

CAMBREX CORP  
Form 10-Q  
November 08, 2018

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D. C. 20549

FORM 10-Q

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

for the quarterly period ended September 30, 2018

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 1-10638

CAMBREX CORPORATION

(Exact name of registrant as specified in its charter)

DELAWARE 22-2476135  
(State or other jurisdiction of (I.R.S. Employer  
incorporation or organization) Identification No.)

ONE MEADOWLANDS PLAZA, EAST RUTHERFORD, NEW JERSEY 07073

(Address of principal executive offices)

(201) 804-3000

(Registrant's telephone number, including area code)

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 (§ 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, a smaller reporting company, or an emerging growth company. See the definitions of “large accelerated filer,” “accelerated filer,” “smaller reporting company,” and “emerging growth company” in Rule 12b-2 of the Exchange Act.

Large accelerated filer Accelerated filer Non-accelerated filer Smaller reporting company

Emerging growth company

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

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

As of October 31, 2018, there were 33,560,061 shares outstanding of the registrant’s Common Stock, \$.10 par value.



CAMBREX CORPORATION AND SUBSIDIARIES

Table of Contents

|  | Page No. |
|--|----------|
| Part I <u>Financial Information</u>  |          |
| <u>Financial Statements</u>  |          |
| <u>Consolidated Balance Sheets</u>   | 3        |
| <u>Consolidated Income Statements</u>  | 4        |
| <u>Consolidated Statements of Comprehensive Income</u>                                       | 5        |
| <u>Consolidated Statements of Cash Flows</u>   | 6        |
| <u>Notes to Consolidated Financial Statements</u>  | 7        |
| <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u> | 32       |
| <u>Quantitative and Qualitative Disclosures about Market Risk</u>                            | 44       |
|  | 44       |

Controls and  
Procedures

Part II Other  
Information

Legal  
Proceedings 45

Risk Factors  
1A. 45

Exhibits  
6. 45

Signatures 46

## Forward-Looking Statements

This document contains “forward-looking statements,” including statements or tables regarding expected performance. These and other forward-looking statements may be identified by the fact that they use words such as “guidance,” “expects,” “anticipates,” “intends,” “estimates,” “believes” or similar expressions. Any forward-looking statements contained herein are based on current plans and expectations and involve risks and uncertainties that could cause actual outcomes and results to differ materially from current expectations. The factors described in Item 1A of Part I of the Company’s Annual Report on Form 10-K for the period ended December 31, 2017 captioned “Risk Factors,” or otherwise described in the Company’s filings with the SEC provide examples of such risks and uncertainties that may cause the Company’s actual results to differ materially from the expectations the Company describes in its forward-looking statements, including, but not limited to, the possibility that the benefits from the acquisition of Halo Pharma may not be as anticipated, customer and product concentration, the Company’s ability to win new customer contracts and renew existing contracts on favorable terms, significant declines in sales of products to the Company’s customers, pharmaceutical outsourcing trends, competitive pricing or product developments, market acceptance and adoption rate of its customers’ products, government legislation and regulations (including those pertaining to environmental issues), tax rate, interest rate, technology, manufacturing and legal issues, including the outcome of outstanding litigation, environmental matters, changes in foreign exchange rates, uncollectible receivables, the timing and/or volume of orders or shipments and the Company’s ability to meet its production plan and customer delivery schedules, expected timing of completion of capacity expansions, our ability to successfully integrate acquired businesses, loss on disposition of assets, cancellations or delays in renewal of contracts, lack of suitable raw materials, the Company’s ability to receive regulatory approvals for its products, continued demand in the U.S. for late stage clinical products and the successful outcome of the Company’s investment in new products.

For further details and a discussion of these and other risks and uncertainties, investors are encouraged to review the Cambrex Annual Report on Form 10-K for the fiscal year ended December 31, 2017, including the Forward-Looking Statement sections therein, and other filings with the SEC. The Company cautions investors and potential investors not to place undue reliance on the forward-looking statements contained in this Quarterly Report on Form 10-Q and to give careful consideration to the risks and uncertainties listed above and contained in the Company’s SEC filings. The forward-looking statements in this Quarterly Report on Form 10-Q speak only as of the date of this document, and the Company undertakes no obligation to update or revise any of these statements.

## Part I - FINANCIAL INFORMATION

## Item 1. Financial Statements

## CAMBREX CORPORATION AND SUBSIDIARIES

## Consolidated Balance Sheets

(in thousands, except share data)

|   | September 30,<br>2018 | December 31,<br>2017 |
|---|-----------------------|----------------------|
|   | (unaudited)           |                      |
| <b>ASSETS</b>   |                       |                      |
| Current assets:   |                       |                      |
| Cash and cash equivalents                                     | \$ 97,135             | \$ 183,284           |
| Trade receivables, net  | 71,582                | 75,144               |
| Contract assets   | 112,845               | -                    |
| Other receivables   | 14,824                | 20,891               |
| Inventories, net  | 103,648               | 138,542              |
| Prepaid expenses and other current assets                     | 16,776                | 4,217                |
| Total current assets  | 416,810               | 422,078              |
| Property, plant and equipment, net                            | 352,947               | 254,299              |
| Goodwill  | 271,424               | 43,626               |
| Intangible assets, net  | 191,959               | 13,868               |
| Deferred income taxes   | 11,557                | 3,198                |
| Other non-current assets                                      | 3,192                 | 3,496                |
| Total assets  | \$ 1,247,889          | \$ 740,565           |
| <b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>                   |                       |                      |
| Current liabilities:  |                       |                      |
| Accounts payable  | \$ 38,205             | \$ 35,017            |
| Contract liabilities, current                                 | 10,269                | 4,707                |
| Taxes payable   | 2,727                 | 43                   |
| Accrued expenses and other current liabilities                | 40,578                | 42,774               |
| Total current liabilities                                     | 91,779                | 82,541               |
| Long-term debt  | 325,000               | -                    |
| Contract liabilities, non-current                             | 43,379                | 39,000               |
| Deferred income taxes   | 66,231                | 7,806                |
| Accrued pension benefits                                      | 38,429                | 41,141               |
| Other non-current liabilities                                 | 23,793                | 25,213               |
| Total liabilities   | 588,611               | 195,701              |
| Stockholders' equity:   |                       |                      |
| Common stock, \$.10 par value; authorized 100,000,000, issued |                       |                      |
| 34,813,949 and 34,270,975 shares at respective dates          | 3,481                 | 3,427                |
| Additional paid-in capital                                    | 181,435               | 165,979              |
| Retained earnings   | 537,251               | 429,826              |
| Treasury stock, at cost, 1,273,888 and 1,424,153 shares at    |                       |                      |
| respective dates  | (10,860 )             | (12,140 )            |
| Accumulated other comprehensive loss                          | (52,029 )             | (42,228 )            |

Edgar Filing: CAMBREX CORP - Form 10-Q

|  |              |            |
|--|--------------|------------|
| Total stockholders' equity                 | 659,278      | 544,864    |
| Total liabilities and stockholders' equity | \$ 1,247,889 | \$ 740,565 |

See accompanying notes to unaudited consolidated financial statements.

3

---



## CAMBREX CORPORATION AND SUBSIDIARIES

## Consolidated Income Statements

(unaudited – in thousands, except per share data)

|  | Three Months Ended |           | Nine Months Ended |           |
|--|--------------------|-----------|-------------------|-----------|
|  | September 30,      |           | September 30,     |           |
|  | 2018               | 2017      | 2018              | 2017      |
| Gross sales  | \$104,231          | \$112,233 | \$390,575         | \$350,431 |
| Commissions, allowances and rebates                    | 240                | 225       | 641               | 1,468     |
| Net sales  | 103,991            | 112,008   | 389,934           | 348,963   |
| Other revenues, net                                    | 627                | 611       | 7,827             | 3,216     |
| Net revenue  | 104,618            | 112,619   | 397,761           | 352,179   |
| Cost of goods sold                                     | 71,893             | 65,676    | 249,389           | 200,802   |
| Gross profit   | 32,725             | 46,943    | 148,372           | 151,377   |
| Operating expenses:                                    |                    |           |                   |           |
| Selling, general and administrative expenses           | 14,514             | 17,167    | 47,037            | 50,678    |
| Research and development expenses                      | 4,191              | 4,233     | 11,943            | 12,590    |
| Acquisition and integration expenses                   | 7,388              | -         | 7,727             | -         |
| Total operating expenses                               | 26,093             | 21,400    | 66,707            | 63,268    |
| Operating profit                                       | 6,632              | 25,543    | 81,665            | 88,109    |
| Other expenses/(income):                               |                    |           |                   |           |
| Interest expense, net                                  | 725                | 337       | 824               | 991       |
| Unrealized gain on investment in equity securities     | (5,611 )           | -         | (10,757 )         | -         |
| Other expenses, net                                    | 109                | 432       | 554               | 1,119     |
| Income before income taxes                             | 11,409             | 24,774    | 91,044            | 85,999    |
| (Benefit)/provision for income taxes                   | (15,406 )          | 7,498     | (872 )            | 22,484    |
| Income from continuing operations                      | 26,815             | 17,276    | 91,916            | 63,515    |
| (Loss)/income from discontinued operations, net of tax | (86 )              | 20        | (710 )            | (1,324 )  |
| Net income   | \$26,729           | \$17,296  | \$91,206          | \$62,191  |
| Basic earnings/(loss) per share of common stock:       |                    |           |                   |           |
| Income from continuing operations                      | \$0.80             | \$0.53    | \$2.77            | \$1.95    |
| Loss from discontinued operations, net of tax          | \$(0.00 )          | \$0.00    | \$(0.02 )         | \$(0.04 ) |
| Net income   | \$0.80             | \$0.53    | \$2.75            | \$1.91    |
| Diluted earnings/(loss) per share of common stock:     |                    |           |                   |           |
| Income from continuing operations                      | \$0.79             | \$0.52    | \$2.73            | \$1.90    |
| Loss from discontinued operations, net of tax          | \$(0.00 )          | \$0.00    | \$(0.02 )         | \$(0.04 ) |
| Net income   | \$0.79             | \$0.52    | \$2.71            | \$1.86    |
| Weighted average shares outstanding:                   |                    |           |                   |           |
| Basic  | 33,406             | 32,749    | 33,130            | 32,612    |
| Effect of dilutive stock based compensation            | 486                | 763       | 573               | 839       |
| Diluted  | 33,892             | 33,512    | 33,703            | 33,451    |

See accompanying notes to unaudited consolidated financial statements.

4

---

## CAMBREX CORPORATION AND SUBSIDIARIES

## Consolidated Statements of Comprehensive Income

(unaudited – in thousands)

|  | Three Months<br>Ended<br>September 30, |          | Nine Months<br>Ended<br>September 30, |          |
|--|--|----------|---------------------------------------|----------|
|  | 2018                                   | 2017     | 2018                                  | 2017     |
| Net income   | \$26,729                               | \$17,296 | \$91,206                              | \$62,191 |
| Other comprehensive income/(loss):   |  |          |                                       |          |
| Foreign currency translation adjustments   | 32                                     | 7,006    | (10,504)                              | 19,753   |
| Pension plan amortization of net actuarial loss and<br>prior service cost, net of tax of \$69, \$118,<br>\$246 and \$350 at respective dates | 202                                    | 250      | 703                                   | 737      |
| Comprehensive income   | \$26,963                               | \$24,552 | \$81,405                              | \$82,681 |

See accompanying notes to unaudited consolidated financial statements.

5

---

## CAMBREX CORPORATION AND SUBSIDIARIES

## Consolidated Statements of Cash Flows

(unaudited – in thousands)

|  | Nine Months Ended<br>September 30, |           |
|--|------------------------------------|-----------|
|  | 2018                               | 2017      |
| Cash flows from operating activities:                        |                                    |           |
| Net income   | \$91,206                           | \$62,191  |
| Adjustments to reconcile net income to net cash provided by  |                                    |           |
| operating activities:  |                                    |           |
| Depreciation and amortization                                | 24,203                             | 23,023    |
| Non-cash deferred revenue                                    | (1,116 )                           | (4,991 )  |
| Increase in inventory reserve                                | 5,687                              | 3,217     |
| Unrealized gain on investment in equity securities           | (10,757 )                          | -         |
| Unrealized gain on foreign currency contracts                | (1,582 )                           | -         |
| Stock based compensation                                     | 4,106                              | 6,321     |
| Deferred income tax provision                                | (14,025 )                          | 1,087     |
| Other  | (146 )                             | 516       |
| Changes in assets and liabilities:                           |                                    |           |
| Account receivables  | 12,144                             | 35,995    |
| Contract assets  | (58,147 )                          | -         |
| Inventories  | 1,747                              | (38,245 ) |
| Prepaid expenses and other current assets                    | 6,446                              | (70 )     |
| Accounts payable and other current liabilities               | (17,476 )                          | (16,422 ) |
| Contract liabilities, current                                | 471                                | 512       |
| Other non-current assets and liabilities                     | (3,338 )                           | (2,282 )  |
| Discontinued operations:                                     |                                    |           |
| Non-current liabilities                                      | 898                                | 2,418     |
| Net cash used in discontinued operations                     | (557 )                             | (1,185 )  |
| Net cash provided by operating activities                    | 39,764                             | 72,085    |
| Cash flows from investing activities:                        |                                    |           |
| Capital expenditures   | (43,545 )                          | (38,241 ) |
| Proceeds from sale of business                               | -                                  | 2,836     |
| Acquisition of business, net of cash acquired                | (418,963)                          | -         |
| Net cash used in investing activities                        | (462,508)                          | (35,405 ) |
| Cash flows from financing activities:                        |                                    |           |
| Borrowings   | 325,000                            | -         |
| Proceeds from stock options exercised                        | 12,685                             | 3,448     |
| Net cash provided by financing activities                    | 337,685                            | 3,448     |
| Effect of exchange rate changes on cash and cash equivalents | (1,090 )                           | 4,134     |
| Net (decrease)/increase in cash and cash equivalents         | (86,149 )                          | 44,262    |
| Cash and cash equivalents at beginning of period             | 183,284                            | 74,141    |
| Cash and cash equivalents at end of period                   | \$97,135                           | \$118,403 |

See accompanying notes to unaudited consolidated financial statements.

6

---

## CAMBREX CORPORATION AND SUBSIDIARIES

### Notes to Consolidated Financial Statements

(in thousands, except share data)

(Unaudited)

#### (1) Basis of Presentation

Unless otherwise indicated by the context, "Cambrex" or the "Company" means Cambrex Corporation and subsidiaries.

On September 12, 2018, the Company acquired Halo Pharma ("Halo"). The results of Halo have been included in the consolidated results since the acquisition date. As a result of the acquisition of Halo, the Company now reports its results in two segments, Active Pharmaceutical Ingredients ("API's") and Finished Dosage Form ("FDF"). See Note 4 for additional information on the Halo acquisition.

The accompanying unaudited consolidated financial statements have been prepared from the records of the Company. In the opinion of management, the financial statements include all adjustments, which are of a normal and recurring nature, except as otherwise described herein, and are necessary for a fair statement of financial position and results of operations in conformity with U.S. generally accepted accounting principles ("GAAP"). These interim financial statements should be read in conjunction with the financial statements for the year ended December 31, 2017.

The results of operations of any interim period are not necessarily indicative of the results expected for the full year.

For all periods presented, financial results for discontinued operations relate to environmental investigation and remediation at sites of divested businesses.

Certain reclassifications have been made to prior year amounts to conform with the current year presentation.

#### (2) Impact of Recently Issued Accounting Pronouncements

The following accounting pronouncements became effective for the Company January 1, 2018:

##### Revenue from Contracts with Customers

In May 2014, the FASB issued ASU 2014-09 which introduces a new five-step revenue recognition model in which an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services.

On January 1, 2018, the Company adopted the new accounting standard ASC Topic 606, Revenue from Contracts with Customers and all the related amendments ("new revenue standard") to all contracts not completed as of January 1, 2018 using the modified retrospective method. The cumulative effect of initially applying the new revenue standard was \$16,219 and has been recorded as an adjustment to increase the opening balance of retained earnings. The cumulative effect adjustment relates primarily to the recognition of revenue and costs for contracts that transfer promised goods or services over time. Gross sales, cost of goods sold, and tax expense of \$51,896, \$31,347, and \$4,330 respectively, were recorded as part of the cumulative effect adjustment. The comparative information has not

been restated and is reported in accordance with accounting standard Topic 605, which was in effect for those periods.

7

---



## CAMBREX CORPORATION AND SUBSIDIARIES

## Notes to Consolidated Financial Statements

(in thousands, except share data)

(Unaudited)

The adoption of the new revenue standard impacted the consolidated financial statements as follows:

## Income Statement

|                                   | For the Three Months     |          |             |
|-----------------------------------|--------------------------|----------|-------------|
|                                   | Ended September 30, 2018 |          |             |
|                                   | Amount                   |          |             |
|                                   | Without                  |          |             |
|                                   | As                       | Effect   | Adoption of |
|                                   | Reported                 | of       | ASC 606     |
|                                   | Change                   |          |             |
| Gross sales                       | \$ 104,231               | \$ 1,914 | \$ 102,317  |
| Net revenue                       | 104,618                  | 1,914    | 102,704     |
| Cost of goods sold                | 71,893                   | 8,475    | 63,418      |
| Gross profit                      | 32,725                   | (6,561 ) | 39,286      |
| Operating profit                  | 6,632                    | (6,561 ) | 13,193      |
| Benefit for income taxes          | (15,406 )                | (1,558 ) | (13,848 )   |
| Income from continuing operations | 26,815                   | (5,003 ) | 31,818      |
| Net income                        | 26,729                   | (5,003 ) | 31,732      |
| Diluted earnings per share from   |                          |          |             |
| continuing operations             | 0.79                     | (0.15 )  | 0.94        |

## For the Nine Months

Ended September 30, 2018  
Amount

Without

As Effect Adoption of  
Reported of  
Change ASC 606

Edgar Filing: CAMBREX CORP - Form 10-Q

|                                      |           |          |           |
|--------------------------------------|-----------|----------|-----------|
| Gross sales                          | \$390,575 | \$58,182 | \$332,393 |
| Net revenue                          | 397,761   | 58,182   | 339,579   |
| Cost of goods sold                   | 249,389   | 33,194   | 216,195   |
| Gross profit                         | 148,372   | 24,988   | 123,384   |
| Operating profit                     | 81,665    | 24,988   | 56,677    |
| (Benefit)/provision for income taxes | (872 )    | 5,076    | (5,948 )  |
| Income from continuing operations    | 91,916    | 19,912   | 72,004    |
| Net income                           | 91,206    | 19,912   | 71,294    |
| Diluted earnings per share from      |           |          |           |
| continuing operations                | 2.73      | 0.59     | 2.14      |

8

---

## CAMBREX CORPORATION AND SUBSIDIARIES

## Notes to Consolidated Financial Statements

(in thousands, except share data)

(Unaudited)

## Balance Sheet

|                             | September 30, 2018 |            |             |
|-----------------------------|--------------------|------------|-------------|
|                             | Balances           |            |             |
|                             | Without            |            |             |
|                             | As                 | Effect of  | Adoption of |
|                             | Reported           | Change     | ASC 606     |
| <b>Current Assets</b>       |                    |            |             |
| Contract assets             | \$ 112,845         | \$ 112,845 | \$ -        |
| Inventory                   | 103,648            | (66,905 )  | 170,553     |
| <b>Current Liabilities</b>  |                    |            |             |
| Taxes payable               | 2,727              | 9,405      | (6,678 )    |
| <b>Stockholders' Equity</b> |                    |            |             |
| Retained earnings           | 537,251            | 36,131     | 501,120     |

## Presentation of Net Periodic Benefit Cost Related to Defined Benefit Plans

In March 2017, the FASB issued ASU 2017-07 which amends the requirements in ASC 715 related to the income statement presentation of the components of net periodic benefit cost for an entity's sponsored defined pension and other postretirement plans. The ASU requires entities to disaggregate the current-service-cost component from the other components of net benefit cost and present it with other current compensation costs for related employees in the income statement and present the other components elsewhere in the income statement and outside of income from operations if such subtotal is presented. This standard became effective for the Company on January 1, 2018. For the three and nine months ended September 30, 2018, the Company recorded \$167 and \$649, respectively, to "Other expenses, net" which formerly would have been recorded as "Selling, general and administrative expenses" or "Cost of goods sold." To conform to the current year presentation, for the three and nine months ended September 30, 2017 the Company reclassified \$384 and \$1,107, respectively, from "Selling, general and administrative expenses" and \$54 and \$161, respectively, from "Cost of goods sold" to "Other expenses, net."

## Scope of Modification Accounting, Stock Based Compensation

In May 2017, the FASB issued ASU 2017-09 which provides clarification on when modification accounting should be used for changes to the terms or conditions of a share-based payment award. This ASU does not change the

accounting for modifications but clarifies that modification accounting guidance should only be applied if there is a change to the value, vesting conditions, or award classification and would not be required if the changes are considered non-substantive. The update became effective on January 1, 2018 and did not have a material impact on the Company's consolidated financial statements.

#### Business Combinations – Clarifying the Definition of a Business

In January 2017, the FASB issued ASU 2017-01 which clarifies the definition of a business to assist entities with evaluating whether transactions should be accounted for as acquisitions or disposals of assets or businesses. The standard introduces a screen for determining when assets acquired are not a business and clarifies that a business must include, at a minimum, an input and a substantive process that contribute to an output to be considered a business. The amendment became effective on January 1, 2018 and did not have a material impact on the Company's consolidated financial statements.

CAMBREX CORPORATION AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(in thousands, except share data)

(Unaudited)

Statement of Cash Flows - Classification of Certain Cash Receipts and Cash Payments

In August 2016, the FASB issued ASU 2016-15 which provides guidance on the presentation and classification in the statement of cash flows for specific cash receipt and payment transactions, including debt prepayment or extinguishment costs, contingent consideration payments made after a business combination, proceeds from the settlement of insurance claims and corporate-owned life insurance policies, and distributions received from equity method investees. The standard became effective on January 1, 2018 and did not have a material impact on the Company's consolidated financial statements.

Statement of Cash Flows – Restricted Cash

In November 2016, the FASB issued ASU 2016-18 which clarifies the presentation requirements of restricted cash within the statement of cash flows. The changes in restricted cash and restricted cash equivalents during the period should be included in the beginning and ending cash and cash equivalents balance reconciliation on the statement of cash flows. When cash, cash equivalents, restricted cash or restricted cash equivalents are presented in more than one line item within the statement of financial position, an entity shall calculate a total cash amount in a narrative or tabular format that agrees to the amount shown on the statement of cash flows. Details on the nature and amounts of restricted cash should also be disclosed. The update became effective on January 1, 2018 and did not have a material impact on the Company's consolidated financial statements.

Recognition and Measurement of Financial Assets and Financial Liabilities

In January 2016, the FASB issued ASU 2016-01, Recognition and Measurement of Financial Assets and Financial Liabilities. The ASU amends guidance on the classification and measurement of financial instruments, including significant revisions in accounting related to the classification and measurement of investments in equity securities and presentation of certain fair value changes for financial liabilities when the fair value option is elected. The ASU requires equity securities to be measured at fair value with changes in fair value recognized through net earnings and amends certain disclosure requirements associated with the fair value of financial instruments. In the period of adoption, the Company is required to reclassify the unrealized gains/losses on equity securities within accumulated other comprehensive income/(loss) to retained earnings. In February 2018, the FASB issued ASU 2018-03, Technical Corrections and Improvements to Financial Instruments—Overall (Subtopic 825-10), which clarified certain aspects of the previously issued ASU. The ASU was adopted by the Company on January 1, 2018 and did not have a material effect on the Company's consolidated financial statements.

The following recently issued accounting pronouncements will become effective for the Company in future periods:

Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income

In February 2018, the FASB issued ASU 2018-02 to address the tax effects of the Tax Cuts & Jobs Act (“TCJA”) on amounts that were initially recognized directly in AOCI. ASU 2018-02 allows an entity to elect a one-time reclassification from AOCI to retained earnings of stranded tax effects due to the enactment of TCJA, equal to the difference between the amount initially charged or credited directly to AOCI at the previously enacted U.S. federal corporate income tax rate and the amount that would have been charged or credited directly to AOCI by using the newly enacted tax rate, excluding the effect of any valuation allowance previously charged to income from continuing operations. ASU 2018-02 is effective for fiscal years beginning after December 15, 2018, and interim periods within those fiscal years. The Company has evaluated the provisions of ASU 2018-02 and has determined it will not elect the reclassification from AOCI to retained earnings addressed in the ASU.

CAMBREX CORPORATION AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(in thousands, except share data)

(Unaudited)

Effects of the Tax Cuts and Jobs Act

In March 2018, the FASB issued ASU 2018-05, Income Taxes (Topic 740): Amendments to SEC Paragraphs Pursuant to SEC Staff Accounting Bulletin No. 118 (“SAB No. 118”) which allowed SEC registrants to record provisional amounts for the year ended December 31, 2017 due to the complexities involved in accounting for the enactment of TCJA. The Company recognized the estimated income tax effects of TCJA in its 2017 Consolidated Financial Statements in accordance with SAB No. 118. Refer to Note 7 for further information. The Company’s accounting for the TCJA one-time toll charge on previously undistributed accumulated foreign earnings has been completed, resulting in a \$2,105 measurement period tax benefit and corresponding reduction in taxes payable. In accordance with SAB No. 118, any additional adjustment to the financial reporting impacts of TCJA will be completed by December 31, 2018.

Improvements to Nonemployee Share-Based Payment Accounting

In June 2018, the FASB issued ASU 2018-07 which aligns the accounting for share-based payment awards issued to nonemployees with those issued to employees. Under the new guidance, the nonemployee awards will be measured on the grant date and compensation costs will be recognized when achievement of the performance condition is probable. This new standard is effective for fiscal years beginning after December 15, 2018, including interim periods within that fiscal year. Early adoption is permitted. The Company is currently evaluating the new guidance and does not expect it to have a material impact on its consolidated financial statements.

Changes to the Disclosure Requirements for Fair Value Measurement

In August 2018, the FASB issued ASU 2018-13 which modifies the disclosure requirements for recurring and nonrecurring fair value measurements, primarily those surrounding Level 3 fair value measurements and transfers between Level 1 and Level 2. The new standard is effective for fiscal years beginning after December 15, 2019, including interim periods within that reporting period. The Company is currently evaluating the new guidance and does not expect it to have an impact on its consolidated financial statements.

Changes to the Disclosure Requirements for Defined Benefit Plans

In August 2018, the FASB issued ASU 2018-14 which adds, modifies and removes certain disclosure requirements to improve the effectiveness of disclosures for defined benefit plans. The new standard is effective for fiscal years beginning after December 15, 2020, including interim periods within that reporting period. The Company is currently evaluating the new guidance and does not expect it to have an impact on its consolidated financial statements.

Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement that is a Service Contract

In August 2018, the FASB issued ASU 2018-15 which states entities should apply the guidance in ASC 350-40 when capitalizing implementation costs related to a hosting arrangement that is a service contract. The capitalized implementation costs should be classified as prepaid expenses and then expensed over the hosting arrangement’s term,

with the expense recorded on the same line of the income statement as the service contract. The new standard is effective for fiscal years beginning after December 15, 2019, including interim periods within that reporting period. The Company is currently assessing the impact that adopting this new accounting standard will have on its consolidated financial statements.



CAMBREX CORPORATION AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(in thousands, except share data)

(Unaudited)

Leases

In February 2016, the FASB issued ASU 2016-02 which requires lessees to recognize right of use assets and lease liabilities on the balance sheet for all leases with terms greater than twelve months. This standard is effective for fiscal years beginning after December 15, 2018, including interim periods within that reporting period. At this time, the Company has no significant financing leases and only a limited number of operating leases. The result of adoption will be an increase to assets and liabilities by the same amount for the identified operating leases. Several updates have been issued in 2018 that provide clarification on a number of specific issues and reporting requirements. The Company is currently evaluating the new guidance and does not expect the adjustment will be material to the Company, assuming there is not an increase in lease activity.

Simplifying the Test for Goodwill Impairment

In January 2017, the FASB issued ASU 2017-04 which simplifies the goodwill impairment test by eliminating Step 2 in the determination on whether goodwill should be considered impaired. Instead, an impairment charge should equal the amount by which a reporting unit's carrying amount exceeds its fair value, not to exceed the amount of goodwill allocated to the reporting unit. The new standard is effective for fiscal years beginning after December 15, 2019, including interim periods within that reporting period. The Company is currently evaluating the new guidance and does not expect it to have an impact on its consolidated financial statements.

Targeted Improvements to Accounting for Hedging Activities

In August 2017, the FASB issued ASU 2017-12 which improves the financial reporting of hedging relationships to better portray the economic results of an entity's risk management activities in its financial statements. The standard also makes certain targeted improvements to simplify the application of the hedge accounting guidance. The amendment is effective for fiscal years beginning after December 15, 2018, including interim periods within that reporting period. The Company is currently assessing the impact that adopting this new accounting standard will have on its consolidated financial statements.

(3) Revenue

In accordance with ASC 606, the Company disaggregates its revenue from customers with contracts by revenue streams. The Company's revenue streams are presented in the following table:

| Three Months<br>Ended<br>September 30,<br>2018 | Nine Months<br>Ended<br>September 30,<br>2018 |
|--|---|
|--|---|

Edgar Filing: CAMBREX CORP - Form 10-Q

|                     |            |            |
|---------------------|------------|------------|
| Single-use products | \$ 58,731  | \$ 205,944 |
| Multi-use products  | 39,037     | 168,310    |
| Service revenue     | 6,463      | 16,321     |
| Total gross sales   | \$ 104,231 | \$ 390,575 |

CAMBREX CORPORATION AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(in thousands, except share data)

(Unaudited)

Revenue is recognized when control over a product or service is transferred to a customer. Revenue is measured as the amount of consideration expected in exchange for transferring goods or providing services.

Sales terms to certain customers include rebates if certain conditions are met. Additionally, sales are generally made with a limited right of return under certain conditions. The Company estimates these rebates and returns at the time of sale based on the terms of agreements with customers and historical experience and estimated orders. The Company recognizes revenue net of these estimated costs which are classified as allowances and rebates.

The Company does not disclose the value of unsatisfied performance obligations for contracts with an original expected length of one year or less. The Company does not have any unsatisfied performance obligations for contracts greater than one year. The costs incurred to obtain or fulfill a contract are not material.

For variable consideration arrangements where the transaction price fluctuates based on quantity, the most likely estimated quantity is assumed using forecasts provided by the customer.

Single-use products

In most single-use product sales, a quantity is ordered and manufactured according to the customer's specifications and typically only one performance obligation is included. The Company also manufactures early phase product that can be included in a contract with services. These services are distinct and separated from the product performance obligations and are shown as a service revenue stream. The products are manufactured exclusively for a specific customer and have no alternative use. Generally, under these customer agreements, the Company is entitled to consideration for progress to date that includes an element of profit margin. To the extent an agreement does not include an element of profit margin for progress to date, it is recognized at a point in time. Revenues that are recognized over time utilize a measure of progress toward satisfaction of the performance obligations. The Company measures progress using an input method which compares the cost of cumulative work in process to date to the most current estimates for the entire performance obligation. The raw materials are excluded from this measurement due to the high value and inclusion in the early stages of the project that would otherwise overstate progress to date.

Multi-use products

The Company's multi-use product sales can be sold to multiple customers and have an alternative use. Both the transaction sales price and shipping terms are agreed upon in the contract. For these products, all revenue is recognized at a point in time, generally when title to products and risk of loss is transferred to the customers based upon shipping terms. These arrangements typically include only one performance obligation.

Service revenue

The service revenue stream represents services provided to a customer to assist with early stages of the regulatory approval process. The customer owns the drug details and process. The Company works with its customers to develop, validate and document the production process in order to comply with the regulatory approval process. These

custom development projects could have one or more performance obligations with no alternative use. The contracts are structured to ensure the Company is paid for in-process work, including a profit margin. Revenues related to this stream are recognized over time by allocating to each performance obligation the best estimate of the standalone selling price of each service. The Company measures progress using an input method which compares the cost of cumulative work in process to date to the most current estimates for the entire performance obligation. Standalone selling prices are generally based on the prices charged to customers or based on an expected cost-plus margin.

13

---

## CAMBREX CORPORATION AND SUBSIDIARIES

## Notes to Consolidated Financial Statements

(in thousands, except share data)

(Unaudited)

## Contract balances

The timing of revenue recognition, billings and cash collections results in billed trade receivables, contracts assets (unbilled receivables), and contract liabilities (customer advances and deferred revenue). For each reporting period presented, the Company reports contract balances in a net contract asset or liability position on a contract-by-contract basis. Contract assets are recorded when the right to consideration is conditioned on something other than the passage of time. When an entity's right to consideration is unconditional, the receivable is recorded within Trade Receivables on the balance sheet. Contract liabilities represent advance payments from customers, and deferred revenue. Contract assets will convert to trade receivables or cash and current contract liabilities will convert into revenue within a one-year period.

Payment terms can vary by the type and location of the customer and the products or services offered. The term between invoicing and when payment is due is not significant. For certain products or services and customer types, payment prior to satisfaction of a performance obligation can be required, and results in recording a contract liability.

The following table details the significant changes in contract assets during the nine months ended September 30, 2018:

|   | Contract  |
|---|-----------|
|   | Assets    |
| Balance as of January 1, 2018                   | \$51,896  |
| Contracts assets acquired                       | 3,749     |
| Revenue recognized from performance obligations |           |
| satisfied                                       | 201,210   |
| Transferred to trade receivables                | (143,094) |
| Currency impact                                 | (916 )    |
| Balance as of September 30, 2018                | \$112,845 |

The Company recognized in revenue \$1,116 during the nine months ended September 30, 2018 for which the contract liability was recorded in a prior period.

## (4) Acquisitions

On September 12, 2018, the Company completed the acquisition of 100% of Halo Pharma ("Halo"), a finished dosage form Contract Development and Manufacturing Organization. The deal was structured as a stock purchase for

consideration of \$425,000. The Company utilized cash on hand and borrowings under the credit facility to pay the purchase price. Cambrex acquired two GMP compliant facilities, one in Whippany, NJ, the other in Mirabel, Quebec.

The addition of Halo adds formulation development and finished dosage manufacturing capabilities to the Company's existing global API manufacturing network. These newly acquired facilities provide formulation development and clinical and commercial manufacturing services, specializing in oral solids, liquids, creams, sterile and non-sterile ointments. The facilities core competencies include developing and manufacturing highly complex and difficult to produce formulations, products for pediatric indications and controlled substances.

## CAMBREX CORPORATION AND SUBSIDIARIES

## Notes to Consolidated Financial Statements

(in thousands, except share data)

(Unaudited)

The following table summarizes the estimated fair value of the assets acquired and liabilities assumed at the acquisition date. Cambrex is in the process of obtaining third-party valuations of certain tangible and intangible assets; thus the provisional measurements of property, plant and equipment, intangible assets, goodwill and deferred income taxes are subject to change.

|  | September<br>12, 2018 |
|--|-----------------------|
| Cash                                   | \$ 2,792              |
| Account receivable and Contract assets | 14,045                |
| Inventory                              | 8,298                 |
| Other current assets                   | 1,110                 |
| Property, plant and equipment          | 78,364                |
| Goodwill                               | 228,504               |
| Intangible assets                      | 180,000               |
| Total assets acquired                  | 513,113               |
| Current liabilities                    | 16,058                |
| Noncurrent liabilities                 | 69,666                |
| Total liabilities assumed              | \$ 85,724             |

Transaction costs have been expensed and totaled \$6,460 for the three and nine months ended September 30, 2018. These costs have been recorded to "Acquisition and integration expenses" on the Company's income statement.

The consolidated income statement from the acquisition date to the period ending September 30, 2018 included revenue of \$5,154 and net income of \$86. These results include integration costs of \$394.

## (5) Net Inventories

Inventories are stated at the lower of cost and net realizable value. Cost is determined on a first-in, first-out basis.

Net inventories consist of the following:

|                 | September 30,<br>2018 | December 31,<br>2017 |
|-----------------|-----------------------|----------------------|
| Finished goods  | \$ 26,016             | \$ 41,521            |
| Work in process | 23,076                | 47,386               |
| Raw materials   | 46,666                | 42,491               |
| Supplies        | 7,890                 | 7,144                |

|       |            |            |
|-------|------------|------------|
| Total | \$ 103,648 | \$ 138,542 |
|-------|------------|------------|



## CAMBREX CORPORATION AND SUBSIDIARIES

## Notes to Consolidated Financial Statements

(in thousands, except share data)

(Unaudited)

## (6) Goodwill and Intangible Assets

The change in the carrying amount of goodwill for the nine months ended September 30, 2018, is as follows:

|                                      |           |
|--------------------------------------|-----------|
| Balance as of December 31, 2017      | \$43,626  |
| Acquisition of business (see Note 4) | 228,504   |
| Translation effect                   | (706 )    |
| Balance as of September 30, 2018     | \$271,424 |

As of September 30, 2018, goodwill of \$228,747 relates to the FDF segment. The remaining goodwill relates to the API segment.

Acquired intangible assets, which are amortized, consist of the following:

|                              | Period        | As of September 30, 2018 |              |             |
|------------------------------|---------------|--------------------------|--------------|-------------|
|                              |               | Gross                    |              | Net         |
|                              |               | Amortization             | Carrying     | Accumulated |
|                              |               | Amount                   | Amortization | Amount      |
| Internal-use software        | 3 - 7 years   | \$7,034                  | \$ (2,636 )  | \$4,398     |
| Technology-based intangibles | 20 years      | 3,519                    | (1,496 )     | 2,023       |
| Customer-related intangibles | 10 - 15 years | 187,942                  | (2,404 )     | 185,538     |
|                              |               | \$198,495                | \$ (6,536 )  | \$191,959   |

  

|                              | Period        | As of December 31, 2017 |              |             |
|------------------------------|---------------|-------------------------|--------------|-------------|
|                              |               | Gross                   |              | Net         |
|                              |               | Amortization            | Carrying     | Accumulated |
|                              |               | Amount                  | Amortization | Amount      |
| Internal-use software        | 3 - 7 years   | \$7,074                 | \$ (1,810 )  | \$5,264     |
| Technology-based intangibles | 20 years      | 3,646                   | (1,413 )     | 2,233       |
| Customer-related intangibles | 10 - 15 years | 7,608                   | (1,237 )     | 6,371       |

\$ 18,328   \$ (4,460   )   \$ 13,868

The change in the gross carrying amount in 2018 is mainly due to the provisional recognition of customer-related intangibles of \$180,000 due to the acquisition of Halo Pharma in September 2018 and the impact of foreign currency translation. The change in the gross carrying amount in 2017 is mainly due to foreign currency translation and additions.

Amortization expense was \$1,134 and \$2,157 for the three and nine months ended September 30, 2018, respectively. This includes amortization expense of \$627 related to the acquisition of Halo Pharma. Amortization expense was \$477 and \$1,375 for the three and nine months ended September 30, 2017, respectively.

Amortization expense related to intangible assets is expected to be approximately \$5,043 for 2018, \$14,053 for 2019, \$14,037 for 2020, \$14,031 for 2021, and \$13,610 for 2022.

CAMBREX CORPORATION AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(in thousands, except share data)

(Unaudited)

(7) Income Taxes

Income tax benefit from continuing operations for the three and nine months ended September 30, 2018 was \$15,406 and \$872, respectively, compared to expense of \$7,498 and \$22,484 for the three and nine months ended September 30, 2017, respectively. The Company's provisional accounting for TCJA's toll charge on previously undistributed accumulated foreign earnings at December 31, 2017 has been completed in the period ending September 30, 2018, resulting in a \$2,105 measurement period tax benefit. In accordance with SAB No. 118, any additional adjustment to the financial reporting impacts of TCJA will be completed by December 31, 2018.

The income tax benefit for the three and nine months ended September 30, 2018 includes the impacts of immediately recognizing certain effects of share-based compensation, acquisition and integration expenses, unrealized gain on investment in equity securities, and benefits for finalizing the TCJA toll charge and New Jersey tax reform. Excluding these items, the effective tax rate would have been 19.6% and 20.5% for the three and nine months ended September 30, 2018, respectively, compared to 33.2% and 32.1% for the three and nine months ended September 30, 2017, respectively.

The Company has determined it will elect the accounting policy to treat tax on global intangible low-taxed income ("GILTI") inclusions under TCJA as a component of current tax expense in its estimated annual effective tax rate. This accounting policy election is now complete.

In July 2018, New Jersey enacted comprehensive corporate income tax reform legislation which includes, among other items, the imposition of a multi-year temporary surtax, mandatory combined reporting, revised net operating loss ("NOL") and dividend exclusion rules, and decoupling from certain federal tax reform provisions. Additionally, in October 2018 New Jersey enacted legislation that included significant technical corrections and clarifications to the July law as well as other substantive changes to the State's corporate tax regime. GAAP requires that the effects of a change in tax law be recorded in the period of enactment. Therefore, the Company has included the effects of New Jersey's July tax law change in the results for the quarter ended September 30, 2018. This includes a discrete benefit of \$11,437 to release valuation allowance against state NOLs and state net deferred tax assets against which the Company had previously maintained a full valuation allowance due to restrictive rules regarding realization, and a discrete benefit of \$752 for revaluing state tax attributes and net deferred tax assets due to the New Jersey surtax. The Company currently estimates it will record a non-cash charge of approximately \$1,600 in the quarter ended December 31, 2018 due to New Jersey's October tax law change.

The Company considers both positive and negative evidence related to the likelihood of realization of deferred tax assets. If, based on the weight of available evidence, it is more likely than not the deferred tax assets will not be realized, the Company records a valuation allowance against all or a portion of the deferred tax assets to adjust the balance to the amount considered more likely than not to be realized. The weight given to the positive and negative evidence is commensurate with the extent to which the evidence may be objectively verified.

CAMBREX CORPORATION AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(in thousands, except share data)

(Unaudited)

This assessment, which is completed on a taxing jurisdiction basis, takes into account a number of types of evidence, including the following:

- Nature, frequency, and severity of current and cumulative financial reporting losses. A pattern of objectively-measured recent financial reporting losses is heavily weighted as a source of negative evidence. The Company generally considers cumulative pre-tax losses in the current three-year period to be significant negative evidence regarding future profitability. The Company also considers the strength and trend of earnings, as well as other relevant factors. In certain circumstances, historical information may not be as relevant due to changes in the Company's business operations;
- Sources of future taxable income. Future reversals of existing taxable temporary differences are heavily-weighted sources of objectively verifiable evidence. Projections of future taxable income exclusive of reversing temporary differences are a source of positive evidence only when the projections are combined with a history of recent profits and can be reasonably estimated; and
- Tax planning strategies. Prudent and feasible tax planning strategies that would be implemented to maximize utilization of expiring tax credit carryforwards are evaluated as a source of additional positive evidence.

New Jersey's change to combined reporting will allow the Company to use existing state NOLs to offset a portion of the Company's combined domestic income that will be taxed by New Jersey. On a New Jersey combined basis the Company has significant existing taxable temporary differences along with a sustained period of profitability and expectations of future profitability of sufficient amounts, therefore the Company has reversed its valuation allowance against certain state NOLs and state net deferred tax assets in the quarter ended September 31, 2018.

(8) Long-term Debt

In May 2016, the Company entered into a \$500,000 five-year Syndicated Senior Revolving Credit Facility ("Credit Facility") which expires in May 2021. The Company pays interest on this Credit Facility at LIBOR plus 1.25% - 2.00% based upon certain financial measurements. The Credit Facility also includes financial covenants regarding interest coverage and leverage ratios. The Company was in compliance with all financial covenants at September 30, 2018 and December 31, 2017. As of September 30, 2018, there was \$325,000 outstanding on the Credit Facility. As of December 31, 2017, the facility was undrawn. The 2018 weighted average interest rate for long-term bank debt was 3.6%.

(9) Derivatives

The Company operates internationally and is exposed to fluctuations in foreign exchange rates and interest rates in the normal course of business. The Company, from time to time, uses derivatives to reduce exposure to market risks resulting from fluctuations in interest rates and foreign exchange rates.

All financial instruments involve market and credit risks. The Company is exposed to credit losses in the event of non-performance by the counterparties to the contracts. While there can be no assurance, the Company does not anticipate non-performance by these counterparties.

Foreign Currency Forward Contracts

The Company periodically enters into foreign currency forward contracts to protect against currency fluctuations of forecasted cash flows and existing balance sheet exposures at its foreign operations, as deemed appropriate. The Company may or may not elect to designate certain forward contracts for hedge accounting treatment.

18

---

## CAMBREX CORPORATION AND SUBSIDIARIES

## Notes to Consolidated Financial Statements

(in thousands, except share data)

(Unaudited)

For derivatives that are not designated for hedge accounting treatment, changes in the fair value are immediately recognized in earnings. This treatment has the potential to increase volatility of the Company's earnings.

None of the foreign currency forward contracts entered into during the nine months ended September 30, 2018 and 2017 were designated for hedge accounting treatment. The notional amounts of the Company's outstanding foreign exchange forward contracts were \$63,918 and \$32,781 at September 30, 2018 and December 31, 2017, respectively. The Company does not hold or purchase any foreign currency forward contracts for trading or speculative purposes and no contractual term is greater than twelve months.

The fair value of the Company's foreign exchange forward contracts outstanding was a gain of \$1,582 and \$83 at September 30, 2018 and December 31, 2017, respectively. Losses are recorded in "Accrued expenses and other current liabilities" and gains are recorded in "Prepaid expenses and other current assets" on the balance sheet and "Other revenues, net" on the income statement.

## (10) Fair Value Measurements

Accounting standards establish a valuation hierarchy for disclosure of the inputs to the valuations used to measure fair value. This hierarchy prioritizes the inputs into three broad levels as follows: Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities; Level 2 inputs are quoted prices for similar assets and liabilities in active markets, quoted prices for identical or similar assets in markets that are not active, inputs other than quoted prices that are observable for the asset or liability, including interest rates, yield curves and credit risks, or inputs that are derived principally from, or corroborated by, observable market data through correlation; Level 3 inputs are unobservable inputs based on the Company's assumptions used to measure assets and liabilities at fair value. A financial asset or liability's classification within the hierarchy is determined based on the lowest level input that is significant to the fair value measurement.

The following table provides the assets carried at fair value, measured on a recurring basis, as of September 30, 2018 and December 31, 2017:

|                                 | September 30, | December 31, |
|---------------------------------|---------------|--------------|
| Fair Value - Level 2            | 2018          | 2017         |
| Foreign currency forwards       | \$ 1,582      | \$ 83        |
| Investment in equity securities | 10,825        | -            |
|                                 | \$ 12,407     | \$ 83        |

The Company's foreign currency forward contracts are measured at fair value using observable market inputs such as forward rates, the Company's credit risk and its counterparties' credit risks. Based on the Company's continued ability to enter into forward contracts, the Company considers the markets for its fair value instruments to be active.

During the second quarter of 2018, the Company acquired a 19.9% equity investment in a European company (“Investee”). The Investee completed an initial public offering on a foreign exchange late in the quarter, which reduced the Company’s ownership share to 16.3%. The Company’s investment is subject to a one-year prohibition on selling the shares. The Company has one seat on the Board of Directors of the investee and concluded it is able to exercise significant influence and that equity accounting would be appropriate. In accordance with ASC 825, the Company has elected to record this investment at fair value. The Company selected an appropriate valuation methodology to compute a discount for the lack of

## CAMBREX CORPORATION AND SUBSIDIARIES

## Notes to Consolidated Financial Statements

(in thousands, except share data)

(Unaudited)

marketability to be applied to the closing market price of the shares as of September 30, 2018. The fair value of the Company's shares increased to \$10,825 during the nine months ended September 30, 2018 resulting in an unrealized gain that was recorded as "Unrealized gain on investment in equity securities" on the income statement. Since the shares owned by the Company are substantially in excess of the daily trade volumes of the stock, it could be difficult to sell the shares in a timely manner when the restrictions lapse and it is possible the ultimate value to be realized by the Company could be significantly less upon a sale of the securities.

The Company's financial instruments also include cash and cash equivalents, accounts receivables and accounts payables. The carrying amount of these instruments approximates fair value because of their short-term nature.

## (11) Accumulated Other Comprehensive Income/(Loss)

The following tables provide the changes in Accumulated other comprehensive income ("AOCI") by component (pension, net of tax) for the three and nine months ended September 30, 2018 and 2017:

|   | Foreign<br>Currency<br>Translation |              | Pension | Total        |
|---|------------------------------------|--------------|---------|--------------|
|   | Adjustments                        | Plans        |         |              |
| Balance as of June 30, 2018                   | \$ (22,576 )                       | \$ (29,687 ) |         | \$ (52,263 ) |
| Other comprehensive income before             |                                    |              |         |              |
| reclassifications                             | 32                                 | -            |         | 32           |
| Amounts reclassified from accumulated other   |                                    |              |         |              |
| comprehensive loss                            | -                                  | 202          |         | 202          |
| Net current-period other comprehensive income | 32                                 | 202          |         | 234          |
| Balance as of September 30, 2018              | \$ (22,544 )                       | \$ (29,485 ) |         | \$ (52,029 ) |

|                             | Foreign<br>Currency<br>Translation |              | Pension | Total        |
|-----------------------------|------------------------------------|--------------|---------|--------------|
|                             | Adjustments                        | Plans        |         |              |
| Balance as of June 30, 2017 | \$ (21,543 )                       | \$ (30,743 ) |         | \$ (52,286 ) |



Other comprehensive income before

|   |            |              |            |
|---|------------|--------------|------------|
| reclassifications                             | 7,006      | -            | 7,006      |
| Amounts reclassified from accumulated other   |            |              |            |
| comprehensive loss                            | -          | 250          | 250        |
| Net current-period other comprehensive income | 7,006      | 250          | 7,256      |
| Balance as of September 30, 2017              | \$ (14,537 | ) \$(30,493) | \$(45,030) |

20

## CAMBREX CORPORATION AND SUBSIDIARIES

## Notes to Consolidated Financial Statements

(in thousands, except share data)

(Unaudited)

|  | Foreign      |            |            |
|--|--------------|------------|------------|
|  | Currency     |            |            |
|  | Translation  | Pension    |            |
|  | Adjustments  | Plans      | Total      |
| Balance as of December 31, 2017                      | \$ (12,040 ) | \$(30,188) | \$(42,228) |
| Other comprehensive loss before                      |              |            |            |
| reclassifications                                    | (10,504 )    | -          | (10,504)   |
| Amounts reclassified from accumulated other          |              |            |            |
| comprehensive loss                                   | -            | 703        | 703        |
| Net current-period other comprehensive (loss)/income | (10,504 )    | 703        | (9,801 )   |
| Balance as of September 30, 2018                     | \$ (22,544 ) | \$(29,485) | \$(52,029) |
|  | Foreign      |            |            |
|  | Currency     |            |            |
|  | Translation  | Pension    |            |
|  | Adjustments  | Plans      | Total      |
| Balance as of December 31, 2016                      | \$ (34,290 ) | \$(31,230) | \$(65,520) |
| Other comprehensive income before                    |              |            |            |
| reclassifications                                    | 19,753       | -          | 19,753     |
| Amounts reclassified from accumulated other          |              |            |            |
| comprehensive loss                                   | -            | 737        | 737        |
| Net current-period other comprehensive income        | 19,753       | 737        | 20,490     |
| Balance as of September 30, 2017                     | \$ (14,537 ) | \$(30,493) | \$(45,030) |

## CAMBREX CORPORATION AND SUBSIDIARIES

## Notes to Consolidated Financial Statements

(in thousands, except share data)

(Unaudited)

The following tables provide the reclassifications from AOCI by component for the three and nine months ended September 30, 2018 and 2017:

| Details about AOCI Components                         | Three Months<br>Ended<br>September 30,<br>2018 | Nine Months<br>Ended<br>September 30,<br>2018 |
|---|--|---|
| <b>Amortization of defined benefit pension items:</b> |  |   |
| Actuarial losses                                      | \$ (273 )                                      | \$ (953 )                                     |
| Prior service credit                                  | 2  | 4   |
| Total before tax                                      | (271 )   | (949 )  |
| Tax benefit   | 69   | 246   |
| Net of tax  | \$ (202 )                                      | \$ (703 )                                     |
| Total reclassification for the period                 | \$ (202 )                                      | \$ (703 )                                     |

| Details about AOCI Components                         | Three Months<br>Ended<br>September 30,<br>2017 | Nine Months<br>Ended<br>September 30,<br>2017 |
|---|--|---|
| <b>Amortization of defined benefit pension items:</b> |  |   |
| Actuarial losses                                      | \$ (355 )                                      | \$ (1,048 )                                   |
| Prior service costs                                   | (13 )  | (39 )   |
| Total before tax                                      | (368 )   | (1,087 )                                      |
| Tax benefit   | 118  | 350   |
| Net of tax  | \$ (250 )                                      | \$ (737 )                                     |
| Total reclassification for the period                 | \$ (250 )                                      | \$ (737 )                                     |

The Company recognizes all components of net periodic benefit cost except service costs in “Other expenses, net” in its income statement. Service costs are recognized in “Selling, general and administrative expenses” and “Cost of goods sold” in its income statement depending on the functional area of the underlying employees included in the plan.

## (12) Stock Based Compensation

The Company recognizes compensation costs for stock options awarded to employees based on their grant-date fair value. The value of each stock option is estimated on the date of grant using the Black-Scholes option-pricing model. The weighted-average fair value per share for the stock options granted to employees during the nine months ended September 30, 2018 was \$24.54. The weighted-average fair value per share for the stock options granted to employees during the nine months ended September 30, 2017 was \$20.14.



## CAMBREX CORPORATION AND SUBSIDIARIES

## Notes to Consolidated Financial Statements

(in thousands, except share data)

(Unaudited)

For the three months ended September 30, 2018 and 2017, the Company recorded \$994 and \$1,187, respectively, in “Selling, general and administrative expenses” for stock options. For the nine months ended September 30, 2018 and 2017, the Company recorded \$3,182 and \$3,313, respectively, in “Selling, general and administrative expenses” for stock options. As of September 30, 2018, the total compensation cost related to unvested stock options not yet recognized was \$6,466. The cost will be amortized on a straight-line basis over the remaining weighted-average vesting period of 1.9 years.

The following table is a summary of the Company’s stock options:

| Options                           | Weighted   |                |
|-----------------------------------|------------|----------------|
|                                   | Number of  | Average        |
|                                   | Shares     | Exercise Price |
| Outstanding at December 31, 2017  | 1,484,914  | \$ 32.53       |
| Exercised                         | (112,669 ) | 24.16          |
| Forfeited or expired              | (5,311 )   | 36.94          |
| Outstanding at March 31, 2018     | 1,366,934  | 33.20          |
| Granted                           | 14,265     | 53.70          |
| Exercised                         | (93,500 )  | 20.07          |
| Forfeited or expired              | (6,759 )   | 35.06          |
| Outstanding at June 30, 2018      | 1,280,940  | 34.38          |
| Exercised                         | (336,805 ) | 24.01          |
| Forfeited or expired              | (53,527 )  | 50.18          |
| Outstanding at September 30, 2018 | 890,608    | 37.35          |
| Exercisable at September 30, 2018 | 207,791    | \$ 30.20       |

The aggregate intrinsic values for all stock options exercised for the three and nine months ended September 30, 2018 were \$12,685 and \$18,494, respectively. The aggregate intrinsic values for all stock options exercised for the three and nine months ended September 30, 2017 were \$2,669 and \$12,011, respectively. The aggregate intrinsic values for all stock options outstanding and exercisable as of September 30, 2018 were \$27,656 and \$7,937, respectively.

## CAMBREX CORPORATION AND SUBSIDIARIES

## Notes to Consolidated Financial Statements

(in thousands, except share data)

(Unaudited)

The following table is a summary of the Company's unvested stock options, restricted stock and performance shares for which the requisite service period has not been rendered but that are expected to vest on the achievement of a performance condition:

|                                | Unvested<br>Stock Options |            | Unvested<br>Restricted Stock |            | Unvested<br>Performance Shares |            |
|--------------------------------|---------------------------|------------|------------------------------|------------|--------------------------------|------------|
|                                | Weighted-<br>Average      | Grant-Date | Weighted-<br>Average         | Grant-Date | Weighted-<br>Average           | Grant-Date |
|                                | Number<br>of Shares       | Fair Value | Number<br>of Shares          | Fair Value | Number<br>of Shares            | Fair Value |
| Unvested at December 31, 2017  | 757,269                   | \$ 15.20   | 265                          | \$ 44.23   | 276,250                        | \$ 42.08   |
| Vested during period           | (21,510 )                 | 13.99      | -                            | -          | -                              | -          |
| Forfeited                      | (5,311 )                  | 13.90      | -                            | -          | (17,250 )                      | 40.65      |
| Unvested at March 31, 2018     | 730,448                   | 15.25      | 265                          | 44.23      | 259,000                        | 42.17      |
| Granted                        | 14,265                    | 24.54      | 9,779                        | 53.70      | 17,250                         | 40.65      |
| Vested during period           | (1,610 )                  | 17.34      | (265 )                       | 44.23      | -                              | -          |
| Forfeited                      | (6,759 )                  | 13.27      | -                            | -          | (28,750 )                      | 41.36      |
| Unvested at June 30, 2018      | 736,344                   | 15.44      | 9,779                        | 53.70      | 247,500                        | 42.16      |
| Forfeited                      | (53,527 )                 | 19.27      | -                            | -          | (42,250 )                      | 42.53      |
| Unvested at September 30, 2018 | 682,817                   | \$ 15.14   | 9,779                        | \$ 53.70   | 205,250                        | \$ 42.08   |

For the three months ended September 30, 2018 and 2017, the Company recorded \$262 and \$280, respectively, in "Selling, general and administrative expenses" for restricted stock awards. For the nine months ended September 30, 2018 and 2017, the Company recorded \$445 and \$474, respectively, in "Selling, general and administrative expenses" for restricted stock awards. As of September 30, 2018, total compensation cost related to unvested restricted stock not yet recognized was \$88. The cost will be amortized on a straight-line basis over the remaining weighted-average vesting period of 0.1 years.

The Company granted equity-settled performance shares ("PS") to certain executives. PS awards provide the recipient the right to receive a certain number of shares of the Company's common stock in the future, which depends on the Company's level of achievement of net revenue and EBITDA growth as compared to the net revenue and EBITDA growth of the members of a specified peer group of companies over a three year period. For the three months ended September 30, 2018 and 2017, the Company recorded a benefit of \$353 and expense of \$821, respectively, in "Selling, general and administrative expenses" related to these PS awards. For the nine months ended September 30, 2018 and

2017, the Company recorded expense of \$479 and \$2,534, respectively, in “Selling, general and administrative expenses” related to these PS awards. As of September 30, 2018, total compensation cost related to unvested performance shares not yet recognized was \$2,768. The cost will be amortized on a straight-line basis over the remaining weighted-average vesting period of 0.9 years.

(13) Retirement Plans

The Company recognizes all components of net periodic benefit cost except service costs in “Other expenses, net” in its income statement. Service costs are recognized in “Selling, general and administrative expenses” and “Cost of goods sold” in its income statement depending on the functional area of the underlying employees included in the plan. As a result of the adoption of ASU 2017-07, the Company recorded \$167 and \$649 to “Other expenses, net” for the three and nine months ended September 30, 2018,

## CAMBREX CORPORATION AND SUBSIDIARIES

## Notes to Consolidated Financial Statements

(in thousands, except share data)

(Unaudited)

respectively, which formerly would have been recorded as “Selling, general and administrative expenses” or “Cost of goods sold.” To conform to the current year presentation, for the three and nine months ended September 30, 2017, the Company reclassified \$384 and \$1,107, respectively, from “Selling, general and administrative expenses” and \$54 and \$161, respectively, from “Cost of goods sold” to “Other expenses, net.”

## Domestic Pension Plan

The components of net periodic benefit (credit)/cost for the Company’s domestic pension plan (which was frozen in 2007) for the three and nine months ended September 30, 2018 and 2017 were as follows:

|  | Three Months<br>Ended<br>September 30,<br>2018 |        | Nine Months<br>Ended<br>September 30,<br>2017 |          |
|--|--|--------|---|----------|
| Components of net periodic benefit (credit)/cost |  |        |   |          |
| Interest cost                                    | \$ 511   | \$ 553 | \$ 1,532                                      | \$ 1,661 |
| Expected return on plan assets                   | (792 )   | (677 ) | (2,376 )                                      | (2,031 ) |
| Recognized actuarial loss                        | 180  | 199    | 539   | 599      |
| Net periodic benefit (credit)/cost               | \$(101 )                                       | \$ 75  | \$(305 )                                      | \$ 229   |

## International Pension Plan

The components of net periodic benefit cost for the Company’s international pension plan for the three and nine months ended September 30, 2018 and 2017 were as follows:

|   | Three Months<br>Ended<br>September 30,<br>2018 |        | Nine Months<br>Ended<br>September 30,<br>2017 |          |
|---|--|--------|---|----------|
| Components of net periodic benefit cost |  |        |   |          |
| Service cost                            | \$ 245   | \$ 247 | \$ 768  | \$ 700   |
| Interest cost                           | 176  | 192    | 552   | 545      |
| Recognized actuarial loss               | 93   | 94     | 292   | 268      |
| Amortization of prior service credit    | (1 )   | (1 )   | (3 )  | (3 )     |
| Net periodic benefit cost               | \$ 513   | \$ 532 | \$ 1,609                                      | \$ 1,510 |



(14) Segment Information

Cambrex is a life sciences company that provides products and services that accelerate and improve the development and commercialization of new and generic therapeutics. The Company primarily supplies its products and services worldwide to innovator and generic pharmaceutical companies.

Including the Company's acquisition of Halo Pharma on September 12, 2018, Cambrex has six manufacturing facilities.

25

---

CAMBREX CORPORATION AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(in thousands, except share data)

(Unaudited)

Operating segments are identified as components of an enterprise for which separate discrete financial information is available for evaluation by the chief operating decision maker (the Company's Chief Executive Officer) in making decisions on how to allocate resources and assess performance. To be in alignment with the financial information received by the Chief Executive Officer and how the business is managed, the Company's operating segments were aggregated to form two reportable segments, Active Pharmaceutical Ingredients ("APIs") and Finished Dosage Form ("FDF"). While there are regulatory similarities between the two segments the products are different in that the API segment produces products that are sold to pharmaceutical companies that further process the Company's product into a finished dosage form product that is then distributed directly to the patient. The FDF segment only manufactures and develops final dosage form products. All purchase accounting adjustments are recorded by the reporting segment.

API's: The Company's API segment is comprised of the custom development and manufacture of pharmaceutical ingredients derived from organic chemistry. Products consist of APIs and pharmaceutical intermediates for use in the production of prescription and over-the-counter drug products.

FDF: The Company's FDF segment consists of contract development and commercial manufacturing of finished dosage form products including oral solids, liquids and creams, and sterile and non-sterile ointments.

The Company's Corporate headquarters provides management and administrative services to support the Company, and consists of certain aspects of the Company's executive management, corporate relations, legal, compliance, human resources, information technology and finance departments. The Company allocates certain corporate expenses to each of its segments. Depreciation and amortization on certain assets are not allocated to the Company's reportable segments.

The Company evaluates the performance of its segments based on segment operating profit. Transactions between reportable segments are not material. The Company does not allocate interest expense or income taxes to the operating segments. Discontinued operations are not recorded by the reportable segments. The Company accounts for total assets on a consolidated basis and does not allocate or disclose it for each reportable segment. The chief operating decision maker does not review segment's assets.

The following table summarizes the Company's financial information by reportable segment:

| Three Months Ended | Nine Months Ended |
|--------------------|-------------------|
| September 30,      | September 30,     |

Edgar Filing: CAMBREX CORP - Form 10-Q

|   | 2018     | 2017      | 2018      | 2017      |
|---|----------|-----------|-----------|-----------|
| <b>Gross sales by segment</b>             |          |           |           |           |
| APIs                                      | \$99,445 | \$112,233 | \$385,789 | \$350,431 |
| FDF                                       | 4,786    | -         | 4,786     | -         |
| Total reported gross sales                | 104,231  | 112,233   | 390,575   | 350,431   |
| <b>Operating profit/(loss) by segment</b> |          |           |           |           |
| APIs                                      | 16,872   | 31,932    | 101,436   | 106,779   |
| FDF                                       | 114      | -         | 114       | -         |
| Total segment operating profit            | 16,986   | 31,932    | 101,550   | 106,779   |
| Corporate operating loss                  | (10,354) | (6,389)   | (19,885)  | (18,670)  |
| Total reported operating profit           | \$6,632  | \$25,543  | \$81,665  | \$88,109  |

26

---

CAMBREX CORPORATION AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(in thousands, except share data)

(Unaudited)

(15) Contingencies

The Company is subject to various investigations, claims and legal proceedings covering a wide range of matters that arise in the ordinary course of its business activities. The Company continually assesses known facts and circumstances as they pertain to applicable legal and environmental matters and evaluates the need for reserves and disclosures as deemed necessary based on these facts and circumstances. These matters, either individually or in the aggregate, could result in actual costs that are significantly higher than the Company's current assessment and could have a material adverse effect on the Company's operating results and cash flows in future reporting periods. Based upon past experience, the Company believes that payments significantly in excess of current reserves, if required, would be made over an extended number of years.

Environmental

In connection with laws and regulations pertaining to the protection of the environment, the Company and its subsidiaries are a party to several environmental proceedings and remediation activities and along with other companies, have been named a potentially responsible party ("PRP") for certain waste disposal sites ("Superfund sites"). All of the liabilities currently recorded on the Company's balance sheet for environmental proceedings are associated with discontinued operations. The Company had insurance policies in place at certain of the discontinued operations for certain years that the Company believes should cover some portion of the recorded liabilities or potential future liabilities and the Company expects the net cash impact related to the contingencies described below to be reduced by the applicable income tax rate.

It is the Company's policy to record appropriate liabilities for environmental matters where remedial efforts are probable and the costs can be reasonably estimated. Such liabilities are based on the Company's estimate of the undiscounted future costs required to complete the remedial work. Each of these matters is subject to various uncertainties, and it is possible that some of these matters will be decided against the Company. The resolution of such matters often spans several years and frequently involves regulatory oversight or adjudication. Additionally, many remediation requirements are fluid and are likely to be affected by future technological, site and regulatory developments. It is not possible at this time for the Company to determine fully the effect of all asserted and unasserted claims on its consolidated financial condition, results of operations or liquidity; however, to the extent possible, where asserted and unasserted claims can be estimated and where such claims are considered probable, the Company would record a liability. Consequently, the ultimate liability with respect to such matters, as well as the timing of cash disbursements, is uncertain.

In matters where the Company is able to reasonably estimate the probable and estimable costs associated with environmental proceedings, the Company accrues for the estimated costs associated with the study and remediation of applicable sites. At September 30, 2018, these reserves were \$17,656, of which \$16,655 is included in "Other non-current liabilities" on the Company's balance sheet. At December 31, 2017, the reserves were \$17,511, of which \$16,976 is included in "Other non-current liabilities" on the Company's balance sheet. The increase in the reserves includes adjustments to reserves of \$898, partially offset by payments of \$753. The reserves are adjusted periodically

as remediation efforts progress or as additional technical, regulatory or legal information becomes available. Given the uncertainties regarding the outcome of investigative and study activities, the status of laws, regulations, enforcement, policies, the impact of other PRPs, technology and information related to individual sites, the Company does not believe it is possible to currently develop an estimate of the range of reasonably possible environmental loss in excess of its reserves.

CAMBREX CORPORATION AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(in thousands, except share data)

(Unaudited)

Bayonne

As a result of the sale of a Bayonne, New Jersey facility, the Company became obligated to investigate site conditions and conduct required remediation under the New Jersey Industrial Site Recovery Act. The Company completed an investigation and sampling plan at the property pursuant to the New Jersey Department of Environmental Protection's ("NJDEP") private oversight program. The results have been used to develop a proposed remedial plan for the site. Among other things, the remedial plan sets forth further details of the proposed cleanup, including the removal and encapsulation of certain impacted soils and implementation of engineering controls and deed restrictions. As of September 30, 2018, the Company's reserve was \$635.

Clifton and Carlstadt

The Company has implemented a sampling and pilot program in Clifton and Carlstadt, New Jersey pursuant to the NJDEP private oversight program. The results of the sampling and pilot program to date have been used to develop an estimate of the Company's future liability for remediation costs, and the Company continues to move forward with the projects at each site in accordance with the established schedules and work plans. As of September 30, 2018, the Company's reserve was \$1,842.

Berry's Creek

The Company received a notice from the United States Environmental Protection Agency ("USEPA") that two subsidiaries of the Company are considered PRPs at the Berry's Creek Study Area in New Jersey. These subsidiaries are among many other PRPs that were listed in the notice. Pursuant to the notice, the PRPs have been asked to perform a remedial investigation ("RI") and feasibility study ("FS") of the Berry's Creek site. The Company has joined the group of PRPs and entered into an Administrative Settlement Agreement ("Agreement") and Order on Consent with the USEPA agreeing to jointly conduct or fund an appropriate remedial investigation and feasibility study of the Berry's Creek site with the other PRPs in the Agreement. The PRPs have engaged consultants to perform the work specified in the Agreement and develop a method to allocate related costs among the PRPs.

In June 2016, the PRPs received a request from USEPA to amend the RI/FS Work Plan to accommodate a phased, iterative approach to the Berry's Creek remediation. USEPA requested an initial Phase I remedy that focuses on a portion of the site, namely, sediments in Upper and Middle Berry's Creek and the marsh in Upper Peach Island Creek. Any subsequent remedial action will occur after the implementation and performance monitoring of this Phase I remedy and the extent of future action is expected to be at least partially determined by the outcome of this initial phase. In April 2017, USEPA approved the requested addendum to the RI/FS Work Plan, which included the description of the phased and adaptive management approach to the Berry's Creek remedy.

In September 2018, USEPA issued its Record of Decision ("ROD") for an interim remedy at Berry's Creek. The interim remedy calls for, among other things, dredging and capping of contaminated sediments. The next step in the process is to design the remedy ("Remedial Design"). USEPA issued a letter to the Berry's Creek PRP Group in September 2018 that provided notice of potential liability and a request that the PRP Group agree to perform the Remedial

Design. USEPA provided a draft settlement agreement and statement of work to implement the Remedial Design. As a member of the Berry's Creek PRP Group, the Company will participate in the PRP Group's response to USEPA, and is coordinating with PRP Group members and PRP Group common counsel on that response.

The estimated costs for the interim remedy may be further developed and the Company's accrual may change based upon revisions to cost estimates. As of September 30, 2018, the Company's reserve was \$9,688. At this time it is not known when the costs for the complete remediation plan will be estimable, and

CAMBREX CORPORATION AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(in thousands, except share data)

(Unaudited)

as such, no accrual beyond the interim remedy has been recorded. The Company's share has been preliminarily estimated by the PRP group at 2.4%. While the Company will defend its position that its share should be reduced from the current level, its share could be increased or decreased depending on the outcome of the final allocation process that will take place in future periods.

While any resolution of this matter is not expected to materially impact the Company's operations or financial position, it could be material to the financial statements in the period recorded.

In July 2014, the Company received a notice from the U.S. Department of the Interior, U.S. Fish & Wildlife Service, regarding the Company's potential liability for natural resource damages at the Berry's Creek site and inviting the Company to participate in a cooperative assessment of natural resource damages. Most members of the Berry's Creek PRP group received such notice letters, and the PRP Group coordinated a joint response, which was to decline participation in a cooperative assessment at this time, given existing investigation work at the site. The cost of any future assessment and the ultimate scope of natural resource damage liability are not yet known.

#### Maybrook Site

A subsidiary of Cambrex is named a PRP of a site in Hamptonburgh, New York by the USEPA in connection with the discharge, under appropriate permits, of wastewater at that site prior to Cambrex's acquisition in 1986. The PRPs implemented soil remediation which was completed in 2012 pending approval by the USEPA. The PRPs will continue implementing the ground water remediation at the site. USEPA completed its 5-year review report in August 2018, and USEPA's review of the site remedy is on-going. It is unclear if such review, together with an agreed proposed modification to the USEPA Consent Decree, will result in any additional site work. As of September 30, 2018, the Company's reserve was \$329, to cover long-term ground water monitoring and related costs.

#### Harriman Site

Subsidiaries of Cambrex and Pfizer are named as responsible parties for the Company's former Harriman, New York production facility by the New York State Department of Environmental Conservation ("NYSDEC"). A final Record of Decision ("ROD") describing the Harriman site remediation responsibilities for Pfizer and the Company was issued in 1997 (the "1997 ROD") and incorporated into a federal court Consent Decree in 1998 (the "Consent Decree"). In December 2013, the Company, Pfizer and the NYSDEC entered into a federal court stipulation, which the court subsequently endorsed as a court order, resolving certain disputes with the NYSDEC about the scope of the obligations under the Consent Decree and the 1997 ROD, and requiring the Company and Pfizer to carry out an environmental investigation and study of certain areas of the Harriman Site.

Site clean-up work under the 1997 ROD, the Consent Decree and the 2013 stipulation is ongoing and is being jointly performed by Pfizer and the Company, with NYSDEC oversight. Since 2014, Pfizer and the Company have performed supplemental remedial investigation measures requested by the NYSDEC, and the findings have been submitted to NYSDEC in various reports, including a study evaluating the feasibility of certain remedial alternatives in August 2016. By letter dated January 5, 2017, NYSDEC disapproved such feasibility study report and requested



certain revisions to the report. The Company and Pfizer engaged in further discussions with NYSDEC and have agreed to submit a revised version of the August 2016 feasibility study to address certain of NYSDEC's requests. In September 2017, the NYSDEC requested that Pfizer, the Company and the current owner of the Harriman Site, ELT Harriman LLC ("ELT"), conduct an investigation of additional constituents not addressed under the 1997 ROD based on the detection of those constituents at the Harriman Site and other properties in the area. The parties have requested more information from the State of New York to evaluate the request, while also responding to NYSDEC that no further investigation was warranted.

CAMBREX CORPORATION AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(in thousands, except share data)

(Unaudited)

As it is too soon to determine whether the NYSDEC's requests or the reports and remedial plans, when finalized, will result in any significant changes to the Company's responsibilities, no change to the reserve has been made. ELT is conducting other investigation and remediation activities under a separate NYSDEC directive.

No final remedy for the site has been determined, which will follow further discussions with the NYSDEC. The Company estimates the range for its share of the liability at the site to be between \$2,000 and \$7,000. As of September 30, 2018, the Company's reserve was \$3,365. At this time, the Company is unable to provide an estimate of the ultimate investigative and remedial costs to the Company for any final remedy selected by the NYSDEC.

The Company intends to enforce all of its contractual rights to recover costs and for indemnification under a 2007 settlement agreement, and has filed such claims in an arbitration proceeding against ELT and the immediately preceding owner, Vertellus Specialties Holdings ("Vertellus"). ELT has filed counterclaims, and has threatened to file additional counterclaims, for contractual indemnification and for breach of the settlement agreement against the Company. Currently, the arbitration proceeding is stayed indefinitely. In May 2016, some but not all of the Vertellus entities who are parties to the Company's 2007 settlement agreement filed for restructuring under Chapter 11 of the U.S. Bankruptcy Code in the United States Bankruptcy Court for the District of Delaware. The Company has filed several claims as creditors in the bankruptcy proceeding and will continue to monitor the bankruptcy proceeding.

#### Scientific Chemical Processing ("SCP") Superfund Site

A subsidiary of Cambrex was named a PRP of the SCP Superfund site, located in Carlstadt, New Jersey, along with approximately 130 other PRPs. The site is a former waste processing facility that accepted various waste for recovery and disposal including processing wastewater from this subsidiary. The PRPs are in the process of implementing a final remedy at the site. The SCP Superfund site has also been identified as a PRP in the Berry's Creek Superfund site (see previous discussion). While the Company continues to dispute the methodology used by the PRP group to arrive at its interim allocation for cash contributions, the Company has paid the funding requests. A final allocation of SCP Site costs (excluding Berry's Creek costs) is expected to be finalized in 2018. As of September 30, 2018, the Company's reserve was \$732, of which approximately \$468 is expected to be covered by insurance.

#### Newark Bay Complex

The USEPA and a private party group are evaluating remediation plans for the Passaic River, Newark Bay, Hackensack River, Arthur Kill, Kill Van Kull and adjacent waters (the "Newark Bay Complex"). Although the Company is not involved in the USEPA action, it continues to monitor developments related to the site due to its past involvement in a previously settled state action relating to the Newark Bay Complex. The USEPA has finalized its decision on a cleanup plan for 8.3 miles of the lower Passaic River, and has estimated the cost of this plan at \$1.38 billion. Due to the uncertainty of the future scope and timing of any possible claims against the Company, no liability has been recorded.

The Company is involved in other related and unrelated environmental matters where the range of liability is not reasonably estimable at this time and it is not foreseeable when information will become available to provide a basis

for adjusting or recording a reserve, should a reserve ultimately be required.

30

---

## CAMBREX CORPORATION AND SUBSIDIARIES

## Notes to Consolidated Financial Statements

(in thousands, except share data)

(Unaudited)

## Litigation and Other Matters

## Lorazepam and Clorazepate

In 1998, the Company and a subsidiary were named as defendants along with Mylan Laboratories, Inc. (“Mylan”) and Gyma Laboratories, Inc. (“Gyma”) in a proceeding instituted by the Federal Trade Commission in the United States District Court for the District of Columbia (the “District Court”). Suits were also commenced by several State Attorneys General and class action complaints by private plaintiffs in various state courts. The suits alleged violations of the Federal Trade Commission Act arising from exclusive license agreements between the Company and Mylan covering two APIs (Lorazepam and Clorazepate).

In 2003, Cambrex paid \$12,415 to Mylan in exchange for a release and full indemnity against future costs or liabilities in related litigation brought by the purchasers of Lorazepam and Clorazepate, as well as potential future claims related to the ongoing matter.

Following trial in 2008 in the sole remaining case brought by four health care insurers, the District Court entered judgment against Mylan, Gyma and Cambrex. The judgment was appealed to the United States Court of Appeals for the District of Columbia Circuit (the “D.C. Circuit”) in 2011, resulting in a remand to the District Court. On remand, the District Court dismissed certain self-funded customer plaintiffs due to their failure to satisfy the requirements of federal jurisdiction. Subsequently, the District Court entered an order remitting certain damages. Without fees, costs, or post-judgment interest, the current judgment against Mylan, Gyma, and Cambrex was \$67,260. Mylan, Gyma, and Cambrex again appealed to the D.C. Circuit. In July 2018, Mylan, Gyma, and Cambrex reached a settlement with the remaining plaintiffs. After the settlement was finalized, the D.C. Circuit issued an order dismissing the appeal. Cambrex has been fully indemnified by Mylan for the settlement payments.

## (16) Discontinued Operations

For all periods presented, financial results for discontinued operations relate to environmental investigation and remediation expenses for divested sites. The following table is a reconciliation of the pre-tax loss on discontinued operations to the net loss on discontinued operations, as presented on the income statement:

|  | Three Months<br>Ended<br>September 30,<br>2018 |        | Nine Months<br>Ended<br>September 30,<br>2017 |            |
|--|--|--------|---|------------|
| (Loss)/income from discontinued operations, pre-tax    | \$ (99 )                                       | \$ 126 | \$ (855)                                      | \$ (1,946) |
| Income tax benefit/(expense)                           | 13   | (106 ) | 145   | 622        |
| (Loss)/income from discontinued operations, net of tax | \$ (86 )                                       | \$ 20  | \$ (710)                                      | \$ (1,324) |

As of September 30, 2018 and December 31, 2017, liabilities recorded on the Company's balance sheet related to discontinued operations were \$17,656 and \$17,511, respectively. At this time, the Company cannot reasonably estimate the period of time during which the involvement is expected to continue. Net cash used in discontinued operations for the nine months ended September 30, 2018 and 2017 were \$557 and \$1,185, respectively. Refer to Note 15 to the Company's consolidated financial statements for further disclosures on the Company's environmental contingencies.

## CAMBREX CORPORATION AND SUBSIDIARIES

(in thousands, except share data)

### Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations Executive Overview

The following summarizes the Company's performance for the third quarter of 2018:

- The Company acquired 100% of Halo Pharma on September 12, 2018 for \$425,000.
- The Company adopted ASC 606 - Revenue from Contracts with Customers on January 1, 2018 using the modified retrospective method. The cumulative effect adjustment recorded to retained earnings as of January 1, 2018 was \$16,219, net of tax.
- Net revenue decreased 7.1% on a reported basis compared to the third quarter of 2017. Net revenue, excluding currency impact, decreased 5.6%. Excluding the impact of the new revenue recognition standard, net revenue decreased 8.8% on a reported basis.
- Gross margins decreased to 31.3% from 41.7% in the third quarter of 2017. Excluding the impact of the new revenue recognition standard, gross margins were 38.3%.
- Net debt was \$227,865 compared to net cash of \$171,348 at June 30, 2018. The change is primarily the result of acquiring Halo Pharma.

#### Critical Accounting Estimates

The Company's critical accounting estimates are those that require the most subjective or complex judgments, often as a result of the need to make estimates about the effect of matters that are inherently uncertain. The Company bases its estimates on historical experience and on other assumptions that are deemed reasonable by management under each applicable circumstance. Actual results or amounts could differ from estimates and the differences could have a material impact on the consolidated financial statements. See the "Critical Accounting Estimates" section of the Company's Annual Report on Form 10-K for the period ended December 31, 2017 for further discussion of the Company's critical accounting policies, the underlying judgments and uncertainties affecting their application and the likelihood that materially different amounts would be reported under different conditions or using different assumptions. The policy updates from the previously filed Form 10-K are as follows:

#### Revenue Recognition

2018 results are accounted for under the following new policy:

The Company adopted Topic 606 Revenue from Contracts with Customers on January 1, 2018 using the modified retrospective method. As a result, the Company has changed its accounting policy for revenue recognition as detailed below. The cumulative effect of initially applying the new revenue standard was recorded as an adjustment to the opening balance of retained earnings. The comparative information has not been restated and continues to be reported under accounting standard Topic 605 which was in effect for those periods.

Revenue is recognized when control over a product or service is transferred to a customer. Revenue is measured as the amount of consideration expected in exchange for transferring goods or providing services.

Sales terms to certain customers include rebates if certain conditions are met. Additionally, sales are generally made with a limited right of return under certain conditions. The Company estimates these rebates and returns at the time of

sale based on the terms of agreements with customers and historical experience and estimated orders. The Company recognizes revenue net of these estimated costs which are classified as allowances and rebates.

Shipping and handling costs are treated as fulfillment costs and estimates for the portion of revenue recognized on performance obligations recognized over time are accrued.

For variable consideration arrangements where the transaction price fluctuates based on quantity, the most likely estimated quantity is assumed using forecasts provided by the customer.

#### Single-use products

In most single-use product sales, a quantity is ordered and manufactured according to the customer's specifications and typically only one performance obligation is included. The Company also manufactures early phase product that can be included in a contract with services. These services are distinct and separated from the product performance obligations and are shown as a service revenue stream. The products are manufactured exclusively for a specific customer and have no alternative use. Generally, under these customer agreements, the Company is entitled to consideration for progress to date that includes an element of profit margin. To the extent an agreement does not include an element of profit margin for progress to date, it is recognized at a point in time. Revenues that are recognized over time utilize a measure of progress toward satisfaction of the performance obligations. The Company measures progress using an input method which compares the cost of cumulative work in process to date to the most current estimates for the entire performance obligation. The raw materials are excluded from this measurement due to the high value and inclusion in the early stages of the project that would otherwise overstate progress to date.

#### Multi-use products

The Company's multi-use product sales can be sold to multiple customers and have an alternative use. Both the transaction sales price and shipping terms are agreed upon in the contract. For these products, all revenue is recognized at a point in time, generally when title to products and risk of loss is transferred to the customers based upon shipping terms. These arrangements typically include only one performance obligation.

#### Service revenue

The service revenue stream represents services provided to a customer to assist with early stages of the regulatory approval process. The customer owns the drug details and process. The Company works with its customers to develop, validate and document the production process in order to comply with the regulatory approval process. These custom development projects could have one or more performance obligations with no alternative use. The contracts are structured to ensure the Company is paid for in-process work, including a profit margin. Revenues related to this stream are recognized over time by allocating to each performance obligation the best estimate of the standalone selling price of each service. The Company measures progress using an input method which compares the cost of cumulative work in process to date to the most current estimates for the entire performance obligation. Standalone selling prices are generally based on the prices charged to customers or based on an expected cost-plus margin.

#### Contract balances

The timing of revenue recognition, billings and cash collections results in billed trade receivables, contracts assets (unbilled receivables), and contract liabilities (customer advances and deferred revenue). For each reporting period presented, the Company reports contract balances in a net contract asset or liability position on a contract-by-contract basis. Contract assets are recorded when the right to consideration is conditioned on something other than the passage of time. When an entity's right to consideration is unconditional, the receivable is recorded within Trade Receivables on the balance sheet. Contract liabilities represent advance payments from customers, and deferred revenue. Contract



assets will convert to trade receivables or cash and current contract liabilities will convert into revenue within a one-year period.

33

---

Payment terms can vary by the type and location of the customer and the products or services offered. The term between invoicing and when payment is due is not significant. For certain products or services and customer types, payment prior to satisfaction of a performance obligation can be required, and results in recording a contract liability.

All prior periods presented are accounted for under the following policy:

Revenues are generally recognized when title to products and risk of loss are transferred to customers. Additional conditions for recognition of revenue are that collection of sales proceeds is reasonably assured and the Company has no further performance obligations.

Amounts billed in advance are recorded as contract liabilities on the balance sheet. Since payments received are sometimes non-refundable, the termination of a contract by a customer prior to its completion could result in an immediate recognition of deferred revenue relating to payments already received but not previously recognized as revenue.

Sales terms to certain customers include rebates if certain conditions are met. Additionally, sales are generally made with a limited right of return under certain conditions. The Company estimates these rebates and returns at the time of sale based on the terms of agreements with customers and historical experience and estimated orders. The Company recognizes revenue net of these estimated costs which are classified as allowances and rebates.

The Company bills a portion of freight cost incurred on shipments to customers. Amounts billed to customers are recorded within net revenues. Freight costs are reflected in cost of goods sold.

#### Income Taxes

#### Assumptions and Approach Used in Assessing the Need for a Valuation Allowance

The Company considers both positive and negative evidence related to the likelihood of realization of deferred tax assets. If, based on the weight of available evidence, it is more likely than not the deferred tax assets will not be realized, the Company records a valuation allowance against all or a portion of the deferred tax assets to adjust the balance to the amount considered more likely than not to be realized. The weight given to the positive and negative evidence is commensurate with the extent to which the evidence may be objectively verified.

This assessment, which is completed on a taxing jurisdiction basis, takes into account a number of types of evidence, including the following:

- Nature, frequency, and severity of current and cumulative financial reporting losses. A pattern of objectively-measured recent financial reporting losses is heavily weighted as a source of negative evidence. The Company generally considers cumulative pre-tax losses in the current three-year period to be significant negative evidence regarding future profitability. The Company also considers the strength and trend of earnings, as well as other relevant factors. In certain circumstances, historical information may not be as relevant due to changes in the Company's business operations;
- Sources of future taxable income. Future reversals of existing taxable temporary differences are heavily-weighted sources of objectively verifiable evidence. Projections of future taxable income exclusive of reversing temporary differences are a source of positive evidence only when the projections are combined with a history of recent profits and can be reasonably estimated; and

- Tax planning strategies. Prudent and feasible tax planning strategies that would be implemented to maximize utilization of expiring tax credit carryforwards are evaluated as a source of additional positive evidence.

## Results of Operations

## Comparison of Third Quarter 2018 versus Third Quarter 2017

Net revenue in the third quarter of 2018 of \$104,618 was \$8,001 or 7.1% lower than the third quarter of 2017. Excluding a 1.5% unfavorable impact of foreign exchange compared to the third quarter of 2017, net revenue decreased 5.6% primarily due to lower volumes (5.7%). The decrease in volumes was driven by the Active Pharmaceutical Ingredients (“APIs”) segment partially offset by Halo revenues, which makes up the Finished Dosage Form (“FDF”) segment.

Excluding the impact of the new revenue recognition standard, net revenue in the third quarter of 2018 decreased 8.8% compared to the third quarter of 2017 to \$102,704.

The following table reflects net revenue by geographic area for the third quarters of 2018 and 2017:

|                   | Third quarter |           |
|-------------------|---------------|-----------|
|                   | 2018          | 2017      |
| Europe            | \$62,146      | \$62,395  |
| North America     | 35,903        | 44,933    |
| Asia              | 3,394         | 2,809     |
| Other             | 3,175         | 2,482     |
| Total net revenue | \$104,618     | \$112,619 |

Gross margins in the third quarter of 2018 decreased to 31.3% from 41.7% in the third quarter of 2017. Gross profit in the third quarter of 2018 was \$32,725 compared to \$46,943 in the same period last year. Excluding the impact of the new revenue recognition standard, gross margins in the third quarter of 2018 decreased to 38.3%. Margins decreased in the APIs segment as discussed below.

## APIs

Net revenue in the third quarter of 2018 of \$99,464 was \$13,348 or 11.8% lower than the third quarter of 2017. Excluding a 1.7% unfavorable impact of foreign exchange compared to the third quarter of 2017, net revenue decreased 10.1% primarily due to lower volumes (10.2%). The decrease in volumes was driven by a decrease in all product categories.

Excluding the impact of the new revenue recognition standard, net revenue in the third quarter of 2018 decreased 14.5% compared to the third quarter of 2017 to \$96,408.

Gross margins in the third quarter of 2018 decreased to 31.2% from 41.8% in the third quarter of 2017. Gross profit in the third quarter of 2018 was \$31,073 compared to \$47,135 in the same period last year. Excluding the impact of the new revenue recognition standard, gross margins in the third quarter of 2018 were 38.9%. The decrease in margins was primarily driven by lower production volumes and higher raw material costs.

Selling, general and administrative (“SG&A”) expenses of \$10,742 in the third quarter of 2018 decreased compared to \$12,160 in the third quarter of 2017. The decrease was mainly due to an accounts receivable write-off in the third quarter of 2017 (approximately \$700), lower consulting costs associated with an operational excellence initiative

(approximately \$400) and the impact of foreign currency (approximately \$300). Sales and marketing expenses were flat compared to the third quarter of 2017. SG&A, as a percentage of net revenue, was 10.8% in the third quarters of 2018 and 2017.

Research and development (“R&D”) expenses of \$3,459 were 3.5% of net revenue in the third quarter of 2018, compared to \$3,043 or 2.7% of net revenue in the third quarter of 2017. The increase was primarily driven by higher personnel costs.

Operating profit in the third quarter of 2018 was \$16,872 compared to \$31,932 in the third quarter of 2017. The decrease in operating profit was due to lower gross profit partially offset by lower operating expenses as described above.

Excluding the impact of the new revenue recognition standard, operating profit in the third quarter of 2018 was \$23,319.

#### FDF

Net revenue in the third quarter of 2018 was \$5,154 for the period from acquisition date, September 12, 2018 through September 30, 2018. Excluding the impact of the new revenue recognition standard, net revenue was \$6,296.

Gross margins in the third quarter of 2018 were 32.1%. Gross profit in the third quarter of 2018 was \$1,652. Excluding the impact of the new revenue recognition standard, gross margins in the third quarter of 2018 were 28.0% and gross profit would have been \$1,766.

SG&A expenses were \$1,141 in the third quarter of 2018. SG&A, as a percentage of net revenue, was 22.1%.

FDF operating profit for the period September 12, 2018 through September 30, 2018 was \$508. Excluding the impact of the new revenue recognition standard, operating profit would have been \$622. Both exclude integration costs of \$394.

The Company's Corporate headquarters provides management and administrative services to support the Company, and consists of certain aspects of the Company's executive management, corporate relations, legal, compliance, human resources, and information technology and finance departments. The Company allocates certain corporate expenses to each of its segments. SG&A expenses of \$2,631 in the third quarter of 2018 decreased compared to \$5,007 in the third quarter of 2017. The decrease was mainly due to lower personnel related costs (approximately \$2,300). R&D expenses of \$729 in the third quarter of 2018 decreased compared to \$1,190 in the same quarter last year. The decrease is due to the timing of spending on the development of generic drug products.

During the third quarter of 2018, the Company completed the acquisition of 100% of Halo, a finished dosage form Contract Development and Manufacturing Organization. The deal was structured as a stock purchase. The Company acquired two GMP compliant facilities, one in Whippany, NJ, USA, the other in Mirabel, Quebec, Canada. All acquisition and integration costs have been expensed and totaled \$7,388 for the three months ended September 30, 2018, of which \$394 was recorded by the FDF segment. These costs have been recorded to "Acquisition and integration expenses" on the Company's income statement.

During the second quarter of 2018, the Company acquired a 19.9% equity investment in a European company ("Investee"). The Investee completed an initial public offering on a foreign exchange late in the quarter, which reduced the Company's ownership share to 16.3%. The Company's investment is subject to a one-year prohibition on selling the shares. The Company has one seat on the Board of Directors of the investee and concluded it is able to exercise significant influence and that equity accounting would be appropriate. In accordance with ASC 825, the Company has elected to record this investment at fair value. The Company selected an appropriate valuation methodology to compute a discount for the lack of marketability to be applied to the closing market price of the shares as of September 30, 2018. The fair value of the Company's shares increased by \$5,611 at September 30, 2018 resulting in an unrealized gain that was recorded as "Unrealized gain on investment in equity securities" on the Company's income statement. Since the shares owned by the Company are substantially in excess of the daily trade volumes of the stock,

it could be difficult to sell the shares in a timely manner when the restrictions lapse and it is possible the ultimate value to be realized by the Company could be significantly less upon a sale of the securities.

Net interest expense was \$725 in the third quarter of 2018 compared to \$337 in the third quarter of 2017. The increase is due to interest expense on borrowings during the quarter to fund the Halo acquisition partially offset by higher interest income generated from higher cash balances. There was \$325,000 outstanding on the Credit Facility at September 30, 2018. The average interest rate on debt was 3.6% in the third quarter of 2018. The Company did not have any debt outstanding as of September 30, 2017.

Income tax expense from continuing operations for the three months ended September 30, 2018 and 2017 was a benefit of \$15,406 compared to an expense of \$7,498, and an effective tax rate of 30.3%, respectively. Excluding the impacts of immediately recognizing certain effects of share-based compensation, acquisition and integration expenses, unrealized gain on investment in equity securities, a \$2,105 benefit for finalizing the TCJA toll charge, and a \$12,189 benefit for release of a state valuation allowance and the revaluation of state deferred tax balances due to New Jersey tax reform enacted during the quarter ended September 30, 2018, the effective tax rate would have been 19.6% for the three months ended September 30, 2018, compared to 33.2% for the three months ended September 30, 2017.

Income from continuing operations in the third quarter of 2018 was \$26,815, or \$0.79 per diluted share, versus \$17,276 or \$0.52 per diluted share in the same period a year ago.

Excluding the impact of the new revenue recognition standard, income from continuing operations in the third quarter of 2018 was \$31,818 or \$0.94 per diluted share.

#### Comparison of First Nine Months of 2018 versus First Nine Months of 2017

Net revenue in the first nine months of 2018 of \$397,761 was \$45,582 or 12.9% higher than the first nine months of 2017. Excluding a 1.8% favorable impact of foreign exchange compared to the first nine months of 2017, net revenue increased 11.1% as a result of higher volumes (11.3%) partially offset by lower pricing (0.2%). The increase in volumes was driven by the APIs segment and the addition of the FDF segment.

Excluding the impact of the new revenue recognition standard, net revenue in the first nine months of 2018 decreased 3.6% compared to the first nine months of 2017 to \$339,579.

The following table reflects net revenue by geographic area for the first nine months of 2018 and 2017:

|                   | First nine months |           |
|-------------------|-------------------|-----------|
|                   | 2018              | 2017      |
| Europe            | \$247,105         | \$199,759 |
| North America     | 127,341           | 131,995   |
| Asia              | 11,246            | 12,875    |
| Other             | 12,069            | 7,550     |
| Total net revenue | \$397,761         | \$352,179 |

Gross margins in the first nine months of 2018 decreased to 37.3% from 43.0% in the first nine months of 2017. Margins decreased in the APIs segment. Gross profit in the first nine months of 2018 was \$148,372 compared to \$151,377 in the same period last year.

Excluding the impact of the new revenue recognition standard, gross margins in the first nine months of 2018 decreased to 36.3%. Gross profit in the first nine months of 2018 would have been \$123,384.





## APIs

Net revenue in the first nine months of 2018 of \$392,687 was \$40,293 or 11.4% higher than the first nine months of 2017. Excluding a 1.8% favorable impact of foreign exchange compared to the first nine months of 2017, net revenue increased 9.6% as a result of higher volumes (9.8%) partially offset by lower pricing (0.2%). The increase in volumes was driven by higher sales of branded APIs and clinical phase products partially offset by lower sales of controlled substances.

Excluding the impact of the new revenue recognition standard, net revenue in the first nine months of 2018 decreased 5.4% compared to the first nine months of 2017 to \$333,363.

Gross margins in the first nine months of 2018 decreased to 37.4% from 43.0% in the first nine months of 2017. Gross profit in the first nine months of 2018 was \$146,800 compared to \$151,592 in the same period last year. Excluding the impact of the new revenue recognition standard, gross margins in the first nine months of 2018 were 36.5%. Gross profit in the first nine months of 2018 would have been \$121,698. The decrease was primarily driven by lower production volumes and higher raw material costs.

SG&A expenses of \$35,236 in the first nine months of 2018 increased compared to \$35,065 in the first nine months of 2017. The increase was mainly due to higher consulting costs associated with an operational excellence initiative (approximately \$800) partially offset by an accounts receivable write-off in the third quarter of 2017 (approximately \$700). Sales and marketing expenses were flat compared to the first nine months of 2017. SG&A, as a percentage of net revenue, was 9.0% and 10.0% in the first nine months of 2018 and 2017, respectively.

Research and development (“R&D”) expenses of \$10,128 were 2.6% of net revenue in the first nine months of 2018, compared to \$9,748 or 2.8% of net revenue in the first nine months of 2017. The increase was primarily driven by higher personnel costs (approximately \$2,000) and the impact of foreign currency (approximately \$200) partially offset by higher absorption of R&D expenses into inventory and cost of goods sold (approximately \$2,000).

Operating profit in the first nine months of 2018 was \$101,436 compared to \$106,779 in the first nine months of 2017. Excluding the impact of the new revenue recognition standard, operating profit in the first nine months of 2018 would have been \$76,334. The decrease in operating profit was due to lower gross profit and higher operating expenses as described above.

## FDF

Net revenue was \$5,154 for the period from acquisition date, September 12, 2018 through September 30, 2018. Excluding the impact of the new revenue recognition standard, net revenue was \$6,296.

Gross margins were 32.1% and gross profit was \$1,652. Excluding the impact of the new revenue recognition standard, gross margins were 28.0% and gross profit would have been \$1,766.

SG&A expenses were \$1,141 in the first nine months of 2018. SG&A, as a percentage of net revenue, was 22.1%.

FDF operating profit for the period September 12, 2018 through September 30, 2018 was \$508. Excluding the impact of the new revenue recognition standard, operating profit would have been \$622. Both exclude integration costs of \$394.

The Company's Corporate headquarters provides management and administrative services to support the Company, and consists of certain aspects of the Company's executive management, corporate relations, legal, compliance, human resources, and information technology and finance departments. The Company allocates certain corporate expenses to each of its segments. SG&A expenses of \$10,660 in the first nine months of

2018 decreased compared to \$15,613 in the first nine months of 2017. The decrease was mainly due to lower personnel related costs (approximately \$3,800) and lower due diligence costs, excluding Halo's acquisition costs (approximately \$700). R&D expenses of \$1,812 in the first nine months of 2018 decreased compared to \$2,842 in the same period last year. The decrease is due to the timing of spending on the development of generic drug products.

During the third quarter of 2018, the Company completed the acquisition of 100% of Halo, a finished dosage form Contract Development and Manufacturing Organization. All acquisition and integration costs have been expensed and totaled \$7,727 for the nine months ended September 30, 2018, of which \$394 was recorded by the FDF segment. These costs have been recorded to "Acquisition and integration expenses" on the Company's income statement.

During the second quarter of 2018, the Company acquired a 19.9% equity investment in a European company ("Investee"). The Investee completed an initial public offering on a foreign exchange late in the quarter, which reduced the Company's ownership share to 16.3%. The Company's investment is subject to a one-year prohibition on selling the shares. The Company has one seat on the Board of Directors of the investee and concluded it is able to exercise significant influence and that equity accounting would be appropriate. In accordance with ASC 825, the Company has elected to record this investment at fair value. The Company selected an appropriate valuation methodology to compute a discount for the lack of marketability to be applied to the closing market price of the shares as of September 30, 2018. The fair value of the Company's shares increased to \$10,825 during the first nine months of 2018 resulting in an unrealized gain that was recorded as "Unrealized gain on investment in equity securities" on the Company's income statement. Since the shares owned by the Company are substantially in excess of the daily trade volumes of the stock, it could be difficult to sell the shares in a timely manner when the restrictions lapse and it is possible the ultimate value to be realized by the Company could be significantly less upon a sale of the securities.

Net interest expense was \$824 in the first nine months of 2018 compared to \$991 in the first nine months of 2017. The decrease is due to higher interest income generated from higher cash balances partially offset by interest expense on borrowings during the quarter to fund the Halo acquisition. There was \$325,000 outstanding on the Credit Facility at September 30, 2018. The average interest rate on debt was 3.6% in the first nine months of 2018. The Company did not have any debt outstanding as of September 30, 2017.

Income tax expense from continuing operations for the nine months ended September 30, 2018 and 2017 was a benefit of \$872 compared to an expense of \$22,484, and an effective tax rate of 26.1%, respectively. Excluding the impacts of immediately recognizing certain effects of share-based compensation, acquisition and integration expenses, unrealized gain on investment in equity securities, a \$2,105 benefit for finalizing the TCJA toll charge, and a \$12,189 benefit for release of a state valuation allowance and the revaluation of state deferred tax balances due to New Jersey tax reform enacted during the quarter ended September 30, 2018, the effective tax rate would have been 20.5% for the nine months ended September 30, 2018, compared to 32.1% for the nine months ended September 30, 2017.

Income from continuing operations in the first nine months of 2018 was \$91,916, or \$2.73 per diluted share, versus \$63,515, or \$1.90 per diluted share in the same period a year ago.

Excluding the impact of the new revenue recognition standard, income from continuing operations in the first nine months of 2018 was \$72,004 or \$2.14 per diluted share.

#### Liquidity and Capital Resources

During the first nine months of 2018, cash provided by operations was \$39,764 versus \$72,085 in the same period a year ago. This decrease was primarily due the timing of accounts receivable collections and unbilled revenue.



Cash flows used in investing activities in the first nine months of 2018 were \$462,508 versus \$35,405 in the same period a year ago. The 2018 cash flows include the acquisition of Halo for \$418,963 and capital expenditures of \$43,545. The 2017 cash flows include capital expenditures of \$38,241 in the same period a year ago. Capital expenditures in the first nine months of 2018 and 2017 primarily expanded the Company's manufacturing capacity to support expected growth.

Cash flows provided by financing activities in the first nine months of 2018 were \$337,685 compared to \$3,448 in the same period a year ago. The 2018 cash flows include borrowings of \$325,000 to partially fund the Halo acquisition and proceeds from stock options exercised of \$12,685. The 2017 cash flows include proceeds from stock options exercised of \$3,448.

The Company expects to spend approximately \$70,000 to \$80,000 on capital expenditures during 2018, excluding acquisitions.

The Company has a \$500,000 Senior Credit Facility. Borrowings under the Credit Facility bear interest at a rate per annum of LIBOR plus a margin ranging from 1.25% to 2%. As of September 30, 2018, there was \$325,000 outstanding on the Credit Facility.

The Company believes that cash flows from operations, along with funds available from the revolving line of credit, will be adequate to meet the operational and debt servicing needs of the Company for the foreseeable future.

In September 2018, the Company completed the acquisition of 100% of Halo Pharma, a finished dosage form Contract Development and Manufacturing Organization. The deal was structured as a stock purchase for consideration of \$425,000. The Company utilized cash on hand and borrowings under the credit facility to pay the purchase price.

The Company's forecasted cash flow from future operations may be adversely affected by various factors including, but not limited to, declines in customer demand, increased competition, the deterioration in general economic and business conditions, increased environmental remediation, returns on assets within the Company's domestic pension plans, as well as other factors.

Our largest product (32.8% of 2017 sales) is used by our customer to produce an anti-viral drug. Our customer's sales of this drug have been trending downwards and, accordingly, we expect our sales of this product to our customer to also trend downwards over the next few years. We have a 5-year supply agreement ending in December 2020 that includes a defined minimum volume for 2019, which represents a further significant decline compared to the volumes we expect to ship in 2018. There is no minimum volume stipulated in the agreement for 2020.

As discussed more fully in Note 15 to the Consolidated Financial Statements, the Company continually receives additional information to develop estimates to record reserves for remediation activities at Berry's Creek and other environmental sites. These matters, either individually or in the aggregate, could result in actual costs that are significantly higher than the Company's current assessment and could have a material adverse effect on the Company's cash flows in future reporting periods. Based upon past experience, the Company believes that payments significantly in excess of current reserves, if required, would be made over an extended number of years.

See the "Risk Factors" section of the Company's Annual Report on Form 10-K for the period ended December 31, 2017 for further explanation of factors that may negatively impact the Company's cash flows.



### Impact of Recent Accounting Pronouncements

The following accounting pronouncements became effective for the Company January 1, 2018:

#### Revenue from Contracts with Customers

In May 2014, the FASB issued ASU 2014-09 which introduces a new five-step revenue recognition model in which an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services.

On January 1, 2018, the Company adopted the new accounting standard ASC Topic 606, Revenue from Contracts with Customers and all the related amendments (“new revenue standard”) to all contracts not completed as of January 1, 2018 using the modified retrospective method. The cumulative effect of initially applying the new revenue standard was \$16,219 and has been recorded as an adjustment to increase the opening balance of retained earnings. The cumulative effect adjustment relates primarily to the recognition of revenue and costs for contracts that transfer promised goods or services over time. Gross sales, cost of goods sold, and tax expense of \$51,896, \$31,347, and \$4,330 respectively, were recorded as part of the cumulative effect adjustment. The comparative information has not been restated and is reported in accordance with accounting standard Topic 605, which was in effect for those periods.

#### Presentation of Net Periodic Benefit Cost Related to Defined Benefit Plans

In March 2017, the FASB issued ASU 2017-07 which amends the requirements in ASC 715 related to the income statement presentation of the components of net periodic benefit cost for an entity’s sponsored defined pension and other postretirement plans. The ASU requires entities to disaggregate the current-service-cost component from the other components of net benefit cost and present it with other current compensation costs for related employees in the income statement and present the other components elsewhere in the income statement and outside of income from operations if such subtotal is presented. This standard became effective for the Company on January 1, 2018. For the three and nine months ended September 30, 2018, the Company recorded \$167 and \$649, respectively, to “Other expenses, net” which formerly would have been recorded as “Selling, general and administrative expenses” or “Cost of goods sold.” To conform to the current year presentation, for the three and nine months ended September 30, 2017 the Company reclassified \$384 and \$1,107, respectively, from “Selling, general and administrative expenses” and \$54 and \$161, respectively, from “Cost of goods sold” to “Other expenses, net.”

#### Scope of Modification Accounting, Stock Based Compensation

In May 2017, the FASB issued ASU 2017-09 which provides clarification on when modification accounting should be used for changes to the terms or conditions of a share-based payment award. This ASU does not change the accounting for modifications but clarifies that modification accounting guidance should only be applied if there is a change to the value, vesting conditions, or award classification and would not be required if the changes are considered non-substantive. The update became effective on January 1, 2018 and did not have a material impact on the Company’s consolidated financial statements.

#### Business Combinations – Clarifying the Definition of a Business



In January 2017, the FASB issued ASU 2017-01 which clarifies the definition of a business to assist entities with evaluating whether transactions should be accounted for as acquisitions or disposals of assets or businesses. The standard introduces a screen for determining when assets acquired are not a business and clarifies that a business must include, at a minimum, an input and a substantive process that contribute to an output to be considered a business. The amendment became effective on January 1, 2018 and did not have a material impact on the Company's consolidated financial statements.

#### Statement of Cash Flows - Classification of Certain Cash Receipts and Cash Payments

In August 2016, the FASB issued ASU 2016-15 which provides guidance on the presentation and classification in the statement of cash flows for specific cash receipt and payment transactions, including debt prepayment or extinguishment costs, contingent consideration payments made after a business combination, proceeds from the settlement of insurance claims and corporate-owned life insurance policies, and distributions received from equity method investees. The standard became effective on January 1, 2018 and did not have a material impact on the Company's consolidated financial statements.

#### Statement of Cash Flows – Restricted Cash

In November 2016, the FASB issued ASU 2016-18 which clarifies the presentation requirements of restricted cash within the statement of cash flows. The changes in restricted cash and restricted cash equivalents during the period should be included in the beginning and ending cash and cash equivalents balance reconciliation on the statement of cash flows. When cash, cash equivalents, restricted cash or restricted cash equivalents are presented in more than one line item within the statement of financial position, an entity shall calculate a total cash amount in a narrative or tabular format that agrees to the amount shown on the statement of cash flows. Details on the nature and amounts of restricted cash should also be disclosed. The update became effective on January 1, 2018 and did not have a material impact on the Company's consolidated financial statements.

#### Recognition and Measurement of Financial Assets and Financial Liabilities

In January 2016, the FASB issued ASU 2016-01, Recognition and Measurement of Financial Assets and Financial Liabilities. The ASU amends guidance on the classification and measurement of financial instruments, including significant revisions in accounting related to the classification and measurement of investments in equity securities and presentation of certain fair value changes for financial liabilities when the fair value option is elected. The ASU requires equity securities to be measured at fair value with changes in fair value recognized through net earnings and amends certain disclosure requirements associated with the fair value of financial instruments. In the period of adoption, the Company is required to reclassify the unrealized gains/losses on equity securities within accumulated other comprehensive income/(loss) to retained earnings. In February 2018, the FASB issued ASU 2018-03, Technical Corrections and Improvements to Financial Instruments—Overall (Subtopic 825-10), which clarified certain aspects of the previously issued ASU. The ASU was adopted by the Company on January 1, 2018 and did not have a material effect on the Company's consolidated financial statements.

The following recently issued accounting pronouncements will become effective for the Company in future periods:

#### Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income

In February 2018, the FASB issued ASU 2018-02 to address the tax effects of the Tax Cuts & Jobs Act ("TCJA") on amounts that were initially recognized directly in AOCI. ASU 2018-02 allows an entity to elect a one-time reclassification from AOCI to retained earnings of stranded tax effects due to the enactment of TCJA, equal to the difference between the amount initially charged or credited directly to AOCI at the previously enacted U.S. federal corporate income tax rate and the amount that would have been charged or credited directly to AOCI by using the newly enacted tax rate, excluding the effect of any valuation allowance previously charged to income from continuing operations. ASU 2018-02 is effective for fiscal years beginning after December 15, 2018, and interim periods within

those fiscal years. The Company has evaluated the provisions of ASU 2018-02 and has determined it will not elect the reclassification from AOCI to retained earnings addressed in the ASU.

#### Effects of the Tax Cuts and Jobs Act

In March 2018, the FASB issued ASU 2018-05, Income Taxes (Topic 740): Amendments to SEC Paragraphs Pursuant to SEC Staff Accounting Bulletin No. 118 (“SAB No. 118”) which allowed SEC registrants to record provisional amounts for the year ended December 31, 2017 due to the complexities involved in accounting for the enactment of TCJA. The Company recognized the estimated income tax effects of TCJA in its 2017 Consolidated Financial Statements in accordance with SAB No. 118. Refer to Note 7 for further information. The Company’s accounting for the TCJA one-time toll charge on previously undistributed accumulated foreign earnings has been completed, resulting in a \$2,105 measurement period tax benefit and corresponding reduction in taxes payable. In accordance with SAB No. 118, any additional adjustment to the financial reporting impacts of TCJA will be completed by December 31, 2018.

#### Improvements to Nonemployee Share-Based Payment Accounting

In June 2018, the FASB issued ASU 2018-07 which aligns the accounting for share-based payment awards issued to nonemployees with those issued to employees. Under the new guidance, the nonemployee awards will be measured on the grant date and compensation costs will be recognized when achievement of the performance condition is probable. This new standard is effective for fiscal years beginning after December 15, 2018, including interim periods within that fiscal year. Early adoption is permitted. The Company is currently evaluating the new guidance and does not expect it to have a material impact on its consolidated financial statements.

#### Changes to the Disclosure Requirements for Fair Value Measurement

In August 2018, the FASB issued ASU 2018-13 which modifies the disclosure requirements for recurring and nonrecurring fair value measurements, primarily those surrounding Level 3 fair value measurements and transfers between Level 1 and Level 2. The new standard is effective for fiscal years beginning after December 15, 2019, including interim periods within that reporting period. The Company is currently evaluating the new guidance and does not expect it to have an impact on its consolidated financial statements.

#### Changes to the Disclosure Requirements for Defined Benefit Plans

In August 2018, the FASB issued ASU 2018-14 which adds, modifies and removes certain disclosure requirements to improve the effectiveness of disclosures for defined benefit plans. The new standard is effective for fiscal years beginning after December 15, 2020, including interim periods within that reporting period. The Company is currently evaluating the new guidance and does not expect it to have an impact on its consolidated financial statements.

#### Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement that is a Service Contract

In August 2018, the FASB issued ASU 2018-15 which states entities should apply the guidance in ASC 350-40 when capitalizing implementation costs related to a hosting arrangement that is a service contract. The capitalized implementation costs should be classified as prepaid expenses and then expensed over the hosting arrangement’s term, with the expense recorded on the same line of the income statement as the service contract. The new standard is effective for fiscal years beginning after December 15, 2019, including interim periods within that reporting period. The Company is currently assessing the impact that adopting this new accounting standard will have on its consolidated financial statements.

#### Leases

In February 2016, the FASB issued ASU 2016-02 which requires lessees to recognize right of use assets and lease liabilities on the balance sheet for all leases with terms greater than twelve months. This standard is effective for fiscal years beginning after December 15, 2018, including interim periods within that reporting period. At this time, the Company has no significant financing leases and only a limited number of

operating leases. The result of adoption will be an increase to assets and liabilities by the same amount for the identified operating leases. Several updates have been issued in 2018 that provide clarification on a number of specific issues and reporting requirements. The Company is currently evaluating the new guidance and does not expect the adjustment will be material to the Company, assuming there is not an increase in lease activity.

#### Simplifying the Test for Goodwill Impairment

In January 2017, the FASB issued ASU 2017-04 which simplifies the goodwill impairment test by eliminating Step 2 in the determination on whether goodwill should be considered impaired. Instead, an impairment charge should equal the amount by which a reporting unit's carrying amount exceeds its fair value, not to exceed the amount of goodwill allocated to the reporting unit. The new standard is effective for fiscal years beginning after December 15, 2019, including interim periods within that reporting period. The Company is currently evaluating the new guidance and does not expect it to have an impact on its consolidated financial statements.

#### Targeted Improvements to Accounting for Hedging Activities

In August 2017, the FASB issued ASU 2017-12 which improves the financial reporting of hedging relationships to better portray the economic results of an entity's risk management activities in its financial statements. The standard also makes certain targeted improvements to simplify the application of the hedge accounting guidance. The amendment is effective for fiscal years beginning after December 15, 2018, including interim periods within that reporting period. The Company is currently assessing the impact that adopting this new accounting standard will have on its consolidated financial statements.

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

There has been no significant change in the Company's exposure to market risk during the first nine months of 2018. For a discussion of the Company's exposure to market risk, refer to Part II, Item 7A, "Quantitative and Qualitative Disclosures about Market Risk," contained in the Company's Annual Report on Form 10-K for the period ended December 31, 2017.

#### Item 4. Controls and Procedures

##### Evaluation of Disclosure Controls and Procedures

As required by Rule 13a-15(b) under the Securities Exchange Act of 1934 (the "Exchange Act"), 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 Form 10-Q. Based on this evaluation, our Chief Executive Officer and Chief Financial Officer have concluded that, as of the end of such period, our disclosure controls and procedures are effective to ensure that information required to be disclosed by us in the reports that we file or submit under the Exchange Act is (i) recorded, processed, summarized and reported, within the time periods specified in the SEC's rules and forms and (ii) accumulated and communicated to management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure.

##### Changes in Internal Control over Financial Reporting

There were no changes in our internal control over financial reporting identified in connection with the evaluation required by paragraph (d) of Exchange Act Rules 13a-15 or 15d-15 that occurred during the quarter covered by this

report that has materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II - OTHER INFORMATION

CAMBREX CORPORATION AND SUBSIDIARIES

Item 1. Legal Proceedings

See the discussion under Part I, Item 1, Note 15 to the Company's Consolidated Financial Statements.

Item 1A. Risk Factors

There have been no material changes to the Company's risk factors and uncertainties during the first nine months of 2018. For a discussion of the Risk Factors, refer to Part I, Item 1A, "Risk Factors," contained in the Company's Annual Report on Form 10-K for the period ended December 31, 2017.

Item 6. Exhibits

Exhibit 31.1\* Section 302 Certification Statement of the Chief Executive Officer.

Exhibit 31.2\* Section 302 Certification Statement of the Chief Financial Officer.

Exhibit 32.1\*\* Section 906 Certification Statements of the Chief Executive Officer and Chief Financial Officer.

Exhibit 101.INS\* XBRL Instance Document

Exhibit 101.SCH\* XBRL Taxonomy Extension Schema

Exhibit 101.CAL\* XBRL Taxonomy Extension Calculation Linkbase

Exhibit 101.DEF\* XBRL Taxonomy Extension Definition Linkbase

Exhibit 101.LAB\* XBRL Taxonomy Extension Label Linkbase

Exhibit 101.PRE\* XBRL Taxonomy Extension Presentation Linkbase

\* Filed herewith



\*\*Furnished herewith

Attached as Exhibit 101 to this report are the following formatted in XBRL (Extensible Business Reporting Language): (i) Consolidated Balance Sheets as of September 30, 2018 and December 31, 2017, (ii) Consolidated Income Statements for the three and nine months ended September 30, 2018 and 2017, (iii) Consolidated Statements of Comprehensive Income for the three and nine months ended September 30, 2018 and 2017, (iv) Consolidated Statements of Cash Flows for the nine months ended September 30, 2018 and 2017, and (v) Notes to Consolidated Financial Statements.

45

---

Signatures

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

CAMBREX CORPORATION

By/s/Gregory P. Sargen  
Gregory P. Sargen  
Executive Vice President and  
Chief Financial Officer  
(On behalf of the Registrant and as the  
Registrant's Principal Financial Officer)

Dated: November 8, 2018