

OIL DRI CORP OF AMERICA
Form 10-Q
March 10, 2017

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D. C. 20549

FORM 10-Q

(Mark One)

Quarterly Report Pursuant to Section 13 or 15(d)
of the
 Securities Exchange Act of 1934
For the Quarterly Period Ended January 31, 2017

or

Transition Report Pursuant to Section 13 or 15(d) of the
o Securities Exchange Act of 1934
For the transition period from _____ to _____

Commission File Number 001-12622

OIL-DRI CORPORATION OF AMERICA
(Exact name of the registrant as specified in its charter)

Delaware 36-2048898
(State or other jurisdiction of incorporation or (I.R.S. Employer
organization) Identification No.)

410 North Michigan Avenue, Suite 400 60611-4213
Chicago, Illinois (Zip Code)
(Address of principal executive offices)

The registrant's telephone number, including area code: (312) 321-1515

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 at least the past 90 days.

Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes No

Edgar Filing: OIL DRI CORP OF AMERICA - Form 10-Q

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

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

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

Yes No

Indicate the number of shares outstanding of each of the issuer’s classes of common stock as of January 31, 2017.

Common Stock – 5,108,389 Shares and Class B Stock – 2,188,771 Shares

CONTENTS

PART I – FINANCIAL INFORMATION	
Item 1: <u>Financial Statements</u>	Page <u>3</u>
Item 2: <u>Management’s Discussion and Analysis of Financial Condition and Results Of Operations</u>	<u>19</u>
Item 3: <u>Quantitative and Qualitative Disclosures About Market Risk</u>	<u>26</u>
Item 4: <u>Controls and Procedures</u>	<u>27</u>
PART II – OTHER INFORMATION	
Item 4: <u>Mine Safety Disclosures</u>	<u>28</u>
Item 6: <u>Exhibits</u>	<u>28</u>
<u>Signatures</u>	<u>29</u>

FORWARD-LOOKING STATEMENTS

Certain statements in this report, including, but not limited to, those under the heading “Management’s Discussion and Analysis of Financial Condition and Results of Operations” and those statements elsewhere in this report and other documents that we file with the Securities and Exchange Commission (“SEC”), contain forward-looking statements that are based on current expectations, estimates, forecasts and projections about our future performance, our business, our beliefs and our management’s assumptions. In addition, we, or others on our behalf, may make forward-looking statements in press releases or written statements, or in our communications and discussions with investors and analysts in the normal course of business through meetings, webcasts, phone calls and conference calls. Words such as “expect,” “outlook,” “forecast,” “would,” “could,” “should,” “project,” “intend,” “plan,” “continue,” “believe,” “seek,” “estimate,” “assume,” and variations of such words and similar expressions are intended to identify such forward-looking statements, which are made pursuant to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995.

Such statements are subject to certain risks, uncertainties and assumptions that could cause actual results to differ materially, including those described in Item 1A, Risk Factors, of our Annual Report on Form 10-K for the fiscal year ended July 31, 2016. Should one or more of these or other risks or uncertainties materialize, or should underlying assumptions prove incorrect, actual results may vary materially from those anticipated, intended, expected, believed, estimated, projected or planned. Investors are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date hereof. Except to the extent required by law, we do not have any intention or obligation to update publicly any forward-looking statements after the distribution of this report, whether as a result of new information, future events, changes in assumptions or otherwise.

TRADEMARK NOTICE

Cat’s Pride, Fresh & Light, Fresh & Light Ultimate Care and Oil-Dri are registered trademarks of Oil-Dri Corporation of America.

PART I - FINANCIAL INFORMATION

ITEM 1. Financial Statements

OIL-DRI CORPORATION OF AMERICA & SUBSIDIARIES

Condensed Consolidated Balance Sheets

(in thousands, except share and per share amounts)

ASSETS	(unaudited) January 31, 2017	July 31, 2016
Current Assets		
Cash and cash equivalents	\$ 17,560	\$ 18,629
Short-term investments	7,358	10,184
Accounts receivable, less allowance of \$881 and \$753 at January 31, 2017 and July 31, 2016, respectively	32,047	30,386
Inventories	23,217	23,251
Deferred income taxes	3,884	3,884
Prepaid repairs expense	4,054	3,938
Prepaid expenses and other assets	4,658	901
Total Current Assets	92,778	91,173
Property, Plant and Equipment		
Cost	217,359	218,025
Less accumulated depreciation and amortization	(135,861)	(137,314)
Total Property, Plant and Equipment, Net	81,498	80,711
Other Assets		
Goodwill	9,034	9,034
Trademarks and patents, net of accumulated amortization of \$279 and \$261 at January 31, 2017 and July 31, 2016,	999	916

respectively				
Customer list, net of				
accumulated				
amortization				
of \$4,031 and				
\$3,460 at January	3,754		4,325	
31, 2017 and July				
31, 2016,				
respectively				
Deferred income				
taxes	12,319		12,754	
Other	6,192		5,902	
Total Other Assets	32,298		32,931	
Total Assets	\$	206,574	\$	204,815

The accompanying notes are an integral part of the Condensed Consolidated Financial Statements.

OIL-DRI CORPORATION OF AMERICA & SUBSIDIARIES

Condensed Consolidated Balance Sheets

(in thousands, except share and per share amounts)

	(unaudited)	
	January 31,	July 31,
	2017	2016
LIABILITIES & STOCKHOLDERS' EQUITY		
Current Liabilities		
Current maturities of notes payable	\$ 3,083	\$ 3,083
Accounts payable	7,316	6,635
Dividends payable	1,485	1,477
Accrued expenses:		
Salaries, wages and commissions	6,675	8,656
Trade promotions and advertising	2,487	2,855
Freight	1,699	1,579
Other	6,753	6,455
Total Current Liabilities	29,498	30,740
Noncurrent Liabilities		
Notes payable, net of unamortized debt issuance costs of \$103 and \$118 at January 31, 2017 and July 31, 2016, respectively	9,147	12,215
Deferred compensation	10,991	10,504
Pension and postretirement benefits	32,915	32,492
Other	3,518	3,313
Total Noncurrent Liabilities	56,571	58,524
Total Liabilities	86,069	89,264
Stockholders' Equity		
Common Stock, par value \$.10 per share, issued 8,015,166 shares at January 31, 2017 and 7,982,243 shares at July 31, 2016	802	798
Class B Stock, par value \$.10 per share, issued 2,513,512 shares at January 31, 2017 and 2,515,735 shares at July 31, 2016	251	252
Additional paid-in capital	35,288	34,294
Retained earnings	153,240	149,945
Accumulated other comprehensive loss:		
Pension and postretirement benefits	(13,289)	(13,867)
Cumulative translation adjustment	(106)	(155)
Total accumulated other comprehensive loss	(13,395)	(14,022)
Less Treasury Stock, at cost (2,906,777 Common and 324,741 Class B shares at January 31, 2017 and 2,912,953 Common and 324,741 Class B shares at July 31, 2016)	(55,681)	(55,716)
Total Stockholders' Equity	120,505	115,551
Total Liabilities & Stockholders' Equity	\$ 206,574	\$ 204,815

The accompanying notes are an integral part of the Condensed Consolidated Financial Statements.

OIL-DRI CORPORATION OF AMERICA & SUBSIDIARIES
Condensed Consolidated Statements of Income and Retained Earnings
(in thousands, except for per share amounts)

	(unaudited)	
	For the Six Months	
	Ended January 31,	
	2017	2016
Net Sales	\$ 131,786	\$ 133,162
Cost of Sales	(91,936)	(93,447)
Gross Profit	39,850	39,715
Selling, General and Administrative Expenses	(31,217)	(26,539)
Income from Operations	8,633	13,176
Other Income (Expense)		
Interest expense	(489)	(511)
Interest income	16	9
Other, net	(237)	(65)
Total Other Expense, Net	(710)	(567)
Income Before Income Taxes	7,923	12,609
Income Taxes	(1,664)	(3,365)
Net Income	6,259	9,244
Retained Earnings:		
Balance at beginning of period	149,945	142,095
Cash dividends declared and treasury stock issuances	(2,964)	(2,846)
Balance at End of Period	\$ 153,240	\$ 148,493
Net Income Per Share		
Basic Common	\$0.93	\$1.39
Basic Class B Common	\$0.70	\$1.04
Diluted Common	\$0.86	\$1.28
Average Shares Outstanding		
Basic Common	5,011	4,978
Basic Class B Common	2,077	2,046
Diluted Common	7,145	7,074
Dividends Declared Per Share		
Basic Common	\$0.4400	\$0.4200
Basic Class B Common	\$0.3300	\$0.3150

The accompanying notes are an integral part of the Condensed Consolidated Financial Statements.

OIL-DRI CORPORATION OF AMERICA & SUBSIDIARIES
 Condensed Consolidated Statements of Comprehensive Income
 (in thousands of dollars)

(unaudited)
 For the Six
 Months Ended
 January 31,
 2017 2016

Net Income	\$6,259	\$9,244
Other Comprehensive Income:		
Pension and postretirement benefits (net of tax)	578	308
Cumulative translation adjustment	49	(150)
Other Comprehensive Income	627	158
Total Comprehensive Income	\$6,886	\$9,402

The accompanying notes are an integral part of the Condensed Consolidated Financial Statements.

OIL-DRI CORPORATION OF AMERICA & SUBSIDIARIES
Condensed Consolidated Statements of Income and Retained Earnings
(in thousands, except for per share amounts)

	(unaudited)	
	For the Three	
	Months Ended	
	January 31,	
	2017	2016
Net Sales	\$65,174	\$65,367
Cost of Sales	(46,049)	(46,305)
Gross Profit	19,125	19,062
Selling, General and Administrative Expenses	(13,538)	(13,662)
Income from Operations	5,587	5,400
Other Income (Expense)		
Interest expense	(238)	(252)
Interest income	8	6
Other, net	(113)	(85)
Total Other Expense, Net	(343)	(331)
Income Before Income Taxes	5,244	5,069
Income Taxes	(994)	(1,248)
Net Income	4,250	3,821
Net Income Per Share		
Basic Common	\$0.63	\$0.57
Basic Class B	\$0.47	\$0.43
Diluted Common	\$0.58	\$0.53
Average Shares Outstanding		
Basic Common	5,019	4,982
Basic Class B	2,088	2,055
Diluted Common	7,155	7,096
Dividends Declared Per Share		
Basic Common	\$0.2200	\$0.2100
Basic Class B	\$0.1650	\$0.1575

The accompanying notes are an integral part of the Condensed Consolidated Financial Statements.

OIL-DRI CORPORATION OF AMERICA & SUBSIDIARIES
 Condensed Consolidated Statements of Comprehensive Income
 (in thousands of dollars)

	(unaudited)	
	For the Three	
	Months Ended	
	January 31,	
	2017	2016
Net Income	\$4,250	\$3,821
Other Comprehensive Income (Loss):		
Pension and postretirement benefits (net of tax)	309	130
Cumulative translation adjustment	63	(139)
Other Comprehensive Income (Loss)	372	(9)
Total Comprehensive Income	\$4,622	\$3,812

The accompanying notes are an integral part of the Condensed Consolidated Financial Statements.

OIL-DRI CORPORATION OF AMERICA & SUBSIDIARIES

Condensed Consolidated Statements of Cash Flows

(in thousands)

	(unaudited)	
	For the Six Months	
	Ended January 31,	
	2017	2016
CASH FLOWS FROM OPERATING ACTIVITIES		
Net Income	\$6,259	\$9,244
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	6,389	5,914
Amortization of investment net discount	(5)	(2)
Non-cash stock compensation expense	777	638
Excess tax benefits for share-based payments	(207)	(55)
Deferred income taxes	354	189
Provision for bad debts and cash discounts	131	131
Loss on the sale of fixed assets	276	202
(Increase) Decrease in assets:		
Accounts receivable	(1,829)	521
Inventories	11	(1,674)
Prepaid expenses	(3,784)	(2,671)
Other assets	(156)	(118)
Increase (Decrease) in liabilities:		
Accounts payable	852	(201)
Accrued expenses	(1,698)	3,295
Deferred compensation	487	104
Pension and postretirement benefits	1,001	554
Other liabilities	235	980
Total Adjustments	2,834	7,807
Net Cash Provided by Operating Activities	9,093	17,051
CASH FLOWS FROM INVESTING ACTIVITIES		
Capital expenditures	(7,279)	(4,795)
Proceeds from sale of property, plant and equipment	2	249
Purchases of short-term investments	(11,555)	(14,125)
Dispositions of short-term investments	14,386	1,225
Net Cash Used in Investing Activities	(4,446)	(17,446)
CASH FLOWS FROM FINANCING ACTIVITIES		
Principal payments on notes payable	(3,083)	(3,484)
Dividends paid	(2,956)	(2,783)
Purchase of treasury stock	(122)	(18)
Proceeds from issuance of treasury stock	—	185
Proceeds from issuance of common stock	170	96
Excess tax benefits for share-based payments	207	55
Net Cash Used in Financing Activities	(5,784)	(5,949)
Effect of exchange rate changes on cash and cash equivalents	68	33
Net Decrease in Cash and Cash Equivalents	(1,069)	(6,311)
Cash and Cash Equivalents, Beginning of Period	18,629	20,138
Cash and Cash Equivalents, End of Period	\$17,560	\$13,827

OIL-DRI CORPORATION OF AMERICA & SUBSIDIARIES
Condensed Consolidated Statements of Cash Flows - Continued
(in thousands)

	(unaudited)	
	For the Six	
	Months Ended	
	January 31,	
	2017	2016
Supplemental disclosure of non-cash investing and financing activities:		
Capital expenditures accrued, but not paid	\$657	\$924
Cash dividends declared and accrued, but not paid	\$1,485	\$1,407

The accompanying notes are an integral part of the Condensed Consolidated Financial Statements.

OIL-DRI CORPORATION OF AMERICA & SUBSIDIARIES

Notes To Condensed Consolidated Financial Statements

(Unaudited)

1. BASIS OF STATEMENT PRESENTATION

The accompanying unaudited Condensed Consolidated Financial Statements have been prepared in accordance with accounting principles generally accepted in the United States of America (“U.S. GAAP”) for interim financial information and in compliance with instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by U.S. GAAP for complete financial statements. The financial statements and the related notes are condensed and should be read in conjunction with the Consolidated Financial Statements and related notes for the fiscal year ended July 31, 2016 included in our Annual Report on Form 10-K filed with the SEC.

The unaudited Condensed Consolidated Financial Statements include the accounts of Oil-Dri Corporation of America and its subsidiaries. All significant intercompany transactions are eliminated. Except as otherwise indicated herein or as the context otherwise requires, references to “Oil-Dri,” the “Company,” “we,” “us” or “our” refer to Oil-Dri Corporation of America and its subsidiaries.

The unaudited Condensed Consolidated Financial Statements reflect all adjustments, consisting of normal recurring accruals and reclassifications which are, in the opinion of management, necessary for a fair presentation of the statements contained herein. Operating results for the three and six months ended January 31, 2017 are not necessarily an indication of the results that may be expected for the fiscal year ending July 31, 2017.

The preparation of the unaudited Condensed Consolidated Financial Statements in conformity with U.S. GAAP requires the use of estimates and assumptions that affect the reported amounts of assets, liabilities, revenues, expenses and related disclosures. Estimates and assumptions are revised periodically. Actual results could differ from these estimates.

We recognize revenue when risk of loss and title are transferred under the terms of our sales agreements with customers at a fixed and determinable price and collection of payment is probable. Trade promotion reserves are provided for sales incentives made directly to consumers, such as coupons, and sales incentives made to customers, such as slotting, discounts based on sales volume, cooperative marketing programs and other arrangements. Such trade promotion costs are netted against sales. Sales returns and allowances are not material.

Selling, general and administrative expenses include salaries, wages and benefits associated with staff outside the manufacturing and distribution functions, all advertising and marketing-related costs, any miscellaneous trade spending expenses not required to be included in net sales, research and development costs, depreciation and amortization related to assets outside the manufacturing and distribution process and all other non-manufacturing and non-distribution expenses.

We record an allowance for doubtful accounts based on our historical experience and a periodic review of our accounts receivable, including a review of the overall aging of accounts and analysis of specific customer accounts. A customer account is determined to be uncollectible when we have completed our internal collection procedures, including termination of shipments, direct customer contact and formal demand of payment.

We mine sorbent materials on property that we either own or lease as part of our overall operations. A significant part of our overall mining cost is incurred during the process of removing the overburden (non-usable material) from the mine site, thus exposing the sorbent material used in a majority of our production processes. These stripping costs are

treated as a variable inventory production cost and are included in cost of sales in the period they are incurred. We defer and amortize the pre-production overburden removal costs associated with opening a new mine.

Additionally, it is our policy to capitalize the purchase cost of land and mineral rights, including associated legal fees, survey fees and real estate fees. The costs of obtaining mineral patents, including legal fees and drilling expenses, are also capitalized. Pre-production development costs on new mines and any prepaid royalties that may be offset against future royalties due upon extraction of the minerals are also capitalized. All exploration related costs are expensed as incurred.

We perform ongoing reclamation activities during the normal course of our overburden removal. As overburden is removed from a mine site, it is hauled to previously mined sites and is used to refill older sites. This process allows us to continuously reclaim older mine sites and dispose of overburden simultaneously, thereby minimizing the costs associated with the reclamation process.

2. NEW ACCOUNTING PRONOUNCEMENTS

Recently Issued Pronouncements

In May 2014, the Financial Accounting Standards Board (“FASB”) issued guidance under Accounting Standard Codification (“ASC”) 606, Revenue from Contract with Customers, which establishes a single comprehensive revenue recognition model for all contracts with customers and will supersede most existing revenue guidance. This guidance requires entities to 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 to receive in exchange. In March, April, May and December of 2016, the FASB issued amended guidance that further clarifies the principles for recognizing revenue. We are currently in the process of performing a comprehensive evaluation of these requirements, including the impact on how we record certain incentives and advertising arrangements. The implementation date for this guidance was deferred and will now be effective at the beginning of our first quarter of fiscal year 2019. Transition options to implement this guidance include either a full or modified retrospective approach and early adoption is permitted. We have not yet selected an implementation method.

In August 2014, the FASB issued guidance under ASC 205, Presentation of Financial Statements - Going Concern, which defines management's responsibility to evaluate whether there is substantial doubt about an organization's ability to continue as a going concern and to provide related footnote disclosures. This guidance will be effective for the fourth quarter of fiscal year 2017. This pronouncement requires additional disclosures only in certain circumstances, and we do not expect a significant impact on our Consolidated Financial Statements.

In July 2015, the FASB issued guidance under ASC 330, Simplifying the Measurement of Inventory. The new guidance requires inventory to be measured at the lower of cost and net realizable value, which is defined as the estimated selling price in the ordinary course of business less reasonably predictable costs of completion, disposal and transportation. This new guidance is effective for our first quarter of fiscal year 2018 and early adoption is permitted. The guidance must be applied prospectively. We are currently evaluating the impact of the adoption of this requirement on our Consolidated Financial Statements.

In November 2015, the FASB issued guidance under ASC 740, Balance Sheet Classification of Deferred Taxes, which requires deferred tax liabilities and assets to be classified as noncurrent in a classified statement of financial position. This guidance is effective for our first quarter of fiscal year 2018 and early adoption is permitted. The guidance may be applied either prospectively or retrospectively to all periods presented. We are currently evaluating the impact of the adoption of this requirement on our Consolidated Financial Statements.

In January 2016, the FASB issued guidance under ASC 825, Recognition and Measurement of Financial Assets and Financial Liabilities. This guidance addresses certain aspects of recognition, measurement, presentation and disclosure of financial instruments. The provisions relevant to us at this time require the use of the exit price notion when measuring the fair value of financial instruments for disclosure purposes, as well as eliminates the requirement to disclose the method and significant assumptions used to estimate the fair value in such disclosure. This guidance is effective for our first quarter of fiscal year 2019 and early adoption is generally not permitted. We are currently evaluating the impact of the adoption of this requirement on our Consolidated Financial Statements.

In February 2016, the FASB issued guidance under ASC 842, Leases, which provides that, for leases with a term greater than 12 months, a lessee must recognize in the statement of financial position both a liability to make lease payments and an asset representing its right to use the underlying asset. Other requirements describe expense recognition, as well as financial statement presentation and disclosure. This guidance is effective for our first quarter of fiscal year 2020 using a modified retrospective approach, which includes a number of optional practical expedients. Early adoption is permitted. We are currently evaluating the impact of the adoption of this requirement on our

Consolidated Financial Statements.

In March 2016, the FASB issued guidance under ASC 718, Compensation-Stock Compensation, which simplifies several aspects of the accounting for share-based payment transactions, including accounting for forfeitures, employer tax withholding on share-based compensation and the financial statement presentation of excess tax benefits or deficiencies. The new guidance also clarifies the statement of cash flows presentation for certain components of share-based awards. This guidance is effective for our first quarter of fiscal year 2018, with early adoption permitted. We are currently evaluating the impact of the adoption of this requirement on our Consolidated Financial Statements. In June 2016, the FASB issued guidance under ASC 326, Financial Instruments-Credit Losses, which requires companies to utilize an impairment model for most financial assets measured at amortized cost and certain other financial instruments, which include trade and other receivables, loans and held-to-maturity debt securities, to record an allowance for credit risk based on expected losses rather than incurred losses. In addition, this new guidance changes the recognition method for credit losses on available-

for-sale debt securities, which can occur as a result of market and credit risk, as well as additional disclosures. In general, this guidance will require modified retrospective adoption for all outstanding instruments that fall under this guidance. This guidance is effective for our first quarter of fiscal year 2021. We are currently evaluating the impact of the adoption of this requirement on our Consolidated Financial Statements.

There have been no other accounting pronouncements issued but not yet adopted by us which are expected to have a material impact on our Consolidated Financial Statements.

Recently Adopted Pronouncements

For the first quarter of fiscal 2017, we adopted FASB guidance under ASC 835, Simplifying the Presentation of Debt Issuance Cost, which requires debt issuance costs related to notes payable to be presented as a direct deduction from the associated debt liability rather than as an asset. Amortization of these costs will continue to be reported as interest expense. We adopted this guidance retrospectively, which resulted in a decrease in Other Assets of \$118,000 with a corresponding decrease in Noncurrent Liabilities in our Condensed Consolidated Balance Sheets as of July 31, 2016. The new requirements had no impact on our results of operations or cash flows.

3. INVENTORIES

The composition of inventories is as follows (in thousands):

	January 31, 2017	July 31, 2016
Finished goods	\$ 14,189	\$14,032
Packaging	4,811	4,672
Other	4,217	4,547
Total Inventories	\$ 23,217	\$23,251

Inventories are valued at the lower of cost (first-in, first-out) or market. Inventory costs include the cost of raw materials, packaging supplies, labor and other overhead costs. We perform a detailed review of our inventory items to determine if an obsolescence reserve adjustment is necessary. The review surveys all of our operating facilities and sales groups to ensure that both historical issues and new market trends are considered. The obsolescence reserve not only considers specific items, but also takes into consideration the overall value of the inventory as of the balance sheet date. The inventory obsolescence reserve values at January 31, 2017 and July 31, 2016 were \$720,000 and \$806,000, respectively.

4. FAIR VALUE MEASUREMENTS

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The inputs used to measure fair value are prioritized into categories based on the lowest level of input that is significant to the fair value measurement. The categories in the fair value hierarchy are as follows:

Level 1: Quoted market prices in active markets for identical assets or liabilities.

Level 2: Observable market-based inputs for similar assets or liabilities or valuation models whose inputs are observable, directly or indirectly.

Level 3: Unobservable inputs.

Cash equivalents of \$4,194,000 and \$7,626,000 as of January 31, 2017 and July 31, 2016, respectively, were classified as Level 1. These cash instruments are primarily money market mutual funds and are included in cash and cash equivalents on the Condensed Consolidated Balance Sheets.

Short-term investments included U.S. Treasury securities and certificates of deposit. We intend and have the ability to hold our short-term investments to maturity; therefore, these investments were reported at amortized cost, which approximated fair value as of January 31, 2017 and July 31, 2016.

Accounts receivable and accounts payable balances approximated their fair values at January 31, 2017 and July 31, 2016 due to the short maturity and nature of those balances.

Notes payable are reported at the face amount of future maturities. The estimated fair value of notes payable, including current maturities, was \$13,194,000 and \$16,651,000 as of January 31, 2017 and July 31, 2016, respectively. Our debt does not trade on a daily basis in an active market, therefore the fair value estimate is based on market observable borrowing rates currently available for debt with similar terms and average maturities and is classified as Level 2.

We apply fair value techniques on at least an annual basis associated with: (1) valuing potential impairment loss related to goodwill, trademarks and other indefinite-lived intangible assets and (2) valuing potential impairment loss related to long-lived assets. See Note 5 for further information about goodwill and other intangible assets.

5. GOODWILL AND OTHER INTANGIBLE ASSETS

Intangible amortization expense was \$307,000 and \$364,000 in the second quarter of fiscal 2017 and 2016, respectively. Intangible amortization expense was \$612,000 and \$727,000 for the first six months of fiscal 2017 and 2016, respectively. Estimated intangible amortization for the remainder of fiscal 2017 is \$612,000. Estimated intangible amortization for the next five fiscal years is as follows (in thousands):

2018 \$1,014

2019 \$827

2020 \$657

2021 \$473

2022 \$323

We have one acquired trademark recorded at a cost of \$376,000 that was determined to have an indefinite life and is not amortized.

We performed our annual goodwill impairment analysis in the fourth quarter of fiscal 2016 and no impairment was identified. There have been no triggering events that would indicate a new impairment analysis is needed.

6. PENSION AND OTHER POSTRETIREMENT BENEFITS

The components of net periodic pension and postretirement health benefit costs were as follows:

	Pension Benefits (in thousands)			
	For the Three Months Ended January 31,		For the Six Months Ended January 31,	
	2017	2016	2017	2016
	Service cost	\$446	\$267	\$913
Interest cost	474	484	931	967
Expected return on plan assets	(411)	(485)	(887)	(962)
Amortization of:				
Prior service costs	—	2	1	4
Other actuarial loss	485	209	914	496
Net periodic benefit cost	\$994	\$477	\$1,872	\$1,261

	Postretirement Health Benefits (in thousands)			
	For the Three Months Ended January 31,		For the Six Months Ended January 31,	
	2017	2016	2017	2016
	Service cost	\$33	\$21	\$63
Interest cost	21	21	39	41
Amortization of:				
Prior service costs	(1)	(1)	(3)	(3)
Other actuarial loss	14	—	20	—
Net periodic benefit cost	\$67	\$41	\$119	\$81

The postretirement health plan is an unfunded plan. We pay insurance premiums and claims from our assets.

The pension plan is funded based upon actuarially determined contributions that take into account the amount deductible for income tax purposes, the normal cost and the minimum contribution required and the maximum contribution allowed under applicable regulations. We contributed \$335,000 and \$636,000 to our pension plan during the second quarter and first six months of fiscal 2017, respectively. We estimate contributions will be \$840,000 for the remainder of fiscal 2017. See Item 3. “Quantitative and Qualitative Disclosures About Market Risk” for a discussion of the potential impact of financial market fluctuations on pension plan assets and future funding contributions.

Assumptions used in the previous calculations were as follows:

Pension Benefits	Postretirement Health Benefits
For the Three and Six Months Ended January 31,	

Edgar Filing: OIL DRI CORP OF AMERICA - Form 10-Q

	2017	2016	2017	2016
Discount rate for net periodic benefit cost	3.36%	4.22%	2.71%	3.51%
Rate of increase in compensation levels	3.50%	3.50%	—	—
Long-term expected rate of return on assets	7.00%	7.50%	—	—

The medical cost trend assumption for postretirement health benefits was 7.35%. The graded trend rate is expected to decrease to an ultimate rate of 4.5% in fiscal 2036.

7. OPERATING SEGMENTS

We have two operating segments: (1) Retail and Wholesale Products Group and (2) Business to Business Products Group. These operating segments are managed separately and each segment's major customers have different characteristics. The Retail and Wholesale Products Group customers include: mass merchandisers; wholesale clubs; drugstore chains; pet specialty retail outlets; dollar stores; retail grocery stores; distributors of industrial cleanup and automotive products; environmental service companies; and sports field product users. The Business to Business Products Group customers include: processors and refiners of edible oils, petroleum-based oils and biodiesel fuel; manufacturers of animal feed and agricultural chemicals; distributors of animal health and nutrition products; and marketers of consumer products.

Our operating segments are also our reportable segments. Net sales and operating income for each segment are provided below. Revenues by product line are not provided because it would be impracticable to do so. The accounting policies of the segments are the same as those described in Note 1 of the Consolidated Financial Statements included in our Annual Report on Form 10-K for the fiscal year ended July 31, 2016.

We do not rely on any segment asset allocations and we do not consider them meaningful because of the shared nature of our production facilities; however, we have estimated the segment asset allocations below for those assets for which we can reasonably determine. The unallocated asset category is the remainder of our total assets. The asset allocation is estimated and is not a measure used by our chief operating decision maker about allocating resources to the operating segments or in assessing their performance. The corporate expenses line includes certain unallocated expenses, including primarily salaries, wages and benefits, purchased services, rent, utilities and depreciation and amortization associated with corporate functions such as research and development, information systems, finance, legal, human resources and customer service. Corporate expenses also include the estimated annual incentive plan bonus accrual.

	Assets	
	January 31, July 31,	
	2017	2016
	(in thousands)	
Business to Business Products	\$59,727	\$61,007
Retail and Wholesale Products	92,191	91,626
Unallocated Assets	54,656	52,182
Total Assets	\$206,574	\$204,815

	For the Six Months Ended January 31,			
	Net Sales		Income	
	2017	2016	2017	2016
	(in thousands)			
Business to Business Products	\$50,734	\$48,446	\$17,223	\$16,745
Retail and Wholesale Products	81,052	84,716	4,480	9,697
Total Sales	\$131,786	\$133,162		
Corporate Expenses			(13,070)	(13,266)
Income from Operations			8,633	13,176
Total Other Expense, Net			(710)	(567)
Income before Income Taxes			7,923	12,609
Income Taxes			(1,664)	(3,365)
Net Income			\$6,259	\$9,244

	For the Three Months Ended			
	January 31,			
	Net Sales		Income	
	2017	2016	2017	2016
	(in thousands)			
Business to Business Products	\$23,261	\$22,625	\$7,815	\$7,576
Retail and Wholesale Products	41,913	42,742	4,987	4,295
Total Sales	\$65,174	\$65,367		
Corporate Expenses			(7,215)	(6,471)
Income from Operations			5,587	5,400
Total Other Expense, Net			(343)	(331)
Income before Income Taxes			5,244	5,069
Income Taxes			(994)	(1,248)
Net Income			\$4,250	\$3,821

8. STOCK-BASED COMPENSATION

We determine the fair value of stock options and restricted stock issued under our long term incentive plans as of the grant date. We recognize the related compensation expense over the period from the date of grant to the date when the award is no longer contingent on the employee providing additional service to the Company.

The Oil-Dri Corporation of America 2006 Long Term Incentive Plan (the “2006 Plan”) permits the grant of stock options, stock appreciation rights, restricted stock, restricted stock units, performance awards and other stock-based and cash-based awards. Our employees and outside directors are eligible to receive grants under the 2006 Plan. The total number of shares of stock subject to grants under the 2006 Plan may not exceed 937,500. Stock options have been granted to our outside directors with a vesting period of one year and stock options granted to employees generally vest 25% two years after the grant date and in each of the three following anniversaries of the grant date. In addition, restricted shares have been issued under the 2006 Plan as described in the restricted stock section below.

Stock Options

A summary of stock options is shown below:

	Number of Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term (Years)	Aggregate Intrinsic Value (in thousands)
Options outstanding and exercisable, July 31, 2016	10	\$ 17.00	0.3	\$ 205
Exercised	(10)	\$ 17.00		\$ 211
Options outstanding and exercisable, January 31, 2017	—			

The amount of cash received from the exercise of stock options during the second quarter of fiscal years 2017 and 2016 was \$170,000 and \$96,000, respectively, and the related tax benefit was \$80,000 and \$40,000, respectively. The amount of cash received from the exercise of stock options during the first six months of fiscal years 2017 and 2016 was \$170,000 and \$281,000, respectively, and the related tax benefit was \$80,000 and \$68,000, respectively.

No stock options were granted during the first six months of either fiscal year 2017 or 2016.

Restricted Stock

All of our non-vested restricted stock as of January 31, 2017 was issued under the 2006 Plan with vesting periods between two years and five years. Under the 2006 Plan, 18,000 and 400 restricted shares of Common Stock were granted during the second quarter of fiscal years 2017 and 2016, respectively.

Stock-based compensation expense related to non-vested restricted stock for the second quarter of fiscal years 2017 and 2016 was \$346,000 and \$306,000, respectively. Stock-based compensation expense related to non-vested restricted stock for the first six months of fiscal years 2017 and 2016 was \$777,000 and \$638,000, respectively.

A summary of restricted stock transactions is shown below:

	Restricted Shares (in thousands)	Weighted Average Grant Date Fair Value
Non-vested restricted stock outstanding at July 31, 2016	194	\$ 29.09
Granted	31	\$ 36.84
Vested	(36)	\$ 26.09
Forfeitures	(1)	\$ 31.48
Non-vested restricted stock outstanding at January 31, 2017	188	\$ 30.95

9. ACCUMULATED OTHER COMPREHENSIVE (LOSS) INCOME

The following table summarizes the changes in accumulated other comprehensive income by component as of January 31, 2017 (in thousands):

	Pension and Postretirement Health Benefits	Cumulative Translation Adjustment	Total Accumulated Other Comprehensive (Loss) Income
Balance as of July 31, 2016	\$ (13,867)	\$ (155)	\$ (14,022)
Other comprehensive income before reclassifications, net of tax	—	49	49
Amounts reclassified from accumulated other comprehensive income, net of tax	578	a)—	578
Net current-period other comprehensive income, net of tax	578	49	627
Balance as of January 31, 2017	\$ (13,289)	\$ (106)	\$ (13,395)

a) Amount is net of tax expense of \$354,000. Amount is included in the components of net periodic benefit cost for the pension and postretirement health plans. See Note 6 for further information.

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

The following discussion and analysis of our financial condition and results of operations should be read together with the financial statements and the related notes included herein and our Consolidated Financial Statements, accompanying notes and Management's Discussion and Analysis of Financial Condition and Results of Operations contained in our Annual Report on Form 10-K for the fiscal year ended July 31, 2016. This discussion contains forward-looking statements that involve risks and uncertainties. Our actual results may differ materially from the results discussed in the forward-looking statements. Factors that might cause a difference include, but are not limited to, those discussed under "Forward-Looking Statements" and Item 1A, Risk Factors, of our Annual Report on Form 10-K for the fiscal year ended July 31, 2016.

OVERVIEW

We develop, mine, manufacture and market sorbent products principally produced from clay minerals and, to a lesser extent, other clay-like sorbent materials. Our principal products include agricultural and horticultural chemical carriers, animal health and nutrition products, bleaching clay and fluid purification aids, cat litter, industrial and automotive floor absorbents and sports field products. Our products are sold to two primary customer groups, including customers who resell our products as originally produced to the end consumer and those who use our products as part of their production process or use them as an ingredient in their final finished product. We have two reportable operating segments based on the different characteristics of our two primary customer groups: Retail and Wholesale Products Group and Business to Business Products Group, as described in Note 7 of the notes to the Condensed Consolidated Financial Statements.

RESULTS OF OPERATIONS

SIX MONTHS ENDED JANUARY 31, 2017 COMPARED TO SIX MONTHS ENDED JANUARY 31, 2016

CONSOLIDATED RESULTS

Consolidated net sales for the six months ended January 31, 2017 were \$131,786,000, a decrease of 1% from net sales of \$133,162,000 for the six months ended January 31, 2016. Net sales were down for our Retail and Wholesale Products Group, but were up for our Business to Business Products Group. Consolidated net income for the first six months of fiscal 2017 was \$6,259,000, a 32% decrease from net income of \$9,244,000 for the first six months of fiscal 2016. Our Retail and Wholesale Products Group reported lower operating income due primarily to lower net sales and approximately \$5,000,000 higher advertising costs, described further below. Operating income for our Business to Business Products Groups increased compared to the first six months of the prior fiscal year. Diluted net income per share was \$0.86 for the first six months of fiscal 2017, compared to \$1.28 for the first six months of fiscal 2016.

Consolidated gross profit as a percentage of net sales for the first six months of fiscal 2017 was 30%, the same as for the first six months of fiscal 2016. Gross profit was positively impacted by approximately 5% lower packaging costs per manufactured ton. A significant amount of our packaging purchases are subject to contractual price adjustments throughout the year based on underlying commodity prices. Prices for commodities may fluctuate considerably, particularly commodities related to our resin and paper-based packaging. The lower packaging costs reflected favorable commodity prices at the time of the most recent price adjustment. Gross profit was negatively impacted by the cost of natural gas used to operate kilns that dry our clay. The cost of natural gas per manufactured ton was approximately 16% higher than the prior year. Other manufacturing costs per ton produced were up approximately 6% compared to the same period the prior fiscal year, including higher salaries, wages, benefits and depreciation

expenses.

Total selling, general and administrative expenses were 18% higher for the first six months of fiscal 2017 compared to the first six months of fiscal 2016. The discussions of the segments' operating incomes below describe the changes in the selling, general and administrative expenses that were allocated to the operating segments, particularly higher advertising expense in the Retail and Wholesale Products Group. The remaining unallocated corporate expenses in the first six months of fiscal 2017 included a lower estimated annual incentive bonus accrual as compared to the prior year. The incentive bonus accruals were based on performance targets established for each fiscal year. The lower bonus accrual was mostly offset by increased pension expense and additional costs related to the implementation of our new enterprise resource planning software.

Our effective tax rate was 21% of pre-tax income for the first six months of fiscal 2017, which was lower than 27% for the first six months of fiscal 2016. Our effective tax rate was based on the estimated level of our taxable income for the year and the assessment of various deductions, including depletion.

19

BUSINESS TO BUSINESS PRODUCTS GROUP

Net sales of the Business to Business Products Group for the first six months of fiscal 2017 were \$50,734,000, an increase of \$2,288,000, or 5%, from net sales of \$48,446,000 for the first six months of fiscal 2016. Net sales of our animal health and nutrition products increased approximately 23%. Sales were up in domestic, Asian and most other foreign markets; however, sales in Latin America were lower due to the transition to a new distributor. See “Foreign Operations” below for further discussion of increased animal health and nutrition sales by our subsidiary in China. Net sales of fluids purification products were up approximately 7%, primarily for sales to edible oil producers. A new customer in Europe, added in the fourth quarter of fiscal 2016, accounted for much of the sales improvement for the first six months of fiscal 2017. Lower sales from normal ordering fluctuations of customers in the petroleum oil processing industry partially offset this increase. Net sales of our agricultural chemical carrier products were essentially flat compared to the prior year. Sales of our co-packaged coarse cat litter were approximately 10% lower due to fewer tons sold and a price adjustment under our co-packaging agreement.

Selling, general and administrative expenses for the Business to Business Products Group were essentially flat compared to the first six months of fiscal 2016.

The Business to Business Products Group’s operating income for the first six months of fiscal 2017 was \$17,223,000, an increase of \$478,000, or 3%, from operating income of \$16,745,000 for the first six months of fiscal 2016. The benefits of higher sales and lower packaging costs more than offset increased natural gas and other manufacturing costs. See “Consolidated Results” above for further discussion of packaging, natural gas and manufacturing costs.

RETAIL AND WHOLESALE PRODUCTS GROUP

Net sales of the Retail and Wholesale Products Group for the first six months of fiscal 2017 were \$81,052,000, a decrease of \$3,664,000, or 4%, from net sales of \$84,716,000 for the first six months of fiscal 2016. Total cat litter net sales declined approximately 6% compared to the first six months of the prior year. Lower sales of both our branded and private label cat litters was attributed to the decision to exit low margin business with two major customers. Instead, we maintained our focus on the lightweight segment of the market through our integrated marketing campaign to generate awareness and trial of lightweight cat litter products. This strategy successfully delivered higher sales of both our Cat's Pride Fresh & Light Ultimate Care and our private label lightweight scoopable litters. We plan to continue our advertising and promotion focus on the lightweight litter market throughout the remainder of fiscal 2017.

Sales of industrial and automotive absorbent products were essentially flat compared to the first six months of fiscal 2016. Total sales for our subsidiary in the United Kingdom declined, while sales for our subsidiary in Canada increased. See “Foreign Operations” below for further discussion about the sales and types of products sold by these foreign subsidiaries.

Selling, general and administrative expenses for the Retail and Wholesale Products Group were 60% higher compared to the first six months of fiscal 2016. Advertising expense increased approximately \$5,000,000 due to the integrated marketing campaign to promote our Fresh & Light Ultimate Care lightweight cat litter, which began in the second quarter of fiscal 2016. We expect to continue this campaign throughout the remainder of fiscal 2017; however, we plan to reallocate some of our anticipated spending between advertising, which is included in selling, general and administrative expenses, and trade promotions, which are included as a reduction of net sales. We expect advertising expense will be significant for the full year of fiscal 2017, but the amount is anticipated to be less than the corresponding expense in fiscal 2016.

The Retail and Wholesale Products Group's operating income for the first six months of fiscal 2017 was \$4,480,000, a decrease of \$5,217,000, or 54%, from operating income of \$9,697,000 for the first six months of fiscal 2016. The decrease in operating income was driven by an additional approximate \$5,000,000 of advertising costs as discussed above. Higher natural gas and other manufacturing costs also negatively impacted the Group's operating results, while some benefit was realized from lower packaging costs. See "Consolidated Results" above for further discussion of these cost changes.

FOREIGN OPERATIONS

Foreign operations include our subsidiaries in Canada and the United Kingdom, which are included in the Retail and Wholesale Products Group, and our subsidiary in China, which is included in the Business to Business Products Group. Net sales by our foreign subsidiaries during the first six months of fiscal 2017 were \$6,475,000, compared to net sales of \$5,532,000 during the first six months of fiscal 2016. Our subsidiary in China reported higher sales for animal health and nutrition products with approximately 42% more tons sold, including sales to new customers. Sales also increased for both branded cat litter and industrial absorbent products sold by our subsidiary in Canada. These increases were partially offset by lower sales of fluids purification

products sold by our subsidiary in the United Kingdom. Reduced orders from one customer and a weak exchange rate for the British Pound to the U.S. Dollar negatively impacted reported sales. Net sales by our foreign subsidiaries represented 5% and 4% of our consolidated net sales during the first six months of fiscal years 2017 and 2016, respectively.

Our foreign subsidiaries reported net income of \$298,000 for the first six months of fiscal 2017 compared to a net loss of \$536,000 for the first six months of fiscal 2016. The improved profitability was driven primarily by the higher sales.

Identifiable assets of our foreign subsidiaries as of January 31, 2017 were \$7,822,000, compared to \$7,814,000 as of January 31, 2016. The increase was due primarily to higher cash, cash equivalents and inventories, which were partially offset by lower accounts receivable and net fixed assets.

THREE MONTHS ENDED JANUARY 31, 2017 COMPARED TO THREE MONTHS ENDED JANUARY 31, 2016

CONSOLIDATED RESULTS

Consolidated net sales for the three months ended January 31, 2017 were \$65,174,000, compared to net sales of \$65,367,000 for the three months ended January 31, 2016. Net sales were down for our Retail and Wholesale Products Group, but were up for our Business to Business Products Group. Consolidated net income was \$4,250,000 for the second quarter of fiscal 2017, an 11% increase compared to \$3,821,000 for the second quarter of fiscal 2016. Operating income increased for both our Business to Business Products and Retail and Wholesale Products Groups compared to the second quarter of the prior year. Diluted net income per share was \$0.58 for the second quarter of fiscal 2017, compared to \$0.53 for the second quarter of fiscal 2016.

Consolidated gross profit as a percentage of net sales for the second quarter of fiscal 2017 was 29%, the same as for the second quarter of fiscal 2016. Slightly lower freight costs were primarily offset by increases in natural gas and other manufacturing costs. The cost per manufactured ton for natural gas used to operate kilns that dry our clay was approximately 28% higher than the second quarter of the prior fiscal year. In addition, other manufacturing costs per ton produced were up approximately 2%. Higher expenses for employee salaries, wages, benefits and depreciation were partially offset by lower repair costs. Packaging costs were essentially flat compared to the second quarter of the prior fiscal year. A significant amount of our packaging purchases are subject to contractual price adjustments throughout the year based on underlying commodity prices. Prices for commodities may fluctuate considerably, particularly commodities related to our resin and paper-based packaging.

Total selling, general and administrative expenses were 1% lower for the second quarter of fiscal 2017 compared to the second quarter of fiscal 2016. The discussion of the segments' operating incomes below describes the selling, general and administrative expenses allocated to the operating segments, particularly lower advertising expense in the Retail and Wholesale Products Group. The remaining unallocated corporate expenses in the second quarter of fiscal 2017 included higher pension expense and additional costs related to the implementation of our new enterprise resource planning software.

Our tax expense was 19% of pre-tax income for the second quarter of fiscal 2017, compared to 25% in the second quarter of fiscal 2016. Our effective tax rate was based on the estimated level of our taxable income for the year and the assessment of various tax deductions, including depletion.

BUSINESS TO BUSINESS PRODUCTS GROUP

Net sales of the Business to Business Products Group for the second quarter of fiscal 2017 were \$23,261,000, an increase of \$636,000, or 3%, from net sales of \$22,625,000 for the second quarter of fiscal 2016. Net sales of fluids purification products were up approximately 8%. Sales to edible oil producers accounted for much of the sales improvement, including a new customer in Europe added in the fourth quarter of fiscal 2016. Net sales of our agricultural chemical carriers to manufacturers of crop protection products were up slightly compared to the prior year. Sales of our animal health and nutrition products decreased approximately 4%. Lower sales in Latin America due to the transition to a new distributor were partially offset by higher sales in domestic and Asian markets. See “Foreign Operations” below for further discussion of increased animal health and nutrition sales by our subsidiary in China. Sales of co-packaged coarse cat litter were approximately 3% lower than in the second quarter of fiscal 2016 due to a price adjustment under our co-packaging agreement.

Selling, general and administrative expenses for the Business to Business Products Group were 7% lower due primarily to lower costs to promote our animal health and nutrition products compared to the second quarter of fiscal 2016.

The Business to Business Products Group’s operating income for the second quarter of fiscal 2017 was \$7,815,000, an increase of \$239,000, or 3%, from operating income of \$7,576,000 in the second quarter of fiscal 2016. The benefits of higher sales and

lower selling, general and administrative expenses more than offset increased natural gas and other manufacturing costs. See “Consolidated Results” above for further discussion of manufacturing and packaging costs.

RETAIL AND WHOLESALE PRODUCTS GROUP

Net sales of the Retail and Wholesale Products Group for the second quarter of fiscal 2017 were \$41,913,000, a decrease of \$829,000, or 2%, from net sales of \$42,742,000 for the second quarter of fiscal 2016. Total cat litter net sales declined approximately 4% compared to the second quarter of the prior year. Lower sales of both our branded and private label cat litters was attributed to the decision to exit low margin business with two major customers. Our focus on the lightweight segment of the market delivered higher sales of both our Cat's Pride Fresh & Light Ultimate Care and our private label lightweight scoopable litters, although we reduced some of our marketing efforts during the quarter. We plan to continue our integrated marketing campaign to generate awareness and trial of lightweight cat litter products throughout the remainder of fiscal 2017.

Sales of industrial and automotive absorbent products were up approximately 7% from the second quarter of fiscal 2016 due primarily to higher sales to existing customers. Total sales for our subsidiary in the United Kingdom declined, while sales for our subsidiary in Canada increased. See “Foreign Operations” below for further discussion about the sales and types of products sold by these foreign subsidiaries.

Selling, general and administrative expenses for the Retail and Wholesale Products Group were 12% lower compared to the second quarter of fiscal 2016. The decrease was driven by approximately \$400,000 lower advertising expense for our integrated marketing campaign to promote our Fresh & Light Ultimate Care lightweight cat litter. This campaign began in the second quarter of fiscal 2016. We expect to continue this campaign throughout the remainder of fiscal 2017; however, we plan to reallocate some of our anticipated spending between advertising, which is included in selling, general and administrative expenses, and trade promotions, which are included as a reduction of net sales. We expect advertising expense will be significant for the full year of fiscal 2017, but the amount is anticipated to be less than the corresponding expense in fiscal 2016.

The Retail and Wholesale Products Group's operating income for the second quarter of fiscal 2017 was \$4,987,000, an increase of \$692,000, or 16%, compared to operating income of \$4,295,000 for the second quarter of fiscal 2016. The increase in operating income was driven by the \$400,000 lower advertising costs discussed above. In contrast, higher natural gas and other manufacturing costs negatively impacted the Group's operating results. See “Consolidated Results” above for further discussion of these cost changes.

FOREIGN OPERATIONS

Foreign operations include our subsidiaries in Canada and the United Kingdom, which are included in the Retail and Wholesale Products Group, and our subsidiary in China, which is included in the Business to Business Products Group. Total net sales by our foreign subsidiaries during the second quarter of fiscal 2017 were \$3,324,000, a 10% increase compared to net sales of \$3,019,000 in the second quarter of fiscal 2016. Our subsidiary in China reported higher sales for animal health and nutrition products with approximately 26% more tons sold, including sales to new customers. Sales also increased for both branded cat litter and industrial absorbent products sold by our subsidiary in Canada. These increases were partially offset by lower sales of fluids purification products by our subsidiary in the United Kingdom. Normal fluctuations in customers' ordering patterns and a weak exchange rate for the British Pound to the U.S. Dollar negatively impacted reported sales. Net sales by our foreign subsidiaries represented approximately 5% and 4% of our consolidated net sales during the second quarters of fiscal 2017 and 2016, respectively.

Our foreign subsidiaries reported net income of \$267,000 for the second quarter of fiscal 2017 compared to a net loss of \$69,000 for the second quarter of fiscal 2016. The improved profitability for the quarter was driven primarily by the

higher sales.

LIQUIDITY AND CAPITAL RESOURCES

Our principal capital requirements include: funding working capital needs; purchasing and upgrading equipment, facilities, information systems and real estate; supporting new product development; investing in infrastructure; repurchasing Common Stock; paying dividends; and business acquisitions. During the first six months of fiscal 2017, we principally used cash generated from operations to fund these requirements. We also have the ability to borrow under our revolving credit agreement with BMO Harris Bank N.A. (“BMO Harris”), as described further below, however we have not borrowed under the credit agreement in recent years. Cash and cash equivalents decreased \$1,069,000 during the first six months of fiscal 2017 to \$17,560,000, and short term investments decreased \$2,826,000 during the same period to \$7,358,000 as of January 31, 2017.

The following table sets forth certain elements of our Condensed Consolidated Statements of Cash Flows (in thousands):

	For the Six Months Ended January 31,	
	2017	2016
Net cash provided by operating activities	\$9,093	\$17,051
Net cash used in investing activities	(4,446)	(17,446)
Net cash used in financing activities	(5,784)	(5,949)
Effect of exchange rate changes on cash and cash equivalents	68	33
Net decrease in cash and cash equivalents	\$(1,069)	\$(6,311)

Net cash provided by operating activities

In addition to net income, as adjusted for depreciation and amortization and other non-cash operating activities, the primary sources and uses of operating cash flows for the first six months of fiscal years 2017 and 2016 were as follows:

Accounts receivable, less allowance for doubtful accounts, increased \$1,698,000 in the first six months of fiscal 2017 compared to a decrease of \$652,000 in the first six months of fiscal 2016. The change in accounts receivable balances reflected differences in the level and timing of sales and collections, as well as the level of sales and the payment terms provided to various customers.

Prepaid expenses increased \$3,784,000 in the first six months of fiscal 2017 compared to an increase of \$2,671,000 in the first six months of fiscal 2016. Prepaid expenses increased in the first six months of both fiscal 2017 and 2016 due to prepayments of annual insurance premiums, as well as prepaid advertising costs. The increase in prepaid expenses in the first six months of fiscal 2017 also included prepayments for computer software licenses.

Accounts payable increased \$852,000 in the first six months of fiscal 2017 compared to a decrease of \$201,000 in the first six months of fiscal 2016. Trade and freight payable varied in both periods due to timing of payments, fluctuations in the cost of goods and services we purchased, production volume levels and vendor payment terms. Current accrued estimated income taxes are also included in accounts payable balances.

Accrued expenses decreased \$1,698,000 in the first six months of fiscal 2017 compared to an increase of \$3,295,000 in the first six months of fiscal 2016. The payout of the prior fiscal year's discretionary incentive bonus drove the decrease in accrued salaries in the first six months of fiscal 2017, while the increase in the first six months of fiscal 2016 was driven by a higher incentive bonus accrual. Accrued plant expenses fluctuated in the first six months of both fiscal 2017 and 2016 due to timing of payments, changes in the cost of goods and services we purchased, production volume levels and vendor payment terms. In addition, accrued trade promotions and advertising varied due to the timing of marketing programs.

Accrued pension and postretirement benefits increased \$1,001,000 in the first six months of fiscal 2017 compared to an increase of \$554,000 in the first six months of fiscal 2016. The discount rate required to estimate the value of these accrued benefits as of the second quarter of fiscal 2017 was lower than the rate used in fiscal 2016, which resulted in a higher liability. See Note 6 of the notes to the unaudited Condensed Consolidated Financial Statements for further information.

Net cash used in investing activities

Cash used in investing activities was \$4,446,000 in the first six months of fiscal 2017 compared to cash used in investing activities of \$17,446,000 in the first six months of fiscal 2016. Cash used for capital expenditures was \$7,279,000 and \$4,795,000 in the first six months of fiscal 2017 and 2016, respectively. Capital expenditures in the first six months of fiscal 2017 included spending for the enterprise resource planning system implementation project and related infrastructure improvements, as well as equipment replacement at our manufacturing facilities. Net dispositions of short-term investments provided cash of \$2,831,000 in the first six months of fiscal 2017, while net purchases used cash of \$12,900,000 in the first six months of fiscal 2016. Purchases and dispositions of investment securities in both periods are impacted by variations in the timing of investment maturities, the operating cash needs of the Company and the availability of investment options.

Net cash used in financing activities

Cash used in financing activities was \$5,784,000 in the first six months of fiscal 2017 compared to cash used in financing activities of \$5,949,000 in the first six months of fiscal 2016. Scheduled payments on long-term debt were \$3,083,000 and \$3,484,000 in the first six months of fiscal 2017 and 2016, respectively. Dividend payments in the first six months of fiscal 2017 were \$2,956,000 compared to \$2,783,000 paid during the same period of fiscal 2016 due to a dividend increase.

Other

Total cash and investment balances held by our foreign subsidiaries of \$1,653,000 as of January 31, 2017 were higher than the January 31, 2016 balances of \$1,499,000. See further discussion in "Foreign Operations" above.

We have a \$25,000,000 unsecured revolving credit agreement with BMO Harris which expires on December 4, 2019. The agreement also provides for a maximum of \$5,000,000 for foreign letters of credit. Under the agreement we may select a variable interest rate based on either the BMO Harris prime rate or a LIBOR-based rate, plus a margin which varies depending on our debt to earnings ratio, or a fixed rate as agreed between us and BMO Harris. At January 31, 2017, the variable rates would have been 3.75% for the BMO Harris prime-based rate or 2.02% for the LIBOR-based rate. The credit agreement contains restrictive covenants that, among other things and under various conditions, limit our ability to incur additional indebtedness or to dispose of assets. The agreement also requires us to maintain a minimum fixed coverage ratio and a minimum consolidated net worth. We did not borrow under the credit agreement during the six months ended January 31, 2017 and 2016, and we were in compliance with its covenants.

As of January 31, 2017, we had remaining authority to repurchase 301,837 shares of Common Stock under a repurchase plan approved by our Board of Directors. These repurchases may be made on the open market (pursuant to Rule 10b5-1 plans or otherwise) or in negotiated transactions. The timing and amount of shares repurchased will be determined by our management.

We believe that cash flow from operations, availability under our revolving credit facility, current cash and investment balances and our ability to obtain other financing, if necessary, will provide adequate cash funds for foreseeable working capital needs, capital expenditures at existing facilities, dividend payments and debt service obligations for at least the next 12 months. We plan to continue promoting our Cat's Pride Fresh & Light Ultimate Care lightweight scoopable litter during fiscal 2017 and we expect total spending for advertising and trade spending to be significant, but slightly less than the total spent in fiscal 2016. We anticipate that our capital expenditures will increase in fiscal 2017, including spending for implementation of an enterprise resource planning software. We do not anticipate that these increased expenditures will dramatically impact our cash position; however our cash requirements are subject to change as business conditions warrant and opportunities arise. We continually evaluate our liquidity position and anticipated cash needs, as well as the financing options available to obtain additional cash reserves. Our ability to fund operations, to make planned capital expenditures, to make scheduled debt payments and to remain in compliance with all financial covenants under debt agreements, including, but not limited to, the current credit agreement, depends on our future operating performance, which, in turn, is subject to prevailing economic conditions and to financial, business and other factors. The timing and size of any new business ventures or acquisitions that we complete may also impact our cash requirements.

The tables in the following subsection summarize our contractual obligations and commercial commitments (in thousands) as of January 31, 2017 for the time-frames indicated.

CONTRACTUAL OBLIGATIONS AND COMMERCIAL COMMITMENTS

Payments Due by Period

Edgar Filing: OIL DRI CORP OF AMERICA - Form 10-Q

Contractual Obligations	Total	Less Than 1 Year	1 – 3 Years	4 – 5 Years	After 5 Years
Notes Payable	\$12,333	\$3,083	\$6,167	\$3,083	\$—
Interest on Notes Payable	1,231	498	611	122	—
Operating Leases	14,708	1,854	2,511	1,538	8,805
Total Contractual Cash Obligations	\$28,272	\$5,435	\$9,289	\$4,743	\$8,805

We made total contributions to our defined benefit pension plan of \$636,000 during the first six months of fiscal 2017. We estimate contributions of approximately \$840,000 will be made during the remainder of fiscal 2017. We have not presented this obligation for future years in the table above because the funding requirement can vary from year to year based on changes in the fair value of plan assets and actuarial assumptions. See “Item 3. Quantitative and Qualitative Disclosures About Market Risk” below for a discussion of the potential impact of financial market fluctuations on pension plan assets and future funding contributions.

	Amount of Commitment Expiration Per Period				
Total	Less Than 1 Year	1 – 3 Years	4 – 5 Years	After 5 Years	
Other Commercial Commitments	\$24,427	\$24,427	\$ —	—\$	—

The other commercial commitments in the table above represent open purchase orders, including blanket purchase orders, for items such as packaging, additives and pallets used in the normal course of operations. The expected timing of payments for these obligations is estimated based on current information. Timing of payments and actual amounts paid may be different depending on the time of receipt of goods or services, or changes to agreed-upon amounts for some obligations.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

This discussion and analysis of financial condition and results of operations is based on our unaudited Condensed Consolidated Financial Statements, which have been prepared in accordance with U.S. GAAP for interim financial information and in compliance with instructions to Form 10-Q and Article 10 of Regulation S-X. The preparation of these financial statements requires the use of estimates and assumptions related to the reporting of assets, liabilities, revenues, expenses and related disclosures. In preparing these financial statements, we have made our best estimates and judgments of certain amounts included in the financial statements. Estimates and assumptions are revised periodically. Actual results could differ from these estimates. See the information concerning our critical accounting policies included under “Management’s Discussion of Financial Condition and Results of Operations” in our Annual Report on Form 10-K for the fiscal year ended July 31, 2016.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

We are exposed to interest rate risk and employ policies and procedures to manage our exposure to changes in the market risk of our cash equivalents and short-term investments. We believe that the market risk arising from holdings of our financial instruments is not material.

We are exposed to foreign currency fluctuation risk, primarily the U.S. Dollar relative to the British Pound, Euro, Canadian Dollar, Chinese Yuan and the Brazilian Real, as related to our foreign subsidiaries, to certain accounts receivable, and to our ability to sell in foreign markets. We are subject to translation exposure of our foreign subsidiaries' financial statements from local currencies to U.S. Dollars. In recent years, our foreign subsidiaries have not generated a substantial portion of our consolidated sales or net income. In addition, the portion of our consolidated accounts receivable denominated in foreign currencies is not significant. Finally, foreign sales of our products may be influenced by the relative strength or weakness of the U.S. Dollar compared to various other currencies, which makes our products relatively more or less expensive than our foreign competitors' products in local marketplaces. Foreign currency fluctuations had some bearing on our operating results in the first six months of fiscal 2017; however, historically the overall foreign currency fluctuation risk has not been material to our Consolidated Financial Statements and in the first six months of fiscal 2017 we did not enter into any hedge contracts in an attempt to offset any adverse effect of changes in currency exchange rates.

We are exposed to market risk as it relates to the investments of plan assets under our defined benefit pension plan. The fair value of these assets is subject to change due to fluctuations in the financial markets. A lower asset value may increase our pension expense and may increase the amount of future funding contributions.

We are exposed to regulatory risk in the fluid purification, animal health and agricultural markets, principally as a result of the risk of increasing regulation of the food chain throughout the world, but particularly in the United States and Europe. We actively monitor developments in this area, both directly and through trade organizations of which we are a member.

We are exposed to commodity price risk with respect to fuel. Factors that could influence the cost of natural gas used in the kilns to dry our clay include the creditworthiness of our natural gas suppliers, the overall general economy, developments in world events, general supply and demand for natural gas, seasonality and the weather patterns throughout the United States and the world. We monitor fuel market trends and, consistent with our past practice, we may purchase fuel at spot rates on a month to month basis and we may contract for a portion of our anticipated fuel needs using forward purchase contracts to mitigate the volatility of our kiln fuel prices. As of January 31, 2017, we have not purchased any natural gas contracts for our planned kiln fuel needs for the remainder of fiscal 2017.

ITEM 4. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

Management conducted an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934 (the “Exchange Act”)) as of the end of the period covered by this Quarterly Report on Form 10-Q. The controls evaluation was conducted under the supervision and with the participation of management, including our Chief Executive Officer (“CEO”) and Chief Financial Officer (“CFO”). Based upon the controls evaluation, our CEO and CFO have concluded that, as of the end of the period covered by this report, our disclosure controls and procedures were effective to provide reasonable assurance that information required to be disclosed in our Exchange Act reports is recorded, processed, summarized and reported within the time periods specified by the SEC, and that such information is accumulated and communicated to management, including the CEO and CFO, 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 (as defined in Rule 13a-15(f) under the Exchange Act) that occurred during the fiscal quarter ended January 31, 2017 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Inherent Limitations on Effectiveness of Controls

Our management, including the CEO and CFO, do not expect that our disclosure controls and procedures or our internal control over financial reporting will prevent or detect all errors and all fraud. A control system, no matter how well designed and operated, can provide only reasonable, not absolute, assurance that the control system’s objectives will be met. The design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Further, because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that misstatements due to error or fraud will not occur or that all control issues and instances of fraud, if any, within the Company have been detected. These inherent limitations include the realities that judgments in decision-making can be faulty and that breakdowns can occur because of simple error or mistake. Controls can also be circumvented by the individual acts of some persons, by collusion of two or more people, or by management override of the controls. The design of any system of controls is based in part on certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions. Projections of any evaluation of controls effectiveness to future periods are subject to risks. Over time, controls may become inadequate because of changes in conditions or deterioration in the degree of compliance with policies or procedures.

PART II – OTHER INFORMATION

Items 1, 1A, 2, 3 and 5 of this Part II are either inapplicable or are answered in the negative and are omitted pursuant to the instructions to Part II.

ITEM 4. MINE SAFETY DISCLOSURES

Our mining operations are subject to regulation by the Mine Safety and Health Administration under authority of the Federal Mine Safety and Health Act of 1977, as amended. Information concerning mine safety violations or other regulatory matters required by section 1503(a) of the Dodd-Frank Wall Street Reform and Consumer Protection Act and Item 104 of Regulation S-K is included in Exhibit 95 to this Quarterly Report on Form 10-Q.

ITEM 6. EXHIBITS

Exhibit No.	Description	SEC Document Reference
11	Statement re: Computation of Earnings per Share.	Filed herewith.
31	Certifications pursuant to Rule 13a–14(a).	Filed herewith.
32	Certifications pursuant to Section 1350 of the Sarbanes-Oxley Act of 2002.	Furnished herewith.
95	Mine Safety Disclosures	Filed herewith.
101.INS	XBRL Taxonomy Instance Document	Filed herewith.
101.SCH	XBRL Taxonomy Extension Schema Document	Filed herewith.
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document	Filed herewith.
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document	Filed herewith.
101.LAB	XBRL Taxonomy Extension Labels Linkbase Document	Filed herewith.
101.PRE	XBRL Taxonomy Extension Presentation Linkbase	Filed herewith.

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.

OIL-DRI CORPORATION OF AMERICA
(Registrant)

BY /s/ Daniel S. Jaffee
Daniel S. Jaffee
President and Chief Executive Officer

BY /s/ Daniel T. Smith
Daniel T. Smith
Vice President and Chief Financial Officer

Dated: March 10, 2017

EXHIBITS

Exhibit No.	Description
11	Statement re: Computation of Earnings per Share.
31	Certifications pursuant to Rule 13a-14(a).
32	Certifications pursuant to Section 1350 of the Sarbanes-Oxley Act of 2002.
95	Mine Safety Disclosures
101.INS	XBRL Taxonomy Instance Document
101.SCH	XBRL Taxonomy Extension Schema Document
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document
101.LAB	XBRL Taxonomy Extension Labels Linkbase Document
101.PRE	XBRL Taxonomy Extension Presentation Linkbase

Note: Stockholders may receive copies of the above listed exhibits, without fee, by written request to Investor Relations, Oil-Dri Corporation of America, 410 North Michigan Avenue, Suite 400, Chicago, Illinois 60611-4213, by telephone at (312) 321-1515 or by e-mail to info@oildri.com.