

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549

FORM 10-Q

(MARK ONE)

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE QUARTERLY PERIOD ENDED JUNE 30, 2019

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE TRANSITION PERIOD FROM \_\_\_\_\_ TO \_\_\_\_\_

COMMISSION FILE NUMBER 1-10596

ESCO TECHNOLOGIES INC.

(Exact name of registrant as specified in its charter)

Missouri  
(State or other jurisdiction of  
incorporation or organization)

43-1554045  
(I.R.S. Employer  
Identification No.)

9900A Clayton Road  
St. Louis, Missouri  
(Address of principal executive offices)

63124-1186  
(Zip Code)

(314) 213-7200

(Registrant's telephone number, including area code)

Securities registered pursuant to section 12(b) of the Act:

<u>Title of each class</u>	<u>Trading Symbol(s)</u>	<u>Name of each exchange on which registered</u>
Common Stock, par value \$0.01 per share	ESE	New York Stock Exchange

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

Yes  No

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (Section 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files).

Yes  No

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

Large accelerated filer	<input checked="" type="checkbox"/>	Accelerated filer	<input type="checkbox"/>
Non-accelerated filer	<input type="checkbox"/>	Smaller reporting company	<input type="checkbox"/>
Emerging growth company	<input type="checkbox"/>		

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

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes  No

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

<u>Class</u>	<u>Shares outstanding at July 31, 2019</u>
Common stock, \$.01 par value per share	25,981,313

## PART I. FINANCIAL INFORMATION

## ITEM 1. FINANCIAL STATEMENTS

ESCO TECHNOLOGIES INC. AND SUBSIDIARIES  
CONSOLIDATED STATEMENTS OF OPERATIONS  
(Unaudited)  
(Dollars in thousands, except per share amounts)

	<b>Three Months Ended</b>	
	<b>June 30,</b>	
	<b>2019</b>	<b>2018</b>
Net sales	\$ 199,766	192,223
Costs and expenses:		
Cost of sales	122,172	122,805
Selling, general and administrative expenses	43,400	39,910
Amortization of intangible assets	4,693	4,605
Interest expense, net	1,973	2,243
Other expenses (income), net	2,636	(656)
Total costs and expenses	<u>174,874</u>	<u>168,907</u>
Earnings before income taxes	24,892	23,316
Income tax expense	4,825	4,297
Net earnings	<u>\$ 20,067</u>	<u>19,019</u>
Earnings per share:		
Basic - Net earnings	<u>\$ 0.77</u>	<u>0.73</u>
Diluted - Net earnings	<u>\$ 0.77</u>	<u>0.73</u>

See accompanying notes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF OPERATIONS  
(Unaudited)  
(Dollars in thousands, except per share amounts)

	Nine Months Ended June 30,	
	2019	2018
Net sales	\$ 576,312	540,496
Costs and expenses:		
Cost of sales	363,026	346,911
Selling, general and administrative expenses	126,066	122,813
Amortization of intangible assets	13,965	13,615
Interest expense, net	5,788	6,464
Other (income) expenses, net	(2,037)	992
Total costs and expenses	<u>506,808</u>	<u>490,795</u>
Earnings before income taxes	69,504	49,701
Income tax expense (benefit)	13,323	(13,983)
Net earnings	<u>\$ 56,181</u>	<u>63,684</u>
Earnings per share:		
Basic - Net earnings	<u>\$ 2.17</u>	<u>2.46</u>
Diluted - Net earnings	<u>\$ 2.15</u>	<u>2.45</u>

See accompanying notes to consolidated financial statements.

ESCO TECHNOLOGIES INC. AND SUBSIDIARIES  
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME  
(Unaudited)  
(Dollars in thousands)

	Three Months Ended June 30,		Nine Months Ended June 30,	
	2019	2018	2019	2018
Net earnings	\$ 20,067	19,019	56,181	63,684
Other comprehensive income net of tax:				
Foreign currency translation adjustments	1,839	(6,865)	(2,013)	(2,740)
Net unrealized (loss) gain on derivative instruments	(7)	(62)	94	93
Total other comprehensive income (loss), net of tax	<u>1,832</u>	<u>(6,927)</u>	<u>(1,919)</u>	<u>(2,647)</u>
Comprehensive income	<u>\$ 21,899</u>	<u>12,092</u>	<u>54,262</u>	<u>61,037</u>

See accompanying notes to consolidated financial statements.

ESCO TECHNOLOGIES INC. AND SUBSIDIARIES  
CONSOLIDATED BALANCE SHEETS  
(Unaudited)  
(Dollars in thousands)

	June 30, 2019	September 30, 2018
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$ 38,956	30,477
Accounts receivable, net	168,675	163,740
Contract assets	99,499	53,034
Inventories	126,816	135,416
Other current assets	16,260	13,356
Total current assets	450,206	396,023
Property, plant and equipment, net of accumulated depreciation of \$125,747 and \$115,728, respectively	151,545	134,954
Intangible assets, net of accumulated amortization of \$106,239 and \$92,274, respectively	336,625	345,353
Goodwill	381,683	381,652
Other assets	6,036	7,140
Total assets	<u>\$ 1,326,095</u>	<u>1,265,122</u>
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>		
Current liabilities:		
Short-term borrowings and current maturities of long-term debt	\$ 20,921	20,000
Accounts payable	59,329	63,033
Contract liabilities	53,758	49,035
Accrued salaries	29,914	29,379
Accrued other expenses	35,814	39,083
Total current liabilities	199,736	200,530
Pension obligations	14,610	16,286
Deferred tax liabilities	66,286	64,794
Other liabilities	36,656	24,102
Long-term debt	197,000	200,000
Total liabilities	514,288	505,712
Shareholders' equity:		
Preferred stock, par value \$.01 per share, authorized 10,000,000 shares	—	—
Common stock, par value \$.01 per share, authorized 50,000,000 shares, issued 30,596,940 and 30,534,786 shares, respectively	306	305
Additional paid-in capital	291,204	291,190
Retained earnings	661,003	606,837
Accumulated other comprehensive loss, net of tax	(33,447)	(31,528)
	919,066	866,804
Less treasury stock, at cost: 4,615,627 and 4,623,958 common shares, respectively	(107,259)	(107,394)
Total shareholders' equity	811,807	759,410
Total liabilities and shareholders' equity	<u>\$ 1,326,095</u>	<u>1,265,122</u>

See accompanying notes to consolidated financial statements.

ESCO TECHNOLOGIES INC. AND SUBSIDIARIES  
CONSOLIDATED STATEMENTS OF CASH FLOWS  
(Unaudited)  
(Dollars in thousands)

	Nine Months Ended June 30,	
	2019	2018
Cash flows from operating activities:		
Net earnings	\$ 56,181	63,684
Adjustments to reconcile net earnings to net cash provided by operating activities:		
Depreciation and amortization	28,763	28,350
Stock compensation expense	3,878	3,864
Changes in assets and liabilities	(41,851)	(9,454)
Change in property, plant and equipment due to gain on sale of building	(8,922)	—
Effect of deferred taxes	1,492	(23,086)
Pension contributions	(2,500)	(9,414)
Net cash provided by operating activities	<u>37,041</u>	<u>53,944</u>
Cash flows from investing activities:		
Acquisition of businesses, net of cash acquired	(937)	(11,445)
Additions to capitalized software	(6,207)	(7,118)
Capital expenditures	(26,457)	(15,539)
Proceeds from sale of building and land	17,201	—
Net cash used by investing activities	<u>(16,400)</u>	<u>(34,102)</u>
Cash flows from financing activities:		
Proceeds from long-term debt	32,921	53,000
Principal payments on long-term debt	(35,000)	(66,000)
Dividends paid	(6,223)	(6,205)
Other	(3,234)	(2,886)
Net cash used by financing activities	<u>(11,536)</u>	<u>(22,091)</u>
Effect of exchange rate changes on cash and cash equivalents	(626)	(8)
Net increase (decrease) in cash and cash equivalents	8,479	(2,257)
Cash and cash equivalents, beginning of period	30,477	45,516
Cash and cash equivalents, end of period	<u>\$ 38,956</u>	<u>43,259</u>
Supplemental cash flow information:		
Interest paid	\$ 5,556	6,333
Income taxes paid (including state and foreign)	<u>18,513</u>	<u>4,343</u>

See accompanying notes to consolidated financial statements.

ESCO TECHNOLOGIES INC. AND SUBSIDIARIES  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
(Unaudited)

1. BASIS OF PRESENTATION

The accompanying consolidated financial statements, in the opinion of management, include all adjustments, consisting of normal recurring accruals, necessary for a fair presentation of the results for the interim periods presented. The consolidated financial statements are presented in accordance with the requirements of Form 10-Q and consequently do not include all the disclosures required for annual financial statements by accounting principles generally accepted in the United States of America (GAAP). For further information, refer to the consolidated financial statements and related notes included in the Company's Annual Report on Form 10-K for the fiscal year ended September 30, 2018.

The Company's results for the three and nine-month periods ended June 30, 2019 are not necessarily indicative of the results for the entire 2019 fiscal year. References to the third quarters of 2019 and 2018 represent the fiscal quarters ended June 30, 2019 and 2018, respectively.

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities. Actual results could differ from those estimates.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES UPDATE

Our significant accounting policies are included in Note 1 of our Annual Report on Form 10-K for the year ended September 30, 2018. On October 1, 2018, we adopted ASU No. 2014-09, *Revenue from Contracts with Customers (ASC 606)*. Significant changes to our policies resulting from the adoption are provided below. We adopted ASC 606 using the modified retrospective transition method applied to contracts that were not substantially complete at the end of fiscal year 2018. We recorded a \$4.2 million adjustment to increase retained earnings to reflect the cumulative impact of adopting this standard at the beginning of fiscal year 2019, primarily related to certain long-term contracts our Filtration and Technical Packaging segments have that converted to the cost-to-cost method for revenue recognition. The comparative information has not been restated and is reported under the accounting standards in effect for those periods. A reconciliation of the financial statement line items impacted for the three and nine months ended June 30, 2019 under ASC 606 to the prior accounting standards is provided in Note 14.

**Revenue Recognition**

Revenue is recognized when control of the goods or services promised under the contract is transferred to the customer either at a point in time (e.g., upon delivery) or over time (e.g., as we perform under the contract). We account for a contract when it has approval and commitment from both parties, the rights and payment terms of the parties are identified, the contract has commercial substance and collectability of consideration is probable. Contracts are reviewed to determine whether there is one or multiple performance obligations. A performance obligation is a promise to transfer a distinct good or service to a customer and represents the unit of accounting for revenue recognition. For contracts with multiple performance obligations, the expected consideration, or the transaction price, is allocated to each performance obligation identified in the contract based on the relative standalone selling price of each performance obligation. Revenue is then recognized for the transaction price allocated to the performance obligation when control of the promised goods or services underlying the performance obligation is transferred.

Payment terms with customers vary by the type and location of the customer and the products or services offered. The Company does not adjust the promised amount of consideration for the effects of significant financing components based on the expectation that the period between when the Company transfers a promised good or service to a customer and when the customer pays for that good or service will be one year or less. Arrangements with customers that include payment terms extending beyond one year are not significant.

**Filtration:** Within the Filtration segment, approximately 48% of revenues (approximately 18% of consolidated revenues) are recognized at a point in time when products are shipped (when control of the goods transfers) to unaffiliated customers. The related contracts are with commercial and military customers and have a single performance obligation as there is only one good promised or the promise to transfer the goods or services is not distinct or separately identifiable from other promises in the contract. The transaction price for these contracts reflects our estimate of returns, rebates and discounts, which are based on historical, current and forecasted information to determine the expected amount to which the Company will be entitled in exchange for transferring the promised goods or services to the customer. The realization of variable consideration occurs within a short period of time from product delivery; therefore, the time value of money effect is not significant. Amounts billed to customers for shipping and handling are included in the transaction price as the related activities are performed prior to customer obtaining control of the products. They generally are not treated as separate performance obligations as these costs fulfill a promise to transfer the product to the customer and are expensed in selling, general, and other costs in the period they are incurred. Taxes collected from customers and remitted to government authorities are recorded on a net basis. We primarily provide standard warranty programs for products in our commercial businesses for periods that typically range from one to two years. These assurance-type programs typically cannot be purchased separately and do not meet the criteria to be considered a performance obligation.

Approximately 52% of the segment's revenues (approximately 19% of consolidated revenues) are accounted for over time as the product does not have an alternative use and the Company has an enforceable right to payment for costs incurred plus a reasonable margin or the inventory is owned by the customer. The related contracts are primarily cost-plus or fixed price contracts related to the design, development and manufacture of complex fluid control products, quiet valves, manifolds, shock and vibration dampening, thermal insulation and systems primarily for the commercial aerospace and military (U.S. Government) markets. The contracts may contain multiple products, which are capable of being distinct as the customer could benefit from each product on its own or together with other readily available resources. Each product is separately identifiable from the other products in the contract. Therefore, each product is distinct in context of the contract and will be accounted for as a separate performance obligation. Our contracts are frequently modified for changes in contract specifications and requirements. Most of our contract modifications are for products that are not distinct from the existing contract and are accounted for as part of that existing contract.

Contracts with the U.S. Government generally contain clauses that provide lien rights to work-in-process along with clauses that allow the customer to unilaterally terminate the contract for convenience, pay us for costs incurred plus a reasonable profit and take control of any work-in-process. Due to the continuous transfer of control to the U.S. Government, we recognize revenue over the time that we perform under the contract.

Selecting the method to measure progress towards completion for the commercial and military contracts requires judgment and is based on the nature of the products or service to be provided. We generally use the cost-to-cost method to measure progress for our Filtration segment contracts the rate at which costs are incurred to fulfill a contract best depicts the transfer of control to the customer. Under this measure, the extent of progress towards completion is measured based on the ratio of costs incurred to date to the estimated costs at completion of the performance obligation, and revenue is recorded proportionally as costs are incurred based on an estimated profit margin.

The transaction price for our contracts represents our best estimate of the consideration we will receive and includes assumptions regarding variable consideration as applicable. Certain of our long-term contracts contain incentive fees that can increase the transaction price. These variable amounts generally are awarded upon achievement of certain performance metrics, program milestones or cost targets and can be based upon customer discretion. We include estimated amounts in the transaction price to the extent it is probable that a significant reversal of cumulative revenue recognized will not occur when the uncertainty associated with the variable consideration is resolved. Our estimates of variable consideration and determination of whether to include estimated amounts in the transaction price are based largely on an assessment of our anticipated performance and all other information that is reasonably available to us.



Total contract cost is estimated utilizing current contract specifications and expected engineering requirements. Contract costs typically are incurred over a period of several months to one or more years, and the estimation of these costs requires judgment. Our cost estimation process is based on the professional knowledge and experience of engineers and program managers along with finance professionals. We review and update our projections of costs quarterly or more frequently when circumstances significantly change.

Under the typical payment terms of our long term fixed price contracts, the customer pays us either performance-based or progress payments. Performance-based payments represent interim payments based on quantifiable measures of performance or on the achievement of specified events or milestones. Progress payments are interim payments of costs incurred as the work progresses. Because of the timing difference of revenue recognition and customer billing, these contracts will often result in revenue recognized in excess of billings and billings in excess of costs incurred, which we present as contract assets and contract liabilities, respectively, in the Consolidated Balance Sheets. Amounts billed and due from our customers are classified in Accounts receivable, net. For short term fixed price and cost-type contracts, we are generally paid within a short period of time.

For contracts where revenue is recognized over time, we generally recognize changes in estimated contract revenues, costs and profits using the cumulative catch-up method of accounting. This method recognizes the cumulative effect of changes on current and prior periods with the impact of the change from inception-to-date recorded in the current period. Anticipated losses on contracts are recognized in full in the period in which the losses become probable and estimable.

**Test:** Within the Test segment, approximately 25% of revenues (approximately 6% of consolidated revenues) are recognized at a point in time when products such as, antennas and probes are shipped (when control of the goods transfers) to unaffiliated customers. The related contracts are with commercial customers. The contracts may contain multiple products which are capable of being distinct as the customer could benefit from each product on its own or together with other readily available resources. Each product is separately identifiable from the other products in the contract. Therefore, each product is distinct in context of the contract and will be accounted for as a separate performance obligation. The transaction price for these contracts reflects our estimate of variable consideration in the form of returns, rebates and discounts, which are based on historical, current and forecasted information to determine the expected amount to which the Company will be entitled in exchange for transferring the promised goods or services to the customer. The realization of variable consideration occurs within a short period of time from product delivery; therefore, the time value of money effect is not significant. Amounts billed to customers for shipping and handling are included in the transaction price as the related activities are performed prior to customer obtaining control of the products. They generally are not treated as separate performance obligations as these costs fulfill a promise to transfer the product to the customer and are expensed in selling, general, and other costs in the period they are incurred. Taxes collected from customers and remitted to government authorities are recorded on a net basis. We primarily provide standard warranty programs for products in our commercial businesses for periods that typically range from one to two years. These assurance-type programs typically cannot be purchased separately and do not meet the criteria to be considered a performance obligation.

Approximately 75% of the segment's revenues (approximately 17% of consolidated revenues) are recorded over time as the product does not have an alternative use and the Company has an enforceable right to payment for costs incurred plus a reasonable margin. Products accounted for under this guidance include the construction and installation of test chambers to a buyer's specifications that provide its customers with the ability to measure and contain magnetic, electromagnetic and acoustic energy. The goods and services related to each installed test chamber are not distinct due to the significant amount of integration provided and each installed chamber is accounted for as a single performance obligation. Selecting the method to measure progress towards completion for these contracts requires judgment and is based on the nature of the products and service to be provided. We use milestones to measure progress for our Test segment contracts because it best depicts the transfer of control to the customer that occurs as we incur costs on our contracts. For arrangements that are accounted for under this guidance, the Company estimates profit as the difference between total revenue and total estimated cost of a contract and recognizes these revenues and costs based primarily on contract milestones. The transaction price for our contracts represents our best estimate of the consideration we will receive and includes assumptions regarding variable consideration as applicable.

Total contract cost is estimated utilizing current contract specifications and expected engineering requirements. Contract costs typically are incurred over a period of several months to a year, and the estimation of these costs requires judgment. Our cost estimation process is based on the professional knowledge and experience of engineers and program managers along with finance professionals. We review and update our projections of costs quarterly or more frequently when circumstances significantly change.

Under the typical payment terms of our fixed price contracts, the customer pays us either performance-based or progress payments. Performance-based payments represent interim payments based on quantifiable measures of performance or on the achievement of specified events or milestones. Progress payments are interim payments of costs incurred as the work progresses. Because of the timing difference of revenue recognition and customer billing, these contracts result in revenue recognized in excess of billings and billings in excess of costs incurred, which we present as contract assets and contract liabilities, respectively, in the Consolidated Balance Sheets. Amounts billed and due from our customers are classified in Accounts receivable, net.

For contracts where revenue is recognized over time, we generally recognize changes in estimated contract revenues, costs and profits using the cumulative catch-up method of accounting. This method recognizes the cumulative effect of changes on current and prior periods with the impact of the change from inception-to-date recorded in the current period. Anticipated losses on contracts are recognized in full in the period in which the losses become probable and estimable.

**USG:** Within the USG segment, approximately 80% of revenues (approximately 24% of consolidated revenues) are recognized at a point in time when products are shipped (when control of the goods transfers) to unaffiliated customers. The related contracts are with commercial customers. The contracts may contain multiple products which are capable of being distinct as the customer could benefit from each product on its own or together with other readily available resources. Each product is separately identifiable from the other products in the contract. Therefore, each product is distinct in context of the contract and will be accounted for as a separate performance obligation. The transaction price for these contracts reflects our estimate of variable consideration in the form of returns, rebates and discounts, which are based on historical, current and forecasted information to determine the expected amount to which the Company will be entitled in exchange for transferring the promised goods or services to the customer. The realization of variable consideration occurs within a short period of time from product delivery; therefore, the time value of money effect is not significant. Amounts billed to customers for shipping and handling are included in the transaction price as the related activities are performed prior to customer obtaining control of the products. They generally are not treated as separate performance obligations as these costs fulfill a promise to transfer the product to the customer and are expensed in selling, general, and other costs in the period they are incurred. Taxes collected from customers and remitted to government authorities are recorded on a net basis. We primarily provide standard warranty programs for products in our commercial businesses for periods that typically range from one to two years. These assurance-type programs typically cannot be purchased separately and do not meet the criteria to be considered a performance obligation.

Approximately 20% of the segment's revenues (approximately 6% of consolidated revenues) are recognized over time as services are performed. The services accounted for under this method include an obligation to provide testing services using hardware and embedded software, software maintenance, training, lab testing, and consulting services. The related contracts contain a bundle of goods and services that are integrated in the context of the contract. Therefore, the goods and services are not distinct and the Company has a single performance obligation. Selecting the method to measure progress towards completion for these contracts requires judgment and is based on the nature of the products and service to be provided. We will recognize revenue as a series of distinct services based on each day of providing services (straight-line over the contract term) for our USG segment contracts. The transaction price for our contracts represents our best estimate of the consideration we will receive and includes assumptions regarding variable consideration as applicable. Under the typical payment terms of our service contracts, the customer pays us in advance of when services are performed. Because of the timing difference of revenue recognition and customer payment, which is typically received upon commencement of the contract, these contracts result in deferred revenue, which we present as contract liabilities, in the Consolidated Balance Sheets.

Included in this category, approximately 8% of the segment's revenues (approximately 2% of consolidated revenues) are recognized based on the terms of the software contract. For contracts that transfer a software license to the customer, revenue will be recognized at a point in time. These type of software contracts represent a right to use the software, or a functional license, in which revenue should be recognized upon transfer of the license. For contracts in software as a service (SaaS) arrangements, revenue will be recognized over time. The customer receives and consumes the benefits of the SaaS arrangement through access to the system which is for a stated period. We will recognize revenue based on each day of providing access (straight-line over the contract term). The transaction price for our contracts represent our best estimate of the consideration we will receive and includes assumptions regarding variable consideration as applicable. Under the typical payment terms of our software contracts, the customer pays us in advance of when services are performed. Because of the timing difference of revenue recognition and customer payment, these contracts result in deferred revenue, which we present as contract liabilities, in the Consolidated Balance Sheets.

**Technical Packaging:** Within the Technical Packaging segment, 100% of the revenues (approximately 10% of consolidated revenues) are recognized over time as the product does not have an alternative use and the Company has an enforceable right to payment. Selecting the method to measure progress towards completion for the contracts requires judgment and is based on the nature of the products to be provided. We use the cost-to-cost method to measure progress for our Technical Packaging segment contracts because it best depicts the transfer of control to the customer that occurs as we incur costs on our contracts. Under this measure, the extent of progress towards completion is measured based on the ratio of costs incurred to date to the estimated costs at completion of the performance obligation, and revenue is recorded proportionally as costs are incurred. The transaction price for our contracts reflects our estimate of variable consideration in the form of returns, rebates and discounts, which are based on historical, current and forecasted information to determine the expected amount to which the Company will be entitled in exchange for transferring the promised goods or services to the customer. The realization of variable consideration occurs within a short period of time from product delivery; therefore, the time value of money effect is not significant.

Total contract cost is estimated utilizing current contract specifications and expected engineering requirements. Contract costs typically are incurred over a period of weeks, minimizing the amount of judgment in developing the cost estimate. Our cost estimation process is based on the professional knowledge and experience of engineers and program managers along with finance professionals. We review and update our projections of costs quarterly or more frequently when circumstances significantly change.

Under the typical payment terms of our contracts, the customer is billed upon shipment of product. Amounts billed and due from our customers are classified in Accounts receivable, net. Because of the timing difference of revenue recognition and customer billing, these contracts result in revenue recognized in excess of billings, which we present as contract assets in the Consolidated Balance Sheets.

For contracts where revenue is recognized over time, we generally recognize changes in estimated contract revenues, costs and profits using the cumulative catch-up method of accounting. This method recognizes the cumulative effect of changes on current and prior periods with the impact of the change from inception-to-date recorded in the current period. Anticipated losses on contracts are recognized in full in the period in which the losses become probable and estimable.

#### **Contract Assets and Liabilities**

Contract assets arise from contracts when revenue is recognized over time and the amount of revenue recognized, including our estimate of variable consideration that has been included in the transaction price, exceeds the amount billed to the customer. These amounts are included in contract assets until the right to payment is no longer conditional on events other than the passage of time. These contract assets are reclassified to receivables when the right to consideration becomes unconditional. Contract liabilities include deposits, deferred revenue, upfront payments and billings in excess of revenue recognized. Liabilities for customer rebates and discounts are included in other current liabilities in the accompanying balance sheet.

### 3. EARNINGS PER SHARE (EPS)

Basic EPS is calculated using the weighted average number of common shares outstanding during the period. Diluted EPS is calculated using the weighted average number of common shares outstanding during the period plus shares issuable upon the assumed exercise of dilutive common share options and vesting of performance-accelerated restricted shares (restricted shares) by using the treasury stock method. The number of shares used in the calculation of earnings per share for each period presented is as follows (in thousands):

	Three Months Ended June 30,		Nine Months Ended June 30,	
	2019	2018	2019	2018
Weighted Average Shares Outstanding - Basic	25,971	25,900	25,935	25,862
Dilutive Options and Restricted Shares	138	150	155	180
Adjusted Shares - Diluted	<u>26,109</u>	<u>26,050</u>	<u>26,090</u>	<u>26,042</u>

### 4. SHARE-BASED COMPENSATION

The Company provides compensation benefits to certain key employees under several share-based plans providing for performance-accelerated restricted shares (restricted shares), and to non-employee directors under a non-employee directors compensation plan.

#### *Performance-Accelerated Restricted Share Awards*

Compensation expense related to the restricted share awards was \$1.0 million and \$3.1 million for the three and nine-month periods ended June 30, 2019, respectively, and \$0.9 million and \$3.1 million for the corresponding periods of 2018. There were 280,504 non-vested shares outstanding as of June 30, 2019.

#### *Non-Employee Directors Plan*

Compensation expense related to the non-employee director grants was \$0.3 million and \$0.8 million for the three and nine-month periods ended June 30, 2019, respectively, and \$0.3 million and \$0.8 million for the corresponding periods of 2018.

The total share-based compensation cost that has been recognized in the results of operations and included within selling, general and administrative expenses (SG&A) was \$1.3 million and \$3.9 million for the three and nine-month periods ended June 30, 2019, respectively, and \$1.2 million and \$3.9 million for the three and nine-month periods ended June 30, 2018. The total income tax benefit recognized in results of operations for share-based compensation arrangements was \$0.2 million and \$0.8 million for the three and nine-month periods ended June 30, 2019, respectively, and \$0.2 million and \$0.9 million for the three and nine-month periods ended June 30, 2018, respectively. As of June 30, 2019, there was \$10.7 million of total unrecognized compensation cost related to share-based compensation arrangements. That cost is expected to be recognized over a remaining weighted-average period of 2.1 years.

## 5. INVENTORIES

Inventories consist of the following:

<u>(In thousands)</u>	<u>June 30, 2019</u>	<u>September 30, 2018</u>
Finished goods	\$ 18,583	26,678
Work in process	42,678	47,765
Raw materials	65,555	60,973
Total inventories	<u>\$ 126,816</u>	<u>135,416</u>

## 6. GOODWILL AND OTHER INTANGIBLE ASSETS

Included on the Company's Consolidated Balance Sheets at June 30, 2019 and September 30, 2018 are the following intangible assets gross carrying amounts and accumulated amortization:

<u>(Dollars in thousands)</u>	<u>June 30, 2019</u>	<u>September 30, 2018</u>
Goodwill	<u>\$ 381,683</u>	<u>381,652</u>
<b>Intangible assets with determinable lives:</b>		
<b>Patents</b>		
Gross carrying amount	\$ 1,880	1,833
Less: accumulated amortization	873	791
Net	<u>\$ 1,007</u>	<u>1,042</u>
<b>Capitalized software</b>		
Gross carrying amount	\$ 77,502	71,294
Less: accumulated amortization	47,206	41,624
Net	<u>\$ 30,296</u>	<u>29,670</u>
<b>Customer relationships</b>		
Gross carrying amount	\$ 185,135	185,333
Less: accumulated amortization	55,641	47,802
Net	<u>\$ 129,494</u>	<u>137,531</u>
<b>Other</b>		
Gross carrying amount	\$ 5,382	5,468
Less: accumulated amortization	2,518	2,056
Net	<u>\$ 2,864</u>	<u>3,412</u>
<b>Intangible assets with indefinite lives:</b>		
Trade names	<u>\$ 172,964</u>	<u>173,698</u>

The changes in the carrying amount of goodwill attributable to each business segment for the nine months ended June 30, 2019 is as follows:

<u>(Dollars in millions)</u>	<u>USG</u>	<u>Test</u>	<u>Filtration</u>	<u>Packaging</u>	<u>Total</u>
Balance as of September 30, 2018	254.1	34.1	73.7	19.8	381.7
Foreign currency translation	0.2	—	—	(0.2)	—
Balance as of June 30, 2019	<u>\$ 254.3</u>	<u>34.1</u>	<u>73.7</u>	<u>19.6</u>	<u>381.7</u>

## 7. BUSINESS SEGMENT INFORMATION

The Company is organized based on the products and services that it offers, and classifies its business operations in four reportable segments for financial reporting purposes: Filtration/Fluid Flow (Filtration), RF Shielding and Test (Test), Utility Solutions Group (USG) and Technical Packaging. The Filtration segment's operations consist of PTI Technologies Inc. (PTI), VACCO Industries (VACCO), Crissair, Inc. (Crissair), Westland Technologies Inc. (Westland), and Mayday Manufacturing Co. and its affiliate Hi-Tech Metals, Inc. (collectively referred to as Mayday). The companies within this segment primarily design and manufacture specialty filtration products, including hydraulic filter elements used in commercial aerospace applications, unique filter mechanisms used in micro-propulsion devices for satellites and custom designed filters for manned and unmanned aircraft; manufacture elastomeric-based signature reduction solutions for the U.S. Navy; and manufacture landing gear components for the aerospace and defense industry. The Test segment's operations consist primarily of ETS-Lindgren Inc.

(ETS-Lindgren). ETS-Lindgren is an industry leader in providing its customers with the ability to identify, measure and contain magnetic, electromagnetic and acoustic energy. The USG segment's operations consist primarily of Doble Engineering Company (Doble), Morgan Schaffer Inc. (Morgan Schaffer), and NRG Systems, Inc. (NRG). Doble provides high-end, intelligent diagnostic test solutions for the electric power delivery industry and is a leading supplier of partial discharge testing instruments used to assess the integrity of high voltage power delivery equipment. Morgan Schaffer provides an integrated offering of dissolved gas analysis, oil testing, and data management solutions for the electric power industry. NRG designs and manufactures decision support tools for the renewable energy industry, primarily wind. The Technical Packaging segment's operations consist of Thermoform Engineered Quality LLC (TEQ) and Plastique Limited and Plastique Sp. z o.o. (together, Plastique). The companies within this segment provide innovative solutions to the medical and commercial markets for thermoformed packages and specialty products using a wide variety of thin gauge plastics and pulp.

Management evaluates and measures the performance of its reportable segments based on "Net Sales" and "EBIT", which are detailed in the table below. EBIT is defined as earnings before interest and taxes.

(In thousands)	Three Months Ended June 30,		Nine Months Ended June 30,	
	2019	2018	2019	2018
<b>NET SALES</b>				
Filtration	\$ 83,067	69,721	228,769	195,531
Test	42,298	45,034	126,459	123,368
USG	52,894	55,489	157,639	157,942
Technical Packaging	21,507	21,979	63,445	63,655
Consolidated totals	<u>\$ 199,766</u>	<u>192,223</u>	<u>576,312</u>	<u>540,496</u>
<b>EBIT</b>				
Filtration	\$ 19,039	14,292	47,092	35,056
Test	5,927	5,902	14,791	13,797
USG	10,148	11,528	40,461	27,805
Technical Packaging	1,625	2,505	3,333	5,355
Corporate (loss)	(9,874)	(8,668)	(30,385)	(25,848)
Consolidated EBIT	26,865	25,559	75,292	56,165
Less: Interest expense	(1,973)	(2,243)	(5,788)	(6,464)
Earnings before income taxes	<u>\$ 24,892</u>	<u>23,316</u>	<u>69,504</u>	<u>49,701</u>

### *Non-GAAP Financial Measures*

The financial measure "EBIT" is presented in the above table and elsewhere in this Report. EBIT on a consolidated basis is a non-GAAP financial measure. Management believes that EBIT is useful in assessing the operational profitability of the Company's business segments because it excludes interest and taxes, which are generally accounted for across the entire Company on a consolidated basis. EBIT is also one of the measures used by

management in determining resource allocations within the Company as well as incentive compensation. A reconciliation of EBIT to net earnings is set forth in Item 2, Management’s Discussion and Analysis of Financial Condition and Results of Operations – EBIT.

The Company believes that the presentation of EBIT provides important supplemental information to investors to facilitate comparisons with other companies, many of which use similar non-GAAP financial measures to supplement their GAAP results. However, the Company’s non-GAAP financial measures may not be comparable to other companies’ non-GAAP financial performance measures. Furthermore, the use of non-GAAP financial measures is not intended to replace any measures of performance determined in accordance with GAAP.

## 8. DEBT

The Company’s debt is summarized as follows:

<u>(In thousands)</u>	<u>June 30,</u> <u>2019</u>	<u>September 30,</u> <u>2018</u>
Total borrowings	\$ 217,921	220,000
Short-term borrowings and current portion of long-term debt	(20,921)	(20,000)
Total long-term debt, less current portion	<u>\$ 197,000</u>	<u>200,000</u>

The Company’s existing credit facility (“the Credit Facility”) matures December 21, 2020. The Credit Facility includes a \$450 million revolving line of credit as well as provisions allowing for the increase of the credit facility commitment amount by an additional \$250 million, if necessary, with the consent of the lenders. The bank syndication supporting the facility is comprised of a diverse group of nine banks led by JPMorgan Chase Bank, N.A., as Administrative Agent.

At June 30, 2019, the Company had approximately \$225 million available to borrow under the Credit Facility, and a \$250 million increase option, in addition to \$39.0 million cash on hand. At June 30, 2019, the Company had \$217.0 million of outstanding borrowings under the Credit Facility, and \$0.9 million of short-term borrowing in addition to outstanding letters of credit of \$7.2 million. The Company classified \$20.9 million as the current portion of long-term debt as of June 30, 2019, as the Company intends to repay this amount within the next twelve month period; however, the Company has no contractual obligation to repay such amount during the next twelve month period.

The Credit Facility requires, as determined by certain financial ratios, a facility fee ranging from 12.5 to 27.5 basis points per year on the unused portion. The terms of the facility provide that interest on borrowings may be calculated at a spread over the London Interbank Offered Rate (LIBOR) or based on the prime rate, at the Company’s election. The facility is secured by the unlimited guaranty of the Company’s material domestic subsidiaries and a 65% pledge of the material foreign subsidiaries’ share equity. The financial covenants of the Credit Facility include a leverage ratio and an interest coverage ratio. The weighted average interest rates were 3.21% and 3.22% for the three and nine-month periods ending June 30, 2019, respectively, and 3.17% and 2.97% for the corresponding periods of 2018. At June 30, 2019, the Company was in compliance with all debt covenants.

## 9. INCOME TAX EXPENSE

The third quarter 2019 effective income tax rate was 19.4% compared to 18.4% in the third quarter of 2018. The income tax expense for the first nine months of 2019 was \$13.3 million compared to income tax benefit of \$14.0 million for the first nine months of 2018. The effective income tax rate for the first nine months of 2019 was 19.2% compared to (28.1)% for the first nine months of 2018.

The income tax expense in the third quarter and first nine months of 2019 was favorably impacted by tax planning strategies to increase foreign tax credits claimed retrospectively. The Company reduced the valuation allowance for excess foreign tax credits by \$2.4 million (\$2.3 million in the second quarter of 2019 and \$0.1 million in third quarter of 2019) and recorded an amended return benefit of \$0.3 million (\$0.2 million in the second quarter of 2019 and \$0.1 million in the third quarter of 2019) which favorably impacted the third quarter and year-to-date effective

tax rate by 1.0% and 4.1%, respectively. Income tax expense in the third quarter of 2019 and first nine months of 2019 was also favorably impacted by additional tax benefits on share-based compensation that vested during the quarter decreasing the effective tax rate by 1.8% and 0.7%, respectively. A non-automatic accounting method change filed with the 2018 tax return was approved by the Internal Revenue Service during the third quarter of 2019 and favorably impacted the third quarter and year-to-date effective tax rate by 1.0% and 0.4%, respectively.

H.R. 1, *Tax Cuts and Jobs Act* (“TCJA”), was signed into law on December 22, 2017. The total impact of the TCJA in the third quarter and first nine months of 2018 was a net expense of \$0.1 million and a net benefit of \$24.3 million, respectively. The impacts were as follows: First, the Company’s 2018 federal statutory rate dropped from 35.0% to 24.5% which required an adjustment to the value of its deferred tax assets and liabilities. This adjustment (\$30.3 million provisional amount recorded in the first quarter of 2018 and \$0.4 million provisional amount in the third quarter of 2018) favorably impacted the third quarter and year-to-date effective tax rate by 1.5% and 61.7%, respectively. Second, the TCJA subjected the Company’s cumulative foreign earnings to deferral income tax (\$4.1 million provisional amount of which \$2.9 million was recorded in the first quarter of 2018, \$0.7 million was recorded in the third quarter of 2018 and \$0.5 million in the third quarter of 2019) which unfavorably impacted the third quarter and year-to-date effective tax rate by 2.1% and 8.2%, respectively.

In the first quarter of 2018, the Company recorded a \$2.3 million provisional estimate of the income tax effects of the future repatriation of the cumulative earnings of its foreign subsidiaries which unfavorably impacted the year-to-date effective tax rate by 4.7%. An additional \$7.5 million pension contribution for the 2017 plan year was approved during the second quarter of 2018 increasing the value of the deferred tax liability by \$1.0 million. This favorable adjustment, net of the \$0.3 million unfavorable impact to the 2017 Domestic Production Deduction, favorably impacted the year-to-date effective tax rate by 1.6%. An accounting method change was filed with the 2017 tax return which resulted in an additional deferred tax liability to be adjusted as a result of the TCJA. A favorable adjustment, net of the \$0.3 million unfavorable impact to the 2018 Domestic Production deduction, favorably impacted the third quarter and year-to-date effective tax rate by 2.9% and 1.4%, respectively. The income tax expense in the third quarter and first nine months of 2018 was favorably impacted by return to provision true-ups decreasing the third quarter and year-to-date effective tax rate by 1.4% and 0.7%, respectively. Income tax expense in the third quarter and first nine months of 2018 was also favorably impacted by additional tax benefits on share-based compensation that vested during the quarter decreasing the effective tax rate by 1.9% and 0.9%, respectively.

Provisions under the TCJA that became effective for the Company in the current fiscal year include a further reduction in the U.S. statutory rate to 21%, a new minimum tax on global intangible low-taxed income (“GILTI”), the benefit of the deduction for foreign-derived intangible income (“FDII”), and changes to IRC Section 162(m) related to the deductibility of executive compensation.



## 10. SHAREHOLDERS' EQUITY

The change in shareholders' equity for the first nine months of 2019 and 2018 is shown below (in thousands):

	<b>Three Months Ended June 30,</b>		<b>Nine Months Ended June 30,</b>	
	<b>2018</b>	<b>2019</b>	<b>2018</b>	<b>2019</b>
<b>Common stock</b>				
Beginning balance	305	305	305	305
Stock plans	—	1	—	1
Ending balance	<u>305</u>	<u>306</u>	<u>305</u>	<u>306</u>
<b>Additional paid-in-capital</b>				
Beginning balance	292,404	293,612	289,785	291,190
Stock plans	(2,298)	(2,408)	321	14
Ending balance	<u>290,106</u>	<u>291,204</u>	<u>290,106</u>	<u>291,204</u>
<b>Retained earnings</b>				
Beginning balance	557,249	643,018	516,718	606,836
Net earnings common stockholders	19,019	20,067	63,684	56,181
Dividends paid	(2,076)	(2,082)	(6,210)	(6,227)
Adoption of accounting standards updates	—	—	—	4,213
Ending balance	<u>574,192</u>	<u>661,003</u>	<u>574,192</u>	<u>661,003</u>
<b>Accumulated other comprehensive income (loss)</b>				
Beginning balance	(23,028)	(35,280)	(27,308)	(31,528)
Foreign currency translation	(6,865)	1,840	(2,801)	(2,013)
Pension	—	—	61	—
Forward exchange contracts	(62)	(7)	93	94
Ending balance	<u>(29,955)</u>	<u>(33,447)</u>	<u>(29,955)</u>	<u>(33,447)</u>
<b>Treasury stock</b>				
Beginning balance	(107,394)	(107,259)	(107,582)	(107,394)
Issued under stock plans	—	—	188	135
Ending balance	<u>(107,394)</u>	<u>(107,259)</u>	<u>(107,394)</u>	<u>(107,259)</u>
<b>Total equity</b>	<u><u>727,254</u></u>	<u><u>811,807</u></u>	<u><u>727,254</u></u>	<u><u>811,807</u></u>

## 11. RETIREMENT PLANS

A summary of net periodic benefit expense for the Company's defined benefit plans for the three and nine-month periods ended June 30, 2019 and 2018 is shown in the following table. Net periodic benefit cost for each period presented is comprised of the following:

<b>(In thousands)</b>	<b>Three Months Ended June 30,</b>		<b>Nine Months Ended June 30,</b>	
	<b>2019</b>	<b>2018</b>	<b>2019</b>	<b>2018</b>
<b>Defined benefit plans</b>				
Interest cost	\$ 875	821	2,626	2,461
Expected return on assets	(1,086)	(975)	(3,259)	(2,924)
<b>Amortization of:</b>				
Prior service cost	—	—	—	—
Actuarial loss	487	548	1,461	1,644
<b>Net periodic benefit cost</b>	<u><u>\$ 276</u></u>	<u><u>394</u></u>	<u><u>828</u></u>	<u><u>1,181</u></u>

## 12. DERIVATIVE FINANCIAL INSTRUMENTS

Market risks relating to the Company's operations result primarily from changes in interest rates and changes in foreign currency exchange rates. The Company is exposed to market risk related to changes in interest rates and selectively uses derivative financial instruments, including forward contracts and swaps, to manage these risks. In 2018, the Company entered into three interest rate swaps with a notional amount of \$150 million to hedge some of its exposure to variability in future LIBOR-based interest payments on variable rate debt. In addition, the Company's Canadian subsidiary Morgan Schaffer enters into foreign exchange contracts to manage foreign currency risk as a portion of their revenue is denominated in U.S. dollars. The Company expects hedging gains or losses to be essentially offset by losses or gains on the related underlying exposures. All derivative instruments are reported in either accrued expenses or other receivables on the balance sheet at fair value. For derivative instruments designated as cash flow hedges, the gain or loss on the derivative is deferred in accumulated other comprehensive income until recognized in earnings with the underlying hedged item. The interest rate swaps entered into during 2018 were not designated as cash flow hedges and, therefore, the gain or loss on the derivative is reflected in earnings each period.

The following is a summary of the notional transaction amounts and fair values for the Company's outstanding derivative financial instruments by risk category and instrument type as of June 30, 2019:

(In thousands)	Notional amount	Fair Value (US\$)	Float Rate	Fix Rate
Forward contracts	6,000	USD (4)		
Interest rate swap	150,000	USD 6	2.38 %	2.09 %
Interest rate swap *	150,000	USD (1,041)	N/A	2.24 %

\*This swap represents a forward contract and will be effective in November 2019.

## 13. FAIR VALUE MEASUREMENTS

The accounting guidance establishes a three-level hierarchy for disclosure of fair value measurements, based upon the transparency of inputs to the valuation of an asset or liability as of the measurement date, as follows:

- Level 1 – inputs to the valuation methodology are quoted prices (unadjusted) for identical assets or liabilities in active markets.
- Level 2 – inputs to the valuation methodology include quoted prices for similar assets and liabilities in active markets, and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial instrument.
- Level 3 – inputs to the valuation methodology are unobservable and significant to the fair value measurement.

### *Financial Assets and Liabilities*

The Company has estimated the fair value of its financial instruments as of June 30, 2019 and September 30, 2018 using available market information or other appropriate valuation methodologies. The carrying amounts of cash and cash equivalents, receivables, inventories, payables, debt and other current assets and liabilities approximate fair value because of the short maturity of those instruments.

*Fair Value of Financial Instruments*

The Company's forward contracts are classified within Level 2 of the valuation hierarchy in accordance with FASB Accounting Standards Codification (ASC) 825, as presented below as of June 30, 2019:

(In thousands)	Level 1	Level 2	Level 3	Total
<b>Assets (Liabilities):</b>				
Forward contracts	\$ —	(1,039)	\$ —	(1,039)

Valuation was based on third party evidence of similarly priced derivative instruments.

*Nonfinancial Assets and Liabilities*

The Company's nonfinancial assets such as property, plant and equipment, and other intangible assets are not measured at fair value on a recurring basis; however they are subject to fair value adjustments in certain circumstances, such as when there is evidence that an impairment may exist. No impairments were recorded during the three and nine-month periods ended June 30, 2019.

14. REVENUES

*Disaggregation of Revenues*

Our revenues by customer type, geographic location, and revenue recognition method for the three and nine-month periods ended June 30, 2019 are presented in the table below as the Company deems it best depicts how the nature, amount, timing and uncertainty of net sales and cash flows are affected by economic factors. The table below also includes a reconciliation of the disaggregated revenue within our reportable segments.

*Three Months Ended June 30, 2019*  
(In thousands)

	Filtration	Test	USG	Technical Packaging	Total
<b>Customer type:</b>					
Commercial	\$ 47,482	\$ 37,980	\$ 52,065	\$ 21,507	\$ 159,034
Government	35,585	4,318	829	—	40,732
Total revenues	<u>\$ 83,067</u>	<u>\$ 42,298</u>	<u>\$ 52,894</u>	<u>\$ 21,507</u>	<u>\$ 199,766</u>
<b>Geographic location:</b>					
United States	\$ 69,872	\$ 26,923	\$ 38,414	\$ 11,559	\$ 146,268
International	13,195	15,375	14,480	9,948	53,498
Total revenues	<u>\$ 83,067</u>	<u>\$ 42,298</u>	<u>\$ 52,894</u>	<u>\$ 21,507</u>	<u>\$ 199,766</u>
<b>Revenue recognition method:</b>					
Point in time	\$ 41,633	\$ 6,485	\$ 40,968	\$ —	\$ 89,092
Over time	41,434	35,813	11,926	21,507	110,674
Total revenues	<u>\$ 83,067</u>	<u>\$ 42,298</u>	<u>\$ 52,894</u>	<u>\$ 21,507</u>	<u>\$ 199,766</u>

*Nine Months Ended June 30, 2019*  
(In thousands)

	Filtration	Test	USG	Technical Packaging	Total
<b>Customer type:</b>					
Commercial	\$ 131,112	\$ 111,577	\$ 154,240	\$ 63,251	\$ 460,180
Government	97,657	14,882	3,399	194	116,132
Total revenues	<u>\$ 228,769</u>	<u>\$ 126,459</u>	<u>\$ 157,639</u>	<u>\$ 63,445</u>	<u>\$ 576,312</u>
<b>Geographic location:</b>					
United States	\$ 190,701	\$ 82,072	\$ 112,289	\$ 32,865	\$ 417,927
International	38,068	44,387	45,350	30,580	158,385

Total revenues	\$ 228,769	\$ 126,459	\$ 157,639	\$ 63,445	\$ 576,312
<b>Revenue recognition method:</b>					
Point in time	\$ 115,852	\$ 29,092	\$ 122,075	\$ -	\$ 267,021
Over time	112,917	97,367	35,564	63,445	309,291
Total revenues	\$ 228,769	\$ 126,459	\$ 157,639	\$ 63,445	\$ 576,312

#### *Remaining Performance Obligations*

Our remaining performance obligations, which is the equivalent of our backlog, represent the expected transaction price allocated to our contracts that we expect to recognize as revenue in future periods when we perform under the contracts. These remaining obligations include amounts that have been formally appropriated under contracts with the U.S. Government, and exclude unexercised contract options and potential orders under ordering-type contracts such as Indefinite Delivery, Indefinite Quantity contracts. At June 30, 2019, we had \$432.5 million in remaining performance obligations of which we expect to recognize revenues of 83% in the next twelve months.

#### *Contract assets and liabilities*

Assets and liabilities related to our contracts with customers are reported on a contract-by-contract basis at the end of each reporting period. At June 30, 2019, contract assets and liabilities totaled \$99.5 million and \$53.8 million, respectively. Upon adoption of ASC 606 on October 1, 2018, contract assets and liabilities related to our contracts with customers were \$87 million and \$51 million, respectively. During the first nine months of 2019, we recognized approximately \$35 million in revenues that were included in the contract liabilities balance at the adoption date.

#### *Reconciliation of ASC 606 to Prior Accounting Standards*

The amount by which each financial statement line item is affected in 2019 as a result of applying the new accounting standard as discussed in Note 2 is presented below:

<i>(In thousands)</i>	<b>June 30, 2019</b>		
	<b>As Reported</b>	<b>Effect of the adoption of ASC 606</b>	<b>Under Prior Accounting</b>
<b>Consolidated Balance Sheets</b>			
Contract assets (1)	\$ 99,499	\$ (43,576)	\$ 55,923
Inventories	126,816	36,089	162,905
Total current assets	450,206	(7,487)	442,719
Total assets	1,326,095	(7,487)	1,318,608
Contract liabilities (2)	53,758	4,549	58,307
Total current liabilities	199,736	4,549	204,285
Deferred tax liabilities	66,286	(1,678)	64,608
Total liabilities	514,288	2,871	517,159
Retained earnings	661,003	(10,358)	650,645
Total shareholders' equity	811,807	(10,358)	801,449
Total liabilities and shareholders' equity	<u>\$ 1,326,095</u>	<u>(7,487)</u>	<u>1,318,608</u>

(1) Previously "cost and estimated earnings on long-term contracts"

(2) Previously "advance payments on long-term contracts" and "current portion of deferred revenue"

<i>(In thousands, except per share amounts)</i>	Three Months Ended June 30, 2019		
	As Reported	Effect of the adoption of ASC 606	Under Prior Accounting
<b>Consolidated Statements of Operations</b>			
Net sales	\$ 199,766	\$ (4,008)	\$ 195,758
Cost of sales	122,172	(1,380)	120,792
Total costs and expenses	174,874	(1,380)	173,494
Earnings before income tax	24,892	(2,628)	22,264
Income tax expense (benefit)	4,825	(399)	4,426
Net earnings	20,067	(2,229)	17,838
Earnings per share:			
Basic:			
Net earnings	\$ 0.77	\$ (0.08)	\$ 0.69
Diluted:			
Net earnings	\$ 0.77	\$ (0.08)	\$ 0.69
<b>Consolidated Statements of Comprehensive Income</b>			
Net earnings	\$ 20,067	\$ (2,229)	\$ 17,838
Comprehensive income	21,899	(2,229)	19,670

<i>(In thousands, except per share amounts)</i>	Nine Months Ended June 30, 2019		
	As Reported	Effect of the adoption of ASC 606	Under Prior Accounting
<b>Consolidated Statements of Operations</b>			
Net sales	\$ 576,312	\$ (9,787)	\$ 566,525
Cost of sales	363,026	(8,360)	354,666
Total costs and expenses	506,808	(8,360)	498,448
Earnings before income tax	69,504	(1,427)	68,077
Income tax expense (benefit)	13,323	(171)	13,152
Net earnings	56,181	(1,256)	54,925
Earnings per share:			
Basic:			
Net earnings	\$ 2.17	\$ (0.05)	\$ 2.12
Diluted:			
Net earnings	\$ 2.15	\$ (0.04)	\$ 2.11
<b>Consolidated Statements of Comprehensive Income</b>			
Net earnings	\$ 56,181	\$ (1,256)	\$ 54,925
Comprehensive income	54,262	(1,256)	53,006
<b>Consolidated Statements of Cash flows</b>			
Net earnings	\$ 56,181	\$ (1,256)	\$ 54,925
Adjustments to reconcile net earnings to net cash provided by operating activities:			
Change in assets and liabilities	\$ (41,851)	1,256	\$ (40,595)
Net cash provided by operating activities	37,041	—	37,041

#### 15. NEW ACCOUNTING STANDARDS

In February 2016, the FASB issued ASU No. 2016-062, "Leases" (ASU 2016-02) which supersedes ASC 840, "Leases" and creates a new topic, ASC 842 "Leases." Subsequent to the issuance of ASU 2016-02, ASC 842 was amended by various updates that amend and clarify the impact and implementation of the aforementioned update. These updates require lessees to recognize a lease liability and a lease asset for all leases, including operating leases, with a term greater than 12 months on its balance sheet. Upon initial application, the provisions of these updates are required to be applied using the modified retrospective method which requires retrospective adoption to each prior

reporting period presented with the cumulative effect of adoption recorded to the earliest reporting period presented. An optional transition method can be utilized which requires retrospective adoption beginning on the date of adoption with the cumulative effect of initially applying these updates recognized at the date of initial adoption. These updates also expand the required quantitative and qualitative disclosures surrounding leases. These updates are effective for fiscal years beginning after December 15, 2018 and interim periods within those fiscal years, with earlier application permitted. We expect to adopt these updates on October 1, 2019 using the optional transition method. We continue to evaluate the impact these updates will have on our consolidated financial statements. Based upon the analysis and preliminary evaluation of the standard, we estimate the adoption will result in the addition of assets and liabilities of less than \$30 million to our consolidated balance sheet, with no significant change to our consolidated statements of operations or cash flows. We believe the updates will also have an impact on our accounting policies, internal controls and disclosures related to leases.

In October 2016, the FASB issued ASU No. 2016-16, *Intra-Entity Transfers of Assets Other Than Inventory*, which eliminates the exception for all intra-entity sale of assets other than inventory. This standard is effective for annual periods beginning after December 15, 2017. There was no significant impact to the Company's consolidated financial statements as a result of adopting this new standard.

#### 16. SUBSEQUENT EVENT

On July 2, 2019, the Company acquired Globe Composite Solutions, LLC (Globe), a supplier of mission-critical composite-based products and solutions for navy, defense, and industrial customers. Globe's operating results from date of acquisition will be included in the Company's Filtration segment.

## ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

### RESULTS OF OPERATIONS

References to the third quarters of 2019 and 2018 represent the three-month periods ended June 30, 2019 and 2018, respectively.

#### OVERVIEW

In the third quarter of 2019, sales, net earnings and diluted earnings per share were \$199.8 million, \$20.1 million and \$0.77 per share, respectively, compared to \$192.2 million, \$19.0 million and \$0.73 per share, respectively, in the third quarter of 2018. In the first nine months of 2019, sales, net earnings and diluted earnings per share were \$576.3 million, \$56.2 million and \$2.15, respectively, compared to \$540.5 million, \$63.7 million and \$2.45 per share, respectively, in the first nine months of 2018.

#### NET SALES

In the third quarter of 2019, net sales of \$199.8 million were \$7.6 million, or 4.0%, higher than the \$192.2 million in the third quarter of 2018. In the first nine months of 2019, net sales of \$576.3 million were \$35.8 million, or 6.6%, higher than the \$540.5 million in the first nine months of 2018. The increase in net sales in the third quarter of 2019 as compared to the third quarter of 2018 was due to a \$13.4 million increase in the Filtration segment, partially offset by a \$2.7 million decrease in the Test segment, a \$2.6 million decrease in the USG segment and a \$0.5 million decrease in the Technical Packaging segment. The increase in net sales in the first nine months of 2019 as compared to the first nine months of 2018 was due to a \$33.3 million increase in the Filtration segment, and a \$3.1 million increase in the Test segment, partially offset by a \$0.3 million decrease in the USG segment and a \$0.2 million decrease in the Technical Packaging segment.

##### *-Filtration*

In the third quarter of 2019, net sales of \$83.1 million were \$13.4 million, or 19.2%, higher than the \$69.7 million in the third quarter of 2018. In the first nine months of 2019, net sales of \$228.8 million were \$33.3 million, or 17.0%, higher than the \$195.5 million in the first nine months of 2018. The increase in the third quarter of 2019 compared to the third quarter of 2018 was mainly due to a \$6.7 million increase in net sales at PTI due to higher aerospace assembly and element shipments, a \$3.3 million increase in net sales at VACCO due to higher shipments of space products and defense spares, a \$2.2 million increase in net sales at Crissair due to higher aerospace shipments, and a \$1.5 million increase in net sales at Mayday due to higher aerospace shipments, partially offset by a \$0.3 million decrease in net sales at Westland due to timing of shipments. The increase in the first nine months of 2019 compared to the first nine months of 2018 was primarily due to an a \$11.7 million increase in net sales at PTI due to higher aerospace assembly and element shipments, \$10.2 million increase in net sales at Crissair due to higher aerospace shipments, a \$4.9 million increase in net sales at Mayday due to higher aerospace shipments \$3.3 million increase in net sales at Westland due to timing of shipments on government programs and a \$3.2 million increase in net sales at VACCO due to higher shipments of defense spares.

##### *-Test*

In the third quarter of 2019, net sales of \$42.3 million were \$2.7 million, or 6.0%, lower than the \$45.0 million in the third quarter of 2018. In the first nine months of 2019, net sales of \$126.5 million were \$3.1 million, or 2.5%, higher than the \$123.4 million in the first nine months of 2018. The decrease in the third quarter of 2019 compared to the third quarter of 2018 was primarily due to lower sales from the segment's U.S. operations due to timing of test and measurement chamber projects. The increase in the first nine months of 2019 compared to the first nine months of 2018 was primarily due to higher sales from the segment's Asian and U.S. operations due to the timing of test and measurement chamber projects.

#### *-Utility Solutions Group (USG)*

In the third quarter of 2019, net sales of \$52.9 million were \$2.6 million, or 4.7%, lower than the \$55.5 million in the third quarter of 2018. In the first nine months of 2019, net sales of \$157.6 million were \$0.3 million lower than the \$157.9 million in the first nine months of 2018. The decrease in the third quarter and first nine months of 2019 compared to the corresponding periods of 2018 was mainly due to lower sales at NRG due to continued softness in the renewable energy market.

#### *-Technical Packaging*

In the third quarter of 2019, net sales of \$21.5 million were \$0.5 million, or 2.3%, lower than the \$22.0 million in the third quarter of 2018. In the first nine months of 2019, net sales of \$63.4 million were \$0.3 million lower than the \$63.7 million in the first nine months of 2018. The decrease in the third quarter and first nine months of 2019 compared to the corresponding periods of 2018 was primarily due to the decrease in net sales from Plastique due to timing of projects.

#### ORDERS AND BACKLOG

Backlog was \$432.5 million at June 30, 2019 compared with \$382.8 million at September 30, 2018. The Company received new orders totaling \$196.2 million in the third quarter of 2019 compared to \$201.1 million in the third quarter of 2018. Of the new orders received in the third quarter of 2019, \$71.2 million related to Filtration products, \$44.1 million related to Test products, \$55.4 million related to USG products, and \$25.4 million related to Technical Packaging products. Of the new orders received in the third quarter of 2018, \$85.9 million related to Filtration products, \$37.9 million related to Test products, \$57.8 million related to USG products, and \$19.5 million related to Technical Packaging products.

The Company received new orders totaling \$626.0 million in the first nine months of 2019 compared to \$588.9 million in the first nine months of 2018. Of the new orders received in the first nine months of 2019, \$255.7 million related to Filtration products, \$147.1 million related to Test products, \$158.5 million related to USG products, and \$64.7 million related to Technical Packaging products. Of the new orders received in the first nine months of 2018, \$219.1 million related to Filtration products, \$144.2 million related to Test products, \$168.0 million related to USG products, and \$57.6 million related to Technical Packaging products.

#### SELLING, GENERAL AND ADMINISTRATIVE EXPENSES

Selling, general and administrative (SG&A) expenses for the third quarter of 2019 were \$43.4 million (21.7% of net sales), compared with \$39.9 million (20.8% of net sales) for the third quarter of 2018. For the first nine months of 2019, SG&A expenses were \$126.1 million (21.9% of net sales) compared to \$122.8 million (22.7% of net sales) for the first nine months of 2018. The increase in SG&A in the third quarter and first nine months of 2019 compared to the corresponding periods of 2018 was mainly due to an increase in the USG segment due to higher sales commissions including additional sales and marketing expenses to support future revenue growth.

#### AMORTIZATION OF INTANGIBLE ASSETS

Amortization of intangible assets was \$4.7 million and \$14.0 million for the third quarter and first nine months of 2019, respectively, compared to \$4.6 million and \$13.6 million for the corresponding periods of 2018. Amortization expenses consist of amortization of acquired intangible assets from acquisitions and other identifiable intangible assets (primarily software). The increase in amortization expense in the first nine months of 2019 compared to the first nine months of 2018 was mainly due to an increase in amortization of intangibles related to the Manta acquisition.

#### OTHER EXPENSES (INCOME), NET

Other expenses, net, was \$2.6 million in the third quarter of 2019 compared to other income, net, of \$0.7 million in the third quarter of 2018. The principal components in other expenses, net, in the third quarter of 2019 were \$1.2 million of restructuring charges related to the closure of Plastique's headquarters in Tunbridge Wells, UK; the consolidation of



VACCO's aircraft/aerospace business into PTI's aerospace facility in Oxnard, California; the completion of other restructuring activities begun in 2018; and losses on derivative instruments. The principal component in other income, net, in the third quarter of 2018 was a gain on derivative instruments of \$0.5 million.

Other income, net, was \$2.0 million in the first nine months of 2019 compared to other expenses, net, of \$1.0 million in the first nine months of 2018. The principal component in other income, net, in the first nine months of 2019 was a gain of approximately \$8 million on the sale of the Doble Watertown, MA building and land, partially offset by certain restructuring activities at Doble, PTI, VACCO and Plastique and losses on derivative instruments. The principal components in other expenses, net, in the first nine months of 2018 were \$2.1 million of charges related to the USG segment restructuring activities as mentioned above, partially offset by gains on derivative instruments.

#### EBIT

The Company evaluates the performance of its operating segments based on EBIT, and provides EBIT on a consolidated basis, which is a non-GAAP financial measure. Please refer to the discussion of non-GAAP financial measures in Note 7 to the Consolidated Financial Statements, above. EBIT was \$26.9 million (13.4% of net sales) for the third quarter of 2019 compared to \$25.6 million (13.3% of net sales) for the third quarter of 2018. For the first nine months of 2019, EBIT was \$75.3 million (13.1% of net sales) compared to \$56.2 million (10.4% of net sales) for the first nine months of 2018.

The following table presents a reconciliation of EBIT to net earnings.

<b>(In thousands)</b>	<b>Three Months Ended</b>		<b>Nine Months Ended</b>	
	<b>June 30,</b>		<b>June 30,</b>	
	<b>2019</b>	<b>2018</b>	<b>2019</b>	<b>2018</b>
Consolidated EBIT	\$ 26,865	25,559	75,292	56,165
Less: Interest expense, net	(1,973)	(2,243)	(5,788)	(6,464)
(Less) Plus: Income tax	(4,825)	(4,297)	(13,323)	13,983
Net earnings	<u>\$ 20,067</u>	<u>19,019</u>	<u>56,181</u>	<u>63,684</u>

#### -Filtration

EBIT in the third quarter of 2019 was \$19.0 million (22.9% of net sales) compared to \$14.3 million (20.5% of net sales) in the third quarter of 2018. EBIT in the first nine months of 2019 was \$47.1 million (20.6% of net sales) compared to \$35.1 million (17.9% of net sales) in the first nine months of 2018. The increase in EBIT in the third quarter and first nine months of 2019 compared to the corresponding periods of 2018 was mainly due to an increase across all companies within the segment due to the higher sales volumes as mentioned above. EBIT in the third quarter and first nine months of 2019 was negatively impacted by restructuring charges incurred related to the consolidation of VACCO's aircraft/aerospace business into PTI's aerospace facility in Oxnard, California, (\$0.3 million in the third quarter of 2019 and \$0.8 million in the first nine months of 2019). These charges consisted primarily of severance and compensation benefits.

#### -Test

EBIT in the third quarter of 2019 was \$5.9 million (14.0% of net sales) compared to \$5.9 million (13.1% of net sales) in the third quarter of 2018. EBIT in the first nine months of 2019 was \$14.8 million (11.7% of net sales) compared to \$13.8 million (11.2% of net sales) in the first nine months of 2018. The increase in EBIT in the first nine months of 2019 compared to the first nine months of 2018 was primarily due to the increased sales volumes mainly from the segment's Asian operations.

#### -Utility Solutions Group

EBIT in the third quarter of 2019 was \$10.1 million (19.2% of net sales) compared to \$11.5 million (20.8% of net sales) in the third quarter of 2018. EBIT in the first nine months of 2019 was \$40.5 million (25.7% of net sales) compared to

EBIT of \$27.8 million (17.6% of net sales) in the first nine months of 2018. The increase in EBIT in the third quarter and first nine months of 2019 compared to the corresponding periods of 2018 was mainly due to the gain on sale of the Doble Watertown facility of approximately \$8 million in the first quarter of 2019, as well as an increase in EBIT from Morgan Schaffer and Manta product lines partially offset by a decrease in EBIT from NRG due to market softness.

*-Technical Packaging*

EBIT in the third quarter of 2019 was \$1.6 million (7.6% of net sales) compared to \$2.5 million (11.4% of net sales) in the third quarter of 2018. EBIT in the first nine months of 2019 was \$3.3 million (5.3% of net sales) compared to \$5.4 million (8.4% of net sales) in the first nine months of 2018. The decrease in EBIT in the third quarter and first nine months of 2019 compared to the corresponding periods of 2018 was mainly due to the restructuring charges incurred related to the Plastique facility consolidation, (\$0.6 million in the third quarter of 2019 and \$1.3 million in the first nine months of 2019). These charges consisted primarily of severance and compensation benefits and asset impairment charges.

*-Corporate*

Corporate costs included in EBIT were \$9.9 million and \$30.4 million in the third quarter and first nine months of 2019, respectively, compared to \$8.7 million and \$25.8 million in the corresponding periods of 2018. The increase in Corporate costs in the third quarter and first nine months of 2019 compared to the corresponding periods of 2018 was primarily due to higher professional fees, acquisition costs and timing of other Corporate costs recorded in the first nine months of 2019.

INTEREST EXPENSE, NET

Interest expense was \$2.0 million and \$5.9 million in the third quarter and first nine months of 2019, respectively, and \$2.2 million and \$6.5 million in the corresponding periods of 2018. The decrease in interest expense in the first nine months of 2019 compared to the first nine months of 2018 was mainly due to lower average outstanding borrowings (\$216 million compared to \$263 million).

INCOME TAX EXPENSE

The third quarter 2019 effective income tax rate was 19.4% compared to 18.4% in the third quarter of 2018. The income tax expense for the first nine months of 2019 was \$13.3 million compared to income tax benefit of \$14.0 million for the first nine months of 2018. The effective income tax rate for the first nine months of 2019 was 19.2% compared to (28.1%) for the first nine months of 2018. The income tax expense in the third quarter and first nine months of 2019 was favorably impacted by tax planning strategies to increase foreign tax credits claimed retrospectively. The Company reduced the valuation allowance for excess foreign tax credits by \$2.4 million (\$2.3 million in the second quarter of 2019 and \$0.1 million in third quarter of 2019) and recorded an amended return benefit of \$0.3 million (\$0.2 million in the second quarter of 2019 and \$0.1 million in the third quarter of 2019) which favorably impacted the third quarter and year-to-date effective tax rate by 1.0% and 4.1%, respectively. Income tax expense in the third quarter of 2019 and first nine months of 2019 was also favorably impacted by additional tax benefits on share-based compensation that vested during the quarter decreasing the effective tax rate by 1.8% and 0.7%, respectively. A non-automatic accounting method change filed with the 2018 tax return was approved by the Internal Revenue Service during the third quarter of 2019 and favorably impacted the third quarter and year-to-date effective tax rate by 1.0% and 0.4%, respectively.

H.R. 1, *Tax Cuts and Jobs Act* ("TCJA"), was signed into law on December 22, 2017. The total impact of the TCJA in the third quarter and first nine months of 2018 was a net expense of \$0.1 million and a net benefit of \$24.3 million, respectively. The impacts were as follows: First, the Company's 2018 federal statutory rate dropped from 35.0% to 24.5% which required an adjustment to the value of its deferred tax assets and liabilities. This adjustment (\$30.3 million provisional amount recorded in the first quarter of 2018 and \$0.4 million provisional amount in the third quarter of 2018) favorably impacted the third quarter and year-to-date effective tax rate by 1.5% and 61.7%, respectively. Second, the TCJA subjected the Company's cumulative foreign earnings to deferral income tax (\$4.1 million provisional amount of which \$2.9 million was recorded in the first quarter of 2018, \$0.7 million was recorded in the third quarter of 2018 and

\$0.5 million in the third quarter of 2019) which unfavorably impacted the third quarter and year-to-date effective tax rate by 2.1% and 8.2%, respectively.

In the first quarter of 2018, the Company recorded a \$2.3 million provisional estimate of the income tax effects of the future repatriation of the cumulative earnings of its foreign subsidiaries which unfavorably impacted the year-to-date effective tax rate by 4.7%. An additional \$7.5 million pension contribution for the 2017 plan year was approved during the second quarter of 2018 increasing the value of the deferred tax liability by \$1.0 million. This favorable adjustment, net of the \$0.3 million unfavorable impact to the 2017 Domestic Production Deduction, favorably impacted the year-to-date effective tax rate by 1.6%. An accounting method change was filed with the 2017 tax return which resulted in an additional deferred tax liability to be adjusted as a result of the TCJA. A favorable adjustment, net of the \$0.3 million unfavorable impact to the 2018 Domestic Production deduction, favorably impacted the third quarter and year-to-date effective tax rate by 2.9% and 1.4%, respectively. The income tax expense in the third quarter and first nine months of 2018 was favorably impacted by return to provision true-ups decreasing the third quarter and year-to-date effective tax rate by 1.4% and 0.7%, respectively. Income tax expense in the third quarter and first nine months of 2018 was also favorably impacted by additional tax benefits on share-based compensation that vested during the quarter decreasing the effective tax rate by 1.9% and 0.9%, respectively.

Provisions under the TCJA that became effective for the Company in the current fiscal year include a further reduction in the U.S. statutory rate to 21%, a new minimum tax on global intangible low-taxed income (“GILTI”), the benefit of the deduction for foreign-derived intangible income (“FDII”), and changes to IRC Section 162(m) related to the deductibility of executive compensation.

#### CAPITAL RESOURCES AND LIQUIDITY

The Company’s overall financial position and liquidity remains strong. Working capital (current assets less current liabilities) increased to \$250.5 million at June 30, 2019 from \$195.5 million at September 30, 2018. Inventories decreased by \$8.6 million during this period mainly due to a \$12.7 million decrease within the Filtration segment resulting primarily from the adoption of ASU No. 2014-09, *Revenue from Contracts with Customers* (ASC 606). Contract assets increased \$46.5 million in the first nine months of 2019 mainly due to the adoption of ASC 606 within the Filtration segment.

Net cash provided by operating activities was \$37.0 million and \$53.9 million in the first nine months of 2019 and 2018, respectively. The decrease in net cash provided by operating activities in the first nine months of 2019 as compared to the first nine months of 2018 was due to higher working capital requirements.

Capital expenditures were \$26.5 million and \$15.5 million in the first nine months of 2019 and 2018, respectively. The increase in the first nine months of 2019 was mainly due to a \$9.1 million facility expansion at TEQ. In addition, the Company incurred expenditures for capitalized software of \$6.2 million and \$7.1 million in the first nine months of 2019 and 2018, respectively.

#### *Credit Facility*

At June 30, 2019, the Company had approximately \$225 million available to borrow under its bank credit facility, a \$250 million increase option, and \$39.0 million cash on hand. At June 30, 2019, the Company had \$217.0 million of outstanding borrowings under the Credit Facility, and \$0.9 million of short-term borrowing in addition to outstanding letters of credit of \$7.2 million. Cash flow from operations and borrowings under the Company’s credit facility are expected to meet the Company’s capital requirements and operational needs for the foreseeable future. The Company’s ability to access the additional \$250 million increase option of the credit facility is subject to acceptance by participating or other outside banks.

#### *New Accounting Standards*

In February 2016, the FASB issued ASU No. 2016-062, “Leases” (ASU 2016-02) which supersedes ASC 840, “Leases” and creates a new topic, ASC 842 “Leases.” Subsequent to the issuance of ASU 2016-02, ASC 842 was amended by

various updates that amend and clarify the impact and implementation of the aforementioned update. These updates require lessees to recognize a lease liability and a lease asset for all leases, including operating leases, with a term greater than 12 months on its balance sheet. Upon initial application, the provisions of these updates are required to be applied using the modified retrospective method which requires retrospective adoption to each prior reporting period presented with the cumulative effect of adoption recorded to the earliest reporting period presented. An optional transition method can be utilized which requires retrospective adoption beginning on the date of adoption with the cumulative effect of initially applying these updates recognized at the date of initial adoption. These updates also expand the required quantitative and qualitative disclosures surrounding leases. These updates are effective for fiscal years beginning after December 15, 2018 and interim periods within those fiscal years, with earlier application permitted. We expect to adopt these updates on October 1, 2019 using the optional transition method. We continue to evaluate the impact these updates will have on our consolidated financial statements. Based upon the analysis and preliminary evaluation of the standard, we estimate the adoption will result in the addition of assets and liabilities of less than \$30 million to our consolidated balance sheet, with no significant change to our consolidated statements of operations or cash flows. We believe the updates will also have an impact on our accounting policies, internal controls and disclosures related to leases.

In October 2016, the FASB issued ASU No. 2016-16, *Intra-Entity Transfers of Assets Other Than Inventory*, which eliminates the exception for all intra-entity sale of assets other than inventory. This standard is effective for annual periods beginning after December 15, 2017. There was no significant impact to the Company's consolidated financial statements as a result of adopting this new standard.

#### *Acquisition*

During the third quarter of 2019, the Company paid a deferred payment of \$0.9 million in connection with the 2016 acquisition of Plastique.

#### *Subsequent Event*

On July 2, 2019, the Company acquired Globe Composite Solutions, LLC (Globe), a supplier of mission-critical composite-based products and solutions for navy, defense, and industrial customers. Globe's operating results from date of acquisition will be included in the Company's Filtration segment.

#### *Dividends*

A quarterly dividend of \$0.08 per share, totaling \$2.1 million, was paid on April 18, 2019 to stockholders of record as of April 3, 2019. Subsequent to June 30, 2019, a quarterly dividend of \$0.08 per share, totaling \$2.1 million, was paid on July 19, 2019 to stockholders of record as of July 5, 2019.

#### OUTLOOK

Management's current expectations for 2019 remain consistent with the details outlined in the Business Outlook in the previous release and expects 2019 Adjusted EPS guidance in the range of \$3.05 to \$3.10 per share. Management is excluding the following expected adjustments to 2019 GAAP EPS: A pre-tax gain from the October 2018 sale of Doble's headquarters building in Watertown, Massachusetts; and pre-tax costs related to the relocation of Doble's headquarters, the closure of Plastique's headquarters in Tunbridge Wells, UK and the consolidation of its product design and administrative functions into its facilities in Nottingham, UK and Poznan, Poland; the consolidation of VACCO's aircraft/aerospace business into PTI's aerospace facility in Oxnard, California; and the completion of other restructuring activities begun in 2018.

#### CRITICAL ACCOUNTING POLICIES

Management has evaluated the accounting policies used in the preparation of the Company's financial statements and related notes and believes those policies to be reasonable and appropriate. Certain of these accounting policies require the application of significant judgment by management in selecting appropriate assumptions for calculating financial estimates. By their nature, these judgments are subject to an inherent degree of uncertainty. These judgments are based

on historical experience, trends in the industry, information provided by customers and information available from other outside sources, as appropriate. The most significant areas involving management judgments and estimates may be found in the Critical Accounting Policies section of Management's Discussion and Analysis and in Note 1 to the Consolidated Financial Statements contained in the Company's Annual Report on Form 10-K for the fiscal year ended September 30, 2018.

## OTHER MATTERS

### *Contingencies*

As a normal incident of the business in which the Company is engaged, various claims, charges and litigation are asserted or commenced against the Company. Additionally, the Company is currently involved in various stages of investigation and remediation relating to environmental matters. In the opinion of management, the aggregate costs involved in the resolution of these matters, and final judgments, if any, which might be rendered against the Company, are adequately reserved, are covered by insurance, or would not have a material adverse effect on the Company's results from operations, capital expenditures, or competitive position.

## FORWARD LOOKING STATEMENTS

Statements contained in this Form 10-Q regarding future events and the Company's future results that reflect or are based on current expectations, estimates, forecasts, projections or assumptions about the Company's performance and the industries in which the Company operates are considered "forward-looking statements" within the meaning of the safe harbor provisions of the Federal securities laws. These include, but are not necessarily limited to, statements about: the amount and timing of future sales, revenues, cash flows, growth, Adjusted EPS and EPS; the adequacy of the Company's credit facility and the Company's ability to increase it; the outcome of current litigation, claims and charges; income taxation of foreign earnings and the future repatriation, reinvestment or distribution of foreign earnings; future income tax liabilities and effective tax rate; timing of the repayment of the current portion of the Company's long-term debt; changes in the amount of unrecognized tax benefits; the recognition and timing of costs related to share-based compensation arrangements; returns on retirement plan assets; estimates or projections made in connection with the Company's accounting policies; market risks relating to the Company's operations and changes in interest rates; the extent to which hedging gains or losses are offset by losses or gains on related underlying exposures; the Company's ability to hedge against or otherwise manage them through the use of derivative financial instruments; and any other statements contained herein which are not strictly historical. Words such as expects, anticipates, targets, goals, projects, intends, plans, believes, estimates, variations of such words, and similar expressions are intended to identify such forward-looking statements.

Investors are cautioned that such statements are only predictions and speak only as of the date of this Form 10-Q, and the Company undertakes no duty to update them except as may be required by applicable laws or regulations. The Company's actual results in the future may differ materially from those projected in the forward-looking statements due to risks and uncertainties that exist in the Company's operations and business environment, including but not limited to those described in Item 1A, "Risk Factors," of the Company's Annual Report on Form 10-K for the fiscal year ended September 30, 2018, and the following: the impacts of natural disasters on the Company's operations and those of the Company's customers and suppliers; the timing and content of future contract awards or customer orders; the appropriation, allocation and availability of Government funds; the termination for convenience of Government and other customer contracts or orders; financial exposure in connection with Company guarantees of certain Aclara contracts; weakening of economic conditions in served markets; the success of the Company's competitors; changes in customer demands or customer insolvencies; competition; intellectual property rights; technical difficulties; the availability of selected acquisitions; delivery delays or defaults by customers; performance issues with key customers, suppliers and subcontractors; material changes in the costs and availability of certain raw materials; labor disputes; changes in U.S. tax laws and regulations; other changes in laws and regulations including but not limited to changes in accounting standards and foreign taxation; changes in interest rates; costs relating to environmental matters arising from current or former facilities; uncertainty regarding the ultimate resolution of current disputes, claims, litigation or arbitration; and the integration of recently acquired businesses.

### ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Market risks relating to the Company's operations result primarily from changes in interest rates and changes in foreign currency exchange rates. The Company is exposed to market risk related to changes in interest rates and selectively uses derivative financial instruments, including forward contracts and swaps, to manage these risks. In 2018, the Company entered into three interest rate swaps with a notional amount of \$150 million to hedge some of its exposure to variability in future LIBOR-based interest payments on variable rate debt. In addition, the Company's Canadian subsidiary Morgan Schaffer enters into foreign exchange contracts to manage foreign currency risk as a portion of their revenue is denominated in U.S. dollars. All derivative instruments are reported on the balance sheet at fair value. For derivative instruments designated as cash flow hedges, the gain or loss on the respective derivative is deferred in accumulated other comprehensive income until recognized in earnings with the underlying hedged item. The interest rate swaps entered into during 2018 were not designated as cash flow hedges and, therefore, the gain or loss on the derivative is reflected in earnings each period. There has been no material change to the Company's market risks since September 30, 2018. See Note 12 to the Consolidated Financial Statements in Item 1 of this Report for a summary of the Company's outstanding derivative financial instruments as of June 30, 2019. Refer to the Company's Annual Report on Form 10-K for the fiscal year ended September 30, 2018 for further discussion about market risk.

### ITEM 4. CONTROLS AND PROCEDURES

The Company carried out an evaluation, under the supervision and with the participation of management, including the Company's Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of the Company's disclosure controls and procedures as of the end of the period covered by this report. Based upon that evaluation, due to the material weakness in the Company's internal control over financial reporting related to the ineffective design and operation of controls impacting the deferred revenue general ledger account, the Company's Chief Executive Officer and Chief Financial Officer concluded that the Company's disclosure controls and procedures were ineffective as of that date.

As previously disclosed in Part II Item 9A in the Company's Annual Report on Form 10-K for the year ended September 30, 2018, management concluded there was a material weakness in the Company's internal control over financial reporting related to the ineffective design and operation of controls impacting the deferred revenue general ledger account. Remedial actions have been identified to address these controls, including enhancing our policies and procedures related to the deferred revenue reconciliation and review, and providing additional training to our segment finance department. These new procedures are in the process of being implemented but have not been in place long enough to provide sufficient assurances to support the conclusion that the above identified material weakness has been fully remediated as of June 30, 2019.

Other than the above, there have been no changes in the Company's internal control over financial reporting (as defined in Rule 13a-15(f) under the Exchange Act) during the period covered by this report that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

## PART II. OTHER INFORMATION

## ITEM 6. EXHIBITS

<u>Exhibit Number</u>	<u>Description</u>	<u>Document Location</u>
3.1(a)	<a href="#"><u>Restated Articles of Incorporation</u></a>	Exhibit 3(a) to Form 10-K for the fiscal year ended September 30, 1999
3.1(b)	<a href="#"><u>Amended Certificate of Designation, Preferences and Rights of Series A Participating Cumulative Preferred Stock of the Registrant</u></a>	Exhibit 4(e) to Form 10-Q for the fiscal quarter ended March 31, 2000
3.1(c)	<a href="#"><u>Articles of Merger effective July 10, 2000</u></a>	Exhibit 3(c) to Form 10-Q for the fiscal quarter ended June 30, 2000
3.1(d)	<a href="#"><u>Amendment of Articles of Incorporation effective February 5, 2018</u></a>	Exhibit 3.1 to Form 8-K filed February 7, 2018
3.2	<a href="#"><u>Bylaws</u></a>	Exhibit 3.2 to Form 8-K filed February 7, 2018
4.1	<a href="#"><u>Specimen revised Common Stock Certificate</u></a>	Exhibit 4.1 to Form 10-Q for the fiscal quarter ended March 31, 2010
4.2	<a href="#"><u>Amended and Restated Credit Agreement dated as of December 21, 2015 among the Registrant, the Foreign Subsidiary Borrowers from time to time party thereto, the Lenders from time to time party thereto, JP Morgan Chase Bank, N.A. as Administrative Agent, and Bank of America, N.A., BMO Harris Bank, N.A., SunTrust Bank and Wells Fargo Bank, National Association as Co-Documentation Agents</u></a>	Exhibit 4.1 to Form 8-K filed December 23, 2015
4.3	<a href="#"><u>Amendment No. 1 to December 21, 2015 Credit Agreement, effective September 30, 2016</u></a>	Exhibit 4.4 to Form 10-K for the fiscal year ended September 30, 2016
4.4	<a href="#"><u>Amendment No. 2 to December 21, 2015 Credit Agreement, effective May 15, 2017</u></a>	Exhibit 4.4 to Form 10-Q for the fiscal quarter ended June 30, 2017
31.1	<a href="#"><u>Certification of Chief Executive Officer relating to Form 10Q for period ended June 30, 2019</u></a>	Filed herewith
31.2	<a href="#"><u>Certification of Chief Financial Officer relating to Form 10Q for period ended June 30, 2019</u></a>	Filed herewith
32	<a href="#"><u>Certification of Chief Executive Officer and Chief Financial Officer relating to Form 10Q for period ended June 30, 2019</u></a>	Filed herewith
101.INS	XBRL Instance Document*	Submitted herewith
101.SCH	XBRL Schema Document*	Submitted herewith
101.CAL	XBRL Calculation Linkbase Document*	Submitted herewith
101.DEF	XBRL Definition Linkbase Document*	Submitted herewith
101.LAB	XBRL Label Linkbase Document*	Submitted herewith
101.PRE	XBRL Presentation Linkbase Document*	Submitted herewith

\* Exhibit 101 to this report consists of documents formatted in XBRL (Extensible Business Reporting Language). The financial information contained in the XBRL – related documents is “unaudited” or “unreviewed”.

SIGNATURE

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.

ESCO TECHNOLOGIES INC.

/s/ Gary E. Muenster

Gary E. Muenster

Executive Vice President and Chief Financial Officer  
(As duly authorized officer and principal accounting and  
financial officer of the registrant)

Dated: August 9, 2019



## CERTIFICATION

I, Victor L. Richey, certify that:

1. I have reviewed this quarterly report on Form 10-Q of ESCO Technologies Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b. Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - c. Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - d. Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: August 9, 2019

/s/ Victor L. Richey

Victor L. Richey  
Chairman, Chief Executive Officer and President

## CERTIFICATION

I, Gary E. Muenster, certify that:

1. I have reviewed this quarterly report on Form 10-Q of ESCO Technologies Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and

procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

- a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b. Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - c. Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - d. Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
- a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: August 9, 2019

/s/ Gary E. Muenster

Gary E. Muenster  
Executive Vice President and Chief Financial Officer

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**Exhibit 32**

CERTIFICATION PURSUANT TO  
18 U.S.C. SECTION 1350,  
AS ADOPTED PURSUANT TO  
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the quarterly report of ESCO Technologies Inc. (the "Company") on Form 10-Q for the period ended June 30, 2019 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), we, Victor L. Richey, Chairman, Chief Executive Officer and President of the Company, and Gary E. Muenster, Executive Vice President and Chief Financial Officer of the Company, certify, to the best of our knowledge, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, that:

- (1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Dated: August 9, 2019

/s/ Victor L. Richey

Victor L. Richey  
Chairman, Chief Executive Officer and President  
ESCO Technologies Inc.

/s/ Gary E. Muenster

Gary E. Muenster  
Executive Vice President and Chief Financial Officer  
ESCO Technologies Inc.

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