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BALCHEM CORP
Form 10-Q
May 10, 2007

FORM 10-Q

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

(Mark One) Quarterly Report Pursuant to Section 13 or 15(d) of
 the Securities Exchange Act of 1934

For The Quarterly Period Ended March 31, 2007

or

 Transition Report Pursuant to Section 13 or 15(d) of
the Securities Exchange Act of 1934

For the transition period from _____ to _____

Commission File Number 1-13648

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

Maryland

13-2578432

(State or other jurisdiction of
incorporation or organization)

(I.R.S. Employer Identification Number)

P.O. Box 600 New Hampton, New York

10958

(Address of principal executive offices)

(Zip Code)

845-326-5600

Registrant's telephone number, including area code:

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

Yes

No

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

Large accelerated filer Accelerated filer Non-accelerated filer

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

Yes No

As of May 3, 2007 the registrant had 17,838,764 shares of its Common Stock, \$.06 2/3 par value, outstanding.

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Part 1 - Financial Information
 Item 1. Financial Statements

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

| Assets | March 2007 |
|---|----------------|
| ----- | ----- |
| Current assets: | |
| Cash and cash equivalents | \$ 1 |
| Accounts receivable | 1 |
| Inventories | 1 |
| Prepaid expenses | |
| Deferred income taxes | |
| | ----- |
| Total current assets | 3 |
| Property, plant and equipment, net | 3 |
| Goodwill | 2 |
| Intangible assets with finite lives, net | 3 |
| | ----- |
| Total assets | \$ 12 ===== |
| Liabilities and Stockholders' Equity | |
| ----- | |
| Current liabilities: | |
| Trade accounts payable | \$ |
| Accrued expenses | |
| Accrued compensation and other benefits | |
| Customer deposits and other deferred revenue | |
| Current portion of long-term debt | |
| Dividends payable | |
| Income tax payable | |
| Other short-term obligations | |
| | ----- |
| Total current liabilities | 1 |
| Long-term debt | 2 |
| Deferred income taxes | |
| Other long-term obligations | |
| | ----- |
| Total liabilities | 4 ----- |
| Stockholders' equity: | |
| Preferred stock, \$25 par value. Authorized 2,000,000 shares; none issued and outstanding | |
| Common stock, \$.0667 par value. Authorized 25,000,000 shares; 17,832,883 shares issued and outstanding at March 31, 2007 and 17,733,849 shares issued and outstanding at | |

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December 31, 2006

Additional paid-in capital

Retained earnings

Accumulated other comprehensive income

Total stockholders' equity

Total liabilities and stockholders' equity

1
6

7

\$ 12
=====

See accompanying notes to condensed consolidated financial statements.

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

| | Three Months Ended | |
|---|--------------------|-----------|
| | March 31, | |
| | 2007 | 2006 |
| | ----- | ----- |
| Net sales | \$ 27,599 | \$ 24,597 |
| Cost of sales | 17,858 | 16,375 |
| | ----- | ----- |
| Gross profit | 9,741 | 8,222 |
| Operating expenses: | | |
| Selling expenses | 2,128 | 1,669 |
| Research and development expenses | 569 | 526 |
| General and administrative expenses | 1,702 | 1,558 |
| | ----- | ----- |
| | 4,399 | 3,753 |
| | ----- | ----- |
| Earnings from operations | 5,342 | 4,469 |
| Other expenses (income): | | |
| Interest (income) | (45) | (62) |
| Interest expense | 84 | 86 |
| Other, net | (11) | -- |
| | ----- | ----- |
| Earnings before income tax expense | 5,314 | 4,445 |
| Income tax expense | 1,873 | 1,587 |
| | ----- | ----- |
| Net earnings | \$ 3,441 | \$ 2,858 |
| | ===== | ===== |
| Net earnings per common share - basic | \$ 0.19 | \$ 0.16 |
| | ===== | ===== |
| Net earnings per common share - diluted | \$ 0.19 | \$ 0.16 |

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See accompanying notes to condensed consolidated financial statements.

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BALCHEM CORPORATION
Condensed Consolidated Statements of Cash Flows
(Dollars in thousands)
(unaudited)

| | Three Months March 31 2007 | ----- |
|--|----------------------------------|-------|
| Cash flows from operating activities: | | |
| Net earnings | \$ 3,441 | \$ |
| Adjustments to reconcile net earnings to net cash provided by operating activities: | | |
| Depreciation and amortization | 952 | |
| Shares issued under employee benefit plans | 130 | |
| Deferred income taxes | (168) | |
| Stock compensation expense | 392 | |
| Gain on sale of equipment | (11) | |
| Changes in assets and liabilities net of effects of acquisition: | | |
| Accounts receivable | (2,244) | |
| Inventories | (692) | |
| Prepaid expenses and other current assets | 180 | |
| Income taxes | 1,573 | |
| Customer deposits and other deferred revenue | (329) | |
| Accounts payable and accrued expenses | (40) | |
| Other long-term obligations | 13 | |
| | ----- | ----- |
| Net cash provided by operating activities | 3,197 | |
| | ----- | ----- |
| Cash flows from investing activities: | | |
| Capital expenditures | (649) | |
| Proceeds from sale of property, plant & equipment | 11 | |
| Cash paid for intangible assets acquired | (116) | |
| Acquisition of assets | (32,085) | |
| | ----- | ----- |
| Net cash used in investing activities | (32,839) | |
| | ----- | ----- |
| Cash flows from financing activities: | | |
| Proceeds from long-term borrowings | 29,000 | |
| Principal payments on long-term debt | -- | |
| Proceeds from stock options exercised | 353 | |
| Excess tax benefits from stock compensation | 386 | |
| Dividends paid | (1,596) | |
| Other financing activities | -- | |
| | ----- | ----- |

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| | | |
|---|----------|----------|
| Net cash provided by financing activities | 28,143 | ----- |
| Decrease in cash and cash equivalents | (1,499) | |
| Cash and cash equivalents beginning of period | 5,189 | ----- |
| Cash and cash equivalents end of period | \$ 3,690 | \$ ===== |

See accompanying notes to condensed consolidated financial statements.

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BALCHEM CORPORATION
Condensed Consolidated Statements of Comprehensive Income
(Dollars in thousands)
(unaudited)

| | Three Months Ended March 31, 2007 | ----- |
|--|---|----------|
| Net Earnings | \$ 3,441 | \$ ----- |
| Other comprehensive income, net of tax: | | |
| Unfunded post retirement benefit plan - prior service cost and gain amortized during period | (3) | ----- |
| Comprehensive income | \$ 3,438 | \$ ===== |

See accompanying notes to condensed consolidated financial statements.

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

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

NOTE 1 - CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

The condensed consolidated financial statements presented herein have been prepared by the Company in accordance with the accounting policies described in its December 31, 2006 consolidated financial statements, and should be read in conjunction with the consolidated financial statements and notes, which appear in our Annual Report on Form 10-K for the year ended December 31, 2006. References in this report to the "Company" mean Balchem Corporation and/or its subsidiaries, including BCP Ingredients, Inc., Balchem Minerals Corporation, and Balchem B.V., as the context requires.

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In the opinion of management, the unaudited condensed consolidated financial statements furnished in this Form 10-Q include all adjustments necessary for a fair presentation of the financial position, results of operations and cash flows for the interim periods presented. All such adjustments are of a normal recurring nature. The condensed consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles governing interim financial statements and the instructions to Form 10-Q and Article 10 of Regulation S-X under the Securities Exchange Act of 1934 and therefore do not include some information and notes necessary to conform to annual reporting requirements. The results of operations for the three months ended March 31, 2007 are not necessarily indicative of the operating results expected for the full year or any interim period.

NOTE 2 - STOCKHOLDERS' EQUITY

STOCK-BASED COMPENSATION

On January 1, 2006, the Company adopted Statement of Financial Accounting Standards ("SFAS") No. 123 (revised 2004), "Share Based Payment" ("SFAS 123R"), which requires all share-based payments, including grants of stock options, to be recognized in the statement of earnings as an operating expense, based on their fair values. SFAS 123R establishes the accounting for transactions in which an entity pays for employee services in share-based payment transactions. SFAS 123R eliminates the ability to account for share-based compensation transactions using the intrinsic value method and requires companies to measure the cost of employee services received in exchange for an award of equity instruments based on the grant-date fair value of the award. The fair value of employee share options and similar instruments is estimated using option-pricing models that take into account the unique characteristics of those instruments. That cost is recognized over the period during which an employee is required to provide service in exchange for the award. The Company adopted SFAS 123R effective January 1, 2006, using the modified prospective transition method. Under this method, compensation cost is recognized for awards granted and for awards modified, repurchased or cancelled in the period after adoption. Compensation cost is also recognized for the unvested portion of awards granted prior to adoption over the remaining requisite service period. The Company's results for the three months ended March 31, 2007 and 2006, respectively, reflected the following compensation cost as a result of adopting SFAS 123R and such

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compensation cost had the following effects on net earnings and basic and diluted earnings per share:

| | Three Months Ended March 31, 2007 | Three Months Ended March 31, 2006 |
|-----------------------------------|---|---|
| Cost of sales | \$ 44 | \$ 27 |
| Operating expenses | 348 | 235 |
| Net earnings | (269) | (254) |
| Basic earnings per common share | (0.02) | (0.01) |
| Diluted earnings per common share | \$ (0.01) | \$ (0.01) |

As required by SFAS 123R, the Company has made an estimate of expected forfeitures, based on its historical experience, and is recognizing compensation

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cost only for those stock-based compensation awards expected to vest.

Additionally, since adoption of SFAS 123R, excess tax benefits related to stock compensation are presented as a cash inflow from financing activities. This change had the effect of decreasing cash flows from operating activities and increasing cash flows from financing activities by \$386 and \$96 for the three months ended March 31, 2007 and March 31, 2006, respectively.

The Company's stock incentive plans allow for the granting of restricted stock awards and options to purchase common stock. Both incentive stock options and nonqualified stock options can be awarded under the plans. No option will be exercisable for longer than ten years after the date of grant. The shares to be issued upon exercise of the outstanding options have been approved, reserved and are adequate to cover all exercises. As of March 31, 2007, the plans had 725,853 shares available for future awards. Compensation expense for stock options and restricted stock awards is recognized on a straight-line basis over the vesting period, generally three years for stock options, four years for employee restricted stock awards, and seven years for non-employee director restricted stock awards. Certain awards provide for accelerated vesting if there is a change in control (as defined in the plans) or other qualifying events.

Option activity for the three months ended March 31, 2007 and 2006 is summarized below:

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| For the three months ended March 31, 2007 | Shares (000s) | Weighted Average Exercise Price | Aggregate Intrinsic Value (\$000s) | Weighted Average Remaining Contractual Term |
|--|---------------|--|---|---|
| Outstanding as of December 31, 2006 | 2,170 | \$ 10.13 | \$ 15,168 | |
| Granted | -- | -- | | |
| Exercised | (101) | 3.49 | | |
| Expired | -- | -- | | |
| Forfeited | (4) | 13.65 | | |
| Outstanding as of March 31, 2007 | 2,065 | \$ 10.45 | \$ 14,920 | 7.3 |
| Exercisable as of March 31, 2007 | 1,187 | \$ 7.77 | \$ 11,770 | 6.3 |

| For the three months ended March 31, 2006 | Shares (000s) | Weighted Average Exercise Price | Aggregate Intrinsic Value (\$000s) | Weighted Average Remaining Contractual Term |
|--|---------------|--|---|---|
| Outstanding as of December 31, 2005 | 2,153 | \$ 8.38 | \$ 10,479 | |
| Granted | 15 | 15.06 | | |
| Exercised | (37) | 5.58 | | |

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| | | | | | |
|-------------------|-------|---------|-----------|-----|--|
| Expired | -- | -- | | | |
| Forfeited | (4) | 9.24 | | | |
| ----- | | | | | |
| Outstanding as of | | | | | |
| March 31, 2006 | 2,127 | \$ 8.48 | \$ 14,700 | 7.2 | |
| ===== | | | | | |
| Exercisable as of | | | | | |
| March 31, 2006 | 1,136 | \$ 6.12 | \$ 10,544 | 5.8 | |
| ===== | | | | | |

The fair value of each option grant is estimated on the date of the grant using the Black-Scholes option-pricing model with the following weighted average assumptions: dividend yields of 0.3% and 0.4%; expected volatilities of 27% and 26%; risk-free interest rates of 4.1% and 3.8%; and expected lives of 3.7 and 4.5 for the three months ended March 31, 2007 and 2006, respectively.

For the three months ended March 31, 2007 and 2006, the Company used a projected expected life for each award granted based on historical experience of employees' exercise behavior. For the three months ended March 31, 2007 and 2006, expected volatility is based on the Company's historical volatility levels. For the three months ended March 31, 2007 and 2006, dividend yields are based on the Company's historical dividend yields. Risk-free interest rates are based on the implied yields currently available on U.S. Treasury zero coupon issues with a remaining term equal to the expected life.

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Other information pertaining to option activity during the three months ended March 31, 2007 and 2006 was as follows:

| | | |
|---|---------------------------------|---------|
| | Three Months Ended March 31, | |
| | 2007 | 2006 |
| ----- | | |
| Weighted-average fair value of options granted | \$ N/A | \$ 3.49 |
| Total intrinsic value of stock options exercised (\$000s) | \$ 1,201 | \$ 320 |
| ----- | | |

Non-vested restricted stock activity for the three months ended March 31, 2007 and 2006 is summarized below:

| | | |
|--|---------------|---|
| | | Weighted Average Grant Date Fair Value |
| Three Months ended March 31, 2007 | Shares (000s) | |
| ----- | | |
| Non-vested balance as of December 31, 2006 | 113 | \$ 16.40 |
| Granted | -- | -- |
| Vested | -- | -- |
| Forfeited | -- | -- |
| Non-vested balance as of March 31, 2007 | 113 | \$ 16.40 |
| ----- | | |

| | | |
|-----------------------------------|---------------|---|
| | | Weighted Average Grant Date Fair Value |
| Three Months ended March 31, 2006 | Shares (000s) | |
| ----- | | |

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| | | | |
|--|----|----|-------|
| Non-vested balance as of December 31, 2005 | 34 | \$ | 13.22 |
| Granted | -- | | -- |
| Vested | -- | | -- |
| Forfeited | -- | | -- |
| Non-vested balance as of March 31, 2006 | 34 | \$ | 13.22 |

As of March 31, 2007 and 2006, there was \$3,619 and \$2,159, respectively, of total unrecognized compensation cost related to non-vested share-based compensation arrangements granted under the plans. As of March 31, 2007, the unrecognized compensation cost is expected to be recognized over a weighted-average period of 2 years. We estimate that share-based compensation expense for 2007 will be approximately \$1,568.

STOCK SPLITS AND REPURCHASE OF COMMON STOCK

On December 8, 2006, the Board of Directors of the Company approved a three-for-two split of the Company's common stock to be effected in the form of a stock dividend to shareholders of record on December 29, 2006. Such stock dividend was made on January 19, 2007. The stock split was recognized by reclassifying the par value of the additional shares resulting from the split, from additional paid-in capital to common stock.

On December 15, 2005, the Board of Directors of the Company approved a three-for-two split of the Company's common stock to be effected in the form of a stock dividend to shareholders of record on December 30, 2005. Such stock dividend was made on January

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20, 2006. The stock split was recognized by reclassifying the par value of the additional shares resulting from the split, from additional paid-in capital to common stock.

All references to number of common shares and per share amounts except shares authorized in the accompanying consolidated financial statements were retroactively adjusted to reflect the effect of the December 2006 and December 2005 stock splits.

In June 1999, the board of directors authorized the repurchase of shares of the Company's outstanding common stock over a two-year period commencing July 2, 1999. Under this program, which was subsequently extended, the Company had, as of December 31, 2004, repurchased a total 772,461 shares at an average cost of \$4.11 per share, none of which remained in treasury at December 31, 2004. In June 2005, the board of directors authorized another extension of the stock repurchase program for up to an additional 900,000 shares, over and above those 772,461 shares previously repurchased under the program. Under this extension, a total of 99,450 shares were purchased at an average cost of \$12.05 per share, none of which remained in treasury at March 31, 2007. During the three months ended March 31, 2007, no additional shares have been purchased. The Company intends to acquire shares from time to time at prevailing market prices if and to the extent it deems it advisable to do so based on its assessment of corporate cash flow, market conditions and other factors.

NOTE 3 - ACQUISITION OF CERTAIN ASSETS

On March 16, 2007, the Company, through its wholly-owned subsidiary BCP Ingredients, Inc. ("BCP"), entered into an asset purchase agreement (the "Asset Purchase Agreement") with Chinook Global Limited ("Chinook"), a privately held

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Ontario corporation, pursuant to which BCP acquired certain of Chinook's choline chloride business assets (the "Chinook Acquisition") for a purchase price of \$29,000, plus the value of certain product inventories estimated at approximately \$1,840. The acquisition closed effective the same date. On March 16, 2007, the Company and its principal bank entered into a new Loan Agreement (the "New Loan Agreement") providing for an unsecured term loan of \$29,000 (the "New Term Loan"), the proceeds of which were used to fund the acquisition. The New Term Loan is payable in equal monthly installments of principal, each equal to 1/60th of the principal of the New Term Loan, together with accrued interest, with remaining principal and interest payable at maturity. The New Term Loan has a maturity date of March 16, 2010 and is subject to a monthly interest rate equal to LIBOR plus 1%. At March 31, 2007, this interest rate was 6.32%. The New Loan Agreement also provides for a short-term revolving credit facility of \$6 million (the "New Revolving Facility"). The New Revolving Facility is subject to a monthly interest rate equal to LIBOR plus 1%, and accrued interest is payable monthly. No amounts have been drawn on the New Revolving Facility as of the date hereof. The New Revolving Facility has a maturity date of May 31, 2009. Management believes that such facility will be renewed in the normal course of business.

The Chinook Acquisition has been accounted for using the purchase method of accounting and the purchase price of the acquisition has been assigned to the net assets acquired based on the fair value of such assets at the date of acquisition. The preliminary allocation of the total purchase price, including acquisition costs, was based on the estimated fair values as of March 16, 2007. Adjustments to these estimates will be included in the allocation of the purchase price of the Chinook Acquisition upon

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settlement of any working capital or other adjustments. The preliminary purchase price has been allocated as follows (in thousands):

| | Fair Value Recorded in Purchase Accounting |
|-----------------------|--|
| Customer list | \$ 29,201 |
| Inventory | 1,840 |
| Short-term receivable | 1,850 |
| Short-term obligation | (870) |
| Other | 73 |
| Total | \$ 32,094 |

NOTE 4 - PRIOR YEAR ACQUISITION OF ASSETS

Effective August 24, 2006, pursuant to an asset purchase agreement of the same date, the Company, through its wholly owned subsidiaries BCP Ingredients and BCP St. Gabriel, acquired from BioAdditives, LLC, CMB Additives, LLC and CMB Realty of Louisiana (the "St. Gabriel Sellers") an animal feed grade aqueous choline chloride manufacturing facility and related assets located in St. Gabriel, Louisiana (the "St. Gabriel Acquisition"). The Company also acquired the St. Gabriel Sellers' remaining interest in a land lease (approximately 21 years) relating to the realty upon which the acquired facility and related assets are located. The acquisition was funded through the Company's cash reserves. In February 2007, the facility was placed in service.

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NOTE 5 - PRIOR YEAR ACQUISITION OF STOCK

On February 8, 2006, the Company, through its wholly owned subsidiary Balchem Minerals Corporation ("BMC"), completed an acquisition (the "CMC Acquisition") of all of the outstanding capital stock of Chelated Minerals Corporation ("CMC"), a privately held Utah corporation, for a purchase price of \$17,350, subject to adjustment based upon CMC's actual working capital and other adjustments. On February 6, 2006, the Company and its principal bank entered into a Loan Agreement (the "Loan Agreement") providing for an unsecured term loan of \$10,000 (the "Term Loan"), the proceeds of which were used to fund the CMC Acquisition, in part. The remaining balance of the purchase price of the CMC Acquisition was funded through the Company's cash reserves. At December 31, 2006, the Term Loan had been repaid in full.

The CMC Acquisition has been accounted for using the purchase method of accounting and the purchase price of the acquisition has been assigned to the net assets acquired based on the fair value of such assets and liabilities at the date of acquisition. The preliminary allocation of the total purchase price, including acquisition costs, of CMC's net tangible and intangible assets was based on the estimated fair values as of February 8, 2006. Adjustments to these estimates will be included in the allocation of the purchase price of CMC upon settlement of any working capital or other adjustments. The excess of the purchase price over the identifiable intangible and net tangible assets was allocated to goodwill. The purchase price has been allocated as follows (in thousands):

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| | Fair Value Recorded in Purchase Accounting |
|-------------------------------|--|
| Accounts receivable | \$ 884 |
| Inventory | 552 |
| Property, plant and equipment | 1,980 |
| Current liabilities | (388) |
| Other long-term liabilities | (2,368) |
| Goodwill | 11,894 |
| Other intangible assets | 5,334 |
| Total | \$ 17,888 |

The consolidated financial statements include the results of operations of CMC from the date of purchase.

Pro Forma Summary of Operations

The following unaudited pro forma information has been prepared as if the CMC Acquisition had occurred on January 1, 2006 and does not include cost savings expected from the transaction. In addition to including the results of operations, the pro forma information gives effect primarily to changes in depreciation and amortization of tangible and intangible assets resulting from the acquisition.

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

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| | Actual March 31, 2007 | Pro Forma March 31, 2006 |
|--------------|-----------------------------|--------------------------------|
| Net sales | \$ 27,599 | \$ 25,331 |
| Net earnings | \$ 3,441 | \$ 2,893 |
| Basic EPS | \$.19 | \$.17 |
| Diluted EPS | \$.19 | \$.16 |

NOTE 6 - INVENTORIES

Inventories at March 31, 2007 and December 31, 2006 consisted of the following:

| | March 31, 2007 | December 31, 2006 |
|-------------------|-------------------|----------------------|
| Raw materials | \$ 4,420 | \$ 4,264 |
| Finished goods | 8,031 | 5,654 |
| Total inventories | \$ 12,451 | \$ 9,918 |

NOTE 7 - PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment at March 31, 2007 and December 31, 2006 are summarized as follows:

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| | March 31, 2007 | December 31, 2006 |
|-----------------------------------|-------------------|----------------------|
| Land | \$ 650 | \$ 650 |
| Building | 11,640 | 11,640 |
| Equipment | 38,545 | 38,545 |
| Construction in Progress | 1,896 | 1,247 |
| | 52,731 | 52,082 |
| Less: Accumulated depreciation | 21,547 | 20,769 |
| Net property, plant and equipment | \$ 31,184 | \$ 31,313 |

NOTE 8 - INTANGIBLE ASSETS

Goodwill represents the excess of costs over fair value of assets of businesses acquired. The Company adopted the provisions of SFAS No. 141, Business Combinations, and SFAS No. 142, Goodwill and Other Intangible Assets, as of January 1, 2002. These standards require the use of the purchase method of accounting for a business combination and define an intangible asset. Goodwill and intangible assets acquired in a purchase business combination and determined to have an indefinite useful life are not amortized, but are instead tested for impairment at least annually in accordance with the provisions of SFAS No. 142.

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SFAS No. 142 also requires that intangible assets with estimable useful lives be amortized over their respective estimated useful lives to their estimated residual values, and reviewed for impairment in accordance with SFAS No. 144, Accounting for Impairment or Disposal of Long-Lived Assets.

As of December 31, 2006, the Company performed an impairment test of its goodwill balance. As of such date, the Company's reporting units' fair values exceeded their carrying amounts, and therefore there was no indication that goodwill was impaired. Accordingly, the Company was not required to perform any further impairment tests. The Company will perform its impairment test next on December 31, 2007.

The Company had goodwill in the amount of \$25,244 and \$25,253 at March 31, 2007 and December 31, 2006, respectively, subject to the provisions of SFAS Nos. 141 and 142.

As of March 31, 2007 and December 31, 2006, the Company had identifiable intangible assets with finite lives with a gross carrying value of approximately \$37,188 and \$7,799, respectively, less accumulated amortization of \$1,060 and \$887, respectively. At March 31, 2007, the gross carrying amount included a customer list acquired as part of the Chinook acquisition, as described in Note 3.

Identifiable intangible assets with finite lives at March 31, 2007 and December 31, 2006 are summarized as follows:

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| | Amortization Period (in years) | Gross Carrying Amount at 3/31/07 | Accumulated Amortization at 3/31/07 | Gross Carrying Amount at 12/31/06 | Accumulat Amortizatio 12/31/06 |
|-------------------------------------|--------------------------------------|---|---|--|--------------------------------------|
| Customer lists | 10 | \$ 34,089 | \$ 619 | \$ 4,888 | \$ 4 |
| Regulatory re-registration costs | 10 | 28 | -- | 28 | |
| Patents & trade secrets | 15-17 | 1,567 | 244 | 1,550 | 2 |
| Trademarks & trade names | 17 | 876 | 107 | 876 | |
| Other | 5 | 628 | 90 | 457 | |
| | | \$ 37,188 | \$ 1,060 | \$ 7,799 | \$ 8 |

Amortization of identifiable intangible assets was approximately \$173 for the first three months of 2007. Assuming no change in the gross carrying value of identifiable intangible assets, the estimated amortization expense for the remainder of 2007 is \$2,670, approximately \$3,545 per annum for 2008 and 2009, \$3,537 per annum for 2010 and 2011 and \$3,520 in 2012. At March 31, 2007, there were no identifiable intangible assets with indefinite useful lives as defined by SFAS No. 142. Identifiable intangible assets are reflected in "Intangible assets with finite lives, net" in the Company's consolidated balance sheets. There were no changes to the useful lives of intangible assets subject to amortization during the three months ended March 31, 2007.

NOTE 9 - NET EARNINGS PER SHARE

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

| Three months ended March 31, 2007 | Net Earnings (Numerator) | Number of Shares (Denominator) | Per Share Amount |
|---|--------------------------------|--------------------------------------|---------------------|
| Basic EPS - Net earnings and weighted average common shares outstanding | \$ 3,441 | 17,686,624 | \$.19 |
| Effect of dilutive securities - stock options | | 697,908 | |
| Diluted EPS - Net earnings and weighted average common shares outstanding and effect of stock options | \$ 3,441 | 18,384,532 | \$.19 |

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| Three months ended March 31, 2006 | Net Earnings (Numerator) | Number of Shares (Denominator) | Per Share Amount |
|---|--------------------------------|--------------------------------------|---------------------|
| Basic EPS - Net earnings and weighted average common shares outstanding | \$ 2,858 | 17,393,940 | \$.16 |
| Effect of dilutive securities - stock options | | 843,838 | |
| Diluted EPS - Net earnings and weighted average common shares outstanding and effect of stock options | \$ 2,858 | 18,237,778 | \$.16 |

The Company had stock options for 384,525 and 493,575 common shares at March 31, 2007 and 2006, respectively, that could potentially dilute basic earnings per share in future periods that were not included in diluted earnings per share because their effect on the period presented was anti-dilutive.

NOTE 10 - INCOME TAXES

Effective January 1, 2007, the Company adopted the provisions of Financial Accounting Standards Board ("FASB") Interpretation No. 48, "Accounting for Uncertainty in Income Taxes" ("FIN 48"). This interpretation, among other things, creates a two-step approach for evaluating uncertain tax positions. Recognition (step one) occurs when an enterprise concludes that a tax position, based solely on its technical merits, is more-likely-than-not to be sustained upon examination. Measurement (step two) determines the amount of benefit that more-likely-than-not will be realized upon settlement. De-recognition of a tax

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position that was previously recognized would occur when a company subsequently determines that a tax position no longer meets the more-likely-than-not threshold of being sustained. FIN 48 specifically prohibits the use of a valuation allowance as a substitute for de-recognition of tax positions, and it has expanded disclosure requirements. The adoption of FIN 48 resulted in, as a cumulative effect, a non-cash charge, net of federal tax benefits, of \$291, recorded as a reduction to beginning retained earnings. The charge before federal tax benefits was \$411. The Company includes interest expense or income as well as potential penalties on unrecognized tax positions as a component of income tax expense in the consolidated statement of operations. The total amount of accrued interest and penalties related to uncertain tax positions at January 1, 2007 was \$89 and is included in other long-term obligations. All of our unrecognized tax benefits, if recognized in future periods, would impact the Company's effective tax rate. The Company remains open for examination by the IRS for 2003 through 2006. For most of its other significant tax jurisdictions (U.S. states), the Company's income tax returns are also open for examination for 2003 through 2006. There was not a significant change in our liabilities for unrecognized tax benefits during the three months ended March 31, 2007. With each year our tax exposure rolls forward with incremental increases expected based on continued growth and no changes are foreseen to this trend at present.

NOTE 11 - SEGMENT INFORMATION

The Company's reportable segments are strategic businesses that offer products and services to different markets. Presently, the Company has three segments: specialty

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products, encapsulated / nutritional products and BCP Ingredients, its unencapsulated feed supplements segment.

Business Segment Net Sales:

| | Three Months Ended March 31 | |
|-----------------------------------|--------------------------------|------------------|
| | 2007 | 2006 |
| Specialty Products | \$ 8,061 | \$ 7,951 |
| Encapsulated/Nutritional Products | 11,500 | 9,789 |
| BCP Ingredients | 8,038 | 6,857 |
| Total | \$ 27,599 | \$ 24,597 |

Business Segment Earnings:

| | Three Months Ended March 31 | |
|-----------------------------------|--------------------------------|----------|
| | 2007 | 2006 |
| Specialty Products | \$ 2,903 | \$ 2,772 |
| Encapsulated/Nutritional Products | 1,243 | 1,039 |
| BCP Ingredients | 1,196 | 658 |
| Interest and other expense | (28) | (24) |

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| | | | | |
|------------------------------|----|-------|----|-------|
| Earnings before income taxes | \$ | 5,314 | \$ | 4,445 |
|------------------------------|----|-------|----|-------|

NOTE 12- SUPPLEMENTAL CASH FLOW INFORMATION

Cash paid during the three months ended March 31, 2007 and 2006 for income taxes and interest is as follows:

| | Three Months Ended March 31 | |
|--------------|--------------------------------|-------|
| | 2007 | 2006 |
| Income taxes | \$ 82 | \$ 2 |
| Interest | \$ 84 | \$ 86 |

NOTE 13 - LONG TERM DEBT AND CREDIT AGREEMENTS

On March 16, 2007, the Company and its principal bank entered into a new Loan Agreement (the "New Loan Agreement") providing for an unsecured term loan of \$29,000 (the "New Term Loan"), the proceeds of which were used to fund the Chinook acquisition (the "Acquisition"), as described in Note 3. The New Term Loan is payable in equal monthly installments of principal, each equal to 1/60th of the principal of the New Term Loan, together with accrued interest, with remaining principal and interest payable at maturity. The New Term Loan has a maturity date of March 16, 2010 and is subject to a monthly interest rate equal to LIBOR plus 1%. At March 31, 2007, this interest rate was 6.32%. The New Loan Agreement also provides for a short-term

revolving credit facility of \$6 million (the "New Revolving Facility"). The New Revolving Facility is subject to a monthly interest rate equal to LIBOR plus 1%, and accrued interest is payable monthly. No amounts have been drawn on the New Revolving Facility as of the date hereof. The New Revolving Facility has a maturity date of May 1, 2008.

NOTE 14 - EMPLOYEE BENEFIT PLANS

The Company sponsors a 401(k) savings and profit sharing plan for eligible employees. The plan allows participants to make pretax contributions and the Company matches certain percentages of those pretax contributions with shares of the Company's common stock. The profit sharing portion of the plan is discretionary and non-contributory. All amounts contributed to the plan are deposited into a trust fund administered by independent trustees.

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

Net periodic benefit cost for such retirement medical plan for the three months ended March 31, 2007 and March 31, 2006 was as follows:

| | 2007 | 2006 |
|--|------|------|
|--|------|------|

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| | | | | |
|---------------------------------------|----|-----|----|-----|
| Service Cost | \$ | 7 | \$ | 8 |
| Interest Cost | | 10 | | 13 |
| Expected return on plan assets | | -- | | -- |
| Amortization of transition obligation | | -- | | -- |
| Amortization of prior service cost | | (5) | | (5) |
| Amortization of (gain) or loss | | (1) | | 1 |
| <hr/> | | | | |
| Net periodic benefit cost | \$ | 11 | \$ | 17 |

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

NOTE 15 - LICENSE AGREEMENT

On November 7, 2005, the Company entered into a license agreement (the "License Agreement") with Project Management and Development Co., Ltd. ("PMD"), a corporation organized under the laws of Great Britain. The License Agreement gives PMD the right to utilize the Company's proprietary continuous manufacturing technology for the production of aqueous choline chloride ("Company Technology") in connection with PMD's construction and operation of an aqueous choline chloride production facility at PMD's Al-JuBail, Saudi Arabia petrochemical facility, currently scheduled for completion in late 2009.

The License Agreement provides PMD with the exclusive right to use Company Technology in certain countries, as well as the non-exclusive right to market, sell and use the products derived from Company Technology on a world-wide basis. The License Agreement further provides that the Company will be PMD's exclusive North American distributor for said products during the term of the agreement. The License Agreement

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terminates either 10 years from the start-up of the PMD's production facility or December 31, 2020, whichever is earlier.

Pursuant to the License Agreement, PMD will pay the Company a license fee of \$1,400 and fees of \$840 for the delivery by the Company of certain preliminary drawings, specifications, process design documents containing Company Technology, and additional training. These fees are to be paid in installments upon achievement of certain performance milestones set forth in the License Agreement.

The Company will provide certain performance guarantees associated with Company Technology. In the event that the PMD manufacturing facility, if properly designed and constructed, fails to attain said performance guarantees, liquidated damages may be assessed, but not exceeding 70% of the license fee.

The Company is using the percentage of completion method to recognize revenue and expenses related to the License Agreement and the efforts-expended method for measuring the progress to completion. As of March 31, 2007, the Company has recognized \$1,000 of income and \$515 in expenses since the inception of the agreement.

NOTE 16 - NEW ACCOUNTING PRONOUNCEMENTS

In February, 2007 the FASB issued SFAS No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities", including an amendment of FASB

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Statement No. 115. This statement permits entities to choose to measure many financial instruments and certain other items at fair value. The objective is to improve financial reporting by providing entities with the opportunity to mitigate volatility in reported earnings caused by measuring related assets and liabilities differently without having to apply complex hedge accounting provisions. This statement is expected to expand the use of fair market value measurement, which is consistent with long-term measurement objectives for accounting for financial instruments. This statement is effective beginning in January 2008. The Company does not expect the adoption of this statement to be significant to its consolidated financial statements.

In September 2006, the FASB issued SFAS 157, "Fair Value Measurements," which defines fair value, establishes a framework for measuring fair value under generally accepted accounting principles, and expands disclosures about fair value measurements. SFAS 157 does not require any new fair value measurements, but provides guidance on how to measure fair value by providing a fair value hierarchy used to classify the source of the information. This statement is effective beginning in January 2008. The Company is evaluating whether adoption of this statement will result in a change to its fair value measurements.

NOTE 17 - SUBSEQUENT EVENTS

On April 30, 2007, the Company, through its European subsidiary, Balchem B.V., completed an acquisition of the methylamines and choline chloride business and manufacturing facilities of Akzo Nobel Chemicals S.p.A., located in Marano Ticino, Italy for a provisional purchase price of approximately \$6,281. Such amount is subject to adjustment after the closing based upon actual finished goods and raw materials inventory as of the closing date, as well as reconciliation of the other estimated constituents of the provisional purchase price. The parties believe the final purchase price will be fully settled no later than 90 days after closing.

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

This Report contains forward-looking statements, within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended, which reflect our expectation or belief concerning future events that involve risks and uncertainties. Our actions and performance could differ materially from what is contemplated by the forward-looking statements contained in this Report. Factors that might cause differences from the forward-looking statements include those referred to or identified in Item 1 of our Annual Report on Form 10-K for the year ended December 31, 2006 and other factors that may be identified elsewhere in this Report. Reference should be made to such factors and all forward-looking statements are qualified in their entirety by the above cautionary statements.

Overview

We develop, manufacture, distribute and market specialty performance ingredients and products for the food, nutritional, pharmaceutical, animal health and medical device sterilization industries. Our reportable segments are strategic businesses that offer products and services to different markets. We presently have three reportable segments: specialty products; encapsulated / nutritional products; and BCP Ingredients.

Specialty Products

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Our specialty products segment operates as ARC Specialty Products.

Ethylene oxide, at the 100% level, is sold as a sterilant gas, primarily for use in the health care industry. It is used to sterilize a wide range of medical devices because of its versatility and effectiveness in treating hard or soft surfaces, composites, metals, tubing and different types of plastics without negatively impacting the performance of the device being sterilized. Our 100% ethylene oxide product is distributed in uniquely designed, recyclable double-walled stainless steel drums to assure compliance with safety, quality and environmental standards as outlined by the U.S. Environmental Protection Agency (the "EPA") and the U.S. Department of Transportation. Our inventory of these specially built drums, along with our two filling facilities, represents a significant capital investment. Contract sterilizers, medical device manufacturers, and medical gas distributors are our principal customers for this product. In addition, we also sell single use canisters with 100% ethylene oxide for use in medical device sterilization. As a fumigant, ethylene oxide blends are highly effective in killing bacteria, fungi, and insects in spices and other seasoning materials.

We sell two other products, propylene oxide and methyl chloride, principally to customers seeking smaller (as opposed to bulk) quantities and whose requirements include timely delivery and safe handling. Propylene oxide is used for fumigation in spice treatment, various chemical synthesis applications, to make paints more durable, and for manufacturing specialty starches and textile coatings. Methyl chloride is used as a raw material in specialty herbicides, fertilizers, pharmaceuticals, malt and wine preservers.

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Encapsulated / Nutritional Products

The encapsulated / nutritional products segment provides microencapsulation, granulation and agglomeration solutions to a variety of applications in food, pharmaceutical and nutritional ingredients to enhance performance of nutritional fortification, processing, mixing, packaging applications and shelf-life. Major product applications are baked goods, refrigerated and frozen dough systems, processed meats, seasoning blends, confections, nutritional supplements and animal nutrition. We also market human grade choline nutrient products through this segment for wellness applications. Choline is recognized to play a key role in the structural integrity of cell membranes, processing dietary fat, reproductive development and neural functions, such as memory and muscle function. Our portfolio of granulated calcium carbonate products are primarily used in, or in conjunction with, novel over-the-counter and prescription pharmaceuticals for the treatment of osteoporosis, gastric disorders and calcium deficiencies in the United States.

In the animal health industry, we market REASHURE(R) Choline, an encapsulated choline product that boosts health and milk production in transition and early lactation cows. Commercial sales are currently derived from the dairy industry where REASHURE(R) delivers nutrient supplements that survive the rumen and are biologically available, providing required nutritional levels during certain weeks preceding and following calving, commonly referred to as the "transition period" of the animal. Also, in animal health, we market NITROSHURETM, an encapsulated urea supplement for lactating dairy cows that is designed to create a slow-release nitrogen source for the rumen, allowing for greater flexibility in feed rations for dairy nutritionists and producers, and NIASHURETM, our microencapsulated niacin product for dairy cows. In addition, CMC manufactures, sells and distributes chelated mineral supplements for use in animal feed throughout the world. CMC's proprietary chelation technology provides enhanced

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nutrient absorption for various species of domestic and companion animals.

BCP Ingredients

This segment manufactures and supplies raw choline chloride, an essential nutrient for animal health, predominantly to the poultry and swine industries. Choline plays a vital role in the metabolism of fat and the building and maintaining of cell structures. Choline deficiency can result in, among other symptoms, reduced growth and perosis in poultry, and fatty liver, kidney necrosis and general poor health conditions in swine. In addition, certain derivatives of choline chloride are also manufactured and sold into industrial applications. Choline chloride is manufactured and sold in both an aqueous and dry form.

We sell products for all three segments through our own sales force, independent distributors and sales agents.

The following tables summarize consolidated net sales by segment and business segment earnings for the three months ended March 31, 2007 and 2006:

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Business Segment Net Sales:

| | Three Months Ended March 31 | |
|-----------------------------------|--------------------------------|-----------|
| | 2007 | 2006 |
| Specialty Products | \$ 8,061 | \$ 7,951 |
| Encapsulated/Nutritional Products | 11,500 | 9,789 |
| BCP Ingredients | 8,038 | 6,857 |
| Total | \$ 27,599 | \$ 24,597 |

Business Segment Earnings:

| | Three Months Ended March 31 | |
|-----------------------------------|--------------------------------|----------|
| | 2007 | 2006 |
| Specialty Products | \$ 2,903 | \$ 2,772 |
| Encapsulated/Nutritional Products | 1,243 | 1,039 |
| BCP Ingredients | 1,196 | 658 |
| Interest and other expense | (28) | (24) |
| Earnings before income taxes | \$ 5,314 | \$ 4,445 |

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RESULTS OF OPERATIONS

Three months ended March 31, 2007 compared to three months ended March 31, 2006

Net Sales

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Net sales for the three months ended March 31, 2007 were \$27,599 compared with \$24,597 for the three months ended March 31, 2006, an increase of \$3,002 or 12.2%. Net sales for the specialty products segment were \$8,061 for the three months ended March 31, 2007 compared with \$7,951 for the three months ended March 31, 2006, an increase of \$110 or 1.4%. This increase was principally due to an increase in sales volume of ethylene oxide for medical device sterilization. Net sales for the encapsulated / nutritional products segment were \$11,500 for the three months ended March 31, 2007 compared with \$9,789 for the three months ended March 31, 2006, an increase of \$1,711 or 17.5%. This increase was due principally to increased volumes sold in the human choline, animal health and chelated mineral markets. This increase was partially offset by decreased volumes sold in the human food and pharmaceutical markets. Net sales of \$8,038 were realized for the three months ended March 31, 2007 for the BCP Ingredients (unencapsulated feed supplements) segment, which markets choline for the poultry and swine industries as well as industrial choline derivative products, as compared with \$6,857 for the three months ended March 31, 2006, an increase of \$1,181 or 17.2%. This increase was due to increased volumes sold in the dry choline, aqueous choline, and specialty industrial product lines. This increase in sales volume was also partially a result of the Chinook acquisition, as described in Note 3.

Gross Margin

Gross margin for the three months ended March 31, 2007 increased to \$9,741 compared to \$8,222 for the three months ended March 31, 2006, an increase of \$1,519 or 18.5%, due largely to the above-noted increase in sales. Gross margin percentage for the three months ended March 31, 2007 was 35.3% compared to 33.4% for the three months ended March 31, 2006. This increase in gross margin percentage was primarily a result of product mix, increased production volumes and lower raw material prices. Gross margin for the specialty products segment increased 6.3% primarily due to increased sales volume. Gross margin in the encapsulated / nutritional products segment increased 18.7% as margins were favorably affected by product mix as well as sales volumes, as described above. Gross margin for BCP Ingredients increased 81.1% and was favorably affected by increased sales volumes of choline chloride and specialty derivative products.

Operating Expenses

Operating expenses for the three months ended March 31, 2007 were \$4,399 compared to \$3,753 for the three months ended March 31, 2006, an increase of \$646 or 17.2%. This increase was primarily a result of increased payroll costs for new hires. Total operating expenses as a percentage of sales were 15.9% for the three months ended March 31, 2007 compared to 15.3% for the three months ended March 31, 2006. During the three months ended March 31, 2007 and 2006, the Company spent \$569 and \$526, respectively, on research and development programs, substantially all of which pertained to the

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Company's encapsulated / nutritional products segment for both food and animal feed applications.

Earnings From Operations

As a result of the foregoing, earnings from operations for the three months ended March 31, 2007 were \$5,342 as compared to \$4,469 for the three months ended March 31, 2006.

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Other Expenses (Income)

Interest income for the three months ended March 31, 2007 totaled \$45 as compared to \$62 for the three months ended March 31, 2006. This decrease is attributable to a decrease in the average total cash balance on-hand during the quarter. Interest expense was \$84 for the three months ended March 31, 2006 compared to \$86 for the three months ended March 31, 2006. Other income of \$11 for the three months ended March 31, 2007 represents the net gain on the sale of equipment.

Income Tax Expense

The Company's effective tax rate for the three months ended March 31, 2007 and 2006 was 35.2% and 35.7%, respectively.

Net Earnings

As a result of the foregoing, net earnings were \$3,441 for the three months ended March 31, 2007 as compared with \$2,858 for the three months ended March 31, 2006, an increase of 20.4%.

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FINANCIAL CONDITION

LIQUIDITY AND CAPITAL RESOURCES

Contractual Obligations

As part of the June 30, 2005 acquisition of certain assets relating to the encapsulation, agglomeration and granulation business of Loders Croklaan USA, LLC, the asset purchase agreement provides for the contingent payment by the Company of additional consideration based upon the volume of sales associated with one particular product acquired by the Company during the three year period following the acquisition. Such contingent consideration will be recorded as an additional cost of the acquired product lines. As of December 31, 2006, such contingent consideration of \$23 has been earned and paid. No such contingent consideration has been earned and paid in 2007.

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

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

The Company expects its operations to continue generating sufficient cash flow to fund working capital requirements and necessary capital investments. The Company is actively pursuing additional acquisition candidates. The Company could seek additional bank loans or access to financial markets to fund such acquisitions, its operations, working capital, necessary capital investments or other cash requirements should it deem it necessary to do so.

Cash

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Cash and cash equivalents decreased to \$3,690 at March 31, 2007 from \$5,189 at December 31, 2006. The \$1,499 decrease resulted primarily from net cash used in investing activities of \$32,839, principally for the acquisition of certain choline chloride business assets of Chinook Global Limited, offset by net cash provided by operating activities and financing activities of \$3,197 and \$28,143, respectively. Working capital amounted to \$18,018 at March 31, 2007 as compared to \$19,295 at December 31, 2006, a decrease of \$1,277.

Operating Activities

Cash flows from operating activities provided \$3,197 for the three months ended March 31, 2007 compared to \$4,199 for the three months ended March 31, 2006. The decrease in cash flows from operating activities was primarily due to increases in accounts receivable and inventories as well as a decrease in customer deposits and deferred revenue. This decrease was partially offset by an increase in net earnings, depreciation and amortization expense, stock compensation expense and income taxes payable.

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Investing Activities

Capital expenditures were \$649 for the three months ended March 31, 2007 compared to \$263 for the three months ended March 31, 2006. Cash paid for the acquisition of certain choline chloride business assets of Chinook Global Limited was \$32,094. Cash received as part of the working capital adjustment for the 2006 acquisition of all the outstanding common stock of Chelated Minerals Corporation was \$9.

Financing Activities

In June 1999, the board of directors authorized the repurchase of shares of the Company's outstanding common stock over a two-year period commencing July 2, 1999. Under this program, which was subsequently extended, the Company had, as of December 31, 2004, repurchased a total 772,461 shares at an average cost of \$4.11 per share, none of which remained in treasury at December 31, 2004. In June 2005, the board of directors authorized another extension of the stock repurchase program for up to an additional 900,000 shares, over and above those 772,461 shares previously repurchased under the program. A total of 99,450 shares were purchased at an average cost of \$12.05 per share, none of which remained in treasury at March 31, 2007. The Company intends to acquire shares from time to time at prevailing market prices if and to the extent it deems it advisable to do so based on its assessment of corporate cash flow, market conditions and other factors.

On March 16, 2007, the Company and its principal bank entered into a new Loan Agreement (the "New Loan Agreement") providing for an unsecured term loan of \$29,000 (the "New Term Loan"), the proceeds of which were used to fund the Chinook acquisition (the "Acquisition"), as described in Note 3. The New Term Loan is payable in equal monthly installments of principal, each equal to 1/60th of the principal of the New Term Loan, together with accrued interest, with remaining principal and interest payable at maturity. The New Term Loan has a maturity date of March 16, 2010 and is subject to a monthly interest rate equal to LIBOR plus 1%. At March 31, 2007, this interest rate was 6.32%. The New Loan Agreement also provides for a short-term revolving credit facility of \$6,000 (the "New Revolving Facility"). The New Revolving Facility is subject to a

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monthly interest rate equal to LIBOR plus 1%, and accrued interest in payable monthly. No amounts have been drawn on the New Revolving Facility as of the date hereof. The New Revolving Facility has a maturity date of May 31, 2009. Management believes that such facility will be renewed in the normal course of business.

On February 6, 2006, the Company and its principal bank entered into a Loan Agreement (the "Loan Agreement") providing for an unsecured term loan of \$10,000 (the "Term Loan"), the proceeds of which were used to fund the CMC acquisition (the "CMC Acquisition"), as described in Note 5, in part. The remaining balance of the purchase price of the CMC Acquisition was funded through Balchem's cash on hand. The Company repaid in full the \$10,000 of principal under the Term Loan in 2006.

Proceeds from stock options exercised totaled \$353 and \$206 for the three months ended March 31, 2007 and 2006, respectively. Dividend payments were \$1,596 and \$1,045 for the three months ended March 31, 2007 and 2006, respectively.

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Other Matters Impacting Liquidity

The Company currently provides postretirement benefits in the form of a retirement medical plan under a collective bargaining agreement covering eligible retired employees of its Verona, Missouri facility. The amount recorded on the Company's balance sheet as of March 31, 2006 for this obligation is \$745. The postretirement plan is not funded. Historical cash payments made under such plan have approximated \$50 per year.

Critical Accounting Policies

Accounting for Uncertainty in Income Taxes

As discussed above, effective January 1 2007, the Company adopted the provisions of FASB Interpretation No. 48, "Accounting for Uncertainty in Income Taxes" ("FIN 48"). This interpretation, among other things, creates a two-step approach for evaluating uncertain tax positions. Recognition (step one) occurs when an enterprise concludes that a tax position, based solely on its technical merits, is more-likely-than-not to be sustained upon examination. Measurement (step two) determines the amount of benefit that more-likely-than-not will be realized upon settlement. De-recognition of a tax position that was previously recognized would occur when a company subsequently determines that a tax position no longer meets the more-likely-than-not threshold of being sustained. FIN 48 specifically prohibits the use of a valuation allowance as a substitute for de-recognition of tax positions, and it has expanded disclosure requirements. The adoption of FIN 48 resulted in a non-cash transition charge of \$291, recorded as a reduction to beginning retained earnings.

Other than the aforementioned adoption of FIN 48, there were no changes to the Company's Critical Accounting Policies, as described in its December 31, 2006 Annual Report on Form 10-K, during the three months ended March 31, 2007.

Related Party Transactions

The Company was not engaged in related party transactions during the three months ended March 31, 2007 and all transactions of the Company during such period were at arms length.

Item 3. Quantitative and Qualitative Disclosures about Market Risk

Cash and cash equivalents are invested primarily in money market accounts. Accordingly, we believe we have limited exposure to market risk for changes in interest rates. The Company has no derivative financial instruments or derivative commodity instruments, nor does the Company have any financial instruments entered into for trading or hedging purposes. Foreign sales are generally billed in U.S. dollars. As of March 31, 2007, the Company's only borrowings were under a bank term loan, which bears interest at LIBOR plus 1.00%. A 100 basis point increase or decrease in interest rates, applied to the Company's borrowings at March 31, 2007, would result in an increase or decrease in annual interest expense and a corresponding reduction or increase in cash flow of approximately \$290. The Company believes that its business operations are not exposed in any material respect to market risk relating to foreign currency exchange risk or commodity price risk.

Item 4. Controls and Procedures

(a) Evaluation of Disclosure Controls and Procedures

Pursuant to the requirements of the Sarbanes-Oxley Act of 2002, the Company's management, under the supervision and with the participation of the Company's Chief Executive Officer and Chief Financial Officer, has evaluated, as of the end of the period covered by this Quarterly Report on Form 10-Q, the effectiveness of the Company's disclosure controls and procedures (including its internal controls and procedures).

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

(b) Changes in Internal Controls

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

Part II. Other Information

Item 1A. Risk Factors

There have been no material changes in the Risk Factors identified in the Company's Annual Report on Form 10-K for the year ended December 31, 2006.

Item 6. Exhibits

Exhibit 31.1 Certification of Chief Executive Officer

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pursuant to Rule 13a-14(a).

- Exhibit 31.2 Certification of Chief Financial Officer pursuant to Rule 13a-14(a).
- Exhibit 32.1 Certification of Chief Executive Officer pursuant to Rule 13a-14(b) and Section 1350 of Chapter 63 of Title 18 of the United States Code.
- Exhibit 32.2 Certification of Chief Financial Officer pursuant to Rule 13a-14(b) and Section 1350 of Chapter 63 of Title 18 of the United States Code.
- Exhibit 32.3 Asset Purchase Agreement dated March 16, 2007, by and between BCP Ingredients, Inc. and Chinook Global Limited (incorporated by reference to Exhibit 2.1 to the Company's Current Report on Form 8-K dated March 21, 2007).
- Exhibit 32.4 Tolling Agreement, dated March 16, 2007 between BCP Ingredients, Inc. and Chinook Global Limited (incorporated by reference to Exhibit 10.1 to the Company's Current Report on Form 8-K dated March 21, 2007).
- Exhibit 32.5 Non-Competition Agreement, dated March 16, 2007 between BCP Ingredients, Inc. and Chinook Global Limited; Chinook Services, LLC; Chinook, LLC; Dean R. Lacy; Ronald Breen, and John N. Kennedy (incorporated by reference to Exhibit 10.2 to the Company's Current Report on Form 8-K dated March 21, 2007).
- Exhibit 32.6 Loan Agreement dated March 16, 2007 by and between Bank of America, N.A. and Balchem Corporation (incorporated by reference to Exhibit 10.3 to the Company's Current Report on Form 8-K dated March 21, 2007).
- Exhibit 32.7 Promissory Note (Term Loan) dated March 16, 2007 from Balchem Corporation to Bank of America, N.A. (incorporated by reference to Exhibit 10.4 to the Company's Current Report on Form 8-K dated March 21, 2007).
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- Exhibit 32.8 Promissory Note (Revolving Line of Credit) dated March 16, 2007 from Balchem Corporation to Bank of America, N.A. (incorporated by reference to Exhibit 10.5 to the Company's Current Report on Form 8-K dated March 21, 2007).
- Exhibit 32.9 Guaranty dated March 16, 2007 from BCP Ingredients, Inc. to Bank of America, N.A. (incorporated by reference to Exhibit 10.6

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to the Company's Current Report on Form 8-K dated March 21, 2007).

Exhibit 32.10 Guaranty dated March 16, 2007 from Balchem Minerals Corporation to Bank of America, N.A. (incorporated by reference to Exhibit 10.7 to the Company's Current Report on Form 8-K dated March 21, 2007).

Exhibit 32.11 Sale and Purchase Agreement dated March 30, 2007, by and between Balchem B.V. and Akzo Nobel Chemicals S.p.A. (incorporated by reference to Exhibit 2.1 to the Company's Current Report on Form 8-K dated April 4, 2007).

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

BALCHEM CORPORATION

By: /s/ Dino A. Rossi

Dino A. Rossi, President and
Chief Executive Officer

Date: May 10, 2007

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Exhibit Index

| Exhibit No. ----- | Description ----- |
|----------------------|---|
| Exhibit 31.1 | Certification of Chief Executive Officer pursuant to Rule 13a-14(a). |
| Exhibit 31.2 | Certification of Chief Financial Officer pursuant to Rule 13a-14(a). |
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- Current Report on Form 8-K dated March 21, 2007).
- Exhibit 32.4 Tolling Agreement, dated March 16, 2007 between BCP Ingredients, Inc. and Chinook Global Limited (incorporated by reference to Exhibit 10.1 to the Company's Current Report on Form 8-K dated March 21, 2007).
- Exhibit 32.5 Non-Competition Agreement, dated March 16, 2007 between BCP Ingredients, Inc. and Chinook Global Limited; Chinook Services, LLC; Chinook, LLC; Dean R. Lacy; Ronald Breen, and John N. Kennedy (incorporated by reference to Exhibit 10.2 to the Company's Current Report on Form 8-K dated March 21, 2007).
- Exhibit 32.6 Loan Agreement dated March 16, 2007 by and between Bank of America, N.A. and Balchem Corporation (incorporated by reference to Exhibit 10.3 to the Company's Current Report on Form 8-K dated March 21, 2007).
- Exhibit 32.7 Promissory Note (Term Loan) dated March 16, 2007 from Balchem Corporation to Bank of America, N.A. (incorporated by reference to Exhibit 10.4 to the Company's Current Report on Form 8-K dated March 21, 2007).
- Exhibit 32.8 Promissory Note (Revolving Line of Credit) dated March 16, 2007 from Balchem Corporation to Bank of America, N.A. (incorporated by reference to Exhibit 10.5 to the Company's Current Report on Form 8-K dated March 21, 2007).
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- Exhibit 32.9 Guaranty dated March 16, 2007 from BCP Ingredients, Inc. to Bank of America, N.A. (incorporated by reference to Exhibit 10.6 to the Company's Current Report on Form 8-K dated March 21, 2007).
- Exhibit 32.10 Guaranty dated March 16, 2007 from Balchem Minerals Corporation to Bank of America, N.A. (incorporated by reference to Exhibit 10.7 to the Company's Current Report on Form 8-K dated March 21, 2007).
- Exhibit 32.11 Sale and Purchase Agreement dated March 30, 2007, by and between Balchem B.V. and Akzo Nobel Chemicals S.p.A. (incorporated by reference to Exhibit 2.1 to the Company's Current Report on Form 8-K dated April 4, 2007).