	Three Months Ended September 30,		Six Months Ended September 30,	
	2017	**2016**	**2017**	**2016**
Revenues	$22,954	$24,409	$45,627	$45,523
Cost of revenues	9,721	10,685	19,723	19,785
Gross profit	13,233	13,724	25,904	25,738
Operating expenses				
Selling	2,288	2,694	4,967	5,118
General and administrative	6,412	5,973	13,269	11,953
Research and development	885	1,045	2,038	2,080
Total operating expenses	9,585	9,712	20,274	19,151
Operating income	3,648	4,012	5,630	6,587
Other expense, net	542	800	1,221	1,206
Earnings before income taxes	3,106	3,212	4,409	5,381
Income taxes	753	854	539	1,093
Net income	$2,353	$2,358	$3,870	$4,288
Net income per share:				
Basic	$0.63	$0.64	$1.03	$1.17
Diluted	0.60	0.62	0.98	1.12
Weighted average common shares outstanding:				
Basic	3,764	3,669	3,754	3,657
Diluted	3,935	3,831	3,934	3,816

See accompanying notes to condensed consolidated financial statements.

Mesa Laboratories, Inc.

Condensed Consolidated Statements of Comprehensive Income

(Unaudited)

(In thousands)

	Three Months Ended September 30,		Six Months Ended September 30,	
	2017	**2016**	**2017**	**2016**
Net Income	$*2,353*	$*2,358*	$*3,870*	$*4,288*
Other comprehensive income (loss), net of tax:				
Foreign currency translation	*948*	*(185)*	*1,699*	*(135)*
Total comprehensive income	$*3,301*	$*2,173*	$*5,569*	$*4,153*

See accompanying notes to condensed consolidated financial statements.

Mesa Laboratories, Inc.

Condensed Consolidated Statements of Cash Flows

(Unaudited)

(In thousands)

	Six Months Ended September 30,	
	2017	**2016**
Cash flows from operating activities:		
Net income	$3,870	$4,288
Depreciation and amortization	4,531	4,411
Stock-based compensation	985	841
Amortization of debt issuance costs	55	--
Deferred income taxes	144	138
Foreign currency adjustments	(533)	(28)
Gain on disposition of assets	(116)	--
Adjustment to contingent consideration	300	--
Change in assets and liabilities, net of effects of acquisitions		
Accounts receivable, net	2,132	1,900
Inventories, net	960	(348)
Prepaid expenses and other	(2,241)	(509)
Accounts payable	(132)	661
Accrued liabilities and taxes payable	(1,819)	(5,392)
Unearned revenues	(312)	(39)
Contingent consideration	(456)	(4,594)
Net cash provided by operating activities	7,368	1,329
Cash flows from investing activities:		
Acquisitions	(62)	(3,401)
Proceeds from sale of assets	1,133	--
Purchases of property, plant and equipment	(2,012)	(6,669)
Net cash used in investing activities	(941)	(10,070)
Cash flows from financing activities:		
Proceeds from the issuance of debt	4,000	9,500
Payments on debt	(7,000)	(2,000)
Dividends	(1,201)	(1,169)
Proceeds from the exercise of stock options	2,064	1,767
Net cash (used in) provided by financing activities	(2,137)	8,098
Effect of exchange rate changes on cash and cash equivalents	158	18

Net increase (decrease) in cash and cash equivalents	*4,448*	*(625*)
Cash and cash equivalents at beginning of period	*5,820*	*5,695*
Cash and cash equivalents at end of period	$*10,268*	$*5,070*
Cash paid for:		
Income taxes	$*2,446*	$*3,140*
Interest	*1,007*	*588*
Supplemental non-cash activity:		
Contingent consideration as part of an acquisition	--	*1,822*

See accompanying notes to condensed consolidated financial statements.

Mesa Laboratories, Inc.

Notes to Condensed Consolidated Financial Statements

Note *1* - Description of Business and Summary of Significant Accounting Policies

Description of Business

Mesa Laboratories, Inc. was incorporated under the laws of the State of Colorado on *March 26, 1982.* The terms "we," "us," "our," the "Company" or "Mesa" are used in this report to refer collectively to the parent company and the subsidiaries through which our various businesses are conducted. We pursue a strategy of focusing primarily on quality control products and services, which are sold into niche markets that are driven by regulatory requirements. We prefer markets where we can establish a strong presence and achieve high gross margins. We are organized into *four* divisions across *ten* physical locations. Our Instruments Division designs, manufactures and markets quality control instruments and disposable products utilized in the healthcare, pharmaceutical, food and beverage, medical device, industrial hygiene, environmental air sampling and semiconductor industries. Our Sterilization and Disinfection Control Division (formerly named the Biological Indicators Division) provides testing services, along with the manufacturing and marketing of both biological and cleaning indicators, and the marketing of chemical indicators used to assess the effectiveness of sterilization and disinfection processes in the hospital, dental, medical device and pharmaceutical industries. Our Cold Chain Monitoring Division designs, develops and markets systems which are used to monitor various environmental parameters such as temperature, humidity and differential pressure to ensure that critical storage and processing conditions are maintained in hospitals, pharmaceutical and medical device manufacturers, blood banks, pharmacies and other laboratory and industrial environments. Our Cold Chain Monitoring Division also provides parameter (primarily temperature) monitoring of products during transport in a cold chain and consulting services such as compliance monitoring and validation or mapping of transport and storage containers. Our Cold Chain Packaging Division provides packaging development consulting services and thermal packaging products such as coolers, boxes, insulation materials and phase-change products to control temperature during transport.

Basis of Presentation

The accompanying condensed consolidated balance sheet as of *March 31, 2017,* has been derived from audited consolidated financial statements. The accompanying unaudited interim condensed consolidated financial statements have been prepared on the same basis as our annual audited consolidated financial statements and in accordance with accounting principles generally accepted in the United States ("GAAP") for interim financial information and the rules and regulations of the Securities and Exchange Commission ("SEC") for interim financial statements. In the opinion of management, such unaudited information includes all adjustments (consisting only of normal recurring accruals)

necessary for a fair presentation of this interim information. Operating results and cash flows for interim periods are *not* necessarily indicative of results that can be expected for the entire year. The information included in this report should be read in conjunction with our audited consolidated financial statements and notes thereto included in our Annual Report on Form *10*-K for the year ended *March 31, 2017.*

The summary of our significant accounting policies is incorporated by reference to our Annual Report on Form *10*-K for the year ended *March 31, 2017.*

Recently Issued Accounting Pronouncements

In *May 2014,* the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") *2014-09, Revenue from Contracts with Customers (Topic 606)*, which will replace most existing revenue recognition guidance in U.S. GAAP and is intended to improve and converge with international standards the financial reporting requirements for revenue from contracts with customers. The core principle of ASU *2014-09* is that an entity should recognize revenue for the transfer of goods or services equal to the amount that it expects to be entitled to receive for those goods or services. ASU *2014-09* also requires additional disclosures about the nature, timing and uncertainty of revenue and cash flows arising from customer contracts, including significant judgments and changes in judgments. ASU *2014-09* allows for adoption either on a full retrospective basis to each prior reporting period presented or on a modified retrospective basis with the cumulative effect of initially applying the new guidance recognized at the date of initial application, which will be effective for the Company beginning *April 1, 2018.*

We plan to adopt ASU *2014-09* and its amendments on a modified retrospective basis and are continuing to assess all future impacts of the guidance by reviewing our current contracts with customers to identify potential differences that could result from applying the new guidance. Based on our preliminary review, we expect that the adoption of ASU *2014-09* will *not* have a material impact on our consolidated financial statements. As we complete our overall assessment, we are evaluating our accounting policies and practices, business processes, systems and controls to determine if changes are necessary to support the new revenue recognition and disclosure requirements. Our assessment will be completed during the year ending *March 31, 2018.*

In *January 2017,* the FASB issued ASU *2017-04, Intangibles – Goodwill and Other*, which eliminates the requirement to calculate the implied fair value of goodwill to measure a goodwill impairment charge. ASU *2017-04* is required to be applied prospectively and we elected to early adopt ASU *2017-04* effective *April 1, 2017.* We do *not* anticipate that the adoption will have a significant impact on our consolidated financial statements.

Note *2* - Acquisitions

For the *six* months ended *September 30, 2017,* our acquisitions of businesses totaled *$62,000,* of which *none* were material in nature (see Item *2. Management's Discussion and Analysis of Financial Condition and Results of Operations).*

Note *3* - Inventories

Inventories consist of the following (in thousands):

	September 30, 2017	**March 31, 2017**
Raw materials	$ *10,293*	$ *10,815*
Work-in-process	*464*	*342*
Finished goods	*3,605*	*3,604*
Less: reserve	*(1,449)*	*(888)*
	$ *12,913*	$ *13,873*

Note *4* - Facility Relocation

In *August 2016,* we announced that we planned to shut down both our Omaha and Traverse City biological indicator manufacturing facilities and relocate those operations to the new Bozeman building. The move of those *two* facilities, along with the current Bozeman operations, began in *March 2017* and is estimated to be completed by *June 30, 2018.* We estimate that the total costs of the relocation will be *$2,100,000* (which is comprised primarily of facility moving expenses, retention bonuses for existing personnel and payroll costs for duplicative personnel during the transition period) of which *$725,000* was incurred during the year ended *March 31, 2017.* We incurred *$622,000* in relocation

costs for the *six* months ended *September 30, 2017,* of which *$353,000* and *$269,000* are reflected in cost of revenues and general and administrative expense, respectively in the accompanying condensed consolidated statements of income. Facility relocation costs, which are associated with our Sterilization and Disinfection Control segment, are as follows for the *six* months ended *September 30, 2017:*

Retention bonuses for existing personnel of *$259,000*
Duplicative employment costs of *$97,000*
Moving costs of *$266,000*

Facility relocation amounts accrued and paid for the *six* months ended *September 30, 2017* are as follows (in thousands):

Balance at March 31, 2017	$*673*
Facility relocation expense	*622*
Cash payments	*(570)*
Balance at September 30, 2017	$*725*

In *July 2017,* we completed the move from the Omaha facility and subsequently sold that building for *$1,116,000* (net of commission costs) which resulted in a gain of *$116,000* which is included in other expense, net in the accompanying condensed consolidated statements of net income for the *six* months ended *September 30, 2017.*

In *July 2017,* we put our old Bozeman facility up for sale. The assets associated with this facility are presented on the accompanying condensed consolidated balance sheets as of *September 30, 2017* as assets held for sale.

Note *5* - Long-Term Debt

Long-term debt consists of the following (in thousands):

	September 30, 2017	**March 31, 2017**
Line of credit (3.0% at September 30, 2017)	$ *33,000*	$*35,500*
Term loan (3.0% at September 30, 2017)	*19,250*	*19,750*
Less: discount	*(420)*	*(450)*
Less: current portion	*(1,375)*	*(1,125)*
Long-term portion	$ *50,455*	$*53,675*

On *March 1, 2017,* we entered into a *five*-year agreement (the "Credit Facility") for an *$80,000,000* revolving line of credit ("Line of Credit"), a *$20,000,000* term loan ("Term Loan") and up to *$2,500,000* of letters of credit with a banking syndicate of *four* banks. In addition, the Credit Facility provides a post-closing accordion feature which allows for the Company to request to increase the Line of Credit or Term Loan up to an additional *$100,000,000.* Funds from the Credit Facility *may* be used to pay down the previous credit facility, finance working capital needs and for general corporate purposes in the ordinary course of business (including, without limitation, permitted acquisitions).

Line of Credit and Term Loan indebtedness bears interest at either: (*1*) LIBOR, as defined, plus an applicable margin ranging from *1.5%* to *2.50%;* or (*2*) the alternate base rate ("ABR"), which is the greater of JPMorgan's prime rate or the federal funds effective rate or the overnight bank funding rate plus *0.5%.* We elect the interest rate with each borrowing under the line of credit. In addition, there is an unused line fee of *0.15%* to *0.35%.* Letter of credit fees are based on the applicable LIBOR rate.

The Term Loan requires *20* quarterly principal payments (the *first* due date was *March 31, 2017)* in the amount of *$250,000* (increasing by *$125,000* each year up to *$750,000* in the *fifth* year). The remaining balance of principal and accrued interest are due on *March 1, 2022.*

The Credit Facility is secured by all of our assets and requires us to maintain a ratio of funded debt to our trailing *four* quarters of EBIDTA (the "Leverage Ratio"), as defined, of less than *3.0* to *1.0,* provided that, we *may* once during the term of the Credit Facility, in connection with a Permitted Acquisition for which the aggregate consideration paid or to be paid in respect thereof equals or exceeds *$20,000,000,* elect to increase the maximum Leverage Ratio permitted hereunder to (i) *3.50* to *1.00* for a period of *four* consecutive fiscal quarters commencing with the fiscal quarter in

which such Permitted Acquisition occurs (the "Initial Holiday Period") and (ii) *3.25* to *1.00* for the period of *four* consecutive fiscal quarters immediately following the Initial Holiday Period. The Credit Facility also requires us to maintain a minimum fixed charge coverage ratio of less than *1.25* to *1.0.* We were compliant with the required covenants at *September 30, 2017.*

We incurred origination and debt issuance costs of *$460,000* which are treated as a debt discount and are netted against amounts outstanding on the condensed consolidated balance sheets.

As of *September 30, 2017,* future contractual maturities of debt as are as follows (in thousands):

Year Ending March 31,	
2018	$*625*
2019	*1,625*
2020	*2,125*
2021	*2,625*
2022	*45,250*
	$*52,250*

In *October 2017,* we made a *$1,000,000* payment under our Line of Credit and a draw of *$7,000,000.*

Note *6* - Stock-Based Compensation

Amounts recognized in the condensed consolidated financial statements related to stock-based compensation are as follows (in thousands, except per share data):

	Three Months Ended		Six Months Ended	
	September 30,		September 30,	
	2017	2016	2017	2016
Total cost of stock-based compensation charged against income before income taxes	$*445*	$*412*	$*985*	$*841*
Amount of income tax benefit recognized in earnings	*108*	*110*	*120*	*171*
Amount charged against net income	$*337*	$*302*	$*865*	$*670*
Impact on net income per common share:				
Basic	$*0.09*	$*0.08*	$*0.23*	$*0.18*
Diluted	*0.09*	*0.08*	$*0.22*	*0.18*

Stock-based compensation expense is included in cost of revenues, selling, and general and administrative expense in the accompanying condensed consolidated statements of income.

The fair value of each stock option grant is estimated on the date of grant using the Black-Scholes option-pricing model ("Black-Scholes"). We use historical data to estimate the expected price volatility, the expected stock option life and expected forfeiture rate. The risk-free interest rate is based on the United States Treasury yield curve in effect at the time of grant for the estimated life of the stock option. The dividend yield is calculated based upon the dividend payments made during the prior *four* quarters as a percent of the average stock price for that period.

The following is a summary of stock option activity for the *six* months ended *September 30, 2017:*

	Number of Shares	Weighted-Average Exercise	Weighted-Average Remaining	Aggregate Intrinsic Value (000s)

		Price per Share	Contractual Term	
Outstanding at March 31, 2017	*510,361*	$ *75.78*	*5.0*	$ *23,956*
Stock options granted	*95,605*	*123.09*	*5.5*	
Stock options forfeited	*(40,661)*	*93.74*	*5.1*	
Stock options expired	*(96)*	*97.78*	*4.5*	
Stock options exercised	*(50,503)*	*61.09*	*--*	
Outstanding at September 30, 2017	*514,706*	*84.58*	*4.8*	$ *33,320*
Exercisable at September 30, 2017	*162,831*	*60.05*	*4.0*	$ *14,536*

The total intrinsic value of stock options exercised was *$4,181,318* and *$3,218,000* for the *six* months ended *September 30, 2017* and *2016,* respectively.

A summary of the status of our unvested stock option shares as of *September 30, 2017,* is as follows:

	Number of Shares	Weighted-Average Grant-Date Fair Value
Unvested at March 31, 2016	*373,766*	$ *22.49*
Stock options granted	*95,605*	*39.00*
Stock options forfeited	*(40,661)*	*26.84*
Stock options vested	*(76,835)*	*20.93*
Unvested at September 30, 2017	*351,875*	*28.41*

As of *September 30, 2017,* there was *$7,860,927* of total unrecognized compensation expense related to unvested stock options. As of *September 30, 2017,* we have *740,379* shares available for future stock option grants.

Note *7* - Net Income Per Share

Basic net income per share is computed by dividing net income by the weighted-average number of common shares outstanding during the reporting period. Diluted net income per share is computed similarly to basic net income per share, except that it includes the potential dilution that could occur if dilutive securities were exercised.

The following table presents a reconciliation of the denominators used in the computation of net income per share - basic and diluted (in thousands, except per share data):

	Three Months Ended September 30,		**Six Months Ended September 30,**	
	2017	**2016**	**2017**	**2016**
Net income available for shareholders	$*2,353*	$*2,358*	$*3,870*	$*4,288*
Weighted average outstanding shares of common stock	*3,764*	*3,669*	*3,754*	*3,657*
Dilutive effect of stock options	*171*	*162*	*180*	*159*
Common stock and equivalents	*3,935*	*3,831*	*3,934*	*3,816*
Net income per share:				
Basic	$*0.63*	$*0.64*	$*1.03*	$*1.17*
Diluted	*0.60*	*0.62*	*0.98*	*1.12*

For both the *three* and *six* months ended *September 30, 2017, 111,000* outstanding stock options were excluded from the calculation of diluted net income per share because their inclusion would have been anti-dilutive.

For the *three* and *six* months ended *September 30, 2016, 112,000* and *120,000* outstanding stock options, respectively, were excluded from the calculation of diluted net income per share because their inclusion would have been anti-dilutive.

Note *8* - Commitments and Contingencies

Under the terms of the PCD Agreement, we are required to pay contingent consideration if the cumulative revenues for our process challenge device business for the *three* years subsequent to the acquisition meet certain levels. The

potential consideration payable ranges from *$0* to *$1,500,000* and is based upon a sliding scale of *three*-year cumulative revenues between *$9,900,000* and *$12,600,000*, with payments made annually. Based upon both historical and projected growth rates, we initially recorded *$300,000* of contingent consideration payable which represented our best estimate of the amount that would ultimately be paid. We paid *$150,000* of the contingent consideration during the year ended *March 31, 2016 (*based upon the then current run rate projected over the entire *three*-year contingent consideration period).

Since the initial payment, the revenues for these products have significantly increased and as a result, during the year ended *March 31, 2017* we recorded an additional *$450,000* accrual (which was paid in our *third* quarter ending *December 31, 2016.).* During the *three* months ended *June 30, 2017* revenues continued to increase and after revising our forecast for the process challenge device ("PCD") product revenues through the end of the earn-out period, we recorded an additional *$300,000* accrual, which is included in other income, net in the accompanying condensed consolidated statement of income for the *six* months ended *September 30, 2017.* The remaining contingent consideration amount is also subject to additional modification at the end of the *third* year of the earn-out period (*October 2017)* based upon the actual revenues earned over the contingent consideration period. Any changes to the contingent consideration ultimately paid will result in additional income or expense in our condensed consolidated statements of income. We will continue to monitor the results of our PCD business and we will adjust the contingent liability on a go forward basis, based on then current information.

Note *9* - Comprehensive Income

The following table summarizes the changes in each component of accumulated other comprehensive income ("AOCI"), net of tax (in thousands):

	Foreign Currency Translation	AOCI
Balance at June 30, 2017	$ *(1,009)*	$*(1,009)*
Quarter ended September 30, 2017:		
Unrealized gain arising during the period	*948*	*948*
Balance at September 30, 2017	$ *(61)*	$*(61)*

	Foreign Currency Translation	AOCI
Balance at June 30, 2016	$ *(1,101)*	$*(1,101)*
Quarter ended September 30, 2016:		
Unrealized loss arising during the period	*(185)*	*(185)*
Balance at September 30, 2016	$ *(1,286)*	$*(1,286)*

	Foreign Currency Translation	AOCI
Balance at March 31, 2017	$ *(1,760)*	$*(1,760)*
Six months ended September 30, 2017:		
Unrealized gain arising during the period	*1,699*	*1,699*
Balance at September 30, 2017	$ *(61)*	$*(61)*

	Foreign Currency Translation	AOCI
Balance at March 31, 2016	$ *(1,151)*	$*(1,151)*
Six months ended September 30, 2016:		
Unrealized loss arising during the period	*(135)*	*(135)*
Balance at September 30, 2016	$ *(1,286)*	$*(1,286)*

Note *10* - Segment Information

We have *four* reporting segments: Sterilization and Disinfection Control (formerly named Biological Indicators), Instruments, Cold Chain Monitoring and Cold Chain Packaging. The following tables set forth our segment information (in thousands):

	Three Months Ended September 30, 2017				
	Sterilization and Disinfection Control	Instruments	Cold Chain Monitoring	Cold Chain Packaging	Total
Revenues	$*9,985*	$ *7,983*	$ *3,151*	$ *1,835*	$*22,954*
Gross profit	$*6,822*	$ *4,963*	$ *1,193*	$ *255*	*13,233*
Reconciling items [1]					*(10,127)*
Earnings before income taxes					$*3,106*

	Three Months Ended September 30, 2016				
	Sterilization and Disinfection Control	Instruments	Cold Chain Monitoring	Cold Chain Packaging	Total
Revenues	$*8,897*	$ *8,693*	$ *3,545*	$ *3,274*	$*24,409*
Gross profit	$*5,833*	$ *5,326*	$ *1,657*	$ *908*	*13,724*
Reconciling items [1]					*(10,512)*
Earnings before income taxes					$*3,212*

	Six Months Ended September 30, 2017	
	Sterilization and	Total

	Disinfection		Cold Chain	Cold Chain	
	Control	Instruments	Monitoring	Packaging	
Revenues	$*20,168*	$ *16,586*	$ *6,068*	$ *2,805*	$*45,627*
Gross profit	$*13,542*	$ *9,871*	$ *2,087*	$ *404*	*25,904*
Reconciling items [1]					*(21,495)*
Earnings before income taxes					$*4,409*

	Six Months Ended September 30, 2016				
	Sterilization and Disinfection		Cold Chain	Cold Chain	Total
	Control	Instruments	Monitoring	Packaging	
Revenues	$*18,364*	$ *16,915*	$ *5,862*	$ *4,382*	$*45,523*
Gross profit	$*11,920*	$ *10,175*	$ *2,324*	$ *1,319*	*25,738*
Reconciling items [1]					*(20,357)*
Earnings before income taxes					$*5,381*

(*1*) Reconciling items include selling, general and administrative, research and development, and other expenses

	September 30, 2017	March 31, 2017
Total assets (in thousands):		
Sterilization and Disinfection Control	$ *67,374*	$*67,233*
Instruments	*34,729*	*40,805*
Cold Chain Monitoring	*34,206*	*35,789*
Cold Chain Packaging	*21,763*	*20,313*
Corporate and administrative	*15,861*	*7,593*
	$ *173,933*	$*171,733*

All long-lived assets are located in the United States except for *$5,730,000* and *$21,968,000* which are associated with our French and Canadian subsidiaries, respectively.

Revenues from external customers are attributed to individual countries based upon locations to which the product is shipped or exported, as follows (in thousands):

	Three Months Ended		Six Months Ended	
	September 30,		September 30,	
	2017	2016	2017	2016
Net revenues from unaffiliated customers:				
United States	$*14,432*	$*15,403*	$*27,443*	$*30,914*
Foreign	*8,522*	*9,006*	*18,184*	*14,609*
	$*22,954*	$*24,409*	$*45,627*	$*45,523*

No foreign country exceeds *10* percent of total revenues.

Note *11* - Income Taxes

For interim income tax reporting, we estimate our annual effective tax rate and apply this effective tax rate to our year to date pre-tax income. Each quarter, the estimate of the annual effective tax rate is updated, and if the estimated effective tax rate changes, a cumulative adjustment is made. There is a potential for volatility of the effective tax rate due to several factors, including changes in the mix of pre-tax income and the jurisdictions to which it relates, changes in tax laws and foreign tax holidays, the impact of excess tax benefits and deficiencies associated with share-based payment awards to employees, settlements with taxing authorities and foreign currency fluctuations.

Our effective income tax rate was *24.2* percent and *26.6* percent for the *three* months ended *September 30, 2017* and *2016,* respectively, and *12.2* percent and *20.3* percent for the *six* months ended *September 30, 2017* and *2016,* respectively. The effective tax rate for the *three* and *six* months ended *September 30, 2017* differed from the statutory federal rate of *34* percent primarily due to the impact of share-based payment awards for employees (which was significant for the *three* and *six* months ended *September 30, 2017),* state income taxes, domestic manufacturing deductions and foreign rate differential. We anticipate that our effective tax rate for the year ending *March 31, 2018* will approximate *36* percent to *39* percent, plus or minus the impact of excess tax benefits and deficiencies associated with share-based payment awards to employees (which *may* vary significantly from year to year).

Since we are subject to audit by various taxing authorities, it is reasonably possible that the amount of unrecognized tax benefits will change during the next *12* months. However, we do *not* expect the change, if any, to have a material effect on our financial condition or results of operations within the next *12* months.

Note *12* - Subsequent Event

In *October 2017,* our Board of Directors declared a quarterly cash dividend of *$0.16* per share of common stock, payable on *December 15, 2017,* to shareholders of record at the close of business on *November 30, 2017.*

Item 2. ***Management's Discussion and Analysis of Financial Condition and Results of Operations***

Forward Looking Statements

This report contains information that may constitute "forward-looking statements." Generally, the words "believe," "estimate," "expect," "project," "anticipate," "intend," "will" and similar expressions identify forward-looking statements, which generally are not historical in nature. However, the absence of these words or similar expressions does not mean that a statement is not forward-looking. All statements that address operating performance, events or developments that we expect or anticipate will occur in the future — including statements relating to revenues growth and statements expressing general views about future operating results — are forward-looking statements. Management believes that these forward-looking statements are reasonable as and when made. However, caution should be taken not to place undue reliance on any such forward-looking statements because such statements speak only as of the date when made. We undertake no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events or otherwise, except as required by law. In addition, forward-looking statements are subject to certain risks and uncertainties that could cause actual results to differ materially from our historical experience and our present expectations or projections. These risks and uncertainties include, but are not limited to those described in Part II, "Item 1A. Risk Factors" and elsewhere in this report and in our Annual Report on Form 10-K for the year ended March 31, 2017, and those described from time to time in our subsequent reports filed with the Securities and Exchange Commission.

General Discussion

We pursue a strategy of focusing primarily on quality control products and services, which are sold into niche markets that are driven by regulatory requirements. We prefer markets where we can establish a strong presence and achieve high gross margins. We are organized into four divisions across ten physical locations. Our Instruments Division designs, manufactures and markets quality control instruments and disposable products utilized in the healthcare, pharmaceutical, food and beverage, medical device, industrial hygiene, environmental air sampling and semiconductor industries. Our Sterilization and Disinfection Control Division provides testing services, along with the manufacturing and marketing of both biological and cleaning indicators, and the marketing of chemical indicators used to assess the effectiveness of sterilization and disinfection processes in the hospital, dental, medical device and pharmaceutical industries. Our Cold Chain Monitoring Division designs, develops and markets systems which are used to monitor various environmental parameters such as temperature, humidity and differential pressure to ensure that critical storage and processing conditions are maintained in hospitals, pharmaceutical and medical device manufacturers, blood banks, pharmacies and other laboratory and industrial environments. Our Cold Chain Monitoring Division also provides parameter (primarily temperature) monitoring of products during transport in a cold chain and consulting services such as compliance monitoring and validation or mapping of transport and storage containers. Our Cold Chain Packaging Division provides packaging development consulting services and thermal packaging products such as coolers, boxes, insulation materials and phase-change products to control temperature during transport.

Our revenues come from two main sources – product sales and services. Product sales are dependent on several factors, including general economic conditions, both domestic and international, customer capital spending trends, competition, introduction of new products and acquisitions. Sterilization and Disinfection and Control products and many of the packaging products of our Cold Chain Packaging Division are disposable and are used on a routine basis, thus product sales are less sensitive to general economic conditions. Instrument products and cold chain monitoring systems and products have a longer life, and their purchase by our customers is somewhat discretionary, so sales are more sensitive to general economic conditions. Service demand is driven by our customers' quality control and regulatory environments, which require periodic repair and recalibration or certification of our instrument products and cold chain monitoring systems. We typically evaluate costs and pricing annually. Our policy is to price our products competitively and, where possible, we pass along cost increases in order to maintain our margins.

Gross profit is affected by our product mix, manufacturing efficiencies and price competition. Historically, as we have integrated our acquisitions and taken advantage of manufacturing efficiencies, our gross margins for some products have improved. There are, however, differences in gross margin percentages between product lines, and ultimately the mix of sales will continue to impact our overall gross margin.

Selling expense is driven primarily by labor costs, including salaries and commissions. Accordingly, it may vary with sales levels. Labor costs and amortization of intangible assets drive the substantial majority of general and administrative expense. Research and development expense is predominantly comprised of labor costs and third-party consultants.

Year Ending March 31, 2018 Acquisitions

During the year ending March 31, 2018, we completed the following two acquisitions (the “2018 Acquisitions”):

In October 2017, we completed a business combination (the “Simicon Acquisition”) whereby we acquired the common stock of SIMICON GMBH (“Simicon”), a company whose business manufactures both biological and cleaning indicators.

In May 2017, we completed a business combination (the “Hucker Acquisition”) whereby we acquired substantially all of the assets (other than cash and accounts receivable) and certain liabilities of Hucker & Hucker GmbH’s (“Hucker”) business segment associated with the distribution of our biological indicator products.

Year Ended March 31, 2017 Acquisitions

During the year ended March 31, 2017, we completed the following six acquisitions (the “2017 Acquisitions”):

In November 2016, we completed a business combination (the “Mydent Acquisition”) whereby we acquired substantially all of the assets (other than cash and accounts receivable) and certain liabilities of Mydent International Corp’s business segment associated with biological indicator mail-in testing services to the dental market in the United States;

In November 2016, we completed a business combination (the “FreshLoc Acquisition”) whereby we acquired substantially all of the assets (other than cash and accounts receivable) and certain liabilities of the cold chain monitoring business of FreshLoc Technologies, Inc.;

In August 2016, we completed a business combination (the “Rapid Aid Acquisition”) whereby we acquired certain assets (consisting primarily of fixed assets) and certain liabilities of Rapid Aid Corp’s (“Rapid Aid”) business segment associated with the manufacture and sale of cold chain packaging gel products;

In July 2016, we completed a business combination (the "HANSAmed Acquisition") whereby we acquired substantially all of the assets (other than cash and accounts receivable) and certain liabilities of HANSAmed Limited's ("HANSAmed") business segment associated with the distribution of our biological indicator products and mail-in testing services to the dental market in Canada;

In April 2016, we completed a business combination (the "ATS Acquisition") whereby we acquired substantially all the assets (other than cash and certain inventories and fixed assets) and certain liabilities of Autoclave Testing Services, Inc. and Autoclave Testing Supplies, Inc., (collectively, "ATS"). ATS was in the business of supplying products and services for dental sterilizer testing in both the U.S. and Canada; and

In April 2016, we completed a business combination (the "Pulse Acquisition") whereby we acquired substantially all of the assets (other than cash and accounts receivable) and certain liabilities of Pulse Scientific, Inc.'s ("Pulse") business segment associated with the distribution of our biological indicator products.

General Trends and Outlook

Our strategic objectives include growth both organically and through further acquisitions. During the year ending March 31, 2018, we continue to build our infrastructure to prepare for future growth, including the relocation of our Omaha, Traverse City and old Bozeman biological indicator manufacturing facilities into the new Bozeman building, the addition of key personnel to our operations, sales and marketing, and research and development teams and the rollout of phase three of our ERP implementation project (European operations).

The markets for sterilization and disinfection control products and cold chain packaging products remain strong, as the disposable nature of these products makes them less sensitive to general economic conditions. The worldwide market for sterilization and disinfection control products is growing as more countries focus on verifying the effectiveness of sterilization and disinfection processes.

In general, our instruments products and cold chain services and monitoring systems are more impacted by general economic conditions than our sterilization and disinfection control and cold chain packaging products. As a result, uncertainty about global economic conditions may cause businesses to postpone spending in response to tighter credit, unemployment, negative financial news and/or declines in income or asset values. Worldwide and regional economic conditions could also reduce the demand for our products and services, as our customers reduce or delay capital equipment and other types of purchases. However, demand for our instruments products, and cold chain services and monitoring systems remains solid and we strive to continue to grow revenues going forward.

We are working on several research and development projects that, if completed, may result in new products for both existing customers and new markets. We are hopeful that we will have new products available for sale in the coming

year.

Overall organic revenues decline for the three months ended September 30, 2017 was seven percent resulting from organic decreases of eight percent, 21 percent and 44 percent from the Instruments, Cold Chain Monitoring and Cold Chain Packaging Divisions, respectively, partially offset by an increase of 12 percent for the Sterilization and Disinfection Control Division. Overall organic revenues decline for the six months ended September 30, 2017 was one percent resulting from organic decreases of two percent, eight percent and 36 percent from the Instruments, Cold Chain Monitoring and Cold Chain Packaging Divisions, respectively, partially offset by an increase of 10 percent for the Sterilization and Disinfection Control Division

Due to the recent introduction of new or modified products and the consolidation of other product sets, during the three months ended June 30, 2017, we elected to discontinue for sale certain products in our Instruments, Cold Chain Monitoring and Sterilization and Disinfection Control Divisions. As part of this process, we analyzed the remaining inventories associated with these products to determine future usability, which resulted in an increase in our inventory reserve for these products of $406,000. Overall gross margin percentage for the six months ended September 30, 2017 was 57 percent but would have been 58 percent without the impact of this additional inventory reserve.

During the six months ended September 30, 2017 our Cold Chain Packaging segment lost the business of one of our larger customers. Additionally, we determined that current year revenues from our largest customer will be significantly decreased as compared to revenues from the same customer for the year ended March 31, 2017. As a result of these two factors and the significant time involved in the sales-cycle for this product set, we believe that revenues for this segment will now be approximately $2,000,000 to $3,000,000 lower for the year ending March 31, 2018 as compared to the year ended March 31, 2017. In addition, the lower revenues will also lead to lower gross margin percentages as a certain portion of the cost of revenues are personnel and warehousing costs which are primarily fixed and as a result, fluctuations in revenues significantly impact the gross profit margin percentage. We are currently evaluating this segment to determine the likelihood that the revenues from our largest customer will return to prior levels going forward, to determine how confident we are in our ability to grow the business in the future through new customer acquisition, and to determine what cost cutting measures can be implemented, if any, to increase the related gross margin percentage. We are hopeful to have these evaluations substantially completed by December 31, 2017, and depending on the findings, it is possible that we may determine that it is more likely than not that this segment is impaired. If we are required to perform an impairment analysis, any resulting impairment charge most likely will be material to our results of operations in the period in which it is recorded.

Results of Operations

The following table sets forth, for the periods indicated, condensed consolidated statements of income data. The table and the discussion below should be read in conjunction with the accompanying condensed consolidated financial statements and the notes thereto appearing elsewhere in this report (in thousands, except percent data):

					Percent			

	Three Months Ended September 30,			
	2017	2016	Change	Change
Revenues	$22,954	$24,409	$(1,455)	(6)%
Cost of revenues	9,721	10,685	(964)	(9)%
Gross profit	$13,233	$13,724	$(491)	(4)%
Gross profit margin	58%	56%	2%	
Operating expenses				
Selling	$2,288	$2,694	$(406)	(15)%
General and administrative	6,412	5,973	439	7%
Research and development	885	1,045	(160)	(15)%
	$9,585	$9,712	$(127)	(1)%
Operating income	$3,648	$4,012	$(364)	(9)%
Net income	2,353	2,358	(5)	--%
Net profit margin	10%	10%	--%	

	Six Months Ended September 30,			Percent
	2017	2016	Change	Change
Revenues	$45,627	$45,523	$ 104	-- %
Cost of revenues	19,723	19,785	(62)	-- %
Gross profit	$25,904	$25,738	$ 166	1 %
Gross profit margin	57 %	57 %	-- %	
Operating expenses				
Selling	$4,967	$5,118	$ (151)	(3)%
General and administrative	13,269	11,953	1,316	11 %
Research and development	2,038	2,080	(42)	(2)%
	$20,274	$19,151	$ 1,123	6 %
Operating income	$5,630	$6,587	$ (957)	(15)%
Net income	3,870	4,288	(418)	(10)%
Net profit margin	8 %	9 %	(1)%	

Revenues

The following table summarizes our revenues by source (in thousands, except percent data):

	Three Months Ended September 30,			Percent
	2017	2016	Change	Change
Sterilization and Disinfection Control	$9,985	$8,897	$ 1,088	12 %
Instruments	7,983	8,693	(710)	(8)%
Cold Chain Monitoring	3,151	3,545	(394)	(11)%
Cold Chain Packaging	1,835	3,274	(1,439)	(44)%
Total	$22,954	$24,409	$ (1,455)	(6)%

	Six Months Ended September 30,			Percent
	2017	2016	Change	Change
Sterilization and Disinfection Control	$20,168	$18,364	$ 1,804	10 %
Instruments	16,586	16,915	(329)	(2)%
Cold Chain Monitoring	6,068	5,862	206	4 %
Cold Chain Packaging	2,805	4,382	(1,577)	(36)%
Total	$45,627	$45,523	$ 104	-- %

Three and six months ended September 30, 2017 versus September 30, 2016

Sterilization and Disinfection Control revenues for the three and six months ended September 30, 2017 increased primarily due to organic growth of 12 percent and 10 percent, respectively which was achieved through existing customers, expansion into new markets, price increases and the continued strengthening of the Euro.

Instruments revenues for the three and six months ended September 30, 2017 decreased due to organic decreases of eight percent and two percent, respectively. The decrease for the three months ended September 30, 2017 is primarily due to the slower than expected adoption of an updated medical product and the discontinuation of its predecessor and the timing of orders between the first and second quarters of our year ending March 31, 2018.

Cold Chain Monitoring revenues for the three months ended September 30, 2017 decreased due to organic decreases of 21 percent, partially offset by revenues related to the FreshLoc Acquisition. Cold Chain Monitoring revenues for the six months ended September 30, 2017 increased primarily due to the FreshLoc Acquisition, partially offset by organic decreases of eight percent. Revenues in this division fluctuate quarter over quarter due to the timing of customer acceptance of certain installations and the nature and timing of orders within any given quarter.

Cold Chain Packaging revenues for the three and six months ended September 30, 2017 decreased due to organic decreases of 44 percent and 36 percent, respectively. The decreases were primarily due to a lower order rate based on timing issues with our largest customer (which accounted for approximately half of division revenues for the year ended March 31, 2017) and longer than expected sales cycles. See *General Trends and Outlook* above for additional discussion.

Gross Profit

The following summarizes our gross profit by segment (in thousands, except percent data):

	Three Months Ended September 30,			Percent
	2017	**2016**	**Change**	**Change**
Sterilization and Disinfection Control	$6,822	$5,833	$ 989	17 %
Gross profit margin	68 %	66 %	2 %	
Instruments	4,963	5,326	(363)	(7)%
Gross profit margin	62 %	61 %	1 %	
Cold Chain Monitoring	1,193	1,657	(464)	(28)%
Gross profit margin	38 %	47 %	(9)%	
Cold Chain Packaging	255	908	(653)	(72)%
Gross profit margin	14 %	28 %	(14)%	
Total gross profit	$13,233	$13,724	$ (491)	(4)%
Gross profit margin	58 %	56 %	2 %	

	Six Months Ended September 30,			Percent
	2017	**2016**	**Change**	**Change**
Sterilization and Disinfection Control	$13,542	$11,920	$ 1,622	14 %
Gross profit margin	67 %	65 %	2 %	
Instruments	9,871	10,175	(304)	(3)%
Gross profit margin	60 %	60 %	-- %	
Cold Chain Monitoring	2,087	2,324	(237)	(10)%
Gross profit margin	34 %	40 %	(6)%	
Cold Chain Packaging	404	1,319	(915)	(69)%
Gross profit margin	14 %	30 %	(16)%	
Total gross profit	$25,904	$25,738	$ 166	1 %
Gross profit margin	57 %	57 %	-- %	

Three and six months ended September 30, 2017 versus September 30, 2016

Sterilization and Disinfection Control gross profit margin percentage increased for the three and six months ended September 30, 2017 primarily due to volume based efficiencies associated with increased revenues and the impact of using internally manufactured biological indicators for our dental sterilizer testing business as opposed to the prior year where we were contractually committed to purchase a significant portion of those biological indicators from an outside supplier at a significantly higher price, partially offset by $353,000 of facility relocation costs (see Note 4 in Item 1. Financial Statements).

Instruments gross margin percentage increased for the three months ended September 30, 2017 primarily due to product and service mix, partially offset by the loss of certain volume based efficiencies associated with the decrease in revenues. Instruments gross margin percentage was flat for the six months ended September 30, 2017 primarily due to a $163,000 increase in the related inventory reserve due to the decision to discontinue for sale certain instruments products and the loss of certain volume based efficiencies associated with the decrease in revenues.

Cold Chain Monitoring gross profit margin percentage decreased for the three months ended September 30, 2017 primarily due to product and service mix and the loss of certain volume based efficiencies associated with the decrease in revenues. Cold Chain Monitoring gross profit margin percentage decreased for the six months ended September 30, 2017 primarily due to a $216,000 increase in the related inventory reserve due to the decision to discontinue for sale certain Cold Chain Monitoring products and product and service mix.

Cold Chain Packaging gross profit margin percentage for the three and six months ended September 30, 2017 decreased primarily due to lower revenues. A certain portion of the cost of revenues are personnel and warehousing costs which are primarily fixed and as a result, fluctuations in revenues significantly impact the gross profit margin percentage for this division. See *General Trends and Outlook* above for additional discussion.

Operating Expenses

Operating expenses for the three and six months ended September 30, 2017 (decreased) increased as compared to the prior year as follows (in thousands):

	Increase (Decrease)	
	Three Months Ended September 30, 2017	**Six Months Ended September 30, 2017**
Selling	$(406)	$ (151)
General and administrative		
Personnel	166	769
Employee moving	--	307
Acquisition related	220	268
Depreciation	(25)	135
Property taxes	70	140
Professional services	80	(131)
Other, net	(72)	(172)
	439	1,316
Research and development	(160)	(42)
Operating expenses	$(127)	$ 1,123

Selling

Three and six months ended September 30, 2017 versus September 30, 2016

Selling expense for the three and six months ended September 30, 2017 decreased primarily due to reductions of selling personnel, trade show activities and outside commissions. As a percentage of revenues, selling expense was 10 percent and 11 percent for the three and six months ended September 30, 2017, respectively as compared to 11 percent for both the three and six months ended September 30, 2016.

Historically selling expense approximates 10 percent to 12 percent of revenues.

General and Administrative

Three and six months ended September 30, 2017 versus September 30, 2016

General and administrative expenses for the three months ended September 30, 2017 increased primarily due to increased personnel, acquisition related, property taxes and professional services expenses.

General and administrative expenses for the six months ended September 30, 2017 increased primarily due to increased personnel, employee moving, acquisition related, depreciation and property taxes expenses, partially offset by decreases in professional services.

Research and Development

Three and six months ended September 30, 2017 versus September 30, 2016

Research and development expenses for the three and six months ended September 30, 2017 decreased due to a decrease in engineers and materials and supplies necessary to support existing businesses during the three months ended September 30, 2017.

Other Expense

Other expense for the three months ended September 30, 2017 is comprised primarily of interest expense associated with our Credit Facility, partially offset by a $116,000 gain from the sale of our Omaha facility.

Other expense for the six months ended September 30, 2017 is comprised primarily of interest expense associated with our Credit Facility and $300,000 related to an additional accrual for the PCD earn-out (see Liquidity and Capital Resources for additional discussion), partially offset by a $116,000 gain from the sale of our Omaha facility.

Net Income

Our income tax rate varies based upon many factors but in general, we anticipate that on a go forward basis, our effective tax rate will approximate 36 percent to 39 percent, plus or minus the impact of excess tax benefits and deficiencies associated with share-based payment awards to employees. The excess tax benefits and deficiencies associated with share-based payment awards to our employees have caused and, in the future, may cause large fluctuations in our realized effective tax rate based on the timing, volume, and nature of stock options exercised under our share-based payment program. Net income for the six months ended September 30, 2017 was significantly impacted by $622,000 of facility relocation costs (see Liquidity and Capital Resources), $300,000 in PCD earn-out accruals, $307,000 of employee moving expenses, a $406,000 expense related to a reserve for inventory due to operational decisions to end of life certain products and a lower effective tax rate due to the volume and nature of stock option exercises that generated a significant excess tax benefit. Otherwise, net income for the six months ended September 30, 2017 varied with the changes in revenues, gross profit and operating expenses (which includes $3,228,000 of non-cash amortization of intangible assets).

Liquidity and Capital Resources

Our sources of liquidity include cash generated from operations, working capital, capacity under our Credit Facility and potential equity and debt offerings. We believe that cash generated from these sources will be sufficient to meet our short-term and long-term needs. Our more significant uses of resources include quarterly dividends to shareholders, payment of debt obligations, long-term capital equipment expenditures and potential acquisitions.

Due to continued organic and acquisition related growth, we outgrew the capacity of our current building in Bozeman, Montana and as a result, we built a new facility in the same general area. Construction began in July 2015 and was completed in September 2017. We spent $17,650,000 on the development of the building and the related land, which

is included in property, plant and equipment, net on the accompanying condensed consolidated balance sheets.

In August 2016, we announced that we plan to shut down both our Omaha and Traverse City Biological Indicator manufacturing facilities and relocate those operations to the new Bozeman building. The move of these two facilities, along with the current Bozeman operations, began in March 2017 and is estimated to be completed by June 30, 2018. We estimate that the total costs of the relocation will be $2,100,000 (which is comprised primarily of facility moving expenses, retention bonuses for existing personnel and payroll costs for duplicative personnel during the transition period) of which $725,000 was incurred during the year ended March 31, 2017 and $622,000 was incurred during the six months ended September 30, 2017, which is reflected in cost of revenues in the accompanying condensed consolidated statements of income (other than $269,000 which is included in general and administrative).

In July 2017, we completed the move from the Omaha facility and subsequently sold that building for $1,116,000 (net of commission costs). After completing the move of the old Bozeman facility, we expect to be able to sell that building for approximately $2,500,000.

Working capital is the amount by which current assets exceed current liabilities. We had working capital of $26,866,000 and $19,218,000 respectively, at September 30, 2017 and March 31, 2017.

On March 1, 2017, we entered into a five-year agreement (the “Credit Facility”) for a $80,000,000 revolving line of credit (“Line of Credit”), a $20,000,000 term loan (“Term Loan”) and up to $2,500,000 of letters of credit with a banking syndicate comprised of four banks. In addition, the Credit Facility provides a post-closing accordion feature which allows the Company to request to increase the Line of Credit or Term Loan up to an additional $100,000,000.

Line of Credit and Term Loan indebtedness bears interest at either: (1) LIBOR, as defined, plus an applicable margin ranging from 1.5% to 2.50%; or (2) the alternate base rate (“ABR”), which is the greater of JPMorgan’s prime rate or the federal funds effective rate or the overnight bank funding rate plus 0.5%. We elect the interest rate with each borrowing under the line of credit. In addition, there is an unused line fee of 0.15% to 0.35%. Letter of credit fees are based on the applicable LIBOR rate.

The Term Loan requires 20 quarterly principal payments (the first due date was March 31, 2017) in the amount of $250,000 (increasing by $125,000 each year up to $750,000 in the fifth year). The remaining balance of principal and accrued interest are due on March 1, 2022.

The Credit Facility is secured by all of our assets and requires us to maintain a ratio of funded debt to our trailing four quarters of EBIDTA (the “Leverage Ratio”), as defined, of less than 3.0 to 1.0, provided that, we may once during the term of the Credit Facility, in connection with a Permitted Acquisition for which the aggregate consideration paid or to be paid in respect thereof equals or exceeds $20,000,000, elect to increase the maximum Leverage Ratio permitted hereunder to (i) 3.50 to 1.00 for a period of four consecutive fiscal quarters commencing with the fiscal quarter in which such Permitted Acquisition occurs (the “Initial Holiday Period”) and (ii) 3.25 to 1.00 for the period of four consecutive fiscal quarters immediately following the Initial Holiday Period. The Credit Facility also requires us to maintain a minimum fixed charge coverage ratio of less than 1.25 to 1.0.

As of October 31, 2017, we had $58,250,000 in outstanding indebtedness and unused capacity under our Credit Facility of $41,000,000 (subject to covenant restrictions).

In April 2015, the SEC declared effective our Universal Shelf Registration Statement which allows us to sell, in one or more public offerings, common stock or warrants, or any combination of such securities for proceeds in an aggregate amount of up to $130,000,000. The terms of any offering, including the type of securities involved, would be established at the time of sale.

We routinely evaluate opportunities for strategic acquisitions. Future material acquisitions may require that we obtain additional capital, assume third party debt or incur other long-term obligations. We believe that we have the option to utilize both equity and debt instruments as vehicles for the long-term financing of our investment activities and acquisitions.

On November 7, 2005, our Board of Directors authorized a program to repurchase up to 300,000 shares of our outstanding common stock. Under the plan, the shares may be purchased from time to time in the open market at prevailing prices or in negotiated transactions off the market. Shares purchased will be canceled and repurchases will be made with existing cash reserves. We do not maintain a set policy or schedule for our buyback program. We have purchased 162,486 shares of common stock under this program from inception through September 30, 2017.

We have been paying regular quarterly dividends since 2003. Dividends per share paid by quarter were as follows:

	Year Ending March 31,	
	2018	2017
First quarter	$0.16	$0.16
Second quarter	0.16	0.16
Third quarter	-	0.16
Fourth quarter	-	0.16

In October 2017, our Board of Directors declared a quarterly cash dividend of $0.16 per share of common stock, payable on December 15, 2017, to shareholders of record at the close of business on November 30, 2017.

Cash Flows

Our cash flows from operating, investing and financing activities were as follows (in thousands):

	Six Months Ended September 30,	
	2017	2016
Net cash provided by operating activities	$7,368	$1,329
Net cash used in investing activities	(941)	(10,070)
Net cash (used in) provided by financing activities	(2,137)	8,098

Net cash provided by operating activities for the six months ended September 30, 2017 increased primarily due to a $960,000 decrease of inventories in the current period and the payment of $4,594,000 of contingent consideration and $5,392,000 in accrued salaries, taxes and various other accrued expenses in the prior period, partially offset by an increase in prepaid expenses and other in the current period.

Net cash used in investing activities for the six months ended September 30, 2017 resulted from $62,000 associated with the 2018 Acquisitions and the purchase of $2,012,000 of property, plant and equipment, partially offset by $1,133,000 of proceeds associated with the sale of the Omaha facility. Net cash used in investing activities for the six months ended September 30, 2016 resulted from $3,401,000 associated with the 2017 Acquisitions and the purchase of $6,669,000 of property, plant and equipment.

Net cash used in financing activities for the six months ended September 30, 2017 resulted from the repayment of debt of $7,000,000 and the payment of dividends of $1,201,000, partially offset by borrowings under our Credit Facility of $4,000,000 and proceeds from the exercise of stock options of $2,064,000. Net cash provided by financing activities for the six months ended September 30, 2016 resulted from borrowings under our Credit Facility of $9,500,000 and proceeds from the exercise of stock options of $1,767,000, partially offset by the repayment of debt of $2,000,000 and the payment of dividends of $1,169,000.

At September 30, 2017, we had contractual obligations for open purchase orders of approximately $3,600,000 for routine purchases of supplies and inventory, which are payable in less than one year.

Under the terms of the PCD Agreement, we are required to pay contingent consideration if the cumulative revenues for our process challenge device business for the three years subsequent to the acquisition meet certain levels. The potential consideration payable ranges from $0 to $1,500,000 and is based upon a sliding scale of three-year cumulative revenues between $9,900,000 and $12,600,000, with payments made annually. Based upon both historical and projected growth rates, we initially recorded $300,000 of contingent consideration payable which represented our best estimate of the amount that would ultimately be paid. We paid $150,000 of the contingent consideration during the year ended March 31, 2016 (based upon the then current run rate projected over the entire three-year contingent consideration period).

Since the initial payment, the revenues for these products have significantly increased and as a result, during the year ended March 31, 2017 we recorded an additional $450,000 accrual (which was paid in our third quarter ending December 31, 2016.). During the three months ended June 30, 2017 revenues continued to increase and after revising our forecast for the PCD product revenues through the end of the earn-out period, we recorded an additional $300,000 accrual, which is included in other income, net in the accompanying condensed consolidated statement of income for the three months ended June 30, 2017. The remaining contingent consideration amount is also subject to additional modification at the end of the third year of the earn-out period (October 2017) based upon the actual revenues earned over the contingent consideration period. Any changes to the contingent consideration ultimately paid will result in additional income or expense in our condensed consolidated statements of income. We will continue to monitor the results of our PCD business and we will adjust the contingent liability on a go forward basis, based on then current information.

Critical Accounting Estimates

Our condensed consolidated financial statements and accompanying notes have been prepared in accordance with U.S. GAAP. The preparation of these financial statements requires management to make estimates, judgments and assumptions that affect reported amounts of assets, liabilities, revenues and expenses. We continually evaluate the accounting policies and estimates used to prepare the condensed consolidated financial statements. The estimates are based on historical experience and assumptions believed to be reasonable under current facts and circumstances.

Actual amounts and results could differ from these estimates made by management. Certain accounting policies that require significant management estimates and are deemed critical to our results of operations or financial position are discussed in our Annual Report on Form 10-K for the year ended March 31, 2017 in the Critical Accounting Policies and Estimates section of “Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations.”

Item 3. ***Quantitative and Qualitative Disclosures about Market Risk***

We have no derivative instruments and minimal exposure to commodity market risks. Approximately ten percent of our revenues are exposed to foreign currency risk, of which all is within stable markets, minimizing our exposure to foreign currency fluctuations.

Item 4. ***Controls and Procedures***

Evaluation of Disclosure Controls and Procedures

We maintain disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended) that are designed to reasonably ensure that information required to be disclosed by us in the reports we file or submit under the Securities Exchange Act of 1934, as amended, is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission’s rules and forms and that such information is accumulated and communicated to our management, including our principal executive and principal financial officers, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure. Our management evaluated, with the participation of our Chief Executive Officer and Chief Financial Officer, the effectiveness of our disclosure controls and procedures as of September 30, 2017. Based on that evaluation, our management concluded that our disclosure controls and procedures were effective at September 30, 2017.

Our management, including our Chief Executive Officer and Chief Financial Officer, is responsible for establishing and maintaining adequate internal control over financial reporting. Our internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements in accordance with generally accepted accounting principles in the United States. Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Therefore, even those systems determined to be effective can provide only reasonable assurance of achieving their control objectives. Management evaluated the effectiveness of our internal control over financial reporting based on the framework in "Internal Control – Integrated Framework" issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) in 2013.

Our management evaluated, with the participation of our Chief Executive Officer and Chief Financial Officer, the effectiveness of our internal control over financial reporting as of September 30, 2017. Based on that evaluation, our management concluded that our internal control over financial reporting was effective at September 30, 2017.

Changes in Internal Control Over Financial Reporting

There were no significant changes in our internal control over financial reporting that occurred during the six months ended September 30, 2017, that have materially affected, or are reasonably likely to materially affect our internal control over financial reporting.

Part II. Other Information

Item 1. ***Legal Proceedings***

See Note 8 – Commitments and Contingencies of the Notes to Condensed Consolidated Financial Statements (Part I, Item 1 of this Form 10-Q) for information regarding any legal proceedings in which we may be involved.

Item 1A. ***Risk factors***

We are affected by risks specific to us as well as factors that affect all businesses operating in a global market. The significant factors known to us that could materially adversely affect our business, financial condition or operating results are described in our Annual Report on Form 10-K for the year ended March 31, 2017, under the heading "Part I –

Item 1A. Risk Factors." There have been no material changes to those risk factors.

Item 2. ***Unregistered Sales of Equity Securities and Use of Proceeds***

On November 7, 2005, our Board of Directors adopted a share repurchase plan which allows for the repurchase of up to 300,000 of our common shares. This plan will continue until the maximum is reached or the plan is terminated by further action of the Board of Directors. We made the following repurchases of our common stock, including settlement of loans to employees for the exercise of stock options:

	Shares Purchased	**Average Price Paid**	**Total Shares Purchased as Part of Publicly Announced Plan**	**Remaining Shares to Purchase Under Plan**
July 2017	--	$ --	162,486	137,514
August 2017	--	--	162,486	137,514
September 2017	--	--	162,486	137,514
Total	--	--		

Item 6. ***Exhibits***

31.1	Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31.2	Certification of Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32.1	Certification of Chief Executive Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
32.2	Certification of Chief Financial Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
101	The following financial information from the quarterly report on Form 10-Q of Mesa Laboratories, Inc. for the quarter ended September 30, 2017, formatted in XBRL (eXtensible Business Reporting Language): (i) Condensed Consolidated Statements of Income, (ii) Condensed Consolidated Balance Sheets, (iii) Condensed Consolidated Statements of Comprehensive Income, (iv) Condensed Consolidated Statements of Cash Flows, and (v) Notes to the Condensed Consolidated Financial Statements.

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.

MESA LABORATORIES, INC.

(Registrant)

DATED: November 6, 2017 BY: /s/ Gary M. Owens.
Gary M. Owens

Chief Executive Officer

DATED: November 6, 2017 BY: /s/ John V. Sakys
John V. Sakys

Chief Financial Officer

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