STANDEX INTERNATIONAL CORP/DE/
Form 10-Q
January 30, 2018

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended December 31, 2017

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

Commission File Number 1-7233

STANDEX INTERNATIONAL CORPORATION

(Exact name of registrant as specified in its charter)

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 [X] 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 [X] NO [ ]

DELAWARE — 31-0596149

(State of incorporation) — *(IRS Employer Identification No.)*

11 KEEWAYDIN DRIVE, SALEM, NEW HAMPSHIRE — 03079

(Address of principal executive offices) — *(Zip Code)*

(603) 893-9701

(Registrant's telephone number, including area code)

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

Large accelerated filer [X] Accelerated filer [ ]

Non-accelerated filer [ ] (Do not check if a smaller reporting company) Smaller Reporting Company [ ]

Indicate by check mark whether the Registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). YES [ ] NO [X]

The number of shares of Registrant's Common Stock outstanding on January 24, 2018 was 12,829,489.

STANDEX INTERNATIONAL CORPORATION

INDEX

1

PART I. FINANCIAL INFORMATION
ITEM 1

STANDEX INTERNATIONAL CORPORATION
Condensed Consolidated Balance Sheets

(In thousands, except per share data)	December 31, 2017 (unaudited)	June 30, 2017
ASSETS		
Current Assets:		
Cash and cash equivalents	$ 109,389	$ 88,566
Accounts receivable, net of reserve for doubtful accounts of $2,946 and $2,406 at December 31, 2017 and June 30, 2017	131,584	127,060
Inventories	130,715	119,401
Prepaid expenses and other current assets	9,604	8,397
Income taxes receivable	1,012	2,469
Deferred tax asset	-	14,991
Total current assets	382,304	360,884
Property, plant, and equipment, net	144,610	133,160
Intangible assets, net	102,216	102,503
Goodwill	249,685	242,690
Deferred tax asset	10,699	1,135
Other non-current assets	27,156	27,304
Total non-current assets	534,366	506,792
Total assets	$ 916,670	$ 867,676
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current Liabilities:		
Accounts payable	$ 93,049	$ 96,487
Accrued liabilities	63,985	58,694
Income taxes payable	6,685	4,783
Total current liabilities	163,719	159,964
Long-term debt	216,157	191,976
Accrued pension and other non-current liabilities	115,862	107,072
Total non-current liabilities	332,019	299,048
Stockholders' equity:		
Common stock, par value $1.50 per share, 60,000,000 shares authorized, 27,984,278 issued, 12,709,238 and 12,662,661 outstanding at December 31, 2017 and June 30, 2017	41,976	41,976
Additional paid-in capital	59,016	56,783

Retained earnings	723,435	716,605
Accumulated other comprehensive loss	(112,075)	(115,938)
Treasury shares: 15,275,040 shares at December 31, 2017		
and 15,321,617 shares at June 30, 2017	(291,420)	(290,762)
Total stockholders' equity	420,932	408,664
Total liabilities and stockholders' equity	$ 916,670	$ 867,676

See notes to unaudited condensed consolidated financial statements

STANDEX INTERNATIONAL CORPORATION

Unaudited Condensed Consolidated Statements of Operations

(In thousands, except per share data)	Three Months Ended December 31, 2017	Three Months Ended December 31, 2016	Six Months Ended December 31, 2017	Six Months Ended December 31, 2016
Net sales	$ 209,751	$ 173,854	$ 424,130	$ 353,454
Cost of sales	138,225	116,960	278,423	234,784
Gross profit	71,526	56,894	145,707	118,670
Selling, general, and administrative expenses	50,679	40,493	100,705	82,105
Acquisition related costs	703	1,503	1,708	1,503
Restructuring costs	1,966	1,664	4,970	2,058
Total operating expenses	53,348	43,660	107,383	85,666
Income from operations	18,178	13,234	38,324	33,004
Interest expense	(1,793)	(850)	(3,514)	(1,547)
Other non-operating income, net	453	332	1,057	766
Income from continuing operations before income taxes	16,838	12,716	35,867	32,223
Provision for income taxes	19,642	2,274	24,672	7,437
Net income (loss) from continuing operations	(2,804)	10,442	11,195	24,786
Income (loss) from discontinued operations, net of income taxes	(3)	6	(2)	(44)
Net income (loss)	$ (2,807)	$ 10,448	$ 11,193	$ 24,742
Basic earnings per share:				
Continuing operations	$ (0.22)	$ 0.82	$ 0.88	$ 1.96
Discontinued operations	-	-	-	-
Total	$ (0.22)	$ 0.82	$ 0.88	$ 1.96
Diluted earnings per share:				
Continuing operations	$ (0.22)	$ 0.82	$ 0.88	$ 1.94
Discontinued operations	-	-	-	-
Total	$ (0.22)	$ 0.82	$ 0.88	$ 1.94
Cash dividends per share	$ 0.18	$ 0.16	$ 0.34	$ 0.30

See notes to unaudited condensed consolidated financial statements

STANDEX INTERNATIONAL CORPORATION

Unaudited Condensed Consolidated Statements of Comprehensive Income

	Three Months Ended December 31,		Six Months Ended December 31,	
(In thousands)	**2017**	**2016**	**2017**	**2016**
Net income (loss)	$ (2,807)	$ 10,448	$ 11,193	$ 24,742
Other comprehensive income (loss):				
Defined benefit pension plans:				
Actuarial gains (losses) and other changes in unrecognized costs	$ (88)	$ 516	$ (338)	$ 631
Amortization of unrecognized costs	1,370	1,427	2,736	2,867
Derivative instruments:				
Change in unrealized gains (losses)	(2,351)	493	(1,577)	554
Amortization of unrealized gains and into interest expense	913	83	1,064	304
Foreign currency translation gains (losses)	(956)	(10,441)	2,455	(11,607)
Other comprehensive income (loss) before tax	$ (1,112)	$ (7,922)	$ 4,340	$ (7,251)
Income tax provision (benefit):				
Defined benefit pension plans:				
Actuarial gains (losses) and other changes in unrecognized costs	$ 425	$ (224)	$ 477	$ (134)
Amortization of unrecognized costs	(327)	(502)	(805)	(1,008)
Derivative instruments:				
Change in unrealized gains and (losses)	5	(188)	(104)	(211)
Amortization of unrealized gains and (losses) into interest expense	(8)	(32)	(44)	(116)
Income tax provision (benefit) to other comprehensive income (loss)	$ 95	$ (946)	$ (476)	$ (1,469)
Other comprehensive gain (loss), net of tax	(1,017)	(8,868)	3,864	(8,720)
Comprehensive income (loss)	$ (3,824)	$ 1,580	$ 15,057	$ 16,022

See notes to unaudited condensed consolidated financial statements

STANDEX INTERNATIONAL CORPORATION

Unaudited Condensed Consolidated Statements of Cash Flows

	Six Months Ended December 31,	
(In thousands)	**2017**	**2016**
Cash flows from operating activities		
Net income	$ 11,193	$ 24,742
Income from discontinued operations	2	44
Income from continuing operations	11,195	24,786
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Depreciation and amortization	14,052	9,044
Stock-based compensation	2,877	2,843
Non-cash portion of restructuring charge	664	42
Contributions to defined benefit plans	(530)	(624)
Net changes in operating assets and liabilities	(2,592)	(15,248)
Net cash provided by operating activities - continuing operations	25,666	20,843
Net cash (used in) operating activities - discontinued operations	(45)	(227)
Net cash provided by operating activities	25,621	20,616
Cash flows from investing activities		
Expenditures for property, plant, and equipment	(15,683)	(13,029)
Expenditures for acquisitions, net of cash acquired	(10,397)	(24,660)
Proceeds from life insurance policies	2,217	24
Other investing activity	1,093	652
Net cash (used in) investing activities	(22,770)	(37,013)
Cash flows from financing activities		
Borrowings on revolving credit facility	108,500	73,000
Payments of revolving credit facility	(87,288)	(41,000)
Activity under share-based payment plans	622	618
Purchases of treasury stock	(1,924)	(6,905)
Cash dividends paid	(4,312)	(3,798)
Net cash provided by financing activities	15,598	21,915
Effect of exchange rate changes on cash and cash equivalents	2,374	(6,205)
Net change in cash and cash equivalents	20,823	(687)
Cash and cash equivalents at beginning of year	88,566	121,988
Cash and cash equivalents at end of period	$ 109,389	$ 121,301

Supplemental Disclosure of Cash Flow Information:		
Cash paid during the year for:		
Interest	$ 2,951	$ 1,272
Income taxes, net of refunds	$ 8,077	$ 9,207

See notes to unaudited condensed consolidated financial statements

STANDEX INTERNATIONAL CORPORATION

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1) Management Statement

In the opinion of management, the accompanying unaudited condensed consolidated financial statements contain all adjustments necessary to present fairly the results of operations for the three and six months ended December 31, 2017 and 2016, the cash flows for the six months ended December 31, 2017 and 2016 and the financial position of Standex International Corporation ("Standex", the "Company", "we", "us", or "our"), at December 31, 2017. The interim results are n necessarily indicative of results for a full year. The following unaudited condensed financial statements have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission. Certain information and note disclosures normally included in annual financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted pursuant to those rules and regulations, although the company believes that the disclosures made are adequate to make the information not misleading. The unaudited condensed consolidated financial statements and notes do not contain information which would substantially duplicate the disclosures contained in the audited annual consolidated financial statements and notes for the year ended June 30, 2017. The condensed consolidated balance sheet at June 30, 2017 was derived from audited financial statements, but does not include all disclosures required by accounting principles generally accepted in the United States of America. The financial statements contained herein should be read in conjunction with the Annual Report on Form 10-K and in particular the audited consolidated financial statements for the year ended June 30, 2017. Certain prior period amounts have been reclassified to conform to the current period presentation. Unless otherwise noted, references to years are to the Company's fiscal years.

On December 22, 2017, the Tax Cuts and Jobs Act (the "Act") was passed which resulted in the Company recording provisional estimates related to foreign earnings and changes in the revaluation of deferred taxes in our consolidated financial statements. Other changes implemented by the Act will not impact the Company until the fiscal year ending June 30, 2019. There have been no other significant changes in our reported financial position, results of operations, cash flows or to our critical accounting policies that were disclosed in our Annual Report on Form 10-K for the fiscal year ended June 30, 2017 that have had a significant impact on our consolidated financial statements or notes herein.

The Company considers events or transactions that occur after the balance sheet date but before the financial statements are issued to provide additional evidence relative to certain estimates or to identify matters that require additional disclosure. We evaluated subsequent events through the date and time our unaudited condensed consolidated financial statements were issued.

During the fourth quarter of fiscal 2017, we adopted Accounting Standards Update (ASU) 2016-09 requiring the recognition of excess tax benefits as a component of income tax expense which were historically recognized in equity. As required, the fiscal results for the three and six months ended December 31, 2016 have been recast to include a tax benefit of $0.2 million and $0.6 million, respectively. In addition, the ASU requires a prospective update to the treasury method of calculating weighted average diluted shares outstanding resulting in the inclusion of additional shares in our diluted EPS calculation for the three and six months ended December 31, 2016.

RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS

In May 2014, the Financial Accounts Standards Board ("FASB") issued ASU No. 2014-09, *Revenue from Contracts with Customers*. This update amends the current guidance on revenue recognition related to contracts with customers. Under ASU No. 2014-09, an entity should recognize revenue when it transfers promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services and requires additional disclosure about the nature, amount, timing, and uncertainty of revenue and cash flows arising from customer contracts, including significant judgments and changes in judgments and assets recognized from costs incurred to obtain or fulfill a contract. In early 2016, the FASB issued additional updates: ASU No. 2016-10, 2016-11 and 2016-12. These updates provide further guidance and clarification on specific items within the previously issued update. The Company anticipates it will adopt Topic 606 under the modified retrospective method and will only apply this method to contracts that are not completed as of the date of adoption. Application of this method will result in a cumulative effect of initially applying the standard as an adjustment to the opening balance of retained earnings at the date of initial application for any open contracts as of the adoption date.

The Company has established a global steering committee with a project plan to analyze the impact of this standard. The assessment phase of the project plan is on-going and includes identifying the various revenue streams, initiating contract reviews and reviewing current accounting policies and practices to identify potential differences that would result from the application of the standard. This assessment includes (1) utilizing questionnaires to assist with the identification of revenue streams, (2) performing sample contract analyses for each revenue stream identified, (3) assessing the noted differences in recognition and measurement that may result from adopting this new standard, (4) performing detailed analyses of contracts with larger customers, and (5) developing plans to test transactions for consistency with contract provisions that affect revenue recognition. The committee is currently analyzing the impact of the standard on its contract portfolio by reviewing a sample of its contracts to identify potential differences that would result from applying the requirements of the new standard. The committee also continues to analyze the impact of requirements for combining contracts, performance obligations, and variable consideration. The global steering committee is apprising both management and the audit committee of project status on a recurring basis. Following the completion of the assessment phase, the Company will initiate efforts to redesign impacted processes, policies, controls and disclosures, as necessary. The Company has not yet finalized its assessment of the impact of Topic 606, but expects to adopt this standard, as required, for the Company's interim and annual reporting periods beginning July 1, 2018. The Company does not expect to early adopt.

In November 2015, the FASB issued ASU Update 2015-17, *Income Taxes (Topic 740): Balance Sheet Classification of Deferred Taxes*, as part of its simplification initiatives. This update requires deferred tax liabilities and assets to be classified as non-current on the consolidated condensed balance sheet for fiscal years beginning after December 15, 2016, and interim periods within those annual periods. Early application is permitted. An entity can elect adoption prospectively or retrospectively to all periods presented. We have adopted ASU 2015-17 prospectively. As a result, we have presented all deferred tax assets and liabilities as noncurrent on our consolidated balance sheet as of December 31, 2017, but have not reclassified current deferred assets and liabilities on our consolidated balance sheet as of June 30, 2017. There was no impact on our results of operations as a result of the adoption of ASU 2015-17.

In February 2016, the FASB issued ASU 2016-02, *Leases (Topic 842)*. ASU 2016-02 increases transparency and comparability among organizations by recognizing lease assets and liabilities on the balance sheet and disclosing key information about leasing arrangements. A modified retrospective transition approach is required for lessees for capital and operating leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements, with certain practical expedients available. For leases with a term of twelve months or less, a lessee is permitted to make an accounting policy election by class of underlying asset not to recognize lease assets and liabilities. ASU 2016-02 is effective for fiscal years beginning after December 15, 2018. While we are continuing to assess the effect of the adoption, we currently believe the most significant potential changes relate to (i) recognition of right-of-use assets and lease liabilities on our balance sheet for equipment and real estate operating leases, and (ii) the derecognition of existing assets and liabilities for certain sale-leaseback transactions that currently do not qualify for sale accounting. The Company anticipates the adoption will have a material impact on the Company's consolidated financial statements due to the materiality of the underlying leases subject to the new guidance, however are unable to quantify that effect until our analysis is complete.

In January 2017, the FASB issued ASU 2017-04, *Simplifying the Test for Goodwill Impairment*, which simplifies the accounting for goodwill impairments by eliminating step two from the goodwill impairment test. Instead, if the carrying amount of a reporting unit exceeds its fair value, an impairment loss shall be recognized in an amount equal to that excess, limited to the total amount of goodwill allocated to that reporting unit. ASU 2017-04 also clarifies the requirements for excluding and allocating foreign currency translation adjustments to reporting units related to an entity's testing of reporting units for goodwill impairment. It further clarifies that an entity should 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. ASU 2017-04 is effective for annual or any interim goodwill impairment tests in fiscal years beginning after December 15, 2019. The Company is currently assessing the potential impact of the adoption of ASU 2017-04 on our consolidated financial statements.

In March 2017, the FASB issued ASU 2017-07, *Compensation-Retirement Benefits (Topic 715): Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost*, which changes how employers that sponsor defined benefit pension or other postretirement benefit plans present the net periodic benefit cost in the income statement. The new guidance requires the service cost component of net periodic benefit cost to be presented in the same income statement line items as other employee compensation costs arising from services rendered during the period. Other components of the net periodic benefit cost are to be stated separately from service cost and outside of operating income. This guidance is effective for fiscal years beginning after December 15, 2017 (fiscal 2019 for the Company) and interim periods within those annual periods. The amendment is to be applied retrospectively. The Company is in the preliminary stages of assessing the potential impact of the adoption of ASU 2017-07 on our consolidated financial statements.

In August 2017, the FASB issued ASU 2017-12, *Derivatives and Hedging (Topic 815); Targeting Improvements to Accounting for Hedging Activities*, which improves the financial reporting of hedging relationships to better portray the economic results of an entity's risk management activities in its financial statements and to make certain targeted improvements to simplify the application of hedge accounting guidance. The new guidance requires additional disclosures including cumulative basis adjustments for fair value hedges and the effect of hedging on individual income statement line items. This guidance is effective for fiscal years beginning after December 15, 2018 (fiscal 2020 for the Company), and interim periods within those fiscal years. The amendment is to be applied prospectively. The Company is in the preliminary stages of assessing the potential impact of the adoption of ASU 2017-12 on our consolidated financial statements.

2. ACQUISITIONS

The Company's recent acquisitions are strategically significant to the future growth prospects of the Company. At the time of the acquisition and December 31, 2017, the Company evaluated the significance of each acquisition on a standalone basis and in aggregate, considering both qualitative and quantitative factors.

Piazza Rosa Group

During the first quarter of fiscal year 2018, the Company acquired the Piazza Rosa Group. The Italy-based privately held company is a leading provider of mold and tool treatment and finishing services for the automotive and consumer products markets. We have included the results of the Piazza Rosa Group in our Engraving segment in our Condensed Consolidated Financial Statements.

The Company paid $10.1 million in cash, net of a $2.8 million payment to satisfy debt of the entity at the time of acquisition, for all of the issued and outstanding equity interests of the Piazza Rosa Group. The final purchase price is subject to net asset value adjustments that have not yet been finalized. The preliminary purchase price was allocated to the net tangible and identifiable intangible assets acquired and liabilities assumed based on their fair values on the closing date. Goodwill recorded from this transaction is attributable to potential revenue increases from the combined competencies with Standex Engraving's worldwide presence and Piazza Rosa Group's texturizing capabilities. The combined companies create a global tool finishing service leader and open additional opportunities in the broader surface engineering market.

Intangible assets of $4.1 million were preliminarily recorded, consisting of $2.3 million of customer relationships to be amortized over a period of eight years, $1.6 million for trademarks, and $0.2 million of other intangibles assets. Since the preliminary valuation, the Company adjusted goodwill by $1.2 million primarily as a result of identification of other identifiable assets. The goodwill of $5.1 million created by the transaction is not deductible for income tax purposes.

The components of the fair value of the Piazza Rosa Group acquisition, including the preliminary allocation of the purchase price at December 31, 2017, are as follows (in thousands):

	Preliminary Allocation	Adjustments	Adjusted Allocation
	September 30, 2017		December 31, 2017
Fair value of business combination:			
Cash payments	$ 12,889	$ -	$ 12,889
Less: cash paid to satisfy acquired debt	(2,833)	-	(2,833)
Total	$ 10,056	$ -	$ 10,056
Identifiable assets acquired and liabilities assumed:			
Other acquired assets	$ 2,678	$ 1,176	$ 3,854
Inventories	637	(2)	635
Property, plant, and equipment	5,005	-	5,005
Identifiable intangible assets	4,087	(1)	4,086
Goodwill	6,218	(1,155)	5,063
Liabilities assumed	(7,387)	-	(7,387)
Deferred taxes	(1,182)	(18)	(1,200)
Total	$ 10,056	$ -	$ 10,056

OKI Sensor Device Corporation

During the third quarter of fiscal year 2017, the Company acquired all of the outstanding shares of OKI Sensor Device Corporation from OKI Electric Industry Co., Ltd. Located in Kofu City, Japan, OKI Sensor Device Corporation is the world's leading designer and supplier of magnetic reed switches. Now named Standex Electronics Japan Corporation ("Standex Electronics Japan"), the acquisition enhances the Company's access to important Asian markets and enables the Company to offer a world class suite of reed switches and related magnetic solutions while continuing to serve Standex Electronics Japan's diverse distribution channels. We have included the results of Standex Electronics Japan in our Electronics segment in our Condensed Consolidated Financial Statements.

The Company paid $129.2 million in cash, net of cash acquired, for 100% of the outstanding stock of Standex Electronics Japan. The preliminary purchase price was allocated to the net tangible and identifiable intangible assets acquired and liabilities assumed based on their fair values on the closing date. Goodwill recorded from this transaction is attributable to potential revenue increases from enhanced access to our Asian markets and synergies created from the vertical integration with a key supplier.

Intangible assets of $51.4 million were preliminarily recorded, consisting of $47.8 million of developed technology to be amortized over a period of 10-20 years, $3.4 million of customer relationships to be amortized over a period of fifteen years, and $0.2 million of product order backlog which was amortized during fiscal year 2017. Since the preliminary valuation, the Company adjusted goodwill by $3.2 million as a result of tax adjustments, a pension adjustment of $1.9 million and purchase accounting changes including a decrease in the fair value of developed technology and customer relationships of $2.3 million and $0.2 million, respectively, and an additional $0.1 million of product order backlog which was amortized during fiscal year 2017. The goodwill of $79.2 million created by the transaction is not deductible for income tax purposes.

The components of the fair value of the Standex Electronics Japan acquisition, including the allocation of the purchase price at December 31, 2017, are as follows (in thousands):

	Preliminary Allocation March 31, 2017	Adjustments	Adjusted Allocation December 31, 2017
Fair value of business combination:			
Cash payments	$ 137,676	$ -	$ 137,676
Less: cash acquired	(8,521)	-	(8,521)
Total	$ 129,155	$ -	$ 129,155
Identifiable assets acquired and liabilities assumed:			
Other acquired assets	$ 12,497	$ (2,158)	$ 10,339
Inventories	7,387	816	8,203
Property, plant, and equipment	12,703	5,750	18,453
Identifiable intangible assets	53,800	(2,400)	51,400
Goodwill	75,985	3,202	79,187
Liabilities assumed	(10,811)	(8,468)	(19,279)
Deferred taxes	(22,406)	3,258	(19,148)
Total	$ 129,155	$ -	$ 129,155

The initial allocation of the purchase price is based upon a preliminary valuation, and accordingly, our estimates and assumptions are subject to change as we obtain additional information during the measurement period.

The following table reflects the unaudited pro forma operating results of the Company for the three and six months ended December 31, 2017 and 2016, which give effect to the acquisition of Standex Electronics Japan as if it had occurred at the beginning of each period presented. The pro forma information combines the historical financial results of the Company and Standex Electronics Japan, adjusted for changes in foreign exchange rates. The pro forma results are not necessarily indicative of the operating results that would have occurred had the acquisition been effective at the beginning of each period, nor are they intended to be indicative of results that may occur in the future. The pro forma information does not include the effects of any synergies related to the Standex Electronics Japan acquisition, transactions between the entities prior to acquisition, or the pre-acquisition impact of other businesses acquired by the Company during this period as they were not material to the Company's historical results of operations.

	(Unaudited Pro Forma)		(Unaudited Pro Forma)	
	Three Months ended December 31,		Six Months Ended December 31,	
In thousands	**2017**	**2016**	**2017**	**2016**
Net Sales	$ 209,751	$ 189,796	$ 424,130	$ 387,060
Net Income	$ (2,804)	$ 12,217	$ 11,020	$ 27,134

Earnings per share:								
Basic	$	(0.22)	$	0.97	$	0.87	$	2.14
Diluted	$	(0.22)	$	0.96	$	0.86	$	2.12

Pro forma earnings during six months ended December 31, 2017 were adjusted to exclude tax-affected acquisition-related costs incurred during the first quarter of $0.2 million.

Pro forma earnings during the three months ended December 31, 2016 were adjusted to include tax-affected expense of $0.7 million for amortization of intangible assets recognized at fair value, depreciation expense of $0.3

million for the fair value adjustment of the acquired fixed assets, $0.4 million of interest expense associated with incremental borrowings under the Company's Credit Facility and $0.2 million of acquisition-related costs.

Pro forma earnings during the six months ended December 31, 2016 were adjusted to include tax-affected expense of $1.4 million for amortization of intangible assets recognized at fair value, depreciation expense of $0.6 million for the fair value adjustment of the acquired fixed assets, $0.7 million of interest expense associated with incremental borrowings under the Company's Credit Facility and $0.2 million of acquisition-related costs.

Horizon Scientific

During the second quarter of fiscal year 2017, the Company acquired Horizon Scientific, a supplier of laboratory refrigerators and freezers, as well as cryogenic equipment for the scientific, bio-medical and pharmaceutical markets. We believe the acquisition of Horizon Scientific enhances Standex's penetration of the refrigeration markets in the growing scientific sector. We have included the operating results of Horizon Scientific in our Food Service Equipment segment in our Condensed Consolidated Financial Statements.

The Company paid $25.0 million in cash, net of cash acquired, for 100% of the outstanding stock of Horizon Scientific. The purchase price was subject to cash and net working capital adjustments of $0.3 million which was paid during the first quarter of fiscal year 2018 along with deferred compensation of up to $8.4 million. The purchase price was allocated to the net tangible and identifiable intangible assets acquired and liabilities assumed based on their fair values on the closing date.

Intangible assets of $16.2 million have been recorded, consisting of $14.5 million of customer relationships which are expected to be amortized over a period of fifteen years, $1.4 million of trademarks which are indefinite lived, and $0.3 million of product order backlog which amortized during the current fiscal year. The goodwill of $6.7 million created by the transaction is not deductible for income tax purposes.

The components of the fair value of the Horizon Scientific acquisition, including the allocation of the purchase price, are as follows (in thousands):

		Final
Fair value of business combination:		
Cash payments	$	26,457
Identified cash and net working capital adjustment		341

Less: cash acquired			(1,797)
Total	$		25,001
Identifiable assets acquired and liabilities assumed:			
Current assets	$		4,863
Inventories			4,470
Property, plant, and equipment			1,616
Identifiable intangible assets			16,150
Goodwill			6,660
Liabilities assumed			(2,374)
Deferred taxes		(6,384)	
Total	$		25,001

The Company finalized the purchase price allocation during fiscal year 2017. Transaction costs associated with this acquisition were immaterial. All transaction costs were recorded as general and administrative expense during the year ended June 30, 2017.

11

Acquisition-Related Costs

Acquisition-related costs include costs related to acquired businesses and other pending acquisitions. These costs consist of (i) deferred compensation and (ii) acquisition-related professional service fees and expenses, including financial advisory, legal, accounting, and other outside services incurred in connection with acquisition activities, and regulatory matters related to acquired entities. These costs do not include purchase accounting expenses, which we define as acquired backlog and the step-up of inventory to fair value, or the amortization of the acquired intangible assets.

Deferred compensation costs relate to payments due to the Horizon Scientific seller of $2.8 million on the second anniversary and $5.6 million on the third anniversary of the closing date of the purchase. For the three and six months ended December 31, 2017, we recorded deferred compensation costs for estimated deferred compensation earned by the Horizon Scientific seller to date of $0.7 million and $1.4 million, respectively. The payments are contingent on the seller remaining an employee of the Company with limited exceptions at each anniversary date.

Acquisition related expenses consist of miscellaneous professional service fees and expenses for our recent acquisitions.

The components of acquisition-related costs are as follows (dollars in thousands):

	Three Months Ended December 31,		Six Months Ended December 31,	
	2017	**2016**	**2017**	**2016**
Deferred compensation arrangements	$ 703	$ 703	$ 1,405	$ 703
Acquisition-related costs	-	800	303	800
Total	$ 703	$ 1,503	$ 1,708	$ 1,503

3) Fair Value Measurements

The financial instruments shown below are presented at fair value. Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Where available, fair value is based on observable market prices or parameters or derived from such prices or parameters. Where observable prices or inputs are not available, valuation models may be applied.

Assets and liabilities recorded at fair value in the consolidated balance sheet are categorized based upon the level of judgment associated with the inputs used to measure their fair values. Hierarchical levels directly related to the amount of subjectivity associated with the inputs to fair valuation of these assets and liabilities and the methodologies used in valuation are as follows:

Level 1 – Quoted prices in active markets for identical assets and liabilities. The Company's deferred compensation plan assets consist of shares in various mutual funds (for the deferred compensation plan, investments are participant-directed) which invest in a broad portfolio of debt and equity securities. These assets are valued based on publicly quoted market prices for the funds' shares as of the balance sheet dates.

Level 2 – Inputs, other than quoted prices in an active market, that are observable either directly or indirectly through correlation with market data. For foreign exchange forward contracts and interest rate swaps, the Company values the instruments based on the market price of instruments with similar terms, which are based on spot and forward rates as of the balance sheet dates. The Company has considered the creditworthiness of counterparties in valuing all assets and liabilities.

Level 3 – Unobservable inputs based upon the Company's best estimate of what market participants would use in pricing the asset or liability.

There were no transfers of assets or liabilities between any levels of the fair value measurement hierarchy at December 31, 2017 and June 30, 2017. The Company's policy is to recognize transfers between levels as of the date they occur.

Cash and cash equivalents, accounts receivable, and accounts payable are carried at cost, which approximates fair value.

Items presented at fair value at December 31, 2017 and June 30, 2017 consisted of the following (in thousands):

	December 31, 2017			
	Total	**Level 1**	**Level 2**	**Level 3**
Assets				
Marketable securities - deferred compensation plan	$ 2,398	$ 2,398	$ -	$ -
Foreign exchange contracts	1,108	-	1,108	-
Interest rate swaps	469	-	469	-
Liabilities				
Foreign exchange contracts	$ 6,235	$ -	$ 6,235	$ -
Interest rate swaps	13	-	13	-
Contingent acquisition payments [(a)]	3,513	-	-	3,513

	June 30, 2017			
	Total	**Level 1**	**Level 2**	**Level 3**
Assets				
Marketable securities - deferred compensation plan	$ 2,397	$ 2,397	$ -	$ -
Foreign exchange contracts	399	-	399	-
Interest rate swaps	3,777	-	3,777	-
Liabilities				
Foreign exchange contracts	$ 3,232	$ -	$ 3,232	$ -

Interest rate swaps	3,958	-	3,958	-
Contingent acquisition payments [a]	2,108	-	-	2,108

[a] The fair value of our contingent consideration arrangement is determined based on our evaluation as to the probability and amount of any deferred compensation that has been earned to date.

Our financial liabilities based upon Level 3 inputs include a contingent consideration arrangement relating to our acquisition of Horizon Scientific. We are contractually obligated to pay contingent consideration payments based on the criteria of continued employment of the seller on the second and third anniversary of the closing date of the acquisition. We will update our assumptions each reporting period based on new developments and record such amounts at fair value based on the revised assumptions until the consideration is paid.

Contingent acquisition payment liabilities are scheduled to be paid in periods through fiscal year 2020. As of December 31, 2017, we could be required to pay up to $8.4 million for contingent consideration arrangements if specific criteria are achieved. We have determined the fair value of the liabilities for the contingent consideration based on a probability-weighted discounted cash flow analysis. This fair value measurement is based on significant inputs not observable in the market and thus represents a Level 3 measurement within the fair value hierarchy. The fair value of the contingent consideration liability associated with future payments was based on several factors, the most significant of which are continued employment of the seller and the risk-adjusted discount rate for the fair value measurement. As of December 31, 2017, neither the amount recognized for the contingent consideration arrangement, nor the range of outcomes or the assumptions used to develop the estimate had changed.

4) Inventories

Inventories are comprised of the following (in thousands):

	December 31, 2017	June 30, 2017
Raw materials	$ 59,175	$ 53,313
Work in process	35,093	28,110
Finished goods	36,447	37,978
Total	$ 130,715	$ 119,401

Distribution costs associated with the sale of inventory, which are recorded as a component of selling, general and administrative expenses in the accompanying Unaudited Condensed Consolidated Statements of Operations, were $5.5 million and $11.5 million for the three and six months ended December 31, 2017, respectively and $4.6 million and $9.6 million for the three and six months ended December 31, 2016, respectively.

5) Goodwill

Changes to goodwill during the period ended December 31, 2017 were as follows (in thousands):

	June 30, 2017	Acquisitions	Translation Adjustment	December 31, 2017
Food Service Equipment	$ 63,464	$ -	$ -	$ 63,464
Engraving	20,000	5,063	286	25,349
Engineering Technologies	44,120	-	342	44,462
Electronics	112,047	286	1,018	113,351
Hydraulics	3,059	-	-	3,059
Total	$ 242,690	$ 5,349	$ 1,647	$ 249,685

6) Intangible Assets

Intangible assets consist of the following (in thousands):

	Customer Relationships	Tradenames (Indefinite-lived)	Developed Technology	Other	Total
December 31, 2017					
Cost	$ 67,095	$ 20,515	$ 47,426	$ 4,908	$ 139,944
Accumulated amortization	(31,450)	-	(2,776)	(3,502)	(37,728)
Balance, December 31, 2017	$ 35,645	$ 20,515	$ 44,650	$ 1,406	$ 102,216
June 30, 2017					
Cost	$ 64,247	$ 18,715	$ 47,586	$ 4,503	$ 135,051
Accumulated amortization	(28,764)	-	(826)	(2,958)	(32,548)
Balance, June 30, 2017	$ 35,483	$ 18,715	$ 46,760	$ 1,545	$ 102,503

Amortization expense for the three months ended December 31, 2017 and 2016 was $2.3 million and $1.1 million, respectively. Amortization expense for the six months ended December 31, 2017 and 2016 was $4.5 million and $2.0 million, respectively. At December 31, 2017, amortization expense of current intangible assets is estimated to be $4.6 million for the remainder of fiscal year 2018, $9.0 million in 2019, $8.4 million in 2020, $7.9 million in 2021, $7.4 million in 2022 and $44.4 million thereafter.

7) Warranties

The expected cost associated with warranty obligations on our products is recorded as a component of cost of sales when the revenue is recognized. The Company's estimate of warranty cost is based on contract terms and historical warranty loss experience that is periodically adjusted for recent actual experience. Since warranty estimates are forecasts based on the best available information, claims costs may differ from amounts provided. Adjustments to initial obligations for warranties are made as changes in the obligations become reasonably estimable.

The changes in warranty reserve, which are recorded as a component of accrued liabilities, as of December 31, 2017 and year ended June 30, 2017 were as follows (in thousands):

	December 31, 2017	**June 30, 2017**
Balance at beginning of year	$ 9,243	$ 9,085
Acquisitions and other	8	301
Warranty expense	4,775	9,203
Warranty claims	(4,709)	(9,346)
Balance at end of period	$ 9,317	$ 9,243

8) Debt

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

	December 31, 2017	**June 30, 2017**
Bank credit agreements	$ 216,500	$ 192,500
Other	-	6

Total funded debt	216,500	192,506
Issuance Cost	(343)	(530)
Total long-term debt		