

MESA LABORATORIES INC /CO
Form 10-Q
February 02, 2015

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 December 31, 2014

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

For the transition period from ___ to ___

Commission File No: 0-11740

MESA LABORATORIES, INC.

(Exact name of registrant as specified in its charter)

| | |
|--------------------------------------------------------------------------------------|-----------------------------------------------------------------|
| Colorado (State or other jurisdiction of incorporation or organization) | 84-0872291 (I.R.S. Employer Identification number) |
|--------------------------------------------------------------------------------------|-----------------------------------------------------------------|

| | |
|---------------------------------------------------------------------------------------------------------|----------------------------|
| 12100 West Sixth Avenue Lakewood, Colorado (Address of principal executive offices) | 80228 (Zip Code) |
|---------------------------------------------------------------------------------------------------------|----------------------------|

Registrant's telephone number, including area code: **(303) 987-8000**

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 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 (Section 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See 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
(Do not check if a 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 the latest practicable date:

There were 3,535,456 shares of the Issuer's common stock, no par value, outstanding as of January 27, 2015.

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Signatures

Certification of Chief Executive Officer Pursuant to Rule 13a-14(a)

Certification of Chief Financial Officer Pursuant to Rule 13a-14(a)

Certification of Chief Executive Officer Pursuant to Rule 13a-14(b) and 18 U.S.C. Section 1350

Certification of Chief Financial Officer Pursuant to Rule 13a-14(b) and 18 U.S.C. Section 1350

Part I. Financial Information**Item 1. Financial Statements****Mesa Laboratories, Inc.****Condensed Consolidated Balance Sheets**

(In thousands, except share amounts)

| ASSETS | December 31, 2014 | March 31, 2014 |
|---------------------------------------------|------------------------------|-------------------------------|
| | (Unaudited) | |
| Current assets: | | |
| Cash and cash equivalents | \$ 1,427 | \$5,575 |
| Accounts receivable, net | 11,849 | 9,278 |
| Inventories, net | 12,596 | 7,771 |
| Prepaid expenses and other | 1,558 | 2,064 |
| Deferred income taxes | 1,878 | 1,878 |
| Total current assets | 29,308 | 26,566 |
| Property, plant and equipment, net | 9,241 | 7,680 |
| Intangibles, net | 33,532 | 25,417 |
| Goodwill | 44,097 | 37,866 |
| Total assets | \$ 116,178 | \$97,529 |
| LIABILITIES AND STOCKHOLDERS' EQUITY | | |
| Current liabilities: | | |
| Accounts payable | \$ 2,840 | \$2,019 |
| Accrued salaries and payroll taxes | 3,968 | 3,567 |
| Unearned revenues | 1,421 | 1,886 |
| Other accrued expenses | 1,450 | 2,743 |
| Current portion of long-term debt | 3,000 | -- |
| Total current liabilities | 12,679 | 10,215 |
| Deferred income taxes | 4,861 | 4,861 |
| Long-term debt | 25,000 | 16,500 |
| Contingent consideration | 1,920 | 1,620 |
| Total liabilities | 44,460 | 33,196 |

Commitments and Contingencies (Note 7)

Stockholders' equity:

| | | |
|--------------------------------------------------------------------------------------------------------------------------------|----------------|--------------|
| Common stock, no par value; authorized 25,000,000 shares; issued and outstanding, 3,535,349 and 3,490,628 shares, respectively | 17,681 | 15,796 |
| Employee loans to purchase stock | -- | (24) |
| Retained earnings | 54,287 | 48,561 |
| Accumulated other comprehensive loss | (250) | -- |
| Total stockholders' equity | 71,718 | 64,333 |
| Total liabilities and stockholders' equity | \$ 116,178 | \$97,529 |

See accompanying notes to condensed consolidated financial statements.

Mesa Laboratories, Inc.**Condensed Consolidated Statements of Income**

(Unaudited)

(In thousands except per share data)

| | Three Months Ended December 31, | | Nine Months Ended December 31, | |
|------------------------------------------------|------------------------------------------------|-------------|-----------------------------------------------|-------------|
| | 2014 | 2013 | 2014 | 2013 |
| Revenues | \$17,830 | \$13,116 | \$52,770 | \$37,010 |
| Cost of revenues | 6,778 | 5,410 | 20,890 | 14,907 |
| Gross profit | 11,052 | 7,706 | 31,880 | 22,103 |
| Operating expenses | | | | |
| Selling | 1,772 | 1,595 | 5,177 | 4,097 |
| General and administrative | 4,740 | 2,781 | 12,581 | 8,003 |
| Research and development | 832 | 524 | 2,459 | 1,639 |
| Total operating expenses | 7,344 | 4,900 | 20,217 | 13,739 |
| Operating income | 3,708 | 2,806 | 11,663 | 8,364 |
| Other income (expense), net | 5 | (79) | (314) | 316 |
| Earnings before income taxes | 3,713 | 2,727 | 11,349 | 8,680 |
| Income taxes | 1,310 | 981 | 4,005 | 3,142 |
| Net income | \$2,403 | \$1,746 | \$7,344 | \$5,538 |
| Net income per share: | | | | |
| Basic | \$0.68 | \$0.51 | \$2.09 | \$1.62 |
| Diluted | 0.66 | 0.48 | 2.01 | 1.54 |
| Weighted average common shares outstanding: | | | | |
| Basic | 3,532 | 3,434 | 3,513 | 3,414 |
| Diluted | 3,654 | 3,637 | 3,649 | 3,591 |

See accompanying notes to condensed consolidated financial statements.

Mesa Laboratories, Inc.

Condensed Consolidated Statements of Comprehensive Income

(Unaudited)

(In thousands except per share data)

| | Three Months Ended December 31, 2014 | | Nine Months Ended December 31, 2013 | |
|---------------------------------------|---------------------------------------------------------|---------|--------------------------------------------------------|---------|
| Net Income | \$2,403 | \$1,746 | \$7,344 | \$5,538 |
| Other comprehensive loss, net of tax: | | | | |
| Foreign currency translation | (250) | -- | (250) | -- |
| Total comprehensive income | \$2,153 | \$1,746 | \$7,094 | \$5,538 |

See accompanying notes to condensed consolidated financial statements.

Mesa Laboratories, Inc.**Condensed Consolidated Statements of Cash Flows**

(Unaudited)

(In thousands)

| | Nine Months Ended December 31, | |
|------------------------------------------------------------------|-----------------------------------------------|-------------|
| | 2014 | 2013 |
| Cash flows from operating activities: | | |
| Net income | \$7,344 | \$5,538 |
| Depreciation and amortization | 4,162 | 2,682 |
| Stock-based compensation | 776 | 629 |
| Loss (gain) on disposition of assets | 16 | (420) |
| Foreign currency adjustments | (169) | -- |
| Change in assets and liabilities, net of effects of acquisitions | | |
| Accounts receivable, net | (1,994) | 1,202 |
| Inventories, net | (3,340) | (684) |
| Prepaid expenses and other | 538 | (425) |
| Accounts payable | 747 | 105 |
| Accrued liabilities and taxes payable | (1,439) | 714 |
| Unearned revenues | (465) | 133 |
| Net cash provided by operating activities | 6,176 | 9,474 |
| Cash flows from investing activities: | | |
| Acquisitions | (19,050) | (22,758) |
| Proceeds from dispositions | -- | 661 |
| Purchases of property, plant and equipment | (2,212) | (808) |
| Net cash used in investing activities | (21,262) | (22,905) |
| Cash flows from financing activities: | | |
| Proceeds from the issuance of debt | 23,000 | 18,000 |
| Payments on debt | (11,500) | (6,000) |
| Dividends | (1,618) | (1,467) |
| Purchase and retirement of common stock | -- | (15) |
| Proceeds from the exercise of stock options | 1,137 | 1,067 |
| Net cash provided by financing activities | 11,019 | 11,585 |
| Effect of exchange rate changes on cash and cash equivalents | (81) | -- |
| Net decrease in cash and cash equivalents | (4,148) | (1,846) |
| Cash and cash equivalents at beginning of period | 5,575 | 4,006 |

| | | |
|----------------------------------------------------|---------|---------|
| Cash and cash equivalents at end of period | \$1,427 | \$2,160 |
| Cash paid for: | | |
| Income taxes | \$2,789 | \$3,248 |
| Interest | 354 | 52 |
| Supplemental non-cash activity: | | |
| Repayment of employee loans for stock options | \$24 | \$92 |
| Contingent consideration as part of an acquisition | 300 | 500 |

See accompanying notes to condensed consolidated financial statements.

Mesa Laboratories, Inc.

Notes to Condensed Consolidated Financial Statements

Note 1 -Description of Business and Summary of Significant Accounting Policies

Description of Business

Mesa Laboratories, Inc. was incorporated under the laws of the State of Colorado on March 26, 1982. The terms “we,” “us,” “our,” the “Company” or “Mesa” are used in this report to refer collectively to the parent company and the subsidiaries through which our various businesses are actually conducted. We pursue a strategy of focusing primarily on quality control products, which are sold into niche markets that are driven by regulatory requirements. We prefer markets that have limited competition where we can establish a commanding presence and achieve high gross margins. We are organized into three divisions across six physical locations. Our Instruments Division designs, manufactures and markets quality control instruments and disposable products utilized in connection with the healthcare, pharmaceutical, food and beverage, medical device, industrial hygiene, environmental air sampling and semiconductor industries. Our Biological Indicators Division manufactures and markets biological indicators and distributes chemical indicators used to assess the effectiveness of sterilization processes, including steam, gas, hydrogen peroxide, ethylene oxide and radiation, in the hospital, dental, medical device and pharmaceutical industries. Our Continuous Monitoring Division designs, develops and markets systems which are used to monitor various environmental parameters such as temperature, humidity and differential pressure to ensure that critical storage and processing conditions are maintained in hospitals, pharmaceutical and medical device manufacturers, blood banks, pharmacies and a number of other laboratory and industrial environments

Basis of Presentation

The accompanying condensed consolidated balance sheet as of March 31, 2014, has been derived from audited consolidated financial statements. The accompanying unaudited interim condensed consolidated financial statements have been prepared on the same basis as our annual audited consolidated financial statements and in accordance with accounting principles generally accepted in the United States (“GAAP”) for interim financial information and the rules and regulations of the Securities and Exchange Commission (“SEC”) for interim financial statements. In the opinion of management, such unaudited information includes all adjustments (consisting only of normal recurring accruals) necessary for a fair presentation of this interim information. Operating results and cash flows for interim periods are not necessarily indicative of results that can be expected for the entire year. The information included in this report should be read in conjunction with our audited consolidated financial statements and notes thereto included in our Annual Report on Form 10-K for the year ended March 31, 2014.

The summary of our significant accounting policies is incorporated by reference to our Annual Report on Form 10-K for the year ended March 31, 2014.

Recently Issued Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board (“FASB”) and International Accounting Standards Board (“IASB”) issued a jointly converged standard on the recognition of revenue from contracts with customers. The issued guidance converges the criteria for reporting revenues, as well as requiring disclosures sufficient to describe the nature, amount, timing and uncertainty of revenues and cash flows arising from these contracts. Companies can transition to the standard either retrospectively or as a cumulative effective adjustment as of the date of adoption. The new standard is effective for our fiscal year (and interim periods within that year) ending March 31, 2018. We are evaluating the impact of this standard on our condensed consolidated financial statements and disclosures.

Note 2 – Acquisitions and Dispositions

Acquisitions

For the nine months ended December 31, 2014, our acquisitions of businesses (net of cash acquired) totaled \$19,050,000, which consisted primarily of the following material acquisitions:

PCD

On October 15, 2014, we completed a business combination (the “PCD Acquisition”) with PCD-Process Challenge Devices, LLC (“PCD”) whereby we acquired substantially all the assets (other than cash and accounts receivable) and certain liabilities of PCD’s process challenge device business. The asset acquisition agreement (the “PCD Agreement”) includes provisions for both contingent consideration based upon the cumulative three year revenues of our process challenge device business subsequent to the acquisition and for a holdback payment (subject to a post-closing adjustment), payable at the one year anniversary of the closing date.

Under the terms of the PCD Agreement, we are required to pay contingent consideration if the cumulative revenues for our process challenge device business for the three years subsequent to the acquisition meet certain levels. The potential consideration payable ranges from \$0 to \$1,500,000 and is based upon a sliding scale of three-year cumulative revenues between \$9,900,000 and \$12,600,000. Based upon both historical and projected growth rates, we recorded \$300,000 of contingent consideration payable which represents our best estimate of the amount that will ultimately be paid. Any changes to the contingent consideration ultimately paid will result in additional income or expense in our condensed consolidated statements of income. We will continue to monitor the results of our process challenge device business and we will adjust the contingent liability on a go forward basis, based on then current information. The contingent consideration is payable in three annual installments beginning in the third quarter of our year ending March 31, 2016.

We expect to achieve savings and generate growth as we integrate the PCD operations and sales and marketing functions. These factors, among others, contributed to a purchase price in excess of the estimated fair value of the net identifiable assets acquired and, as a result, we recorded goodwill in connection with this transaction. The goodwill is expected to be deductible for tax purposes and it was assigned to our Biological Indicators segment.

The PCD Acquisition constituted the acquisition of a business and was recognized at fair value. Due to the recent nature of the transaction, the purchase price allocation was based upon a preliminary estimated fair value of the assets and liabilities acquired as we are in the process of finalizing our valuation of the assets acquired and liabilities assumed. We determined the preliminary estimated fair values using discounted cash flow analyses and estimates made by management. The following reflects our preliminary allocation of the consideration, subject to customary purchase price adjustments in accordance with the PCD Agreement (in thousands):

| | |
|------------------------------------|---------|
| Cash consideration | \$5,000 |
| Holdback payment liability | 250 |
| Contingent consideration liability | 300 |
| Aggregate consideration | \$5,550 |
| Inventories, net | \$137 |
| Property, plant and equipment, net | 7 |
| Intangibles, net | 3,678 |
| Goodwill | 1,743 |
| Accrued expenses | (15) |
| Total purchase price allocation | \$5,550 |

The accompanying condensed consolidated statements of income include the results of the PCD Acquisition from the acquisition date of October 15, 2014. The pro forma effects of the acquisition on the results of operations as if the acquisition had been completed on April 1, 2014 and 2013, are as follows (in thousands, except per share data):

| | Three Months Ended | | Nine Months Ended | |
|------------------------------|---------------------------|-------------|--------------------------|-------------|
| | December 31, 2014 | 2013 | December 31, 2014 | 2013 |
| Revenues | \$18,056 | \$13,915 | \$54,494 | \$39,424 |
| Net income | 2,415 | 1,853 | 7,433 | 5,862 |
| Net Income per common share: | | | | |
| Basic | \$0.68 | \$0.54 | \$2.12 | \$1.72 |
| Diluted | 0.66 | 0.51 | 2.04 | 1.63 |

BGI

On April 15, 2014, we completed a business combination (the “BGI Acquisition”) whereby we acquired substantially all of the assets (other than cash and accounts receivable) and certain liabilities of BGI, Incorporated and BGI Instruments, Inc. (collectively “BGI”), a business focused on the sale of equipment primarily used for particulate air sampling. The purchase price for the acquired assets was \$10,268,000.

We expect to achieve savings and generate growth as we integrate the BGI operations and sales and marketing functions. These factors, among others, contributed to a purchase price in excess of the estimated fair value of the net identifiable assets acquired and, as a result, we recorded goodwill in connection with this transaction. The goodwill is expected to be deductible for tax purposes and it was assigned to our Instruments segment.

The BGI Acquisition constituted the acquisition of a business and was recognized at fair value. We determined the estimated fair values using discounted cash flow analyses and estimates made by management. The following reflects our allocation of the consideration, subject to customary purchase price adjustments in accordance with the BGI Agreement (in thousands):

| | |
|------------------------------------|----------|
| Inventories, net | \$1,268 |
| Property, plant and equipment, net | 47 |
| Intangibles, net | 5,711 |
| Goodwill | 3,295 |
| Accrued expenses | (53) |
| Total purchase price allocation | \$10,268 |

The accompanying condensed consolidated statements of income include the results of the BGI Acquisition from the acquisition date of April 15, 2014. The pro forma effects of the acquisition on the results of operations as if the acquisition had been completed on April 1, 2014 and 2013, are as follows (in thousands, except per share data):

| | Three Months Ended | | Nine Months Ended | |
|------------------------------|-------------------------------|-------------|------------------------------|-------------|
| | December 31, | | December 31, | |
| | 2014 | 2013 | 2014 | 2013 |
| Revenues | \$17,830 | \$15,032 | \$53,088 | \$42,758 |
| Net income | 2,403 | 2,281 | 7,422 | 7,144 |
| Net Income per common share: | | | | |
| Basic | \$0.68 | \$0.66 | \$2.11 | \$2.09 |
| Diluted | 0.66 | 0.63 | 2.03 | 1.99 |

Dispositions

On August 12, 2013, we entered into an agreement whereby we sold our NuSonics product line for \$661,000. The carrying value of this product line was \$193,000 which resulted in a pre-tax gain of \$468,000.

Note 3 - Inventories

Inventories consist of the following (in thousands):

| | December 31, 2014 | March 31, 2014 |
|-----------------|------------------------------|-------------------------------|
| Raw materials | \$ 10,301 | \$5,758 |
| Work-in-process | 1,013 | 272 |
| Finished goods | 1,944 | 2,068 |
| Less: reserve | (662) | (327) |
| | \$ 12,596 | \$7,771 |

Note 4 - Long-Term Debt

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

| | December 31, 2014 | March 31, 2014 |
|---------------------------------------------|------------------------------|-------------------------------|
| Line of credit (1.67% at December 31, 2014) | \$ 14,500 | \$16,500 |
| Term loan (2.17% at December 31, 2014) | 13,500 | -- |
| Less: current portion | (3,000) | -- |
| Long-term portion | \$ 25,000 | \$ 16,500 |

In February 2012, we entered into a three year agreement (the "Credit Facility") for a \$20,000,000 revolving line of credit ("Line of Credit") and up to \$1,000,000 of letters of credit, maturing in February 2015. Funds from the Credit Facility were used for general working capital and corporate needs, retiring existing debt, and supporting acquisitions.

In April 2014, the Credit Facility was amended to include a \$15,000,000 term loan (the "Term Loan") and to extend the maturity date of the Credit Facility to June 30, 2017.

Under the Line of Credit, indebtedness bears interest at either: (1) LIBOR, as defined, plus an applicable margin ranging from 1.25% to 2%; or (2) the bank's commercial bank floating rate ("CBFR"), which is the greater of the bank's prime rate or one month LIBOR + 2.50%, adjusted down, from 1.25% to 0.50%. We elect the interest rate with each borrowing under the line of credit. In addition, there is an unused capacity fee of 0.15% to 0.30%. The adjustments and unused capacity fee depend on the ratio of funded debt (including amounts outstanding under the Term Loan) to our trailing four quarters of EBITDA, as defined, with four tiers ranging from a ratio of less than one to greater than two. Letter of credit fees are based on the applicable LIBOR rate.

The Term Loan bears interest at LIBOR, as defined, plus 2% and requires 11 quarterly principal payments (the first due date was July 15, 2014) in the amount of \$750,000 with the remaining balance of principal and accrued interest due on April 15, 2017. The proceeds from the Term Loan were used to support acquisition financing and to repay amounts outstanding under the Line of Credit.

The Credit Facility is secured by all of our assets and requires us to maintain a ratio of funded debt to our trailing four quarters of EBIDTA, as defined, of 2.5 to 1.0, and a minimum fixed charge coverage ratio of 1.35 to 1.0. We were in compliance with these covenants at December 31, 2014.

Future contractual maturities of debt are as follows (in thousands):

| Year ending March 31, | |
|------------------------------|----------|
| 2015 | \$750 |
| 2016 | 3,000 |
| 2017 | 3,000 |
| 2018 | 21,250 |
| | \$28,000 |

In October 2014, we borrowed \$5,000,000 under the terms of the Line of Credit in order to fund the PCD Acquisition (see Note 2). During the three months ended December 31, 2014 we made a \$750,000 required principal payment on the Term Loan and principal payments of \$2,000,000 on the Line of Credit.

In January 2015 we made a \$750,000 required principal payment on the Term Loan.

Note 5 - Stock-Based Compensation

Amounts recognized in the condensed consolidated financial statements related to stock-based compensation are as follows (in thousands, except per share data):

| | Three Months Ended | | Nine Months Ended | |
|-----------------------------------------------------------------------------------|-----------------------------------|-------------|------------------------------|-------------|
| | December 31, | | December 31, | |
| | 2014 | 2013 | 2014 | 2013 |
| Total cost of stock-based compensation charged against income before income taxes | \$260 | \$272 | \$776 | \$629 |
| Amount of income tax benefit recognized in earnings | 92 | 98 | 274 | 228 |
| Amount charged against net income | \$168 | \$174 | 502 | 401 |
| Impact on net income per common share: | | | | |
| Basic | \$0.05 | \$0.05 | \$0.14 | \$0.12 |
| Diluted | 0.05 | 0.05 | \$0.14 | 0.11 |

Stock-based compensation expense is included in cost of revenues, selling, and general and administrative expense in the accompanying condensed consolidated statements of income.

The fair value of each stock option grant is estimated on the date of grant using the Black-Scholes option-pricing model (“Black-Scholes”). We use historical data to estimate the expected price volatility, the expected stock option life and expected forfeiture rate. The risk-free interest rate is based on the United States Treasury yield curve in effect at the time of grant for the estimated life of the stock option. The dividend yield is calculated based upon the dividend payments made during the prior four quarters as a percent of the average stock price for that period.

The following is a summary of stock option activity for the nine months ended December 31, 2014:

| | Number of Shares | Weighted- Average Exercise Price per Share | Weighted- Average Remaining Contractual Term | Aggregate Intrinsic Value (000s) |
|----------------------------------|---------------------------------|-------------------------------------------------------------------|---------------------------------------------------------------------|-----------------------------------------------------|
| Outstanding at March 31, 2014 | 398,172 | \$ 38.75 | 4.4 | \$ 20,505 |
| Stock options granted | 147,720 | 88.62 | 7.3 | |
| Stock options forfeited | (26,066) | 64.24 | 5.5 | |
| Stock options expired | -- | -- | | |
| Stock options exercised | (48,865) | 29.68 | | |
| Outstanding at December 31, 2014 | 470,961 | 53.84 | 4.8 | 12,662 |
| Exercisable at December 31, 2014 | 196,523 | 32.38 | 3.2 | 8,828 |

The total intrinsic value of stock options exercised was \$2,003,000 and \$2,889,000 for the nine months ended December 31, 2014 and 2013, respectively.

A summary of the status of our unvested stock option shares as of December 31, 2014 is as follows:

| | Number of Shares | Weighted-Average Grant-Date Fair Value |
|-------------------------------|---------------------------------|-------------------------------------------------------|
| Unvested at March 31, 2014 | 257,347 | \$ 11.86 |
| Stock options granted | 147,720 | 24.16 |
| Stock options forfeited | (26,066) | 17.19 |
| Stock options vested | (104,563) | 10.36 |
| Unvested at December 31, 2014 | 274,438 | 18.43 |

As of December 31, 2014, there was \$3,540,000 of total unrecognized compensation expense related to unvested stock options.

On August 8, 2014 we adopted The Mesa Laboratories, Inc. 2014 Equity Plan (the "2014 Plan"), which was subsequently approved by our shareholders on October 2, 2014 at our 2014 Annual Meeting of Shareholders. The purpose of the 2014 Plan is to promote the success and enhance the value of the Company by linking the personal interests of our employees, officers and directors to those of our shareholders by providing such persons with an incentive for outstanding performance. A total of 1,100,000 shares of common stock were reserved for issuance under

the 2014 Plan and are subject to terms as set by the Compensation Committee of the Board of Directors at the time of grant. As a result of the approval of the 2014 Plan by our shareholders, no further awards will be made under the 2006 Plan and it will remain in effect only as long as awards previously made thereunder remain outstanding. As of December 31, 2014, we have 1,097,680 shares available for future stock option grants.

Note 6 - Net Income Per Share

Basic net income per share is computed by dividing net income by the weighted-average number of common shares outstanding during the reporting period. Diluted net income per share is computed similarly to basic net income per share, except that it includes the potential dilution that could occur if dilutive securities were exercised.

The following table presents a reconciliation of the denominators used in the computation of net income per share - basic and diluted (in thousands, except per share data):

| | Three Months Ended December 31, | | Nine Months Ended December 31, | |
|-----------------------------------------------------|------------------------------------------------|-------------|-----------------------------------------------|-------------|
| | 2014 | 2013 | 2014 | 2013 |
| Net income available for shareholders | \$2,403 | \$1,746 | \$7,344 | \$5,538 |
| Weighted average outstanding shares of common stock | 3,532 | 3,434 | 3,513 | 3,414 |
| Dilutive effect of stock options | 122 | 203 | 136 | 177 |
| Common stock and equivalents | 3,654 | 3,637 | 3,649 | 3,591 |
| Net income per share: | | | | |
| Basic | \$0.68 | \$0.51 | \$2.09 | \$1.62 |
| Diluted | 0.66 | 0.48 | 2.01 | 1.54 |

For both the three and nine months ended December 31, 2014, 155,000 and 173,000 outstanding stock options, respectively, were excluded from the calculation of diluted net income per share because the exercise prices of the stock options were greater than or equal to the average price of the common shares and, therefore, their inclusion would have been anti-dilutive.

For both the three and nine months ended December 31, 2013, 27,000 and 60,000 outstanding stock options, respectively, were excluded from the calculation of diluted net income per share because the exercise prices of the stock options were greater than or equal to the average price of the common shares and, therefore, their inclusion would have been anti-dilutive.

Note 7- Commitments and Contingencies

Under the terms of the Amega Agreement, we are required to pay contingent consideration (the “Amega Earn Out”) if the cumulative revenues for our Continuous Monitoring Division for the three years subsequent to the acquisition meet certain levels. The potential consideration payable ranges from \$0 to \$10,000,000 and is based upon a sliding scale of three-year cumulative revenues between \$31,625,000 and \$43,500,000. Based upon both historical and projected growth rates, we recorded \$500,000 of contingent consideration payable which represents our best estimate of the amount that will ultimately be paid. Any changes to the contingent consideration ultimately paid will result in additional income or expense in our condensed consolidated statements of income. We will continue to monitor the results of our Continuous Monitoring Division and we will adjust the contingent liability on a go forward basis, based on then current information. The contingent consideration is payable in the third quarter of our year ending March 31, 2017.

In November 2014, Amega Scientific Corporation (“Amega”) and its owner Anthony Amato (“Amato”) filed a complaint in the United States District Court for the district of Colorado alleging, among other items, that our termination of Amato as an employee impacted his ability to maximize the potential consideration payable under the Amega Earn Out and to exercise stock options that failed to vest. In addition, Amato has alleged that we improperly withheld certain amounts from the holdback consideration under the Amega Agreement. These amounts (which were recorded as liabilities in our original purchase accounting) remain recorded as other accrued expenses on the accompanying condensed consolidated balance sheets and will remain so until a final ruling by the court is made. In January 2015 we filed a motion to dismiss the complaint with prejudice. Given that the complaint is in the early stages of the process, we are unable to make a reasonable estimate of the potential loss or range of losses, if any, that might arise from this matter. We believe that we acted in a matter consistent with employment law and the provisions of the Amega Agreement and we intend to defend our position vigorously.

Under the terms of the Bios Agreement, we are required to pay contingent consideration if the cumulative revenues related to the acquisition for the three years subsequent to the acquisition exceed \$22,127,000. The potential future payment that we could be required to make ranges from \$0 to \$6,710,000. Based upon historical growth rates, we initially recorded \$2,140,000 of contingent consideration payable which represented our best estimate of the amount that would ultimately be paid. Based upon actual results and current run rates, during the year ended March 31, 2014, we revised our estimate of the ultimate contingent liability that would be paid, which resulted in reducing the contingent consideration payable to \$1,120,000. Any further changes to the contingent consideration ultimately paid would result in additional income or expense in our condensed consolidated statements of income. We will continue to monitor the results associated with the Bios Acquisition and we will adjust the contingent liability on a go forward basis, based on then current information. The contingent consideration is payable in the first quarter of our year ending March 31, 2016.

Under the terms of the PCD Agreement, we are required to pay contingent consideration if the cumulative revenues for our process challenge device business for the three years subsequent to the acquisition meet certain levels. The potential consideration payable ranges from \$0 to \$1,500,000 and is based upon a sliding scale of three-year cumulative revenues between \$9,900,000 and \$12,600,000. Based upon both historical and projected growth rates, we recorded \$300,000 of contingent consideration payable which represents our best estimate of the amount that will ultimately be paid. Any changes to the contingent consideration ultimately paid will result in additional income or expense in our condensed consolidated statements of income. We will continue to monitor the results of our process challenge device business and we will adjust the contingent liability on a go forward basis, based on then current information. The contingent consideration is payable in three annual installments beginning in the third quarter of our year ending March 31, 2016.

A company is required to collect and remit state sales tax from certain of its customers if that company is determined to have “nexus” in a particular state. The determination of nexus varies state by state and often requires knowledge of each jurisdiction’s tax case law. During the year ended March 31, 2013, we determined that there are states in which we most likely had established nexus during prior periods without properly collecting and remitting sales tax. We recorded an estimate of \$100,000 associated with one specific state but we were unable to estimate our remaining exposure at that time. The ultimate amount due in remaining states will depend upon a number of factors, including the amount of sales that were made to customers who are either exempt or have already paid the tax, the number of years of exposure, and any penalties or interest that might be due. During the year ended March 31, 2014, we completed our analysis associated with the remaining states and we recorded an estimate of \$1,408,000, which was included in other accrued expenses on the consolidated balance sheets and in general and administrative expense on the consolidated statements of income for the year ended March 31, 2014. That estimate was based upon facts and circumstances known at such time and our ultimate liability was subject to change as further analysis is completed and state sales tax returns are filed.

During the nine months ended December 31, 2014 we successfully completed and filed several state sales tax returns which concluded our obligation for historical sales taxes in those states. In addition we continued to work through the process in the remaining states. As a result of this work, we determined that our exposure had increased above and beyond our original accrual and as a result, we recorded an additional accrual of \$460,000 during the three months ended December 31, 2014. We are hopeful that we are far enough in the process that we have accrued for the ultimate amount of liability that will be paid but our work was based upon facts and circumstances known at such time and our ultimately liability is subject to change as further analysis is completed and state sales tax returns are filed.

Note 8 – Comprehensive Income

Amounts recognized in the condensed consolidated financial statements related to comprehensive income are as follows (in thousands):

| | Three Months Ended December 31, 2014 | | | Three Months Ended December 31, 2013 | | |
|---------------------------------------|-----------------------------------------------------|------------|------------|-----------------------------------------------------|------------|------------|
| | Pretax | Tax | Net | Pretax | Tax | Net |
| Net income available for shareholders | | | \$2,403 | | | \$1,746 |
| Other comprehensive loss: | | | | | | |
| Foreign currency translation | \$(250) | -- | (250) | \$-- | -- | -- |
| Other comprehensive loss | \$(250) | -- | (250) | \$-- | -- | -- |
| Total comprehensive income | | | \$2,153 | | | \$1,746 |

| | Nine Months Ended December 31, 2014 | | | Nine Months Ended December 31, 2013 | | |
|---------------------------------------|------------------------------------------------|------------|------------|----------------------------------------------------|------------|------------|
| | Pretax | Tax | Net | Pretax | Tax | Net |
| Net income available for shareholders | | | \$7,344 | | | \$5,538 |
| Other comprehensive loss: | | | | | | |
| Foreign currency translation | \$(250) | -- | (250) | \$-- | -- | -- |
| Other comprehensive loss | \$(250) | -- | (250) | \$-- | -- | -- |
| Total comprehensive income | | | \$7,094 | | | \$5,538 |

Accumulated other comprehensive loss balances, net of tax effects, consist of the following (in thousands):

| | December 31, 2014 | March 31, 2014 |
|--------------------------------------|------------------------------|-------------------------------|
| Foreign currency translation | \$ (250) | \$ -- |
| Accumulated other comprehensive loss | \$ (250) | \$ -- |

Note 9 - Segment Information

We have three reporting segments: Biological Indicators, Instruments and Continuous Monitoring. The following tables set forth our segment information (in thousands):

| | Three Months Ended December 31, 2014 | | | |
|----------------------------------|---------------------------------------------|--------------------|-------------------|-------------------|
| | Biological | Instruments | | Continuous |
| | Indicators | Monitoring | Monitoring | Total |
| Revenues | \$6,964 | \$ 8,216 | \$ 2,650 | \$ 17,830 |
| Gross profit | \$4,194 | \$ 5,412 | \$ 1,446 | \$ 11,052 |
| Selling expenses | 365 | 919 | 488 | 1,772 |
| | \$3,829 | \$ 4,493 | \$ 958 | 9,280 |
| Reconciling items ⁽¹⁾ | | | | (5,567) |
| Earnings before income taxes | | | | \$3,713 |

| | Three Months Ended December 31, 2013 | | | |
|----------------------------------|---------------------------------------------|--------------------|-------------------|-------------------|
| | Biological | Instruments | | Continuous |
| | Indicators | Monitoring | Monitoring | Total |
| Revenues | \$5,317 | \$ 6,438 | \$ 1,361 | \$ 13,116 |
| Gross profit | \$2,976 | \$ 4,137 | \$ 593 | \$ 7,706 |
| Selling expenses | 404 | 1,047 | 144 | 1,595 |
| | \$2,572 | \$ 3,090 | \$ 449 | 6,111 |
| Reconciling items ⁽¹⁾ | | | | (3,384) |
| Earnings before income taxes | | | | \$2,727 |

Nine Months Ended December 31, 2014

| | Biological | Continuous | Total |
|--|-------------------|-------------------|--------------|
|--|-------------------|-------------------|--------------|

| | Indicators | Instruments | Monitoring | |
|----------------------------------|-------------------|--------------------|-------------------|----------|
| Revenues | \$19,822 | \$ 24,966 | \$ 7,982 | \$52,770 |
| Gross profit | \$12,029 | \$ 15,794 | \$ 4,057 | \$31,880 |
| Selling expenses | 766 | 3,093 | 1,318 | 5,177 |
| | \$11,263 | \$ 12,701 | \$ 2,739 | 26,703 |
| Reconciling items ⁽¹⁾ | | | | (15,354) |
| Earnings before income taxes | | | | \$11,349 |

Nine Months Ended December 31, 2013

| | Biological | | Continuous | Total |
|----------------------------------|-------------------|--------------------|-------------------|--------------|
| | Indicators | Instruments | Monitoring | |
| Revenues | \$16,181 | \$ 19,468 | \$ 1,361 | \$37,010 |
| Gross profit | \$9,019 | \$ 12,491 | \$ 593 | \$22,103 |
| Selling expenses | 1,350 | 2,603 | 144 | 4,097 |
| | \$7,669 | \$ 9,888 | \$ 449 | 18,006 |
| Reconciling items ⁽¹⁾ | | | | (9,326) |
| Earnings before income taxes | | | | \$8,680 |

⁽¹⁾ Reconciling items include general and administrative, research and development, and other expenses.

| | December 31, 2014 | March 31, 2014 |
|------------------------------|------------------------------|-------------------------------|
| Total assets | | |
| Biological Indicators | \$ 25,921 | \$ 22,771 |
| Instruments | 54,308 | 36,797 |
| Continuous Monitoring | 31,086 | 28,578 |
| Corporate and administrative | 4,863 | 9,383 |
| | \$ 116,178 | \$ 97,529 |

All long-lived assets are located in the United States except for \$3,269,000 which are associated with our subsidiary which is located in Chassieu, France.

Revenues from external customers are attributed to individual countries based upon locations to which the product is shipped or exported, as follows (in thousands):

| | Three Months Ended December 31, 2014 | | Nine Months Ended December 31, 2014 | |
|-------------------------------------------|---------------------------------------------------------|------------------|--------------------------------------------------------|------------------|
| | 2014 | 2013 | 2014 | 2013 |
| Net revenues from unaffiliated customers: | | | | |
| United States | \$ 11,423 | \$ 7,054 | \$ 29,612 | \$ 20,877 |
| Foreign | 6,407 | 6,062 | 23,158 | 16,133 |
| | \$ 17,830 | \$ 13,116 | \$ 52,770 | \$ 37,010 |

No foreign country exceeds 10% of total revenues.

Note 10 - Subsequent Event

In January 2015, our Board of Directors declared a quarterly cash dividend of \$0.16 per share of common stock, payable on March 16, 2015, to shareholders of record at the close of business on February 27, 2015.

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

Forward Looking Statements

This report contains information that may constitute "forward-looking statements." Generally, the words "believe," "expect," "intend," "anticipate," "estimate," "project," "will" and similar expressions identify forward-looking statements, which generally are not historical in nature. However, the absence of these words or similar expressions does not mean that a statement is not forward-looking. All statements that address operating performance, events or developments that we expect or anticipate will occur in the future — including statements relating to revenue growth and statements expressing general views about future operating results — are forward-looking statements. Management believes that these forward-looking statements are reasonable as and when made. However, caution should be taken not to place undue reliance on any such forward-looking statements because such statements speak only as of the date when made. We undertake no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events or otherwise, except as required by law. In addition, forward-looking statements are subject to certain risks and uncertainties that could cause actual results to differ materially from our historical experience and our present expectations or projections. These risks and uncertainties include, but are not limited to those described in Part II, "Item 1A. Risk Factors" and elsewhere in this report and in our Annual Report on Form 10-K for the year ended March 31, 2014, and those described from time to time in our subsequent reports filed with the Securities and Exchange Commission.

General Discussion

We pursue a strategy of focusing primarily on quality control products, which are sold into niche markets that are driven by regulatory requirements. We prefer markets that have limited competition where we can establish a commanding presence and achieve high gross margins. We are organized into three divisions across six physical locations. Our Instruments Division designs, manufactures and markets quality control instruments and disposable products utilized in connection with the healthcare, pharmaceutical, food and beverage, medical device, industrial hygiene, environmental air sampling and semiconductor industries. Our Biological Indicators Division manufactures and markets biological indicators and distributes chemical indicators used to assess the effectiveness of sterilization processes, including steam, gas, hydrogen peroxide, ethylene oxide and radiation, in the hospital, dental, medical device and pharmaceutical industries. Our Continuous Monitoring Division designs, develops and markets systems which are used to monitor various environmental parameters such as temperature, humidity and differential pressure to ensure that critical storage and processing conditions are maintained in hospitals, pharmaceutical and medical device manufacturers, blood banks, pharmacies and a number of other laboratory and industrial environments. We follow a philosophy of manufacturing a high quality product and providing a high level of on-going service for those products.

Our revenues come from two main sources – products sales and services. Product sales are dependent on several factors, including general economic conditions, both domestic and international, customer capital spending trends, competition, introduction of new products and acquisitions. Biological indicator products are disposable and are used on a routine basis for quality control, thus product sales are less sensitive to general economic conditions. Instrument products and continuous monitoring systems have a longer life, and their purchase by our customers is somewhat discretionary, so sales are more sensitive to general economic conditions. Service demand is driven by our customers' quality control and regulatory environments, which require periodic repair and recalibration or certification of our instrument products and continuous monitoring systems. We typically evaluate costs and pricing annually. Our policy is to price our products and systems competitively and, where possible, we try to pass along cost increases in order to maintain our margins.

Gross profit is affected by our product mix, manufacturing efficiencies and price competition. Historically, as we have integrated our acquisitions and taken advantage of manufacturing efficiencies, our gross margins for some of the products have improved. There are, however, differences in gross margins between different product lines, and ultimately the mix of sales will continue to impact our overall gross margin.

Selling expense is driven primarily by labor costs, including salaries and commissions. Accordingly, it may vary with sales levels. Labor costs and amortization of intangible assets drive the substantial majority of general and administrative expense. Research and development expense is predominantly comprised of labor costs and third party consultants.

In October 2014, we completed a business combination (the “ATI Acquisition”) whereby we acquired substantially all the assets (other than cash and accounts receivable) and certain liabilities of ATI Atlas Limited (“ATI”), a distributor of our biological indicator products.

In October 2014, we completed the PCD Acquisition whereby we acquired substantially all of the assets (other than cash and accounts receivable) and certain liabilities of PCD's business which is focused on the sale of process challenge devices (“PCD's) which are used for quality control purposes in the field of ethylene oxide sterilization of medical devices.

In April 2014, we completed the BGI Acquisition whereby we acquired substantially all of the assets (other than cash and accounts receivable) and certain liabilities of BGI's business which is focused on the sale of equipment primarily used for particulate air sampling.

In April 2014, we completed a business combination (the "Amilabo Acquisition") whereby we acquired all of the common stock of Amilabo SAS ("Amilabo"), a distributor of our biological indicator products.

In November 2013, we completed a business combination (the "TempSys Acquisition") whereby we acquired all of the common stock of TempSys, Inc. ("TempSys"), a company in the business of providing continuous monitoring systems to regulated industries.

In November 2013, we completed a business combination (the "Amega Acquisition") whereby we acquired substantially all the assets and certain liabilities of Amega Scientific Corporation's ("Amega") business which provides continuous monitoring systems to regulated industries.

In July 2013, we completed a business combination (the "Suretorque Acquisition") whereby we acquired substantially all of the assets of ST Acquisitions, LLC's ("ST Acquisitions") business involving the design, manufacturing, sale and service of its SureTorque line of bottle cap torque testing instrumentation.

General Trends and Outlook

Our strategic objectives include growth both organically and through further acquisitions. During the nine months ended December 31, 2014, we continued to build our infrastructure to prepare for future growth, including the addition of key personnel to our operations, research and development, and finance teams. We also invested in upgrading our information systems and intend to continue doing so.

The markets for our biological indicators remain strong, as the disposable nature of these products makes them less sensitive to general economic conditions. The worldwide market for biological indicators is growing as more countries focus on verifying the effectiveness of sterilization processes. General economic conditions over the past few years have, at times, hampered the organic growth of our instruments business, due to the discretionary nature of these products. Additionally, uncertainty about global economic conditions may cause businesses to postpone spending in response to tighter credit, unemployment, negative financial news and/or declines in income or asset values. Worldwide and regional economic conditions could also reduce the demand for our products and services, as our customers reduce or delay capital equipment and other types of purchases. Demand for our instruments products

and our continuous monitoring systems, however, is still strong and we strive to grow revenues going forward.

We are working on several research and development projects that, if completed, may result in new products for both existing customers and in new markets. We are hopeful that all of our divisions will have new products available for sale in the coming year.

Results of Operations

The following table sets forth, for the periods indicated, condensed consolidated statements of income data. The table and the discussion below should be read in conjunction with the accompanying condensed consolidated financial statements and the notes thereto appearing elsewhere in this report (in thousands, except percent data):

| | Three Months Ended December 31, | | | Percent | |
|----------------------------|---------------------------------------|----------|---------|---------|---|
| | 2014 | 2013 | Change | Change | |
| Revenues | \$17,830 | \$13,116 | \$4,714 | 36 | % |
| Cost of revenues | 6,778 | 5,410 | 1,368 | 25 | % |
| Gross profit | \$11,052 | \$7,706 | \$3,346 | 43 | % |
| Gross profit margin | 62 | % 59 | % -- | % | |
| Operating expenses | | | | | |
| Selling | \$1,772 | \$1,595 | \$177 | 11 | % |
| General and administrative | 4,740 | 2,781 | 1,959 | 70 | % |
| Research and development | 832 | 524 | 308 | 59 | % |
| | \$7,344 | \$4,900 | \$2,444 | 50 | % |
| Operating income | \$3,708 | \$2,806 | \$902 | 32 | % |
| Net income | 2,403 | 1,746 | 657 | 38 | % |
| Net profit margin | 13 | % 13 | % -- | % | |

| | Nine Months Ended December 31, | | | Percent | |
|----------------------------|--------------------------------------|----------|----------|---------|---|
| | 2014 | 2013 | Change | Change | |
| Revenues | \$52,770 | \$37,010 | \$15,760 | 43 | % |
| Cost of revenues | 20,890 | 14,907 | 5,983 | 40 | % |
| Gross profit | \$31,880 | \$22,103 | \$9,777 | 44 | % |
| Gross profit margin | 60 % | 60 % | -- % | | |
| Operating expenses | | | | | |
| Selling | \$5,177 | \$4,097 | \$1,080 | 26 | % |
| General and administrative | 12,581 | 8,003 | 4,578 | 57 | % |
| Research and development | 2,459 | 1,639 | 820 | 50 | % |
| | \$20,217 | \$13,739 | \$6,478 | 47 | % |
| Operating income | \$11,663 | \$8,364 | \$3,299 | 39 | % |
| Net income | 7,344 | 5,538 | 1,806 | 33 | % |
| Net profit margin | 14 % | 15 % | (1) % | | |

Revenues

The following table summarizes our revenues by source (in thousands, except percent data):

| | Three Months Ended December 31, | | | Percent | |
|-----------------------|---------------------------------------|----------|---------|---------|---|
| | 2014 | 2013 | Change | Change | |
| Biological Indicators | \$6,964 | \$5,317 | \$1,647 | 31 | % |
| Instruments | 8,216 | 6,438 | 1,778 | 28 | % |
| Continuous Monitoring | 2,650 | 1,361 | 1,289 | 95 | % |
| Total | \$17,830 | \$13,116 | \$4,714 | 36 | % |

| | Nine Months Ended December 31, | | | Percent | |
|-----------------------|--------------------------------------|----------|----------|---------|---|
| | 2014 | 2013 | Change | Change | |
| Biological Indicators | \$19,822 | \$16,181 | \$3,641 | 23 | % |
| Instruments | 24,966 | 19,468 | 5,498 | 28 | % |
| Continuous Monitoring | 7,982 | 1,361 | 6,621 | 486 | % |
| Total | \$52,770 | \$37,010 | \$15,760 | | |