STEPAN CO
Form 10-Q
August 01, 2018

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 JUNE 30, 2018

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 1-4462

STEPAN COMPANY

(Exact name of registrant as specified in its charter)

| Delaware | 36-1823834 |
|---|---|
| (State or other jurisdiction of incorporation or organization) | (I.R.S. Employer Identification Number) |

Edens and Winnetka Road, Northfield, Illinois 60093

(Address of principal executive offices)

Registrant's telephone number (847) 446-7500

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 (§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.

| Class | Outstanding at July 20, 2018 |
|---|---|
| Common Stock, $1 par value | 22,522,507 Shares |

Part I FINANCIAL INFORMATION

Item 1 - Financial Statements

STEPAN COMPANY

CONDENSED CONSOLIDATED STATEMENTS OF INCOME

Unaudited

| (In thousands, except per share amounts) | Three Months Ended June 30 2018 | Three Months Ended June 30 2017 | Six Months Ended June 30 2018 | Six Months Ended June 30 2017 |
|---|---|---|---|---|
| Net Sales | $519,866 | $495,101 | $1,019,201 | $963,370 |
| Cost of Sales[a] | 430,586 | 405,113 | 840,351 | 781,263 |
| Gross Profit[a] | 89,280 | 89,988 | 178,850 | 182,107 |
| Operating Expenses: | | | | |
| Selling[a] | 13,369 | 13,230 | 28,259 | 26,686 |
| Administrative[a] | 18,098 | 17,769 | 37,537 | 35,661 |
| Research, development and technical services[a] | 13,720 | 14,254 | 27,334 | 27,633 |
| Deferred compensation expense | (865) | 5,016 | 749 | 5,392 |
| | 44,322 | 50,269 | 93,879 | 95,372 |
| Business restructuring expenses (Note 15) | (273) | (586) | (631) | (1,372) |
| Operating Income[a] | 44,685 | 39,133 | 84,340 | 85,363 |
| Other Income (Expense): | | | | |
| Interest, net | (2,672) | (2,863) | (5,823) | (5,855) |
| Other, net[a] (Note 14) | 484 | 793 | 1,644 | 1,885 |
| | (2,188) | (2,070) | (4,179) | (3,970) |
| Income Before Provision for Income Taxes | 42,497 | 37,063 | 80,161 | 81,393 |
| Provision for Income Taxes (Note 17) | 9,574 | 9,167 | 16,522 | 21,585 |
| Net Income | 32,923 | 27,896 | 63,639 | 59,808 |
| Net (Income) Loss Attributable to Noncontrolling Interests (Note 2) | 2 | (14) | 9 | (13) |
| Net Income Attributable to Stepan Company | $32,925 | $27,882 | $63,648 | $59,795 |
| Net Income Per Common Share Attributable to Stepan Company (Note 9): | | | | |
| Basic | $1.43 | $1.21 | $2.76 | $2.61 |
| Diluted | $1.41 | $1.19 | $2.73 | $2.56 |
| Shares Used to Compute Net Income Per Common Share Attributable to Stepan Company (Note 9): | | | | |
| Basic | 23,039 | 22,953 | 23,059 | 22,927 |
| Diluted | 23,295 | 23,381 | 23,341 | 23,356 |

| | | | | |
|---|---|---|---|---|
| Dividends Declared Per Common Share | $0.23 | $0.21 | $0.45 | $0.41 |

(a) The 2017 amounts for the noted line items have been immaterially changed from the amounts originally reported as a result of the Company's first quarter 2018 adoption of Accounting Standards Update (ASU) No. 2017-7, Compensation –Retirement Benefits (Topic 715): Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost.

The accompanying Notes to Condensed Consolidated Financial Statements are an integral part of these financial statements.

2

STEPAN COMPANY

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

Unaudited

| | Three Months Ended | | Six Months Ended | |
|---|---|---|---|---|
| (In thousands) | June 30 | | June 30 | |
| | 2018 | 2017 | 2018 | 2017 |
| Net income | $32,923 | $27,896 | $63,639 | $59,808 |
| Other comprehensive income : | | | | |
| Foreign currency translation adjustments (Note 10) | (35,059) | 5,997 | (26,242) | 16,451 |
| Defined benefit pension adjustments, net of tax (Note 10) | 752 | 567 | 1,505 | 1,132 |
| Derivative instrument activity, net of tax (Note 10) | (2) | (3) | (5) | (5) |
| Total other comprehensive income | (34,309) | 6,561 | (24,742) | 17,578 |
| Comprehensive income (loss) | (1,386) | 34,457 | 38,897 | 77,386 |
| Comprehensive (income) loss attributable to noncontrolling interests (Note 2) | 49 | (34) | 24 | (46) |
| Comprehensive income (loss) attributable to Stepan Company | $(1,337) | $34,423 | $38,921 | $77,340 |

The accompanying Notes to Condensed Consolidated Financial Statements are an integral part of these financial statements.

STEPAN COMPANY

CONDENSED CONSOLIDATED BALANCE SHEETS

Unaudited

| (In thousands) | June 30, 2018 | December 31, 2017 |
|---|---|---|
| Assets | | |
| Current Assets: | | |
| Cash and cash equivalents | $256,736 | $298,894 |
| Receivables, net | 312,220 | 293,541 |
| Inventories (Note 6) | 188,461 | 172,748 |
| Other current assets | 23,136 | 23,553 |
| Total current assets | 780,553 | 788,736 |
| Property, Plant and Equipment: | | |
| Cost | 1,632,103 | 1,603,286 |
| Less: Accumulated depreciation | (1,032,955) | (1,004,843) |
| Property, plant and equipment, net | 599,148 | 598,443 |
| Goodwill, net | 22,972 | 25,118 |
| Other intangible assets, net | 16,035 | 18,538 |
| Long-term investments (Note 3) | 27,229 | 28,270 |
| Other non-current assets | 12,848 | 11,756 |
| Total assets | $1,458,785 | $1,470,861 |
| Liabilities and Equity | | |
| Current Liabilities: | | |
| Current maturities of long-term debt (Note 13) | $24,312 | $22,500 |
| Accounts payable | 201,313 | 204,977 |
| Accrued liabilities | 80,088 | 92,776 |
| Total current liabilities | 305,713 | 320,253 |
| Deferred income taxes | 14,060 | 10,962 |
| Long-term debt, less current maturities (Notes 13) | 262,504 | 268,299 |
| Other non-current liabilities | 114,474 | 130,433 |
| Commitments and Contingencies (Note 7) | | |
| Equity: | | |
| Common stock, $1 par value; authorized 60,000,000 shares; 26,278,816 issued shares in 2018 and 26,070,787 issued shares in 2017 | 26,279 | 26,071 |
| Additional paid-in capital | 177,779 | 170,408 |
| Accumulated other comprehensive loss (Note 10) | (124,290) | (99,563) |
| Retained earnings | 775,031 | 721,741 |
| Less: Common treasury stock, at cost, 3,756,309 shares in 2018 and 3,561,509 shares in 2017 | (93,559) | (78,561) |
| Total Stepan Company stockholders' equity | 761,240 | 740,096 |
| Noncontrolling interests (Note 2) | 794 | 818 |
| Total equity | 762,034 | 740,914 |

| Total liabilities and equity | $1,458,785 | $1,470,861 |
| --- | --- | --- |

The accompanying Notes to Condensed Consolidated Financial Statements are an integral part of these financial statements.

STEPAN COMPANY

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

Unaudited

| (In thousands) | Six Months Ended June 30 | |
|---|---|---|
| | 2018 | 2017 |
| Cash Flows From Operating Activities | | |
| Net income | $63,639 | $59,808 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Depreciation and amortization | 40,500 | 37,729 |
| Deferred compensation | 749 | 5,392 |
| Realized and unrealized gains on long-term investments | (504) | (2,576) |
| Stock-based compensation | 3,387 | 4,551 |
| Deferred income taxes | 2,463 | 2,741 |
| Other non-cash items | 830 | 2,972 |
| Changes in assets and liabilities: | | |
| Receivables, net | (23,969) | (33,697) |
| Inventories | (14,409) | (1,477) |
| Other current assets | 442 | (2,050) |
| Accounts payable and accrued liabilities | (18,579) | (11,777) |
| Pension liabilities | (122) | (58) |
| Environmental and legal liabilities | (479) | (469) |
| Deferred revenues | (162) | (162) |
| Net Cash Provided By Operating Activities | 53,786 | 60,927 |
| Cash Flows From Investing Activities | | |
| Expenditures for property, plant and equipment | (43,741) | (38,331) |
| Business acquisition (Note 16) | (21,475) | (4,339) |
| Other, net | 1,775 | (2,184) |
| Net Cash Used In Investing Activities | (63,441) | (44,854) |
| Cash Flows From Financing Activities | | |
| Revolving debt and bank overdrafts, net | 1,893 | (7,221) |
| Other debt repayments | (5,714) | (5,714) |
| Dividends paid | (10,160) | (9,225) |
| Company stock repurchased | (12,000) | (1,500) |
| Stock option exercises | 3,274 | 2,518 |
| Other, net | (4,432) | (1,586) |
| Net Cash Used In Financing Activities | (27,139) | (22,728) |
| Effect of Exchange Rate Changes on Cash | (5,364) | 4,730 |
| Net Decrease in Cash and Cash Equivalents | (42,158) | (1,925) |
| Cash and Cash Equivalents at Beginning of Period | 298,894 | 225,743 |
| Cash and Cash Equivalents at End of Period | $256,736 | $223,818 |
| Supplemental Cash Flow Information | | |

| | | |
|---|---|---|
| Cash payments of income taxes, net of refunds/payments | $19,739 | $18,288 |
| Cash payments of interest | $6,444 | $7,101 |

The accompanying Notes to Condensed Consolidated Financial Statements are an integral part of these financial statements.

STEPAN COMPANY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

June 30, 2018

Unaudited

## 1. CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

The condensed consolidated financial statements included herein have been prepared by Stepan Company (the Company), without audit, pursuant to the rules and regulations of the Securities and Exchange Commission (SEC). Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America (GAAP) have been condensed or omitted pursuant to such rules and regulations, although management believes that the disclosures are adequate and make the information presented not misleading. In the opinion of management, all adjustments, consisting only of normal recurring accruals, necessary to present fairly the Company's financial position as of June 30, 2018, results of operations for the three and six months ended June 30, 2018 and 2017, and cash flows for the six months ended June 30, 2018 and 2017, have been included. These financial statements and related footnotes should be read in conjunction with the financial statements and related footnotes included in the Company's 2017 Annual Report on Form 10-K.

## 2. RECONCILIATIONS OF EQUITY

Below are reconciliations of total equity, Company equity and equity attributable to noncontrolling interests for the six months ended June 30, 2018 and 2017:

| (In thousands) | Total Equity | Stepan Company Equity | Noncontrolling Interests' Equity [3] |
|---|---|---|---|
| Balance at January 1, 2018 | $740,914 | $740,096 | $ 818 |
| Net income | 63,639 | 63,648 | (9) |
| Dividends | (10,160) | (10,160) | |
| Common stock purchases [1] | (15,184) | (15,184) | |
| Stock option exercises | 3,274 | 3,274 | |
| Defined benefit pension adjustments, net of tax | 1,505 | 1,505 | |
| Translation adjustments | (26,242) | (26,227) | (15) |
| Derivative instrument activity, net of tax | (5) | (5) | |
| Other [2] | 4,293 | 4,293 | |

| | | | |
|---|---|---|---|
| Balance at June 30, 2018 | $762,034 | $761,240 | $ 794 |

| (In thousands) | Total Equity | Stepan Company Equity | Noncontrolling Interests' Equity [3] |
|---|---|---|---|
| Balance at January 1, 2017 | $635,916 | $634,604 | $ 1,312 |
| Net income | 59,808 | 59,795 | 13 |
| Dividends | (9,225 ) | (9,225 ) | — |
| Common stock purchases [1] | (3,191 ) | (3,191 ) | — |
| Stock option exercises | 2,518 | 2,518 | — |
| Defined benefit pension adjustments, net of tax | 1,132 | 1,132 | — |
| Translation adjustments | 16,451 | 16,418 | 33 |
| Derivative instrument activity, net of tax | (5 ) | (5 ) | — |
| Other [2] | 5,295 | 5,295 | — |
| Balance at June 30, 2017 | $708,699 | $707,341 | $ 1,358 |

[1] Includes the value of Company shares purchased in the open market and from the Company's retirement plans and the value of Company common shares tendered by employees to settle statutory withholding taxes related to distributions of deferred performance awards and deferred management incentive compensation and exercises of stock appreciation rights.

[2] Primarily comprised of activity related to stock-based compensation and deferred compensation. Beginning in 2018, also includes beginning retained earnings adjustment as a result of the Company's first quarter 2018 adoption of ASU No. 2016-16, Income Taxes (Topic 740): Intra-Entity Transfers of Assets Other Than Inventory.

[3] Reflects the noncontrolling interest in the Company's China joint venture.

3. FAIR VALUE MEASUREMENTS

The following were the financial instruments held by the Company at June 30, 2018, and December 31, 2017, and the methods and assumptions used to estimate the instruments' fair values:

Cash and cash equivalents

Carrying value approximated fair value because of the short maturity of the instruments.

Derivative assets and liabilities

Derivative assets and liabilities included the foreign currency exchange contracts discussed in Note 4. Fair value and carrying value were the same because the contracts were recorded at fair value. The fair values of the foreign currency contracts were calculated as the difference between the applicable forward foreign exchange rates at the reporting date and the contracted foreign exchange rates multiplied by the contracted notional amounts. See the table that follows the financial instrument descriptions for the reported fair values of derivative assets and liabilities.

Long-term investments

Long-term investments included the mutual fund assets the Company held to fund a portion of its deferred compensation liabilities and all of its non-qualified supplemental executive defined contribution obligations (see the defined contribution plans section of Note 8). Fair value and carrying value were the same because the mutual fund assets were recorded at fair value. Fair values for the mutual funds were calculated using the published market price per unit at the reporting date multiplied by the number of units held at the reporting date. See the table that follows the financial instrument descriptions for the reported fair value of long-term investments.

Debt obligations

The fair value of debt with original maturities greater than one year comprised the combined present values of scheduled principal and interest payments for each of the various loans, individually discounted at rates equivalent to those which could be obtained by the Company for new debt issues with durations equal to the average life to maturity of each loan. The fair values of the remaining Company debt obligations approximated their carrying values due to the short-term nature of the debt. The Company's fair value measurements for debt fall within level 2 of the fair value hierarchy.

At June 30, 2018, and December 31, 2017, the fair values and related carrying values of debt, including current maturities, were as follows (the fair value and carrying value amounts are presented without regard to unamortized debt issuance costs of $1,067,000 and $987,000 as of June 30, 2018 and December 31, 2017, respectively):

| (In thousands) | June 30, 2018 | December 31, 2017 |
|---|---|---|
| Fair value | $284,254 | $293,272 |
| Carrying value | 287,883 | 291,786 |

The following tables present financial assets and liabilities measured on a recurring basis at fair value as of June 30, 2018, and December 31, 2017, and the level within the fair value hierarchy in which the fair value measurements fall:

| (In thousands) | June 30, 2018 | Level 1 | Level 2 | Level 3 |
|---|---|---|---|---|
| Mutual fund assets | $27,229 | $27,229 | $— | $ — |
| Derivative assets: | | | | |
| Foreign currency contracts | 295 | — | 295 | — |
| Total assets at fair value | $27,524 | $27,229 | $295 | $ — |
| Derivative liabilities: | | | | |
| Foreign currency contracts | $441 | $— | $441 | $ — |

7

| (In thousands) | December 31, 2017 | Level 1 | Level 2 | Level 3 |
|---|---|---|---|---|
| Mutual fund assets | $ 28,270 | $28,270 | $— | $ — |
| Derivative assets: | | | | |
| Foreign currency contracts | 335 | — | 335 | — |
| Total assets at fair value | $ 28,605 | $28,270 | $335 | $ — |
| Derivative liabilities : | | | | |
| Foreign currency contracts | $ 94 | $— | $94 | $ — |

4. DERIVATIVE INSTRUMENTS

The Company is exposed to certain risks relating to its ongoing business operations. The primary risk managed by the use of derivative instruments is foreign currency exchange risk. The Company holds forward foreign currency exchange contracts that are not designated as any type of accounting hedge as defined by GAAP. The Company uses these contracts to manage its exposure to exchange rate fluctuations on certain Company subsidiary cash, accounts receivable, accounts payable and other obligation balances that are denominated in currencies other than the entities' functional currencies. The forward foreign exchange contracts are recognized on the balance sheet as either an asset or a liability measured at fair value. Gains and losses arising from recording the foreign exchange contracts at fair value are reported in earnings as offsets to the losses and gains reported in earnings arising from the re-measurement of the asset and liability balances into the applicable functional currencies. At June 30, 2018, and December 31, 2017, the Company had open forward foreign currency exchange contracts, all with durations of one to three months, to buy or sell foreign currencies with U.S. dollar equivalent amounts of $48,492,032 and $41,197,000, respectively.

The fair values of the derivative instruments held by the Company on June 30, 2018, and December 31, 2017, are disclosed in Note 3. Derivative instrument gains and losses for the three- and six- month periods ending June 30, 2018 and 2017, were immaterial. For amounts reclassified out of accumulated other comprehensive income (loss) (AOCI) into earnings for the three- and six- month periods ended June 30, 2018 and 2017, see Note 10.

5. STOCK-BASED COMPENSATION

On June 30, 2018, the Company had stock options and stock awards outstanding under its 2006 Incentive Compensation Plan and stock options, stock awards and stock appreciation rights (SARs) outstanding under its 2011 Incentive Compensation Plan. SARs granted prior to 2015 are cash-settled, and SARs granted after 2014 are stock-settled. Stock options and SARs granted prior to 2017 generally cliff vested after two years. Starting in 2017, stock options and SARs have a three-year graded vesting feature, with one-third of the awards vesting each year. The Company has elected the straight-line method of expense attribution for the stock options and SARs with the graded vesting feature.

Compensation expense recorded for all stock options, stock awards and SARs was as follows:

| (In thousands) | |
|---|---|
| Three Months Ended | Six Months Ended |

| June 30 | | June 30 | |
|---|---|---|---|
| 2018 | 2017 | 2018 | 2017 |
| $1,155 | $3,166 | $3,387 | $4,551 |

The year-over-year and quarter-over-quarter decrease in stock-based compensation expense was primarily attributable to cash-settled SARs. SARs compensation expense decreased due to a decrease in the fair values of cash-settled SARs that resulted from a decline in the market value of Company common stock during the first six months of 2018.

Unrecognized compensation costs for stock options, stock awards and SARs were as follows:

| (In thousands) | June 30, 2018 | December 31, 2017 |
|---|---|---|
| Stock options | $ 2,175 | $ 1,179 |
| Stock awards | 5,105 | 3,737 |
| SARs | 4,674 | 2,398 |

The increases in unrecognized compensation costs for stock options, stock awards and SARs reflected the 2018 grants of:

| | Shares |
|---|---|
| Stock options | 76,409 |
| Stock awards (at target) | 48,911 |
| SARs | 169,245 |

The unrecognized compensation costs at June 30, 2018, are expected to be recognized over weighted-average periods of 2.2 years, 1.9 years and 2.2 years for stock options, stock awards and SARs, respectively.

6. INVENTORIES

The composition of inventories at June 30, 2018, and December 31, 2017, was as follows:

| (In thousands) | June 30, 2018 | December 31, 2017 |
|---|---|---|
| Finished goods | $124,959 | $ 117,529 |
| Raw materials | 63,502 | 55,219 |
| Total inventories | $188,461 | $ 172,748 |

Inventories are priced primarily using the last-in, first-out inventory valuation method. If the first-in, first-out inventory valuation method had been used for all inventories, inventory balances would have been approximately $35,846,000 and $33,518,000 higher than reported at June 30, 2018, and December 31, 2017, respectively.

7. CONTINGENCIES

There are a variety of legal proceedings pending or threatened against the Company. Some of these proceedings may result in fines, penalties, judgments or costs being assessed against the Company at some future time. The Company's operations are subject to extensive local, state and federal regulations, including the U.S. Comprehensive Environmental Response, Compensation and Liability Act of 1980 (CERCLA) and the Superfund amendments of 1986 (Superfund) as well as similar regulations in other countries where the Company operates. Over the years, the Company has received requests for information related to or has been named by the government as a potentially responsible party (PRP) at a number of waste disposal sites where cleanup costs have been or may be incurred under CERCLA and similar state statutes. In addition, damages are being claimed against the Company in general liability actions for alleged personal injury or property damage in the case of some disposal and plant sites and in other commercial disputes. The Company believes that it has made adequate provisions for the costs it may incur with respect to these matters.

As of June 30, 2018, the Company estimated a range of possible environmental and legal losses of $23.8 million to $45.2 million. At June 30, 2018, and December 31, 2017, the Company's accrued liability for such losses, which represented the Company's best estimate within the estimated range of possible environmental and legal losses, was $23.8 million and $24.2 million, respectively. Cash outlays related to legal and environmental matters approximated $0.6 million and $1.0 million for the six-month periods ended June 30, 2018 and 2017, respectively.

For certain sites, the Company has responded to information requests made by federal, state or local government agencies but has received no response confirming or denying the Company's stated positions. As such, estimates of the total costs, or range of possible costs, of remediation, if any, or the Company's share of such costs, if any, cannot be determined with respect to these sites. Consequently, the Company is unable to predict the effect thereof on the Company's financial position, cash flows and results of operations. Given the information available, management believes the Company has no liability at these sites. Based upon the Company's present knowledge with respect to its involvement at these sites, the possibility of other viable entities' responsibilities for cleanup, and the extended period over which any costs would be incurred, the Company believes that these matters, individually and in the aggregate, will not have a material effect on the Company's financial position. However, in the event of one or more adverse determinations with respect to such sites in any annual or interim period, the effect on the Company's cash flows and results of operations for those periods could be material.

Following are summaries of the material contingencies at June 30, 2018:

Maywood, New Jersey Site

The Company's property in Maywood, New Jersey and property formerly owned by the Company adjacent to its current site and other nearby properties (Maywood site) were listed on the National Priorities List in September 1983 pursuant to the provisions of CERCLA because of certain alleged chemical contamination. Pursuant to an Administrative Order on Consent entered into between the U.S. Environmental Protection Agency (USEPA) and the Company for property formerly owned by the Company, and the issuance of an order by USEPA to the Company for property currently owned by the Company, the Company has completed various Remedial Investigation Feasibility Studies (RI/FS), and in September, 2014, the USEPA issued its Record of Decision (ROD) for chemically-contaminated soil. The USEPA has not yet issued a ROD for chemically-contaminated groundwater for the Maywood site. Based on the most current information available, the Company believes its recorded liability represents its best estimate of the cost of remediation for the Maywood site. The best estimate of the cost of remediation for the Maywood site could change as the Company continues to hold discussions with the USEPA, as the design of the remedial action progresses, if a groundwater ROD is issued or if other PRPs are identified. The ultimate amount for which the Company is liable could differ from the Company's current recorded liability.

In April 2015, the Company entered into an Administrative Settlement Agreement and Administrative Order on Consent with the USEPA which requires payment of certain costs and performance of certain investigative and design work for chemically-contaminated soil. Based on the Company's review and analysis of this order, no changes to the Company's recorded liability for claims associated with soil remediation of chemical contamination were required.

In addition, under the terms of a settlement agreement reached on November 12, 2004, the U. S. Department of Justice and the Company agreed to fulfill the terms of a Cooperative Agreement reached in 1985 under which the United States will take title to and responsibility for radioactive waste removal at the Maywood site, including past and future remediation costs incurred by the United States. As such, the Company recorded no liability related to this settlement agreement.

D'Imperio Property Site

During the mid-1970's, Jerome Lightman and the Lightman Drum Company disposed of hazardous substances at several sites in New Jersey. The Company was named as a PRP in a lawsuit in the U.S. District Court for the District of New Jersey that involved the D'Imperio Property Site located in New Jersey. In 2016, the PRPs were provided with updated remediation cost estimates which were considered in the Company's determination of its range of estimated possible losses and liability balance. The changes in range of possible losses and liability balance were immaterial. Remediation work is continuing at this site. Based on current information, the Company believes that its recorded liability represents its best estimate of the cost of remediation for the D'Imperio site. Depending on the ultimate cost of the remediation at this site, the amount for which the Company is liable could differ from the current estimates.

Wilmington Site

The Company is currently contractually obligated to contribute to the response costs associated with the Company's formerly-owned site in Wilmington, Massachusetts. Remediation at this site is being managed by its current owner, to whom the Company sold the property in 1980. Under the agreement, once total site remediation costs exceed certain levels, the Company is obligated to contribute up to five percent of future response costs associated with this site with no limitation on the ultimate amount of contributions. The Company has paid the current owner $2.6 million for the Company's portion of environmental response costs through June 30, 2018. The Company has recorded a liability for its portion of the estimated remediation costs for the site. Depending on the ultimate cost of the remediation at this site, the amount for which the Company is liable could differ from the current estimates.

The Company and other prior owners also entered into an agreement in April 2004 waiving certain statute of limitations defenses for claims which may be filed by the Town of Wilmington, Massachusetts, in connection with this site. While the Company has denied any liability for any such claims, the Company agreed to this waiver while the parties continue to discuss the resolution of any potential claim which may be filed.

Other U.S. Sites

Through the regular environmental monitoring of its plant production sites, the Company discovered levels of chemical contamination that were above thresholds allowed by law at two of its U.S plants. The Company voluntarily reported its results to the applicable state environmental agencies. As a result, the Company is required to perform self-remediation of the affected areas. In the fourth quarter of 2016, the Company recognized a charge for the estimated cost of remediating the sites. Based on

current information, the Company believes that its recorded liability for the remediation represents its best estimate of expected costs. However, actual costs could differ from current estimates.

## 8. POSTRETIREMENT BENEFIT PLANS

### Defined Benefit Pension Plans

The Company sponsors various funded qualified and unfunded non-qualified defined benefit pension plans, the most significant of which cover employees in the U.S. and U.K. locations. The U.S. and U.K. defined benefit pension plans are frozen and service benefits are no longer being accrued.

Components of Net Periodic Benefit Cost

| | UNITED STATES | | | |
|---|---|---|---|---|
| | Three Months Ended | | Six Months Ended | |
| (In thousands) | June 30 | | June 30 | |
| | 2018 | 2017 | 2018 | 2017 |
| Interest cost | $1,540 | $1,662 | $3,079 | $3,323 |
| Expected return on plan assets | (2,321) | (2,322) | (4,642) | (4,643) |
| Amortization of net actuarial loss | 936 | 788 | 1,873 | 1,576 |
| Net periodic benefit cost | $155 | $128 | $310 | $256 |

| | UNITED KINGDOM | | | |
|---|---|---|---|---|
| | Three Months Ended | | Six Months Ended | |
| (In thousands) | June 30 | | June 30 | |
| | 2018 | 2017 | 2018 | 2017 |
| Interest cost | $144 | $147 | $ 292 | $ 290 |
| Expected return on plan assets | (226) | (198) | (457) | (390) |
| Amortization of net actuarial loss | 56 | 95 | 113 | 187 |
| Net periodic benefit cost (income) | $(26) | $44 | $ (52) | $ 87 |

In the first quarter of 2018, the Company implemented ASU No. 2017-07, Compensation-Retirement Benefits (Topic 715): Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost, which amended the guidance for the presentation of the components of net periodic cost in the income statement. The guidance requires the service cost component of net periodic benefit cost to be included in employee compensation costs in the income statement and all other components elsewhere in the income statement outside of income from operations. The Company does not have a service component of the net periodic benefit cost because the defined benefit plans (both U.S. and U.K. locations) are frozen. The other components of net periodic benefit cost such as interest cost, amortization of net actuarial loss and expected return on plan assets are included in the line item Other, net within Other Income (Expense) section of the Income statement. See Note 14 for more details.

Employer Contributions

U.S. Plans

As a result of pension funding relief provisions included in the Highway and Transportation Funding Act of 2014, the Company is not required to make contributions to the funded U.S. qualified defined benefit plans. Approximately $312,000 is expected to be paid related to the unfunded non-qualified plans in 2018. Of such amount, $200,000 had been paid related to the non-qualified plans as of June 30, 2018.

U.K. Plan

The Company's U.K. subsidiary expects to contribute approximately $415,000 to its defined benefit pension plan in 2018. Of such amount, $251,000 had been contributed to the plan as of June 30, 2018.

Defined Contribution Plans

The Company sponsors retirement savings defined contribution plans that cover eligible U.S. and U.K. employees. The Company's U.S. retirement plans include two qualified plans, one of which is a 401(k) plan and one of which is an employee stock ownership plan, and one non-qualified supplemental executive plan. Historically, the Company made profit sharing contributions into the qualified retirement plans for its U.S. employees. Profit sharing contributions were determined each year using a formula that was applied to Company earnings. The contributions, which were made partly in cash paid to the 401(k) plan and partly in Company common stock, are allocated to participant accounts on the basis of participant base earnings. Effective January 1, 2018, the Company amended its U.S. retirement saving plan and profit sharing formula, which resulted in a higher potential contribution percentage to the U.S. retirement savings plan and a lower potential profit sharing contribution percentage relative to prior years.

Defined contribution plan expenses for the Company's retirement savings plans and profit sharing were as follows:

| (In thousands) | Three Months Ended June 30 | | Six Months Ended June 30 | |
|---|---|---|---|---|
| | 2018 | 2017 | 2018 | 2017 |
| Retirement savings plans | $1,706 | $1,224 | $3,463 | $2,483 |
| Profit sharing | 1,068 | 2,108 | 2,010 | 3,951 |
| Total defined contribution expense | $2,774 | $3,332 | $5,473 | $6,434 |

The Company has a rabbi trust to fund the obligations of its non-qualified supplemental executive defined contribution plans (supplemental plans). The trust comprises various mutual fund investments selected by the participants of the supplemental plans. In accordance with the accounting guidance for rabbi trust arrangements, the assets of the trust and the obligations of the supplemental plans are reported on the Company's consolidated balance sheets. The Company elected the fair value option for the mutual fund investment assets so that offsetting changes in the mutual fund values and defined contribution plan obligations would be recorded in earnings in the same period. Therefore, the mutual funds are reported at fair value with any subsequent changes in fair value recorded in the consolidated statements of income. The liabilities related to the supplemental plans increase (i.e., supplemental plan expense is recognized) when the value of the trust assets appreciates and decrease when the value of the trust assets declines (i.e., supplemental plan income is recognized). At June 30, 2018, the balance of the trust assets was $1,670,000, which equaled the balance of the supplemental plan liabilities (see the long-term investments section in Note 3 for further information regarding the Company's mutual fund assets).

## 9. EARNINGS PER SHARE

Below are the computations of basic and diluted earnings per share for the three and six months ended June 30, 2018 and 2017:

| (In thousands, except per share amounts) | Three Months Ended June 30 2018 | 2017 | Six Months Ended June 30 2018 | 2017 |
|---|---|---|---|---|
| Computation of Basic Earnings per Share | | | | |
| Net income attributable to Stepan Company | $32,925 | $27,882 | $63,648 | $59,795 |
| Weighted-average number of common shares outstanding | 23,039 | 22,953 | 23,059 | 22,927 |
| Basic earnings per share | $1.43 | $1.21 | $2.76 | $2.61 |
| Computation of Diluted Earnings per Share | | | | |
| Net income attributable to Stepan Company | $32,925 | $27,882 | $63,648 | $59,795 |
| Weighted-average number of shares outstanding | 23,039 | 22,953 | 23,059 | 22,927 |
| Add weighted-average net shares from assumed exercise of options (under treasury stock method) [1] | 87 | 172 | 103 | 177 |
| Add weighted-average net shares related to unvested stock awards (under treasury stock method) | 2 | 8 | 2 | 8 |
| Add weighted-average net shares from assumed exercise of SARs (under treasury stock method) [1] | 99 | 143 | 111 | 143 |
| Add weighted-average contingently issuable net shares related to performance stock awards (under treasury stock method) | 68 | 105 | 66 | 101 |
| Weighted-average shares applicable to diluted earnings | 23,295 | 23,381 | 23,341 | 23,356 |
| Diluted earnings per share | $1.41 | $1.19 | $2.73 | $2.56 |

[1] Options/SARs to acquire 194,949 and 98,878 shares of Company common stock were excluded from the computations of diluted earnings per share for the three- and six- months ended June 30, 2018, respectively. Options/SARs to acquire 37,261 shares of Company common stock were excluded from the computations of diluted earnings per share for the six months ended June 30, 2017. Inclusion of the instruments would have had antidilutive effects on the computations of the earnings per share.

10. ACCUMULATED OTHER COMPREHENSIVE INCOME (LOSS)

Below is the change in the Company's AOCI balance by component (net of income taxes) for the three and six months ended June 30, 2018 and 2017:

| (In thousands) | Foreign Currency Translation Adjustments | Defined Benefit Pension Plan Adjustments | Cash Flow Hedge Adjustments | Total |
|---|---|---|---|---|
| Balance at March 31, 2017 | $ (86,334) | $ (30,225) | $ 98 | $ (116,461) |
| Other comprehensive income before reclassifications | 5,977 | — | — | 5,977 |
| Amounts reclassified from AOCI | — | 567 | (3) | 564 |
| Net current-period other comprehensive income | 5,977 | 567 | (3) | 6,541 |
| Balance at June 30, 2017 | $ (80,357) | $ (29,658) | $ 95 | $ (109,920) |
| | | | | |
| Balance at March 31, 2018 | $ (61,776) | $ (28,340) | $ 88 | $ (90,028) |
| Other comprehensive income before reclassifications | (35,012) | — | — | (35,012) |
| Amounts reclassified from AOCI | — | 752 | (2) | 750 |
| Net current-period other comprehensive income | (35,012) | 752 | (2) | (34,262) |
| Balance at June 30, 2018 | $ (96,788) | $ (27,588) | $ 86 | $ (124,290) |
| | | | | |
| Balance at December 31, 2016 | $ (96,775) | $ (30,790) | $ 100 | $ (127,465) |
| Other comprehensive income before reclassifications | 16,418 | — | — | 16,418 |
| Amounts reclassified from AOCI | — | 1,132 | (5) | 1,127 |
| Net current-period other comprehensive income | 16,418 | 1,132 | (5) | 17,545 |
| Balance at June 30, 2017 | $ (80,357) | $ (29,658) | $ 95 | $ (109,920) |
| | | | | |
| Balance at December 31, 2017 | $ (70,561) | $ (29,093) | $ 91 | $ (99,563) |
| Other comprehensive income before reclassifications | (26,227) | — | — | (26,227) |
| Amounts reclassified from AOCI | — | 1,505 | (5) | 1,500 |
| Net current-period other comprehensive income | (26,227) | 1,505 | (5) | (24,727) |
| Balance at June 30, 2018 | $ (96,788) | $ (27,588) | $ 86 | $ (124,290) |

Information regarding the reclassifications out of AOCI for the three and six month periods ended June 30, 2018 and 2017, is displayed below:

| (In thousands) | Amount Reclassified from AOCI (a) | | |
|---|---|---|---|
| AOCI Components | Three Months Ended June 30, | Six Months Ended June 30, | Affected Line Item in Consolidated Statements |

| | | | | | of Income |
|---|---|---|---|---|---|
| | 2018 | 2017 | 2018 | 2017 | |
| Amortization of defined benefit pension actuarial losses | $(992) | $(883) | $(1,986) | $(1,763) | (b) |
| | 240 | 316 | 481 | 631 | Tax benefit |
| | $(752) | $(567) | $(1,505) | $(1,132) | Net of tax |
| Gains and losses on cash flow hedges: | | | | | |
| Foreign exchange contracts | 2 | 3 | 5 | 5 | Cost of sales |
| | 2 | 3 | 5 | 5 | Total before tax |
| | — | — | — | — | Tax benefit |
| | $2 | $3 | $5 | $5 | Net of tax |
| Total reclassifications for the period | $(750) | $(564) | $(1,500) | $(1,127) | Net of tax |

(a) Amounts in parentheses denote expense to statement of income.
(b) This component of accumulated other comprehensive income is included in the computation of net periodic benefit cost (see Note 8 for additional details).

11. SEGMENT REPORTING

The Company has three reportable segments: Surfactants, Polymers and Specialty Products. Net sales by segment for the three and six months ended June 30, 2018 and 2017, were as follows:

| | Three Months Ended | | Six Months Ended | |
|---|---|---|---|---|
| (In thousands) | June 30 | | June 30 | |
| | 2018 | 2017 | 2018 | 2017 |
| Segment Net Sales | | | | |
| Surfactants | $356,884 | $329,334 | $715,824 | $651,937 |
| Polymers | 140,867 | 141,187 | 262,800 | 267,797 |
| Specialty Products | 22,115 | 24,580 | 40,577 | 43,636 |
| Total | $519,866 | $495,101 | $1,019,201 | $963,370 |

Segment operating income and reconciliations of segment operating income to consolidated income before income taxes for the three and six months ended June 30, 2018 and 2017, are summarized below:

| | Three Months Ended | | Six Months Ended | |
|---|---|---|---|---|
| (In thousands) | June 30 | | June 30 | |
| | 2018 | 2017[2] | 2018 | 2017[2] |
| Segment Operating Income | | | | |
| Surfactants | $34,218 | $31,164 | $74,469 | $69,535 |
| Polymers | 19,458 | 21,283 | 36,352 | 42,708 |
| Specialty Products | 4,240 | 5,451 | 3,890 | 6,737 |
| Segment operating income | 57,916 | 57,898 | 114,711 | 118,980 |
| Business restructuring | (273) | (586) | (631) | (1,372) |
| Unallocated corporate expenses [1] | (12,958) | (18,179) | (29,740) | (32,245) |
| Consolidated operating income | 44,685 | 39,133 | 84,340 | 85,363 |
| Interest expense, net | (2,672) | (2,863) | (5,823) | (5,855) |
| Other, net | 484 | 793 | 1,644 | 1,885 |
| Consolidated income before income taxes | $42,497 | $37,063 | $80,161 | $81,393 |

[1] Unallocated corporate expenses primarily comprise corporate administrative expenses (e.g., corporate finance, legal, human resources, information systems, deferred compensation and environmental remediation) that are not included in segment operating income and not used to evaluate segment performance.

[2] The 2017 data has been immaterially changed from the amounts originally reported as a result of the Company's first quarter 2018 adoption of ASU No. 2017-7, Compensation-Retirement Benefits (Topic 715): Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost.

## 12. REVENUE FROM CONTRACTS WITH CUSTOMERS

In the majority of instances the Company deems a contract with a customer to exist when a purchase order is received from a customer for a specified quantity of product or products and the Company acknowledges receipt of such purchase order. In some instances the Company has entered into manufacturing supply agreements with customers but these agreements typically do not bind a customer to any purchase volume requirements and thus an obligation is not created until the customer submits a purchase order to the Company. The Company's contracts typically have a single performance obligation that is satisfied at the time product is shipped. For a small portion of the business, performance obligations are deemed satisfied when product is delivered to a customer location. Revenue is recognized when performance obligations under terms of a contract with a customer have been satisfied, which is predominantly at a point in time. With the 2018 adoption of ASU 2014-09, revenue is currently recognized when a customer obtains control of a product as compared to the "risk and rewards" criteria used in prior years. However, the adoption of ASU 2014-09 did not have a material impact on the Company's financial position or results of operations during the first six months of 2018.

Payment terms on sales of product typically range from 30 to 60 days and ordinarily do not exceed 75 days. As a result, the Company has concluded it does not provide any significant benefits of financing to its customers.

The Company has elected to account for shipping and handling as activities to fulfill a promise to transfer the good. As such, shipping and handling fees billed to customers in a sales transaction are recorded in Net Sales and shipping and handling costs incurred are recorded in Cost of Sales. The Company has elected to exclude from Net Sales any value added, sales and other taxes that it collects concurrently with revenue producing activities. These accounting policy elections are consistent with the manner in which the Company has historically recorded shipping and handling fees and taxes.

In some instances, a customer may qualify for a rebate based on the volume of purchases made over a specified period of time, typically a quarterly or annual period. The Company estimates the expected volume of total purchases using actual volumes, customer projections and historical order patterns and accrues for these rebates based on the best available information at the time. These estimated rebates are treated as a reduction to Net Sales with the offset being recognized within Current Liabilities. This methodology is consistent with the manner in which the Company has historically estimated and recorded volume based rebates. In other instances, discounts for early payments are offered to certain customers. These discounts are principally accrued for based on a customer's historical use of discounts. These estimated early payment discounts are accounted for similarly to volume rebates. These forms of variable consideration are considered part of the transaction price.

The Company warrants its products from defects. The Company has concluded that these represent assurance-type warranties as opposed to service-type warranties. Product defects are rare in occurrence. As a result, the Company does not maintain any warranty accruals until such time as it is probable a product defect exists.

As of June 30, 2018, the Company did not have any contract assets or contract liabilities. A contract liability would typically arise when an advance or deposit is received from a customer before the Company recognizes revenue. In practice, this is extremely rare as it would require a customer to make a payment prior to a performance obligation being satisfied. If such a situation did arise the Company would maintain a deferred revenue liability until the time a performance obligation has been satisfied. The Company did not recognize any revenue in the current period from any pre-existing contract liability balance.

The tables below provides a geographic disaggregation of net sales for the three and six months ended June 30, 2018 and 2017. The Company's business segmentation by geographic region most effectively captures the nature and economic characteristics of the Company's revenue streams impacted by economic factors. This regional data is the predominant information used by senior management to assess the financial performance of operating segments and make resource allocation decisions.

| (In thousands) | For the Three Months Ended June 30, 2018 | | | |
|---|---|---|---|---|
| | Surfactants | Polymers | Specialty Products | Total |
| Geographic Market | | | | |
| North America | $218,029 | $86,966 | $18,674 | $323,669 |
| Europe | 66,065 | 45,028 | 3,441 | 114,534 |
| Latin America | 56,579 | 633 | — | 57,212 |
| Asia | 16,211 | 8,240 | — | 24,451 |
| Total | $356,884 | $140,867 | $22,115 | $519,866 |

| (In thousands) | For the Three Months Ended June 30, 2017 | | | |
|---|---|---|---|---|
| | Surfactants | Polymers | Specialty Products | Total |
| Geographic Market | | | | |
| North America | $199,016 | $86,925 | $16,203 | $302,144 |
| Europe | 65,289 | 46,854 | 8,377 | 120,520 |
| Latin America | 48,559 | 960 | — | 49,519 |
| Asia | 16,470 | 6,448 | — | 22,918 |
| Total | $329,334 | $141,187 | $24,580 | $495,101 |

| (In thousands) | For the Six Months Ended June 30, 2018 | | | |
|---|---|---|---|---|
| | Surfactants | Polymers | Specialty Products | Total |
| Geographic Market | | | | |
| North America | $438,434 | $160,440 | $33,488 | $632,362 |
| Europe | 144,436 | 86,812 | 7,089 | 238,337 |
| Latin America | 98,267 | 1,460 | — | 99,727 |
| Asia | 34,687 | 14,088 | — | 48,775 |
| Total | $715,824 | $262,800 | $40,577 | $1,019,201 |

| (In thousands) | For the Six Months Ended June 30, 2017 | | | |
|---|---|---|---|---|
| | Surfactants | Polymers | Specialty Products | Total |
| Geographic Market | | | | |
| North America | $397,259 | $165,289 | $31,138 | $593,686 |
| Europe | 128,712 | 89,257 | 12,498 | 230,467 |
| Latin America | 92,064 | 2,258 | — | 94,322 |
| Asia | 33,902 | 10,993 | — | 44,895 |
| Total | $651,937 | $267,797 | $43,636 | $963,370 |

13. DEBT

At June 30, 2018, and December 31, 2017, debt comprised the following:

| (In thousands) | Maturity Dates | June 30, 2018 | December 31, 2017 |
|---|---|---|---|
| Unsecured private placement notes | | | |
| 3.95% (net of unamortized debt issuance cost of $381 and $346 for 2018 and 2017, respectively) | 2021-2027 | $99,619 | $99,654 |
| | 2019-2025 | 99,625 | 99,657 |

| | | | |
|---|---|---|---|
| 3.86% (net of unamortized debt issuance cost of $375 and $343 for 2018 and 2017, respectively) | | | |
| 4.86% (net of unamortized debt issuance cost of $205 and $191 for 2018 and 2017, respectively) | 2018-2023 | 55,509 | 55,523 |
| 5.88% (net of unamortized debt issuance cost of $99 and $95 for 2018 and 2017, respectively) | 2018-2022 | 22,758 | 28,476 |
| 5.69% (net of unamortized debt issuance cost of $7 and $12 for 2018 and 2017, respectively) | 2018 | 5,707 | 5,703 |
| Debt of foreign subsidiaries | | | |
| Unsecured bank debt, foreign currency | 2018 | 3,598 | 1,786 |
| Total debt | | $286,816 | $290,799 |
| Less current maturities | | 24,312 | 22,500 |
| Long-term debt | | $262,504 | $268,299 |

On January 30, 2018, the Company entered into a five year committed $350 million multi-currency revolving credit facility that matures on January 30, 2023 with a syndicate of banks. This credit facility replaced the Company’s prior $125 million credit agreement. The Company’s outstanding Note Purchase Agreements were amended effective January 30, 2018 to make certain covenants consistent with those included in the credit agreement. The Company maintains standby letters of credit under its workers’ compensation insurance agreements and for other purposes, as needed from time to time, which are issued under the revolving credit agreement. As of June 30, 2018, the Company had outstanding letters of credit totaling $5,302,000 and no outstanding debt under this agreement. There was $344,698,000 available under the revolving credit agreement as of June 30, 2018.

The Company's loan agreements contain provisions which, among others, require maintenance of certain financial ratios and place limitations on additional debt, investments and payment of dividends. Based on the loan agreement provisions that place limitations on dividend payments, unrestricted retained earnings (i.e., retained earnings available for dividend distribution) were $154,639,000 and $190,495,000 at June 30, 2018 and December 31, 2017, respectively.

14. OTHER, NET

Other, net in the consolidated statements of income included the following:

| | Three Months Ended | | Six Months Ended | |
|---|---|---|---|---|
| (In thousands) | June 30, | | June 30, | |
| | 2018 | 2017 | 2018 | 2017 |
| Foreign exchange gains (losses) | $116 | $(15 ) | $1,169 | $(499 ) |
| Investment income | 90 | 49 | 229 | 151 |
| Realized and unrealized gains on investments | 407 | 931 | 504 | 2,576 |
| Net periodic benefit cost | (129) | (172) | (258 ) | (343 ) |
| Other, net | $484 | $793 | $1,644 | $1,885 |

Based on requirements of ASU No. 2017-07, Compensation-Retirement Benefits (Topic 715): Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost, the Company reclassified Net periodic benefit cost outside of income from operations for the prior year periods. See Note 8 for more details for the components of Net periodic benefit cost.

15. BUSINESS RESTRUCTURING

In May 2016, the Company announced plans to shut down its Longford Mills, Ontario, Canada (Longford Mills) manufacturing facility, a part of the Surfactant reportable segment, by December 31, 2016. The shutdown plan was developed as an effort to improve the Company's asset utilization in North America and to reduce the Company's fixed cost base. Manufacturing operations at the Longford Mills plant ceased by the end of 2016, and production of goods manufactured at the facility was transferred to other Company production sites in the United States. Decommissioning of the assets is expected to continue throughout 2018. As of June 30, 2018, $5,470,000 of aggregate restructuring expense has been recognized, reflecting $1,594,000 of termination benefits for approximately 30 employees and $3,876,000 for other expenses, principally asset decommissioning costs.

Below is a reconciliation of the restructuring liabilities as of March 31, 2018 and June 30, 2018:

| (In thousands) | Termination | Other | Total |
|---|---|---|---|

| | Benefits | Expense | |
|---|---|---|---|
| Restructuring liability at December 31, 2017 | $ 592 | $ 99 | $691 |
| Expense recognized | — | 358 | 358 |
| Amounts paid | (140 ) | (409 ) | (549) |
| Foreign currency translation | (3 ) | (4 ) | (7 ) |
| Restructuring liability at March 31, 2018 | $ 449 | $ 44 | $493 |
| Expense recognized | — | 273 | 273 |
| Amounts paid | (79 ) | (226 ) | (305) |
| Foreign currency translation | (7 ) | (2 ) | (9 ) |
| Restructuring liability at June 30, 2018 | $ 363 | $ 89 | $452 |

In June 2017, the Company eliminated 11 positions from manufacturing operations at its Singapore plant, which is part of the Company's Surfactant segment. The reduction in positions was made to better align the number of personnel with business requirements and to reduce costs at that site. As a result of the reduction in workforce, termination expense of $132,000 was recognized in the consolidated statements of income for the three and six months ended June 30, 2017. There is no more termination liability remaining for this site.

## 16. ACQUISITION

### 2018 Acquisition

On March 26, 2018, the Company, through a subsidiary in Mexico, acquired BASF Mexicana, S.A.DE C.V.'s (BASF) production facility in Ecatepec, Mexico and a portion of its related surfactants business. The facility, which is near Mexico City, has over 50,000 metric tons of capacity, 124,000 square feet of warehouse space, a large laboratory and office space. The acquired assets and business are included in the Company's Surfactants segment. The purchase price of the acquisition was $21,475,000 and was paid with cash on hand. The primary assets acquired were land, buildings, machinery and equipment and inventory. The acquisition was accounted for as a business combination, and, accordingly, the assets acquired were measured and recorded at their estimated fair values. The purchase price allocation remains preliminary as of June 30, 2018 pending finalization of the value of inventory acquired.

| (In thousands) | |
|---|---|
| Assets: | |
| Property, plant and equipment | $14,464 |
| Inventory | 4,500 |
| Value-added tax receivables | 2,511 |
| Total assets acquired | $21,475 |

The acquired business is expected to have minimal impact on the Company's 2018 financial results. Pro forma financial information for the first six months of 2017 and 2018 has not been included because revenues and earnings of the Company would not have been significantly different than reported had the acquisition date been January 1, 2017.

## 17. INCOME TAXES

On December 22, 2017, the U.S. government enacted comprehensive tax legislation commonly referred to as the Tax Cuts and Jobs Act (Tax Act). The Tax Act made broad and complex changes to the U.S. tax code. For various reasons that are discussed more fully below, we have not completed our accounting for the income tax effects of certain elements of the Tax Act. If we were able to make reasonable estimates of the effects of elements for which our analysis is not yet complete, we recorded provisional adjustments. If we were not yet able to make reasonable estimates of the impact of certain elements, we have not recorded any adjustments related to those elements and have continued accounting for them in accordance with ASC 740 on the basis of the tax laws in effect before the Tax Act.

Our accounting for the Tax Act is incomplete. As noted at year-end, we were able to reasonably estimate certain effects and, therefore, recorded the provisional adjustments related to the following:

Reduction of U.S. federal corporate tax rate: The Tax Act reduced the corporate tax rate to 21 percent, effective January 1, 2018. We recorded a provisional adjustment for certain of our deferred tax assets and liabilities associated with the tax rate reduction for the year ended December 31, 2017.

We have not made any additional measurement-period adjustments in the first six months of 2018 because such adjustments may be affected by other analyses related to the Tax Act, including, but not limited to, our calculation of deemed repatriation of deferred foreign income and the state tax effect of adjustments made to federal temporary differences. However, we are continuing to gather additional information to complete our accounting for this item and expect to complete our accounting within the prescribed measurement period.

Deemed Repatriation Transition Tax: The Transition Tax is a tax on previously untaxed accumulated and current earnings and profits of certain of our foreign subsidiaries. We recorded a provisional Transition Tax obligation for the year ended December 31, 2017.

We have not made any additional measurement-period adjustments in the quarter because we are continuing to gather additional information to more precisely compute the amount of the Transition Tax. However, we expect to complete our accounting within the prescribed measurement period.

Our accounting for the Tax Act is incomplete. As noted at year-end, we were not yet able to reasonably estimate the effects for the items set forth below. Therefore, no provisional adjustments were recorded:

Global intangible low taxed income (GILTI): The Tax Act requires the Company to include certain income (GILTI) of its foreign subsidiaries in gross income. The amount of this inclusion is determined under complex rules, and depends, in part,

on the character of income earned by the foreign subsidiaries, the tax bases of those subsidiaries' assets and the amount of certain interest expenses.

Under GAAP, we are allowed to make an accounting policy choice of either (1) treating taxes due on future income inclusions related to GILTI as a current-period expense when incurred (the period cost method) or (2) accounting for such amounts in measuring deferred taxes (the deferred method). Our selection of an accounting policy with respect to the new GILTI tax rules will depend, in part, on analyzing our global income to determine whether we expect to have future income inclusions related to GILTI and, if so, what the impact is expected to be. These determinations depend not only on our current structure and estimated future results of global operations but also our intent and ability to modify our structure and/or our business. Therefore, we have not made any adjustments or estimates related to any potential deferred tax liabilities related to GILTI in our financial statements and have not made a policy decision regarding whether to record deferred tax liabilities related to GILTI.

Deductibility of Executive Compensation: The Tax Act amended certain aspects of Section 162(m) of the Internal Revenue Code (Section 162(m)), which generally disallows a tax deduction for annual compensation paid to "covered employees" in excess of $1 million, including eliminating an exception to the deduction limit for "qualified performance-based compensation," effective for tax years beginning after December 31, 2017. The Tax Act provides for a grandfather provision, pursuant to which remuneration that is provided pursuant to a written binding contract in effect on November 2, 2017, and which has not been modified in any material respect on or after that date, will not be subject to the amendments made to Section 162(m) by the Tax Act and will remain eligible for deduction as qualified performance-based compensation. To the extent available, we intend to continue to treat "qualified performance-based compensation" that is grandfathered under the Tax Act as deductible compensation. We have not yet completed our evaluation of our existing compensation arrangements to determine whether any amounts payable to our Section 162(m) covered employees may continue to constitute qualified performance-based compensation under Section 162(m) and qualify under the grandfather provision. Therefore, we have not made any adjustments or estimates related to any potential tax liabilities in our financial statements related to the amendments to Section 162(m).

Cost recovery: We have not yet completed all of the computations necessary or completed an inventory of our 2017 expenditures that qualify for immediate expensing. Therefore, we have not made any adjustments or estimates related to any potential tax liabilities in our financial statements related to immediate expensing.

Valuation allowances: The Company must assess whether valuation allowances assessments are affected by various aspects of the Tax Act (e.g., GILTI inclusions and new categories of foreign tax credits). Because, as discussed herein, the Company has recorded no amounts related to certain portions of the Tax Act, any corresponding determination of the need for or change in a valuation allowance has not been completed and no changes to valuation allowances as a result of the Tax Act have been recorded.

18. RECENT ACCOUNTING PRONOUNCEMENTS

In May 2014, the Financial Accounting Standards Board (FASB) issued ASU No. 2014-9, Revenue from Contracts with Customers (Topic 606). The new update was later amended by ASU No. 2015-14, Revenue from Contracts with Customers (Topic 606): Deferral of the Effective Date. The standard outlines a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers. In addition, the ASU requires expanded disclosures about revenue recognition that enable the users of the financial statements to understand the nature, amount, timing and uncertainty of revenue and cash flows arising from contracts with customers. ASU No. 2014-09 supersedes most of the previous revenue recognition guidance. For public entities, the new guidance, as amended, is effective for annual reporting periods beginning after December 15, 2017, including interim periods within that reporting period. On January, 1, 2018, the Company adopted ASU No. 2014-9, which did not have a material effect on the Company’s financial position, results of operations or cash flows. The Company has added Note 12 – Revenue from Contracts with Customers to comply with the expanded disclosure requirements of ASU No. 2014-9.

In February 2016, the FASB issued ASU No. 2016-2, Leases (Topic 842). This guidance requires a dual approach for lessee accounting whereby a lessee will account for lease arrangements with terms greater than 12 months as either finance leases or operating leases. Both finance leases and operating leases will be recognized on the lessee’s balance sheet as right-of-use assets and corresponding lease liabilities, with differing methodologies for income statement recognition. In addition, the ASU requires expanded qualitative and quantitative disclosures about the Company’s lease arrangements. This guidance is effective for public business entities for fiscal years, and interim periods within those years, beginning after December 15, 2018. Early adoption is permitted. A modified retrospective approach is required for all leases existing or entered into after the beginning of the earliest comparative period in the consolidated financial statements. Most of the Company’s operating leases

will be required to be placed on the balance sheet. The Company is currently in the process of collecting and reviewing its lease data and assessing the quantitative impact that adoption of ASU No. 2016-2 will have on its financial position, results of operations and cash flows.

In August 2016, the FASB issued ASU No. 2016-15, Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments, which adds or clarifies guidance on the classification of eight specific types of cash flows. The update is intended to reduce the existing diversity in practice with respect to the specific cash flow items. The amendments in ASU No. 2016-15 are effective for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years. Early adoption is permitted. On January 1, 2018, the Company adopted ASU No. 2016-15, which had an immaterial impact on the cash flow presentation and did not impact the Company's financial position or results of operations.

In October 2016, the FASB issued ASU No. 2016-16, Income Taxes (Topic 740): Intra-Entity Transfers of Assets Other Than Inventory. The update requires an entity to recognize the income tax consequences of an intra-entity transfer of an asset other than inventory when the transfer occurs. Current accounting guidance prohibits the recognition of current and deferred income taxes for an intra-entity asset transfer until the asset has been sold to an outside party. The amendments in ASU No. 2016-16 are effective for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years. Early adoption is permitted for all entities as of the beginning of an annual reporting period for which financial statements (interim or annual) have not been issued or made available for issuance. That is, earlier adoption should be in the first interim period if an entity issues interim financial statements. The amendments in this update should be applied on a modified retrospective basis through a cumulative-effect adjustment directly to retained earnings as of the beginning of the period of adoption. On January 1, 2018, the Company adopted ASU No. 2016-16, which did not have a material effect on the Company's financial position or results of operations and cash flows.

In January 2017, the FASB issued ASU No. 2017-4, Intangibles – Goodwill and Other (Topic 350): Simplifying the Test for Goodwill Impairment, which eliminates Step 2 from the goodwill impairment test. When an indication of impairment was identified after performing the first step of the goodwill impairment test, Step 2 required that an entity determine the fair value at the impairment testing date of its assets and liabilities (including unrecognized assets and liabilities) using the same procedure that would be required in determining the fair value of assets acquired and liabilities assumed in a business combination. Under the amendments in ASU No. 2017-4, an entity would perform its annual, or interim, goodwill impairment test by comparing the fair value of a reporting unit with its carrying value. An entity would recognize an impairment charge for the amount by which the carrying value exceeds the reporting unit's fair value. In addition, an entity must consider income tax effects from any tax deductible goodwill on the carrying amount of the reporting unit when measuring the goodwill impairment loss, if applicable. A public business entity that is a SEC filer should adopt the amendments in ASU No. 2017-4 for its annual, or any interim, goodwill impairment tests in fiscal years beginning after December 15, 2019. It is not expected that the adoption of the guidance in ASU No. 2017-4 will have a material effect on the Company's financial position, results of operations or cash flows.

In January 2017, the FASB issued ASU No. 2017-1, Business Combination (Topic 805): Clarifying the Definition of a Business, with the objective of adding guidance to assist with evaluating whether transactions should be accounted for as an acquisition (or disposal) of assets or a business. This update provides criteria to help determine when a set of assets and activities comprise a business as opposed to an acquisition of assets. This guidance is effective for annual periods beginning after December 15, 2017, including interim periods within those periods. On January 1, 2018, the Company adopted ASU No. 2017-1, which did not have a material effect on the Company's financial position, results of operations or cash flows.

In March 2017, the FASB issued ASU No. 2017-7, Compensation – Retirement Benefits (Topic 715): Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost, which amends existing

guidance for the income statement presentation of the components of net periodic benefit cost for an entity's sponsored defined benefit pension and other postretirement plans. The amended guidance requires entities to include the current service component of net periodic benefit cost in employee compensation costs in the income statement and to include all other components elsewhere in the income statement outside of income from operations. In addition, only the service cost component of net benefit cost is eligible for capitalization. For the Company, ASU No. 2017-7 is effective for interim and annual periods beginning after December 31, 2017, with early adoption permitted as of the beginning of any annual period for which an entity's financial statements have not been issued. The requirements for the separate presentation of the service cost component and the other components of net periodic benefit cost must be adopted on a retrospective basis. The requirement to capitalize only the service component of net periodic benefit cost must be adopted on a prospective basis. On January 1, 2018, the Company adopted ASU No. 2017-7, which did not have a material effect on the Company's financial position or cash flows but affected the presentation of the Company's results of operations. For amounts reclassified on the Company's statements of the results of operations, see Note 8 and Note 14.

In August 2017, the FASB issued ASU No. 2017-12, Derivatives and Hedging (Topic 815): Targeted Improvements to Accounting for Hedging Activities, which amends previous guidance regarding hedge accounting recognition and presentation requirements. The updated guidance alters the hedge accounting model to make achieving hedge accounting easier for an entity



---

and to have such accounting better reflect an entity's risk management activities. ASU No. 2017-12 also adds new, and amends previous, disclosure requirements. For the Company, ASU No. 2017-12 is effective for interim and annual periods beginning after December 15, 2018. Early adoption is permitted. Entities must apply a modified retrospective approach to existing hedging relationships as of the adoption date. At present, because the Company has not entered into any transactions designated as accounting hedges, adoption of ASU No. 2017-12 is not expected to have a material effect on the Company's financial position, results of operations and cash flows.

In January 2018, the FASB issued ASU No. 2018-01, Leases (Topic 842): Land Easement Practical Expedient for Transition to Topic 842, which permits an entity to select an optional transition practical expedient to not evaluate under Topic 842 existing or expired land easements that were not previously accounted for as leases under the current leases guidance in Topic 840. An entity that elects this practical expedient should apply the practical expedient consistently to all of its existing or expired land easements that were not previously accounted for as leases under Topic 840. Once an entity adopts Topic 842, it should apply that Topic prospectively to all new (or modified) land easements to determine whether the arrangement should be accounted for as a lease. An entity that does not elect this practical expedient should evaluate all existing or expired land easements in connection with the adoption of the new lease requirements in Topic 842 to assess whether they meet the definition of a lease. An entity should continue to apply its current accounting policy for accounting for land easements that existed before the entity's adoption of Topic 842. This update is effective for public business entities for fiscal years, and interim periods within those years, beginning after December 15, 2018. Early adoption is permitted. The Company is assessing the quantitative impact that adoption of ASU No. 2018-01 will have on its financial position, results of operations and cash flows.

In February 2018, the FASB issued ASU No. 2018-02, Income Statement-Reporting Comprehensive Income (Topic 220): Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income, which permits a reclassification from accumulated other comprehensive income to retained earnings for stranded tax effects resulting from the Tax Cuts and Jobs Act. Consequently, the update eliminates the stranded tax effects resulting from the Tax Cuts and Jobs Act and will improve the usefulness of information reported to financial statement users. However, because the amendments only relate to the reclassification of the income tax effects of the Tax Cuts and Jobs Acts, the underlying guidance that requires that the effects of the change in tax laws or rates be included in income from continuing operations is not affected. The amendments in this update also require certain disclosures about stranded tax effects. This update is effective for public business entities for fiscal years, and interim periods within those years, beginning after December 15, 2018. Early adoption is permitted. The Company is assessing the quantitative impact that adoption of ASU No. 2018-02 will have on its financial position, results of operations and cash flows.

Item 2 - Management’s Discussion and Analysis of Financial Condition and Results of Operations

The following is management’s discussion and analysis (MD&A) of certain significant factors that have affected the Company’s financial condition and results of operations during the interim periods included in the accompanying condensed consolidated financial statements.

Certain statements in this Quarterly Report on Form 10-Q, other than purely historical information, are “forward-looking statements” within the meaning of the Private Securities Litigation Reform Act of 1995, Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended (the Exchange Act). These statements include statements about Stepan Company’s and its subsidiaries’ (the Company) plans, objectives, strategies, financial performance and outlook, trends, the amount and timing of future cash distributions, prospects or future events and involve known and unknown risks that are difficult to predict. As a result, the Company’s actual financial results, performance, achievements or prospects may differ materially from those expressed or implied by these forward-looking statements. In some cases, forward-looking statements can be identified by the use of words such as “may,” “could,” “expect,” “intend,” “plan,” “seek,” “anticipate,” “believe,” “estimate,” “ “predict,” “potential,” “continue,” “likely,” “will,” “would,” “should,” “illustrative” and variations of these terms and similar expressions, or the negative of these terms or similar expressions. Such forward-looking statements are necessarily based upon estimates and assumptions that, while considered reasonable by the Company and its management based on their knowledge and understanding of the business and industry, are inherently uncertain. These statements are not guarantees of future performance, and stockholders should not place undue reliance on forward-looking statements. There are a number of risks, uncertainties and other important factors, many of which are beyond the Company’s control, that could cause the Company’s actual results to differ materially from the forward-looking statements contained in this Quarterly Report on Form 10-Q.

Such risks, uncertainties and other important factors, include, among others, the risks, uncertainties and factors set forth under “Part I-Item IA. Risk Factors” in the Company’s Annual Report on Form 10-K for the year ended December 31, 2017 inclusive of: (a) the risks and uncertainties related to accidents, unplanned production shutdowns or disruptions in any of the Company’s manufacturing facilities; (b) global competition and the Company’s ability to successfully compete; (c) volatility of raw material, natural gas and electricity costs as well as any disruption in their supply; (d) disruptions in transportation or significant changes in transportation costs; (e) reduced demand for Company products due to customer product reformulations or new technologies; (f) the Company’s ability to make acquisitions of suitable candidates and successfully integrate acquisitions; (g) the Company’s ability to keep and protect its intellectual property rights; (h) international business risks, including fluctuations in currency exchange rates, legal restrictions and taxes; (i) potentially adverse tax consequences due to the international scope of the Company’s operations; (j) the impact of changes in the tax code as a result of recent U.S. federal tax legislation and uncertainty as to how some of those changes may be applied; (k) compliance with anti-corruption, environmental, health and safety and product registration laws; (l) the Company’s inability to accurately estimate and maintain appropriate levels of recorded liabilities for existing and future contingencies; (m) the Company’s ability to operate within the limitations of its debt covenants; (n) downgrades to the Company’s credit ratings or disruptions to the Company’s ability to access well-functioning capital markets; (o) downturns in certain industries and general economic downturns; (p) conflicts, military actions, terrorist attacks and general instability, particularly in certain energy-producing nations, along with increased security regulations; (q) cost overruns, delays and miscalculations in capacity needs with respect to the Company’s expansion or other capital projects; (r) interruption of, damage to or compromise of the Company’s IT systems and failure to maintain the integrity of customer, colleague or Company data; (s) unfavorable resolution of litigation against the Company; (t) and the Company’s ability to retain its executive management and other key personnel.

These factors are not necessarily all of the important factors that could cause the Company’s actual financial results, performance, achievements or prospects to differ materially from those expressed in or implied by any of its forward-looking statements. Other unknown or unpredictable factors also could harm the Company’s results. All forward-looking statements attributable to the Company or persons acting on the Company’s behalf are expressly

qualified in their entirety by the cautionary statements set forth above. Forward-looking statements speak only as of the date they are made, and the Company does not undertake or assume any obligation to update publicly any of these forward-looking statements to reflect actual results, new information or future events, changes in assumptions or changes in other factors affecting forward-looking statements, except to the extent required by applicable laws. If the Company updates one or more forward-looking statements, no inference should be drawn that the Company will make additional updates with respect to those or other forward-looking statements. The "Company," "we," "our" or "us" means Stepan Company and one or more of its subsidiaries only.

Overview

The Company produces and sells intermediate chemicals that are used in a wide variety of applications worldwide. The overall business comprises three reportable segments:

- Surfactants – Surfactants, which accounted for 70 percent of Company consolidated net sales for the first half of 2018, are principal ingredients in consumer and industrial cleaning products such as detergents for washing clothes, dishes, carpets, floors and walls, as well as shampoos and body washes. Other applications include fabric softeners, germicidal quaternary compounds, lubricating ingredients, emulsifiers for spreading agricultural products and industrial applications such as latex systems, plastics and composites. Surfactants are manufactured at five sites in the United States, three European sites (United Kingdom, France and Germany), five Latin American sites (one site in Colombia and two sites in Brazil and Mexico) and two Asian sites

(Philippines and Singapore). In 2016, the Company shut down its production facility in Canada, moving the production of goods previously manufactured in Canada to other Company production sites in the United States. Manufacturing operations at that facility ceased in the fourth quarter of 2016 but decommissioning activities were incurred in 2017 and will continue throughout 2018. In March 2018, the Company, through a subsidiary in Mexico, acquired a production facility and a portion of its related surfactant business from BASF Mexicana, S.A. DE C.V. See the "2018 Acquisition" paragraph below for additional details.

- Polymers – Polymers, which accounted for 26 percent of consolidated net sales for the first half of 2018, include polyurethane polyols, polyester resins and phthalic anhydride. Polyurethane polyols are used in the manufacture of rigid foam for thermal insulation in the construction industry and are also a base raw material for coatings, adhesives, sealants and elastomers (collectively, CASE products). Powdered polyester resins are used in coating applications. CASE and polyester resins are collectively referred to as specialty polyols. Phthalic anhydride is used in unsaturated polyester resins, alkyd resins and plasticizers for applications in construction materials and components of automotive, boating and other consumer products. In addition, the Company uses phthalic anhydride internally in the production of polyols. In the United States, polyurethane polyols and phthalic anhydride are manufactured at the Company's Millsdale, Illinois, site and specialty polyols are manufactured at the Company's Columbus, Georgia, site. In Europe, polyurethane polyols are manufactured by the Company's subsidiary in Germany, and specialty polyols are manufactured by the Company's Poland subsidiary. In China, polyurethane polyols and specialty polyols are manufactured at the Company's Nanjing, China, plant.

- Specialty Products – Specialty products, which accounted for four percent of consolidated net sales for the first half of 2018, include flavors, emulsifiers and solubilizers used in food, flavoring, nutritional supplement and pharmaceutical applications. Specialty products are primarily manufactured at the Company's Maywood, New Jersey, site and, in some instances, at outside contractors.

2018 Acquisition

On March 26, 2018, the Company, through a subsidiary in Mexico, acquired BASF Mexicana, S.A. DE C.V.'s (BASF) production facility in Ecatepec, Mexico, and a portion of its related surfactants business. The facility, which is near Mexico City, has over 50,000 metric tons of capacity, 124,000 square feet of warehouse space, a laboratory and office space. The acquisition supports the Company's growth strategy in Latin America. The Company believes that this acquisition should enhance its market position and supply capabilities for surfactants in Mexico and position the Company to grow in both the consumer and functional surfactants markets. See Note 16 for additional details.

Deferred Compensation Plans

The accounting for the Company's deferred compensation plans can cause period-to-period fluctuations in Company expenses and profits. Compensation expense results when the values of Company common stock and mutual fund investment assets held for the plans increase, and compensation income results when the values of Company common stock and mutual fund investment assets decline. The pretax effect of all deferred compensation-related activities (including realized and unrealized gains and losses on the mutual fund assets held to fund the deferred compensation obligations) and the income statement line items in which the effects of the activities were recorded are displayed in the following table:

| | Income (Expense) For the Three |
|---|---|

| (In millions) | Months<br><br>Ended June 30,<br>2018 | 2017 | Change | |
|---|---|---|---|---|
| Deferred Compensation (Operating expenses) | $0.9 | $(5.0) | $ 5.9 | (1) |
| Realized/Unrealized Gains on Investments (Other, net) | 0.4 | 0.9 | (0.5) | |
| Investment Income (Other, net) | — | — | — | |
| Pretax Income Effect | $1.3 | $(4.1) | $ 5.4 | |

| (In millions) | Income (Expense) For the Six Months<br><br>Ended June 30,<br>2018 | 2017 | Change | |
|---|---|---|---|---|
| Deferred Compensation (Administrative expense) | $(0.7) | $(5.4) | $ 4.7 | (1) |
| Realized/Unrealized Gains on Investments (Other, net) | 0.5 | 2.5 | (2.0) | |
| Investment Income (Other, net) | 0.2 | 0.1 | 0.1 | |
| Pretax Income Effect | $- | $(2.8) | $ 2.8 | |

(1) See the applicable Corporate Expenses sections of this MD&A for details regarding the changes in deferred compensation expense.

Effects of Foreign Currency Translation

The Company's foreign subsidiaries transact business and report financial results in their respective local currencies. As a result, foreign subsidiary income statements are translated into U.S. dollars at average foreign exchange rates appropriate for the reporting period. Because foreign exchange rates fluctuate against the U.S. dollar over time, foreign currency translation affects period-to-period comparisons of financial statement items (i.e., because foreign exchange rates fluctuate, similar period-to-period local currency results for a foreign subsidiary may translate into different U.S. dollar results). The following table presents the effects that foreign currency translation had on the period-over-period changes in consolidated net sales and various income line items for the three and six months ended June 30, 2018 and 2017:

| | Three Months Ended June 30, | | | |
|---|---|---|---|---|
| (In millions) | 2018 | 2017[(1)] | Increase (Decrease) | Increase Due to Foreign Translation |
| Net Sales | $519.9 | $495.1 | $ 24.8 | $ 4.6 |
| Gross Profit | 89.3 | 90.0 | (0.7 ) | 0.5 |
| Operating Income | 44.7 | 39.1 | 5.6 | 0.2 |
| Pretax Income | 42.5 | 37.1 | 5.4 | 0.3 |

| | Six Months Ended June 30, | | | |
|---|---|---|---|---|
| (In millions) | 2018 | 2017[(1)] | Increase (Decrease) | Increase Due to Foreign Translation |
| Net Sales | $1,019.2 | $963.4 | $ 55.8 | $ 22.1 |
| Gross Profit | 178.9 | 182.1 | (3.2 ) | 2.6 |
| Operating Income | 84.3 | 85.4 | (1.1 ) | 1.3 |
| Pretax Income | 80.2 | 81.4 | (1.2 ) | 1.4 |

(1) The 2017 gross profit and operating income line items have been immaterially changed from the amounts originally reported as a result of the Company's first quarter 2018 adoption of ASU No. 2017-07 Compensation-Retirement Benefits (Topic 715).

RESULTS OF OPERATIONS

Three Months Ended June 30, 2018 and 2017

Summary

Net income attributable to the Company for the second quarter of 2018 increased 18 percent to $32.9 million, or $1.41 per diluted share, from $27.9 million, or $1.19 per diluted share, for the second quarter of 2017. Adjusted net income increased four percent to $32.1 million, or $1.38 per diluted share, from $30.9 million, or $1.32 per diluted share, in 2017 (see the "Reconciliation of Non-GAAP Adjusted Net Income and Diluted Earnings per Share" section of this MD&A for a reconciliation between reported net income attributable to the Company and related earnings per diluted share and non-GAAP adjusted net income and related earnings per diluted share). Below is a summary discussion of the major factors leading to the quarter-over-quarter changes in net sales, profits and expenses. A detailed discussion of segment operating performance for the second quarter of 2018 compared to the second quarter of 2017 follows the summary.

Consolidated net sales increased $24.8 million, or five percent in the second quarter of 2018 compared to the second quarter of 2017. The increase was mostly attributable to a five percent increase in sales volume, which favorably impacted the quarter-over-quarter change in net sales by $26.6 million. Most of the sales volume increase related to the Surfactant segment. Foreign currency translation positively impacted the quarter-over-quarter net sales change by $4.6 million. The favorable foreign currency translation effect primarily reflected a weaker U.S. dollar against the European euro, British pound sterling and Polish zloty. Lower average selling prices negatively impacted the quarter-over-quarter change in net sales by $6.4 million.

Operating income for the second quarter of 2018 increased $5.6 million, or 14 percent, compared to operating income reported for the second quarter of 2017. Most of this consolidated operating income increase was related to lower 2018 deferred compensation expense which declined by $5.9 million quarter-over-quarter. With respect to the segments, Surfactant operating income improved by

$3.1 million but was largely offset by lower Polymer and Specialty Product operating income of $1.8 million and $1.2 million, respectively.

Operating expenses (including deferred compensation and business restructuring expenses) decreased $6.3 million, or 12 percent, between quarters. Changes in the individual income statement line items that comprise the Company's operating expenses were as follows:

- Selling expenses increased $0.1 million, or one percent, quarter over quarter.

- Administrative expenses increased $0.3 million, or two percent, quarter over quarter.

- Research, development and technical service (R&D) expenses decreased $0.5 million, or four percent, quarter over quarter primarily due to lower U.S. fringe benefit expenses.

- Deferred compensation expense decreased $5.9 million, quarter over quarter, primarily due to a second quarter 2018 decrease in the value of Company common stock compared to a second quarter 2017 increase in Company common stock value. See the "Overview" and "Segment Results - Corporate Expenses" sections of this MD&A for further details.

- Business restructuring charges totaled $0.3 million in the second quarter of 2018 versus $0.6 million in 2017. The 2018 restructuring charges related to decommissioning costs associated with the Company's manufacturing facility in Canada that ceased operations in the fourth quarter of 2016. The 2017 restructuring charges related to decommissioning costs associated with the Canadian plant ($0.5 million) and a reduction in workforce at the Company's Singapore plant ($0.1 million).

Net interest expense for the second quarter of 2018 decreased $0.2 million, or seven percent, from net interest expense for the same quarter of last year primarily due to lower average debt levels and higher interest income earned on excess cash.

Other, net was $0.5 million of income for the second quarter of 2018 compared to $0.8 million of income for the same period of 2017. The Company recognized $0.5 million of investment income (including realized and unrealized gains and losses) for the Company's deferred compensation and supplemental defined contribution mutual fund assets in the second quarter of 2018 compared to $1.0 million of income in last year's second quarter. In addition, the Company reported foreign exchange gains of $0.1 million in the second quarter of 2018 versus less than $0.1 million of losses in the second quarter of 2017. The Company also reported $0.1 million of net periodic pension cost in the second quarter of 2018 versus $0.2 million of expense in the second quarter of 2017.

The Company's effective tax rate was 22.5 percent for the second quarter of 2018 compared to 24.7 percent for the second quarter of 2017. The decrease was primarily attributable to a lower U.S. statutory tax rate of 21 percent in the second quarter of 2018 versus 35 percent in the second quarter of 2017. This benefit was partially offset by lower excess tax benefits derived from stock based compensation awards exercised or distributed in the second quarter of 2018 versus the second quarter of 2017.

Segment Results

For the Three
Months Ended

| (Dollars in thousands) Net Sales | June 30, 2018 | June 30, 2017 | Increase (Decrease) | Percent Change |
|---|---|---|---|---|
| Surfactants | $356,884 | $329,334 | $ 27,550 | 8 |
| Polymers | 140,867 | 141,187 | (320 ) | — |
| Specialty Products | 22,115 | 24,580 | (2,465 ) | -10 |
| Total Net Sales | $519,866 | $495,101 | $ 24,765 | 5 |

| (Dollars in thousands)<br>Operating Income | For the Three Months Ended<br>June 30, 2018 | <br>June 30, 2017[1] | Increase (Decrease) | Percent Change |
|---|---|---|---|---|
| Surfactants | $34,218 | $31,164 | $ 3,054 | 10 |
| Polymers | 19,458 | 21,283 | (1,825 ) | -9 |
| Specialty Products | 4,240 | 5,451 | (1,211 ) | -22 |
| Segment Operating Income | $57,916 | $57,898 | $ 18 | — |
| Corporate Expenses, Excluding Deferred Compensation and Restructuring | 13,823 | 13,163 | 660 | 5 |
| Deferred Compensation Expense | (865 ) | 5,016 | (5,881 ) | NM |
| Business Restructuring | 273 | 586 | (313 ) | -53 |
| Total Operating Income | $44,685 | $39,133 | $ 5,552 | 14 |

(1) The segment and total operating income line items have been immaterially changed from the amounts originally reported as a result of the Company’s first quarter 2018 adoption of ASU No. 2017-07 Compensation-Retirement Benefits (Topic 715).

Surfactants

Surfactants net sales for the second quarter of 2018 increased $27.6 million, or eight percent, over net sales for the second quarter of 2017. Higher sales volume had a favorable $22.6 million effect on the quarter-over-quarter change in net sales. All regions, with the exception of Europe, experienced sales volume growth. Higher selling prices and the favorable effects of foreign currency translation positively impacted net sales by $4.0 million and $1.0 million, respectively. A quarter-over-quarter comparison of net sales by region follows:

| (Dollars in thousands)<br>Net Sales | For the Three Months Ended<br>June 30, 2018 | <br>June 30, 2017 | Increase (Decrease) | Percent Change |
|---|---|---|---|---|
| North America | $218,029 | $199,016 | $ 19,013 | 10 |
| Europe | 66,065 | 65,289 | 776 | 1 |
| Latin America | 56,579 | 48,559 | 8,020 | 17 |
| Asia | 16,211 | 16,470 | (259 ) | -2 |
| Total Surfactants Segment | $356,884 | $329,334 | $ 27,550 | 8 |

Net sales for North American operations increased 10 percent between quarters. Higher sales volume, selling prices, and the favorable effects of foreign currency translation positively impacted the quarter-over-quarter change in net sales by $17.2 million, $1.5 million and $0.3 million, respectively. Sales volume increased nine percent primarily due to the sale of products used in laundry and cleaning, personal care and oilfield applications. Sales volumes of general surfactants to our distribution partners also increased. The foreign currency impact reflected a weaker U.S. dollar relative to the Canadian dollar.

Net sales for European operations increased one percent between quarters.  The favorable effects of foreign currency translation favorably impacted the quarter-over-quarter change in net sales by $4.6 million.  A weaker U.S. dollar against the European euro and British pound sterling led to the foreign currency translation effect.  Lower selling prices and a two percent decrease in sales volume unfavorably impacted the quarter-over-quarter change in net sales by $2.5 million and $1.3 million, respectively.

Net sales for Latin American operations increased 17 percent due to higher selling prices and an 11 percent increase in sales volume.  These items favorably impacted the quarter-over-quarter change in net sales by $6.1 million and $5.2 million respectively.  The higher selling prices were primarily due to the pass through of increased raw material costs to customers.  The higher sales volume is mostly related to the Company's 2018 first quarter acquisition in Ecatepec, Mexico, partially offset by lower demand and lost commodity business for products used in laundry and cleaning applications in Brazil.  Foreign currency translation negatively impacted the quarter-over-quarter change in net sales by $3.3 million.  The quarter-over-quarter strengthening of the U.S. dollar against the Brazilian real and the Mexican peso accounted for the majority of the unfavorable foreign currency effect.

Net sales for Asian operations decreased two percent primarily due to the negative impact of foreign currency translation and lower selling prices.  These items negatively impacted the quarter-over-quarter change in net sales by $0.7 million and $0.6 million, respectively.  A weaker Philippine peso relative to the U.S. dollar caused the negative foreign currency translation effect.  Sales volume increased six percent which positively impacted the quarter-over-quarter change in net sales by $1.0 million.  This sales volume growth was primarily driven by stronger demand for surfactants sold to our distribution partners.

Surfactants operating income for the second quarter of 2018 increased $3.1 million, or 10 percent, over operating income for the second quarter of 2017. Gross profit increased $3.0 million on improved results from all regions except Latin America. Operating expenses were flat. Quarter-over-quarter comparisons of gross profit by region and total segment operating expenses and operating income follow:

| (Dollars in thousands) | For the Three Months Ended June 30, 2018 | June 30, 2017[(1)] | Increase (Decrease) | Percent Change |
|---|---|---|---|---|
| Gross Profit and Operating Income | | | | |
| North America | $40,141 | $37,064 | $ 3,077 | 8 |
| Europe | 7,109 | 5,767 | 1,342 | 23 |
| Latin America | 5,441 | 7,690 | (2,249 ) | -29 |
| Asia | 4,827 | 4,034 | 793 | 20 |
| Surfactants Segment Gross Profit | $57,518 | $54,555 | $ 2,963 | 5 |
| Operating Expenses | 23,300 | 23,391 | (91 ) | |
| Surfactants Segment Operating Income | $34,218 | $31,164 | $ 3,054 | 10 |

The 2017 North America gross profit and the total operating expenses line items have been immaterially changed from the amounts originally reported as a result of the Company's first quarter 2018 adoption of ASU No. 2017-07 Compensation-Retirement Benefits (Topic 715).

(1)The 2017 North America gross profit and the total operating expenses line items have been immaterially changed from the amounts originally reported as a result of the Company's first quarter 2018 adoption of ASU No. 2017-07 Compensation-Retirement Benefits (Topic 715).

Gross profit for North American operations increased eight percent quarter over quarter principally due to higher sales volumes. Higher quarter-over-quarter sales of products used in laundry and cleaning, personal care and oilfield applications and products sold to our distribution partners contributed to the 2018 volume growth. Higher sales volumes favorably impacted the quarter-over-quarter change in gross profit by $3.2 million.

Gross profit for European operations increased 23 percent, or $1.3 million, between quarters primarily due to improved margins and the favorable impact of foreign currency translation. These items favorably impacted the quarter-over-quarter change in gross profit by $1.0 million and $0.5 million, respectively.

Gross profit for Latin American operations decreased 29 percent, or $2.2 million, quarter over quarter. This decrease was primarily due to lower unit margins and the unfavorable impact of foreign currency translation. These items negatively impacted the quarter-over-quarter change in gross profit by $2.5 million and $0.5 million, respectively. The lower unit margins were largely due to higher integration and start-up costs associated with the Company's 2018 first quarter acquisition in Ecatepec, Mexico. An 11 percent increase in sales volume, principally driven by the first quarter acquisition in Ecatepec, Mexico favorably impacted the quarter-over-quarter change in

gross profit by $0.8 million.

Gross profit for Asian operations increased 20 percent, or $0.8 million, between quarters, largely due to a six percent increase in sales volume and higher quarter-over-quarter production volume in Singapore, which led to lower unit overhead costs.

Operating expenses for the Surfactants segment were flat quarter over quarter.

Polymers

Polymers net sales for the second quarter of 2018 decreased $0.3 million versus net sales for the same period of 2017. A one percent increase in sales volume and the favorable impact of foreign currency translation positively impacted the quarter-over-quarter change in net sales by $1.6 million and $3.4 million, respectively. Lower selling prices negatively impacted the quarter-over-quarter change in net sales by $5.3 million. A quarter-over-quarter comparison of net sales by region follows:

| (Dollars in thousands) | For the Three Months Ended | | | |
|---|---|---|---|---|
| Net Sales | June 30, 2018 | June 30, 2017 | Increase (decrease) | Percent change |
| North America | $86,966 | $86,925 | $ 41 | — |
| Europe | 45,028 | 46,854 | (1,826) | -4 |
| Asia and Other | 8,873 | 7,408 | 1,465 | 20 |
| Total Polymers Segment | $140,867 | $141,187 | $ (320) | — |

Net sales for North American operations were flat versus prior year. Sales volume increased one percent which favorably impacted the net sales change by $1.0 million. The higher sales volume primarily reflects quarter-over-quarter growth within

specialty polyols and phthalic anhydride, partially offset by a decline in polyols used in rigid foam insulation due to lost market share. Selling prices decreased one percent, which had a $1.0 million negative effect on the quarter-over-quarter change in net sales.

Net sales for European operations decreased four percent. Lower selling prices and a one percent decrease in sales volume accounted for $4.3 million and $0.3 million, respectively, of the quarter-over-quarter net sales decrease. The lower selling prices primarily reflect the pass through of raw material price decreases. The favorable effects of foreign currency translation positively impacted the quarter-over-quarter change in net sales by $2.8 million.

Net sales for Asia and Other operations increased 20 percent quarter over quarter primarily due to an 11 percent increase in sales volume and the favorable effects of foreign currency translation. These items positively impacted the change in nets sales by $0.8 million and $0.5 million, respectively. The growth in sales volume was driven by polyols used in rigid foam applications.

Polymers operating income for the second quarter of 2018 declined $1.8 million, or nine percent, from operating income for the second quarter of last year. Gross profit decreased $1.8 million, or six percent, primarily due to reduced margins in North America partially offset by higher volumes and margins in Asia. Operating expenses were flat quarter-over-quarter. Quarter-over-quarter comparisons of gross profit by region and total segment operating expenses and operating income follow:

| | For the Three Months Ended | | | |
|---|---|---|---|---|
| (Dollars in thousands) | June 30, 2018 | June 30, 2017[(1)] | Increase (Decrease) | Percent Change |
| Gross Profit and Operating Income | | | | |
| North America | $18,880 | $ 21,405 | $ (2,525) | -12 |
| Europe | 6,950 | 7,208 | (258) | -4 |
| Asia and Other | 791 | (166) | 957 | NM |
| Polymers Segment Gross Profit | $26,621 | $ 28,447 | $ (1,826) | -6 |
| Operating Expenses | 7,163 | 7,164 | (1) | — |
| Polymers Segment Operating Income | $19,458 | $ 21,283 | $ (1,825) | -9 |

(1) The 2017 North America gross profit and the total operating expenses line items have been immaterially changed from the amounts originally reported as a result of the Company’s first quarter 2018 adoption of ASU No. 2017-07 Compensation-Retirement Benefits (Topic 715).

Gross profit for North American operations declined 12 percent quarter over quarter primarily due to reduced unit margins. The reduced margins reflects higher raw material costs that, due to competitive reasons, could not entirely be passed on to customers and less favorable product mix. A one percent increase in sales volume positively impacted the quarter-over-quarter change in gross profit by $0.3 million.

Gross profit for European operations decreased four percent due to lower margins that were mostly offset by the favorable effects of foreign currency translation. The lower margins negatively impacted the quarter-over-quarter change in gross profit by $0.7 million and foreign currency translation had a $0.4 million positive impact. A one percent decline in sales volume negatively impacted the quarter-over-quarter change in gross profit by less than $0.1 million.

Gross profit for Asia and Other operations increased $1.0 million primarily due to an 11 percent increase in sales volume.

Specialty Products

Net sales for the second quarter of 2018 declined $2.5 million, or 10 percent, from net sales for the second quarter of 2017. Lower sales volume and selling prices led to the net sales decline. Operating income declined $1.2 million quarter-over-quarter. The decline in operating income reflected a less favorable mix of sales, partially attributable to the timing of orders for certain products used in flavoring applications, and lower margins in the food and nutritional business.

Corporate Expenses

Corporate expenses, which are comprised of deferred compensation and other operating expenses that are not allocated to the reportable segments, decreased $5.5 million between quarters. Corporate expenses were $13.2 million in the second quarter of 2018 versus $18.8 million in 2017. The decrease was primarily attributable to deferred compensation income of $0.9 million recorded in the second quarter of 2018 versus deferred compensation expense of $5.0 million recorded a year ago. Partially offsetting this decrease were higher salaries and legal expenses.

.

The $5.9 million decrease in deferred compensation expense reflected a $5.17 per share decrease in the value of Company common stock in the second quarter of 2018 compared to an $8.33 per share increase for the second quarter of last year. The following table presents the quarter-end Company common stock market prices used in the computation of deferred compensation expenses for the three months ended June 30, 2018 and 2017:

| | 2018 | | 2017 | |
|---|---|---|---|---|
| | June 30 | March 31 | June 30 | March 31 |
| Company Common Stock Price | $78.01 | $83.18 | $87.14 | $78.81 |

Six Months Ended June 30, 2018 and 2017

Summary

Net income attributable to the Company for the first half of 2018 increased six percent to $63.6 million, or $2.73 per diluted share, from $59.8 million, or $2.56 per diluted share, for the first half of 2017. Adjusted net income increased two percent to $64.1 million, or $2.75 per diluted share, from $62.6 million, or $2.68 per diluted share (see the "Reconciliation of Non-GAAP Adjusted Net Income and Diluted Earnings per Share" section of this MD&A for reconciliations between reported net income attributable to the Company and related earnings per diluted share and non-GAAP adjusted net income and related earnings per diluted share). Below is a summary discussion of the major factors leading to the year-over-year changes in net sales, profits and expenses. A detailed discussion of segment operating performance for the first half of 2018 compared to the first half of 2017 follows the summary.

Consolidated net sales increased $55.8 million, or six percent, between years. Higher sales volume, the favorable impact of foreign currency translation and higher selling prices positively impacted net sales by $30.2 million, $22.1 million and $3.5 million respectively. Sales volume increased three percent in total. Sales volume in the Surfactant segment increased five percent while sales volume in the Polymer and Specialty Product segments declined four percent each. The favorable foreign currency translation effect primarily reflected a weaker U.S. dollar against the European currencies for countries where the Company has foreign operations, partially offset by a stronger U.S. dollar against the Brazil real and the Philippine peso.

Operating income for the first half of 2018 declined $1.0 million, or one percent, from operating income reported for the first half of 2017. Surfactant operating income improved year over year but was more than offset by a decline in Polymer and Specialty Products results.

Operating expenses (including deferred compensation and business restructuring expenses) declined $2.2 million, or two percent, between years. Changes in the individual income statement line items that comprise the Company's operating expenses were as follows:

- Selling expenses increased $1.6 million, or six percent, year over year largely due to higher bad debt expense, higher legal and consulting fees, higher salaries and an accumulation of other increases, none of which were individually significant.

- Administrative expenses increased $1.9 million, or five percent, year over year primarily due to higher U.S. legal expenses ($0.8 million) and salaries ($0.7 million).

- R&D expenses declined $0.3 million, or one percent, year over year largely due to lower U.S. fringe benefits expense.

- Deferred compensation expense decreased $4.6 million, or 86 percent, year over year primarily due to a decline in the value of Stepan stock during the first six months of 2018 versus an increase in the value of Stepan stock during the first half of 2017. See the "Overview" and "Segment Results - Corporate Expenses" sections of this MD&A for further details.

- Business restructuring expenses were $0.6 million in the first half of 2018 compared to $1.4 million in the first half of 2017. The first half of 2018 restructuring charges related to decommissioning costs associated with the Company's manufacturing facility in Canada which ceased operations in the fourth quarter of 2016. The first half of 2017 restructuring charges related to decommissioning costs associated with the Canadian plant ($1.3 million) and workforce reduction expense at the Company's Singapore plant ($0.1 million). See Note 15 to the condensed consolidated financial statements for additional information regarding the Company's restructuring activities.

Net interest expense for the first half of 2018 was flat with net interest expense for the first half of 2017.

Other, net was $1.6 million of income for the first half of 2018 compared to $1.9 million of income for the same period of last year. The Company recognized $0.7 million of investment gains (including realized and unrealized gains and losses) for the

Company's deferred compensation and supplemental defined contribution mutual fund assets in the first half of 2018 compared to $2.7 million of investment gains in the first half of 2017. In addition, the Company reported foreign exchange gains of $1.2 million in the first half of 2018 compared to foreign exchange losses of $0.5 million in the first half of 2017. The Company also reported $0.3 million of net periodic pension cost in both the first six months of 2018 and 2017.

The effective tax rate was 20.6 percent for the first half of 2018 compared to 26.5 percent for the first half of 2017. The decrease was primarily attributable to a lower U.S. statutory tax rate of 21 percent in the first half of 2018 versus a rate of 35 percent in the first half of 2017.

Segment Results

| (In thousands) Net Sales | For the Six Months Ended June 30, 2018 | June 30, 2017 | Increase (Decrease) | Percent Change |
|---|---|---|---|---|
| Surfactants | $715,824 | $651,937 | $ 63,887 | 10 |
| Polymers | 262,800 | 267,797 | (4,997) | -2 |
| Specialty Products | 40,577 | 43,636 | (3,059) | -7 |
| Total Net Sales | $1,019,201 | $963,370 | $ 55,831 | 6 |

| (In thousands) Operating Income | For the Six Months Ended June 30, 2018 | June 30, 2017[1] | Increase (Decrease) | Percent Change |
|---|---|---|---|---|
| Surfactants | $74,469 | $69,535 | $ 4,934 | 7 |
| Polymers | 36,352 | 42,708 | (6,356) | -15 |
| Specialty Products | 3,890 | 6,737 | (2,847) | -42 |
| Segment Operating Income | $114,711 | $118,980 | $ (4,269) | -4 |
| Corporate Expenses, Excluding Deferred Compensation and Restructuring | $28,991 | $26,853 | $ 2,138 | 8 |
| Deferred Compensation Expense (Income) | 749 | 5,392 | (4,643) | -86 |
| Business Restructuring | 631 | 1,372 | (741) | -54 |
| Total Corporate Expenses | $30,371 | $33,617 | $ (3,246) | -10 |
| Total Operating Income | $84,340 | $85,363 | $ (1,023) | -1 |

(1) The segment and total operating income line items have been immaterially changed from the amounts originally reported as a result of the Company's first quarter 2018 adoption of ASU No. 2017-07 Compensation-Retirement Benefits (Topic 715).

Surfactant net sales for the first half of 2018 increased $63.9 million, or 10 percent, over net sales for the first half of 2017. Higher sales volume and selling prices favorably impacted the year-over-year change in net sales by $34.7 million and $18.0 million, respectively. Sales volume increased five percent year-over-year. The favorable effects of foreign currency translation positively impacted the year-over-year change in net sales by $11.2 million. A year-over-year comparison of net sales by region follows:

For the Six Months Ended

| (In thousands) | June 30, 2018 | June 30, 2017 | Increase (Decrease) | Percent Change |
|---|---|---|---|---|
| North America | $438,434 | $397,259 | $ 41,175 | 10 |
| Europe | 144,436 | 128,712 | 15,724 | 12 |
| Latin America | 98,267 | 92,064 | 6,203 | 7 |
| Asia | 34,687 | 33,902 | 785 | 2 |
| Total Surfactants Segment | $715,824 | $651,937 | $ 63,887 | 10 |

Net sales for North American operations increased 10 percent year over year. Sales volume increased seven percent which favorably impacted the change in net sales by $28.0 million. The sales volume growth was largely driven by higher sales of products used in laundry and cleaning, personal care, agricultural and oilfield applications. Sales volumes of general surfactants to our distribution partners also increased. Average selling prices increased three percent between years and positively impacted the year-over-year change in net sales by $12.5 million. The increase in selling prices reflects the pass through of certain higher raw material costs to customers and a more favorable mix of sales. Foreign currency translation positively impacted the change in net sales by $0.7 million. The foreign currency impact reflected a weaker U.S. dollar relative to the Canadian dollar.

Net sales for European operations increased 12 percent due to the favorable effects of foreign currency translation and a two percent increase in sales volume. These two items positively impacted the year-over-year change in net sales by $14.6 million and $2.9 million, respectively. A weaker U.S. dollar relative to the British pound sterling and European euro led to the foreign currency translation effect. Lower selling prices of one percent unfavorably impacted the year-over-year change in net sales by $1.8 million.

Net sales for Latin American operations increased seven percent due to higher selling prices and a three percent increase in sales volume. These two items accounted for $6.5 million and $2.7 million, respectively, of the year-over-year increase in net sales. The higher selling prices primarily reflect the pass through to customers of increased raw material costs. The higher volume is mostly related to the Company's first quarter acquisition in Ecatepec, Mexico partially offset by lower demand and lost commodity business in Brazil. Foreign currency translation negatively impacted the year-over-year change in net sales by $3.0 million. The foreign currency translation effect primarily reflects the year-over-year weakening of the Brazilian real to the U.S. dollar.

Net sales for Asian operations increased two percent primarily due to a six percent increase in sales volume that positively affected the year-over-year change in net sales by $2.0 million. The unfavorable effects of foreign currency translation negatively impacted the net sales change by $1.1 million. The foreign currency impact primarily reflected a weaker Philippine peso relative to the U.S. dollar.

Surfactant operating income for the first half of 2018 increased $4.9 million, or seven percent, over operating income for the first half of 2017. Gross profit increased $6.6 million, primarily due to improved results for North American and European operations. Operating expenses increased $1.7 million, or four percent. Year-over-year comparisons of gross profit by region and total segment operating expenses and operating income follow:

| | For the Six Months Ended | | Increase | Percent |
|---|---|---|---|---|
| (In thousands) | June 30, 2018 | June 30, 2017[1] | (Decrease) | Change |
| Gross Profit | | | | |
| North America | $84,278 | $80,112 | $ 4,166 | 5 |
| Europe | 16,485 | 11,813 | 4,672 | 40 |
| Latin America | 10,861 | 14,934 | (4,073 ) | -27 |
| Asia | 10,418 | 8,534 | 1,884 | 22 |
| Surfactants Segment Gross Profit | $122,042 | $115,393 | $ 6,649 | 6 |
| Operating Expenses | 47,573 | 45,858 | 1,715 | 4 |
| Operating Income | $74,469 | $69,535 | $ 4,934 | 7 |

(1) The 2017 North America gross profit and the total operating expenses line items have been immaterially changed from the amounts originally reported as a result of the Company's first quarter 2018 adoption of ASU No. 2017-07 Compensation-Retirement Benefits (Topic 715).

Gross profit for North American operations increased five percent, or $4.2 million, between years. This increase was primarily due to the seven percent increase in sales volume.

Gross profit for European operations increased 40 percent, or $4.7 million, year-over-year primarily due to higher unit margins, the favorable effect of foreign currency translation and a two percent increase in sales volume. These items favorably impacted the change in year-over-year gross profit by $2.7 million, $1.7 million and $0.3 million, respectively.

Gross profit for Latin American operations decreased 27 percent, or $4.1 million, year-over-year primarily due to lower unit margins and the negative impact of foreign currency translation.  These items unfavorably impacted the change in year-over-year gross profit by $4.0 million and $0.5 million, respectively.  The lower unit margins principally related to higher integration and start-up costs associated with the Company's first quarter 2018 acquisition in Ecatepec, Mexico.  Sales volume growth of three percent positively impacted current year gross profit by $0.4 million.  This growth primarily reflects the Company's first quarter acquisition in Ecatepec, Mexico partially offset by lower demand and lost commodity business in Brazil.

Gross profit for Asian operations improved 22 percent, or $1.9 million, largely due to the six percent increase in sales volume and higher year-over-year production volume in Singapore, which led to lower unit overhead costs.

Operating expenses for the Surfactant segment increased $1.7 million, or four percent, year over year. Most of this increase was due to higher legal and consulting fees and salaries as well as an accumulation of smaller items.

Polymers

Polymer net sales for the first half of 2018 decreased $5.0 million, or two percent, over net sales for the same period of 2017. Lower sales volumes and selling prices negatively impacted the year-over-year change in net sales by $10.0 million and $5.2 million, respectively. The favorable effects of foreign currency translation positively impacted the year-over-year change in net sales by $10.2 million. A year-over-year comparison of net sales by region follows:

| (Dollars in thousands) | For the Six Months Ended | | | |
|---|---|---|---|---|
| Net Sales | June 30, 2018 | June 30, 2017 | Increase (decrease) | Percent change |
| North America | $160,440 | $165,289 | $ (4,849 ) | -3 |
| Europe | 86,812 | 89,257 | (2,445 ) | -3 |
| Asia and Other | 15,548 | 13,251 | 2,297 | 17 |
| Total Polymers Segment | $262,800 | $267,797 | $ (4,997 ) | -2 |

Net sales for North American operations declined three percent primarily due to lower sales volume that was slightly offset by higher selling prices. Sales volume declined three percent which unfavorably impacted the net sales change by $5.2 million. Sales volume of polyols used in rigid foam applications declined mainly due to lost market share and the negative impact of extended winter weather which delayed the start of the construction projects. Phthalic anhydride sales volume increased primarily due to a competitor's shutdown and new business. Sales volume of specialty polyols increased year-over-year. Selling prices increased slightly which had a $0.3 million positive effect on the year-over-year change in net sales.

Net sales for European operations decreased three percent primarily due to a seven percent decrease in sales volume and lower selling prices which negatively impacted the year-over-year change in net sales by $6.2 million and $5.4 million, respectively. The lower volume was principally due to customer inventory builds prior to end of 2017, the carryover effect of the 2017 MDI shortage and extended winter weather which delayed the start of construction projects. The effects of foreign currency translation positively impacted the year-over-year change in net sales by $9.2 million.

Net sales for Asia and Other operations increased 17 percent year-over-year primarily due an 11 percent increase in sales volume and the favorable effects of foreign currency translation. These items positively impacted the change in net sales by $1.4 million and $1.0 million, respectively.

Polymer operating income for the first half of 2018 declined $6.4 million, or 15 percent, from operating income for the first half of 2017. Gross profit decreased $6.4 million, or 11 percent, primarily due to a four percent decline in sales volumes. Operating expenses were flat year-over-year. Year-over-year comparisons of gross profit by region and total segment operating expenses and operating income follow:

| (In thousands) | For the Six Months Ended | | | |
|---|---|---|---|---|
| | June 30, 2018 | June 30, 2017[1] | Increase | Percent |

| | | | (Decrease) | Change |
|---|---|---|---|---|
| Gross Profit and Operating Income | | | | |
| North America | $37,036 | $42,664 | $ (5,628 ) | -13 |
| Europe | 12,914 | 14,566 | (1,652 ) | -11 |
| Asia and Other | 646 | (237 ) | 883 | NM |
| Polymers Segment Gross Profit | $50,596 | $56,993 | $ (6,397 ) | -11 |
| Operating Expenses | 14,244 | 14,285 | (41 ) | — |
| Polymers Segment Operating Income | $36,352 | $42,708 | $ (6,356 ) | -15 |

(1) The 2017 North America gross profit and the total operating expenses line items have been immaterially changed from the amounts originally reported as a result of the Company's first quarter 2018 adoption of ASU No. 2017-07 Compensation-Retirement Benefits (Topic 715).

Gross profit for North American operations declined 13 percent year-over-year primarily due to the three percent decline in sales volume and lower margins that reflect less favorable product mix.

Gross profit for European operations declined 11 percent due to the seven percent decline in sales volumes and reduced sales margins arising from increased raw material costs that could not be entirely passed through to customers. These items negatively impacted the year-over-year change in gross profit b $1.0 million and $2.0 million, respectively. The favorable impact of foreign currency translation positively impacted the year-over-year change in gross profit by $1.3 million.

Gross profit for Asia and Other operations improved $0.9 million due to an 11 percent increase in sales volume and higher unit margins.

Specialty Products

Net sales for the first half of 2018 declined $3.1 million over net sales for the same period of 2017. Sales volume declined four percent, principally due to order timing differences versus prior year. Operating income decreased $2.8 million year over year due to a less favorable mix of sales partially attributable to the timing of orders for certain products used in flavoring applications and lower margins in the food and nutritional business.

Corporate Expenses

Corporate expenses decreased $3.2 million to $30.4 million for the first six months of 2018 from $33.6 million for the first half of 2017. The decrease was primarily attributable to a $4.6 million decrease in deferred compensation expenses reported in the first six months of 2018 versus the first six months of 2017. In addition, consulting fees decreased $1.2 million between years. Partially offsetting these decreases were higher legal expenses and salaries.

Deferred compensation expense decreased $4.6 million between years. The result reflected a decrease in the value of the Company common stock ($0.96 per share decrease for the first half of 2018 compared to $5.66 per share increase for the first half of 2017). The following table presents the period-end Company common stock market prices used in the computation of deferred compensation expenses for the six months ended June 30, 2018 and 2017:

| | 2018 | 2017 | | 2016 |
|---|---|---|---|---|
| | June 30 | December 31 | June 30 | December 31 |
| Company Common Stock Price | $78.01 | $78.97 | $87.14 | $ 81.48 |

LIQUIDITY AND CAPITAL RESOURCES

Overview

For the six months ended June 30, 2018, operating activities were a cash source of $53.8 million versus a source of $60.9 million for the comparable period in 2017. For the current year, investing activities were a use of $63.4 million, as compared to a use of $44.9 million in the prior year period, and financing activities were a use of $27.1 million, as compared to a use of $22.7 million in the prior year period. Cash and cash equivalents decreased by $42.2 million compared to December 31, 2017, including an unfavorable exchange rate impact of $5.4 million.

As of June 30, 2018, the Company's cash and cash equivalents totaled $256.7 million. Cash in U.S. demand deposit accounts totaled $75.0 million and cash of the Company's non-U.S. subsidiaries held outside the U.S. totaled $181.7 million.

Operating Activity

Net income increased by $3.8 million in the first half of 2018 versus the comparable period in 2017. Working capital was a cash use of $56.5 million versus a use of $49.0 million for the comparable year-ago period.

Year-to-date accounts receivable were a use of $24.0 million compared to a use of $33.7 million for the comparable period in 2017. Inventories were a use of $14.4 million in 2018 versus a use of $1.5 million in 2017. Accounts payable

and accrued liabilities were a use of $18.6 million in 2018 compared to a use of $11.8 million for the same period in 2017.

Working capital requirements were higher year-to-date, compared to the same period in 2017, primarily due to the changes noted above. The 2018 accounts receivable increase was primarily due to higher Surfactant sales volume and selling prices. The current year inventory increase was primarily due to higher quantities. It is management’s opinion that the Company’s liquidity is sufficient to provide for any additional potential increases in working capital requirements during the remainder of 2018.

As disclosed in Note 8 (Postretirement Benefit Plans) the Company is not required to make contributions to the funded U.S. qualified defined benefit plans in 2018 as a result of the funding relief provisions included in the Highway and Transportation Funding Act of 2014. Although not required, the Company is evaluating whether to make any voluntary contributions to the funded U.S. qualified defined benefit plans in the second half of 2018.

Investing Activity

Cash outflows for investing activities were up by $18.6 million year-over-year. Cash outflows from investing activities year-to-date included capital expenditures of $43.7 million compared to $38.3 million for the comparable period last year. Other investing activities consumed $19.7 million of cash in 2018 versus a use of $6.5 million in 2017. The increase in other investing activities was primarily attributable to the $21.5 million cash outflow related to the Company's first quarter 2018 acquisition of BASF's surfactant production facility in Ecatepec, Mexico and a portion of related surfactant business.

For 2018, the Company estimates that total capital expenditures will range from $90 million to $100 million including infrastructure and optimization spending in the United States, Germany and Mexico.

Financing Activity

Cash flow used for financing activities was a use of $27.1 million in 2018 versus a use of $22.7 million in 2017.

The Company purchases shares of its common stock in the open market or from its benefit plans from time to time to fund its own benefit plans and also to mitigate the dilutive effect of new shares issued under its benefit plans. The Company may, from time to time, seek to retire or purchase additional amounts of its outstanding equity and/or debt securities through cash purchases and/or exchanges for other securities, in open market purchases, privately negotiated transactions or otherwise, including pursuant to plans meeting the requirements of Rule 10b5-1 promulgated by the SEC. Such repurchases or exchanges, if any, will depend on prevailing market conditions, the Company's liquidity requirements, contractual restrictions and other factors. The amounts involved may be material. For the six months ended June 30, 2018, the Company purchased 163,162 shares at a total cost of $12.0 million. At June 30, 2018, there were 520,275 shares remaining under the current share repurchase authorization.

Debt and Credit Facilities

Consolidated balance sheet debt decreased by $4.0 million during the first half of 2018 compared to December 31, 2017. Consolidated balance sheet debt was $286.8 million at June 30, 2018 versus $290.8 million at December 31, 2017. Net debt (which is defined as total debt minus cash – see the "Reconciliation of Non-GAAP Net Debt" section of this MD&A) increased by $38.2 million in the current year, from a negative $8.1 million to a positive $30.1 million, primarily due to a $42.2 million decrease of cash between December 31, 2017 and June 30, 2018.

As of June 30, 2018, the ratio of total debt to total debt plus shareholders' equity was 27.3 percent compared to 28.2 percent at December 31, 2017. As of June 30, 2018, the ratio of net debt to net debt plus shareholders' equity was 3.8 percent, compared to negative 1.1 percent at December 31, 2017. At June 30, 2018, the Company's debt included $283.2 million of unsecured private placement loans with maturities ranging from 2018 through 2027. These loans are the Company's primary source of long-term debt financing and are supplemented by bank credit facilities to meet short and medium-term needs.

On January 30, 2018, the Company entered into a five year committed $350 million multi-currency revolving credit facility that matures on January 30, 2023 with a syndicate of banks. This credit facility replaced the Company's prior $125 million credit agreement. The Company's outstanding Note Purchase Agreements were amended effective January 30, 2018 to make certain covenants consistent with those included in the credit agreement. As of June 30, 2018, the Company had outstanding letters of credit totaling $5.3 million under the revolving credit agreement and no

borrowings, with $344.7 million remaining available.

The Company anticipates that cash from operations, committed credit facilities and cash on hand will be sufficient to fund anticipated capital expenditures, working capital, dividends and other planned financial commitments for the foreseeable future.



---

Certain foreign subsidiaries of the Company maintain short-term bank lines of credit in their respective local currencies to meet working capital requirements as well as to fund capital expenditure programs and acquisitions. At June 30, 2018, the Company's foreign subsidiaries had outstanding debt of $3.6 million.

The Company has material debt agreements that require the maintenance of minimum interest coverage and minimum net worth. These agreements also limit the incurrence of additional debt as well as the payment of dividends and repurchase of treasury shares. As of June 30, 2018, testing for these agreements was based on the Company's consolidated financial statements. Under the most restrictive of these debt covenants:

1. The Company is required to maintain a minimum interest coverage ratio, as defined within the agreements, of 3.50 to 1.00, for the preceding four calendar quarters.

2. The Company is required to maintain a maximum net leverage ratio, as defined within the agreements, not to exceed 3.50 to 1.00.

3. The Company is required to maintain net worth of at least $325.0 million.
4. The Company is permitted to pay dividends and purchase treasury shares after December 31, 2017, in amounts of up to $100.0 million plus 100 percent of net income and cash proceeds of stock option exercises, measured cumulatively beginning December 31, 2017. The maximum amount of dividends that could have been paid within this limitation is disclosed as unrestricted retained earnings in Note 6 to the condensed consolidated financial statements.

The Company believes it was in compliance with all of its loan agreements as of June 30, 2018.

ENVIRONMENTAL AND LEGAL MATTERS

The Company's operations are subject to extensive federal, state and local environmental laws and regulations and similar laws in the other countries in which the Company does business.  Although the Company's environmental policies and practices are designed to ensure compliance with these laws and regulations, future developments and increasingly stringent environmental regulation may require the Company to make additional environmental expenditures.  The Company will continue to invest in the equipment and facilities necessary to comply with existing and future regulations.  For the six months ended June 30, 2018 and 2017, the Company's expenditures for capital projects related to the environment were $2.1 million and $1.2 million, respectively.  These projects are capitalized and depreciated over their estimated useful lives, which are typically 10 years.  Recurring costs associated with the operation and maintenance of facilities for waste treatment and disposal and managing environmental compliance in ongoing operations at the Company's manufacturing locations were $14.0 million and $13.0 million for the six months ended June 30, 2018 and 2017, respectively.

Over the years, the Company has received requests for information related to or has been named by the government as a potentially responsible party at a number of waste disposal sites where cleanup costs have been or may be incurred under CERCLA and similar state or foreign statutes.  In addition, damages are being claimed against the Company in general liability actions for alleged personal injury or property damage in the case of some disposal and plant

sites. The Company believes that it has made adequate provisions for the costs it may incur with respect to the sites and in other commercial disputes. It is the Company's accounting policy to record liabilities when environmental assessments and/or remedial efforts are probable and the cost or range of possible costs can be reasonably estimated. When no amount within the range is a better estimate than any other amount, the minimum is accrued. Some of the factors on which the Company bases its estimates include information provided by feasibility studies, potentially responsible party negotiations and the development of remedial action plans. After partial remediation payments at certain sites, the Company has estimated a range of possible environmental and legal losses of $23.8 million to $45.2 million at June 30, 2018, compared to $24.2 million to $45.4 million at December 31, 2017. At June 30, 2018, and December 31, 2017, the Company's accrued liability for such losses, which represented the Company's best estimate within the estimated range of possible environmental and legal losses, was $23.8 million and $24.2 million, respectively. Because the liabilities accrued are estimates, actual amounts could differ from the amounts reported. During the six-month period ended June 30, 2018, cash outlays related to legal and environmental matters approximated $0.6 million compared to $1.0 million for the same period in 2017.

For certain sites, the Company has responded to information requests made by federal, state or local government agencies but has received no response confirming or denying the Company's stated positions. As such, estimates of the total costs, or range of possible costs, of remediation, if any, or the Company's share of such costs, if any, cannot be determined with respect to these sites. Consequently, the Company is unable to predict the effect thereof on the Company's financial position, cash flows and results of operations. Given the information available, management believes the Company has no liability at these sites. However, in the event

of one or more adverse determinations with respect to such sites in any annual or interim period, the effect on the Company's cash flows and results of operations for those periods could be material. Based upon the Company's present knowledge with respect to its involvement at these sites, the possibility of other viable entities' responsibilities for cleanup, and the extended period over which any costs would be incurred, the Company believes that these matters, individually and in the aggregate, will not have a material effect on the Company's financial position. Certain of these matters are discussed in Item 1, Part 2, Legal Proceedings, in this report and in other filings of the Company with the SEC, which are available upon request from the Company. See also Note 7 to the condensed consolidated financial statements for a summary of the environmental proceedings related to certain environmental sites.

OUTLOOK

The Company believes Surfactants will continue to build upon its strong first half of 2018 and further benefit from its diversification efforts into functional products, new technologies, improved internal efficiencies and expanded sales into a broad customer base globally. The Company believes that despite margin challenges within the North American Polymer business, additional volume opportunities should benefit the second half of 2018. The Company believes full year Specialty Products results should improve versus the prior year. Overall, the Company remains optimistic about the remainder of the year.

CRITICAL ACCOUNTING POLICIES

There have been no changes to the critical accounting policies disclosed in the Company's 2017 Annual Report on Form 10-K with the exception of revenue recognition. During the first quarter of 2018 the Company adopted ASU 2014-19 which changed the criteria for revenue recognition to the time when the Company satisfies its performance obligation by transferring control of product to the customer as compared to the "risk and rewards" criteria used in prior years. Adoption of ASU 2014-19 did not have a material impact on the Company's financial position as of June 30, 2018 or results of operations for the three and six months ended June 30, 2018 and 2017. See Note 12 for additional details.

RECONCILIATION OF NON-GAAP ADJUSTED NET INCOME AND DILUTED EARNINGS PER SHARE

| | Three Months Ended June 30, | | | |
|---|---|---|---|---|
| (In millions, except per share amounts) | 2018 | | 2017 | |
| | Net Income | Diluted EPS | Net Income | Diluted EPS |
| Net Income Attributable to the Company as Reported | $32.9 | $1.41 | $27.9 | $1.19 |
| | | | | |
| Deferred Compensation (Income) Expense (including related investment activity) | (1.4 ) | (0.05 ) | 4.1 | 0.17 |
| Business Restructuring | 0.3 | 0.01 | 0.6 | 0.03 |
| Cumulative Tax Effect on Above Adjustment Items | 0.3 | 0.01 | (1.7 ) | (0.07 ) |
| Adjusted Net Income | $32.1 | $1.38 | $30.9 | $1.32 |

| | Six Months Ended June 30, | | | |
|---|---|---|---|---|
| (In millions, except per share amounts) | 2018 | | 2017 | |
| | Net Income | Diluted EPS | Net Income | Diluted EPS |
| Net Income Attributable to the Company as Reported | $63.6 | $2.73 | $59.8 | $2.56 |
| | | | | |
| Deferred Compensation (Income) Expense (including related investment activity) | — | — | 2.8 | 0.12 |
| Business Restructuring | 0.6 | 0.03 | 1.4 | 0.06 |
| Cumulative Tax Effect on Above Adjustment Items | (0.1 ) | (0.01 ) | (1.4 ) | (0.06 ) |
| Adjusted Net Income | $64.1 | $2.75 | $62.6 | $2.68 |

The Company believes that certain non-GAAP measures, when presented in conjunction with comparable GAAP measures, are useful for evaluating the Company's operating performance and provide better clarity on the impact of non-operational items. Internally, the Company uses this non-GAAP information as an indicator of business performance and evaluates management's effectiveness with specific reference to these indicators. These measures should be considered in addition to, not a substitute for or superior to, measures of financial performance prepared in accordance with GAAP. The cumulative tax effect was calculated using the statutory tax rates for the jurisdictions in which the noted transactions occurred.

RECONCILIATION OF NON-GAAP NET DEBT

| (In millions) | June 30, 2018 | December 31, 2017 |
|---|---|---|
| Current Maturities of Long-Term Debt as Reported | $24.3 | $ 22.5 |
| Long-Term Debt as Reported | 262.5 | 268.3 |
| Total Debt as Reported | 286.8 | 290.8 |
| Less Cash and Cash Equivalents as Reported | (256.7) | (298.9) |
| Net Debt | $30.1 | $ (8.1) |

Management uses the non-GAAP net debt metric to gain a more complete picture of the Company’s overall liquidity, financial flexibility and leverage level. This adjusted measure should be considered supplemental to and not a substitute for financial information prepared in accordance with GAAP. The Company's definition of this adjusted measure may differ from similarly titled measures used by other entities.

Item 3 – Quantitative and Qualitative Disclosures about Market Risk

There have been no material changes to the market risks described in the Company's 2017 Annual Report on Form 10-K.

Item 4 – Controls and Procedures

a. Evaluation of Disclosure Controls and Procedures

We have conducted an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act, as of June 30, 2018. Based on this evaluation of our disclosure controls and procedures, our Chief Executive Officer and our Chief Financial Officer have concluded that our disclosure controls and procedures were effective as of June 30, 2018, such that the information required to be disclosed in our Securities and Exchange Commission reports is recorded, processed, summarized and reported within the time periods specified by the rules and forms of the Exchange Act and is accumulated and communicated to management, including our Chief Executive Officer and our Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosures.

b. Changes in Internal Control Over Financial Reporting

There were no changes in the Company's internal controls over financial reporting (as defined in Rule 13a-15(f) under the Exchange Act) that occurred during the quarter ended June 30, 2018, 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

There have been no material changes to the legal proceedings disclosed in the Company's 2017 Annual Report on Form 10-K.

Item 1A – Risk Factors

There have been no material changes to the risk factors disclosed in the Company's 2017 Annual Report on Form 10-K.

Item 2 – Unregistered Sales of Equity Securities and Use of Proceeds

Below is a summary by month of share purchase by the Company during the second quarter of 2018:

| Month | Total Number of Shares Purchased | Average Price Paid per Share | Total Number of Shares Purchased as Part of Publicly Announced | Maximum Number of Shares that May Yet |
| --- | --- | --- | --- | --- |

| | | | | Plans or Programs | Be Purchased Under the Plans or Programs |
|---|---|---|---|---|---|
| April 2018 | 19,579 | (a)(b) | $ 77.49 | — | — |
| May 2018 | 114,197 | (b) | $ 70.05 | — | — |
| June 2018 | — | | — | — | — |
| Total | 133,776 | | $ 71.14 | — | — |

(a) Includes 192 shares of Company common stock tendered by employees to settle statutory withholding taxes related to distributions of deferred performance stock awards and deferred management incentive compensation and to the exercise of SARs.
(b) Includes shares of Company common stock purchased on the open market.

Item 3 – Defaults Upon Senior Securities

None

Item 4 – Mine Safety Disclosures

Not applicable

Item 5 – Other Information

None

Item 6 – Exhibits

| Exhibit No. | Description |
| --- | --- |
| 31.1 | – Certification of President and Chief Executive Officer pursuant to Exchange Act Rule 13a-14(a)/15d-14(a) |
| 31.2 | – Certification of Vice President and Chief Financial Officer pursuant to Exchange Act Rule 13a-14(a)/15d-14(a) |
| 32 | – Certification pursuant to 18 U.S.C. Section 1350 |
| 101.INS | – XBRL Instance Document |
| 101.SCH | – XBRL Taxonomy Extension Schema Document |
| 101.CAL | – XBRL Taxonomy Extension Calculation Linkbase Document |
| 101.DEF | – XBRL Taxonomy Extension Definition Document |
| 101.LAB | – XBRL Taxonomy Extension Label Linkbase Document |
| 101.PRE | – XBRL Taxonomy Presentation Linkbase Document |

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.

STEPAN COMPANY

Date: August 1, 2018

/s/ Luis Rojo
Luis Rojo
Vice President and Chief Financial Officer

(Authorized Officer and Principal Financial Officer)