

**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, DC 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, 2019
or

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

For the transition period from _____ to _____
Commission file number 000-04065

Lancaster Colony Corporation

(Exact name of registrant as specified in its charter)

Ohio

(State or other jurisdiction of
incorporation or organization)

13-1955943

(I.R.S. Employer
Identification No.)

380 Polaris Parkway Suite 400
Westerville Ohio
(Address of principal executive offices)

43082
(Zip Code)

(614) 224-7141

(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ☒ No ☐

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes ☒ No ☐

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

Large accelerated filer	☒	Accelerated filer	☐
Non-accelerated filer	☐	Smaller reporting company	☐
		Emerging growth company	☐

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

Indicate by check mark whether the registrant is a shell company (as defined by Rule 12b-2 of the Exchange Act). Yes ☐ No ☒
Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Trading Symbol	Name of each exchange on which registered
Common Stock, without par value	LANC	NASDAQ Global Select Market

As of January 17, 2020, there were approximately 27,513,000 shares of Common Stock, without par value, outstanding.

LANCASTER COLONY CORPORATION AND SUBSIDIARIES
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PART I – FINANCIAL INFORMATION

Item 1. Condensed Consolidated Financial Statements

LANCASTER COLONY CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
(UNAUDITED)

(Amounts in thousands, except share data)	December 31, 2019	June 30, 2019
ASSETS		
Current Assets:		
Cash and equivalents	\$ 202,226	\$ 196,288
Receivables	77,061	75,691
Inventories:		
Raw materials	39,199	30,647
Finished goods	51,284	55,425
Total inventories	90,483	86,072
Other current assets	10,503	10,518
Total current assets	380,273	368,569
Property, Plant and Equipment:		
Land, buildings and improvements	187,813	163,094
Machinery and equipment	370,011	340,232
Total cost	557,824	503,326
Less accumulated depreciation	266,853	256,282
Property, plant and equipment-net	290,971	247,044
Other Assets:		
Goodwill	208,371	208,371
Other intangible assets-net	67,729	70,277
Operating lease right-of-use assets	24,617	—
Other noncurrent assets	11,742	11,138
Total	\$ 983,703	\$ 905,399
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current Liabilities:		
Accounts payable	\$ 86,151	\$ 76,670
Accrued liabilities	47,135	43,036
Total current liabilities	133,286	119,706
Noncurrent Operating Lease Liabilities	19,704	—
Other Noncurrent Liabilities	32,308	35,938
Deferred Income Taxes	25,647	22,882
Commitments and Contingencies		
Shareholders' Equity:		
Preferred stock-authorized 3,050,000 shares; outstanding-none		
Common stock-authorized 75,000,000 shares; outstanding-December-27,510,912 shares; June-27,491,497 shares	123,007	122,844
Retained earnings	1,406,837	1,359,782
Accumulated other comprehensive loss	(10,169)	(10,308)
Common stock in treasury, at cost	(746,917)	(745,445)
Total shareholders' equity	772,758	726,873
Total	\$ 983,703	\$ 905,399

See accompanying notes to condensed consolidated financial statements.

LANCASTER COLONY CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF INCOME
(UNAUDITED)

	Three Months Ended December 31,		Six Months Ended December 31,	
	2019	2018	2019	2018
(Amounts in thousands, except per share data)				
Net Sales	\$ 355,117	\$ 349,581	\$ 692,171	\$ 666,235
Cost of Sales	255,228	258,189	500,174	493,644
Gross Profit	99,889	91,392	191,997	172,591
Selling, General and Administrative Expenses	45,747	39,842	85,202	71,921
Change in Contingent Consideration	64	(9,605)	127	(9,605)
Restructuring and Impairment Charges	—	—	886	—
Operating Income	54,078	61,155	105,782	110,275
Other, Net	877	1,039	2,304	2,353
Income Before Income Taxes	54,955	62,194	108,086	112,628
Taxes Based on Income	11,531	14,287	23,917	25,693
Net Income	\$ 43,424	\$ 47,907	\$ 84,169	\$ 86,935
Net Income Per Common Share:				
Basic	\$ 1.58	\$ 1.74	\$ 3.06	\$ 3.16
Diluted	\$ 1.58	\$ 1.73	\$ 3.06	\$ 3.15
Weighted Average Common Shares Outstanding:				
Basic	27,443	27,435	27,443	27,429
Diluted	27,489	27,566	27,503	27,540

See accompanying notes to condensed consolidated financial statements.

LANCASTER COLONY CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(UNAUDITED)

(Amounts in thousands)	Three Months Ended December 31,		Six Months Ended December 31,	
	2019	2018	2019	2018
Net Income	\$ 43,424	\$ 47,907	\$ 84,169	\$ 86,935
Other Comprehensive Income:				
Defined Benefit Pension and Postretirement Benefit Plans:				
Amortization of loss, before tax	137	102	273	205
Amortization of prior service credit, before tax	(46)	(45)	(91)	(91)
Total Other Comprehensive Income, Before Tax	91	57	182	114
Tax Attributes of Items in Other Comprehensive Income:				
Amortization of loss, tax	(33)	(24)	(64)	(48)
Amortization of prior service credit, tax	11	10	21	21
Total Tax Expense	(22)	(14)	(43)	(27)
Other Comprehensive Income, Net of Tax	69	43	139	87
Comprehensive Income	\$ 43,493	\$ 47,950	\$ 84,308	\$ 87,022

See accompanying notes to condensed consolidated financial statements.

LANCASTER COLONY CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(UNAUDITED)

(Amounts in thousands)	Six Months Ended December 31,	
	2019	2018
Cash Flows From Operating Activities:		
Net income	\$ 84,169	\$ 86,935
Adjustments to reconcile net income to net cash provided by operating activities:		
Impacts of noncash items:		
Depreciation and amortization	17,911	14,458
Change in contingent consideration	127	(9,605)
Deferred income taxes and other changes	2,834	2,885
Stock-based compensation expense	2,859	3,362
Restructuring and impairment charges	(268)	—
Pension plan activity	(336)	(455)
Changes in operating assets and liabilities:		
Receivables	(1,371)	2,985
Inventories	(4,411)	27
Other current assets	(1,970)	2,291
Accounts payable and accrued liabilities	5,835	10,332
Net cash provided by operating activities	105,379	113,215
Cash Flows From Investing Activities:		
Payments for property additions	(57,700)	(27,938)
Cash paid for acquisitions, net of cash acquired	—	(58,191)
Other-net	(222)	(324)
Net cash used in investing activities	(57,922)	(86,453)
Cash Flows From Financing Activities:		
Payment of dividends	(37,114)	(34,370)
Purchase of treasury stock	(1,472)	(1,759)
Tax withholdings for stock-based compensation	(2,696)	(1,766)
Other-net	(237)	(88)
Net cash used in financing activities	(41,519)	(37,983)
Net change in cash and equivalents	5,938	(11,221)
Cash and equivalents at beginning of year	196,288	205,752
Cash and equivalents at end of period	\$ 202,226	\$ 194,531
Supplemental Disclosure of Operating Cash Flows:		
Net cash payments for income taxes	\$ 18,783	\$ 19,987

See accompanying notes to condensed consolidated financial statements.

LANCASTER COLONY CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY
(UNAUDITED)

	Six Months Ended December 31, 2019					
	Common Stock Outstanding		Retained Earnings	Accumulated Other Comprehensive Loss	Treasury Stock	Total Shareholders' Equity
	Shares	Amount				
(Amounts in thousands, except per share data)						
Balance, June 30, 2019	27,491	\$ 122,844	\$ 1,359,782	\$ (10,308)	\$ (745,445)	\$ 726,873
Net income			40,745			40,745
Net pension and postretirement benefit gains, net of \$21 tax effect				70		70
Cash dividends - common stock (\$0.65 per share)			(17,869)			(17,869)
Purchase of treasury stock	(10)				(1,465)	(1,465)
Stock-based plans	4	(125)				(125)
Stock-based compensation expense		1,436				1,436
Balance, September 30, 2019	27,485	\$ 124,155	\$ 1,382,658	\$ (10,238)	\$ (746,910)	\$ 749,665
Net income			43,424			43,424
Net pension and postretirement benefit gains, net of \$22 tax effect				69		69
Cash dividends - common stock (\$0.70 per share)			(19,245)			(19,245)
Purchase of treasury stock	—				(7)	(7)
Stock-based plans	26	(2,571)				(2,571)
Stock-based compensation expense		1,423				1,423
Balance, December 31, 2019	27,511	\$ 123,007	\$ 1,406,837	\$ (10,169)	\$ (746,917)	\$ 772,758

See accompanying notes to condensed consolidated financial statements.

LANCASTER COLONY CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY (continued)
(UNAUDITED)

	Six Months Ended December 31, 2018					
	Common Stock Outstanding		Retained Earnings	Accumulated Other Comprehensive Loss	Treasury Stock	Total Shareholders' Equity
	Shares	Amount				
(Amounts in thousands, except per share data)						
Balance, June 30, 2018	27,488	\$ 119,232	\$ 1,279,343	\$ (8,259)	\$ (738,034)	\$ 652,282
Net income			39,028			39,028
Net pension and postretirement benefit gains, net of \$13 tax effect				44		44
Cash dividends - common stock (\$0.60 per share)			(16,495)			(16,495)
Purchase of treasury stock	(10)				(1,593)	(1,593)
Stock-based plans	12	(778)				(778)
Stock-based compensation expense		1,531				1,531
Balance, September 30, 2018	27,490	\$ 119,985	\$ 1,301,876	\$ (8,215)	\$ (739,627)	\$ 674,019
Net income			47,907			47,907
Net pension and postretirement benefit gains, net of \$14 tax effect				43		43
Cash dividends - common stock (\$0.65 per share)			(17,875)			(17,875)
Purchase of treasury stock	(1)				(166)	(166)
Stock-based plans	16	(988)				(988)
Stock-based compensation expense		1,831				1,831
Balance, December 31, 2018	27,505	\$ 120,828	\$ 1,331,908	\$ (8,172)	\$ (739,793)	\$ 704,771

See accompanying notes to condensed consolidated financial statements.

LANCASTER COLONY CORPORATION AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Tabular amounts in thousands, except per share data)

Note 1 – Summary of Significant Accounting Policies

Basis of Presentation

The accompanying unaudited condensed consolidated financial statements include the accounts of Lancaster Colony Corporation and our wholly-owned subsidiaries, collectively referred to as “we,” “us,” “our,” “registrant” or the “Company” and have been prepared in accordance with U.S. generally accepted accounting principles (“GAAP”) for interim financial information and SEC Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements. In our opinion, the interim condensed consolidated financial statements reflect all adjustments necessary for a fair presentation of the results of operations and financial position for such periods. All such adjustments reflected in the interim condensed consolidated financial statements are considered to be of a normal recurring nature. Intercompany transactions and accounts have been eliminated in consolidation. The results of operations for any interim period are not necessarily indicative of results for the full year. Accordingly, these condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto contained in our 2019 Annual Report on Form 10-K. Unless otherwise noted, the term “year” and references to a particular year pertain to our fiscal year, which begins on July 1 and ends on June 30; for example, 2020 refers to fiscal 2020, which is the period from July 1, 2019 to June 30, 2020.

Property, Plant and Equipment

Property, plant and equipment are recorded at cost, except for those acquired as part of a business combination, which are recorded at fair value at the time of purchase. We use the straight-line method of computing depreciation for financial reporting purposes based on the estimated useful lives of the corresponding assets. Purchases of property, plant and equipment included in Accounts Payable and excluded from the property additions and the change in accounts payable in the Condensed Consolidated Statements of Cash Flows were as follows:

	December 31,	
	2019	2018
Construction in progress in Accounts Payable	\$ 8,810	\$ 2,376

Earnings Per Share

Earnings per share (“EPS”) is computed based on the weighted average number of shares of common stock and common stock equivalents (restricted stock and stock-settled stock appreciation rights) outstanding during each period. Unvested shares of restricted stock granted to employees are considered participating securities since employees receive nonforfeitable dividends prior to vesting and, therefore, are included in the earnings allocation in computing EPS under the two-class method. Basic EPS excludes dilution and is computed by dividing income available to common shareholders by the weighted average number of common shares outstanding during the period. Diluted EPS is computed by dividing income available to common shareholders by the diluted weighted average number of common shares outstanding during the period, which includes the dilutive potential common shares associated with nonparticipating restricted stock and stock-settled stock appreciation rights.

LANCASTER COLONY CORPORATION AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Tabular amounts in thousands, except per share data)

Basic and diluted net income per common share were calculated as follows:

	Three Months Ended December 31,		Six Months Ended December 31,	
	2019	2018	2019	2018
Net income	\$ 43,424	\$ 47,907	\$ 84,169	\$ 86,935
Net income available to participating securities	(68)	(96)	(133)	(176)
Net income available to common shareholders	<u>\$ 43,356</u>	<u>\$ 47,811</u>	<u>\$ 84,036</u>	<u>\$ 86,759</u>
Weighted average common shares outstanding – basic	27,443	27,435	27,443	27,429
Incremental share effect from:				
Nonparticipating restricted stock	2	2	2	4
Stock-settled stock appreciation rights	44	129	58	107
Weighted average common shares outstanding – diluted	<u>27,489</u>	<u>27,566</u>	<u>27,503</u>	<u>27,540</u>
Net income per common share – basic	\$ 1.58	\$ 1.74	\$ 3.06	\$ 3.16
Net income per common share – diluted	\$ 1.58	\$ 1.73	\$ 3.06	\$ 3.15

Accumulated Other Comprehensive Loss

The following table presents the amounts reclassified out of accumulated other comprehensive loss by component:

	Three Months Ended December 31,		Six Months Ended December 31,	
	2019	2018	2019	2018
Accumulated other comprehensive loss at beginning of period	\$ (10,238)	\$ (8,215)	\$ (10,308)	\$ (8,259)
Defined Benefit Pension Plan Items:				
Amortization of unrecognized net loss	143	112	286	224
Postretirement Benefit Plan Items:				
Amortization of unrecognized net gain	(6)	(10)	(13)	(19)
Amortization of prior service credit	(46)	(45)	(91)	(91)
Total other comprehensive income, before tax	91	57	182	114
Total tax expense	(22)	(14)	(43)	(27)
Other comprehensive income, net of tax	69	43	139	87
Accumulated other comprehensive loss at end of period	<u>\$ (10,169)</u>	<u>\$ (8,172)</u>	<u>\$ (10,169)</u>	<u>\$ (8,172)</u>

Significant Accounting Policies

There were no changes to our Significant Accounting Policies from those disclosed in our 2019 Annual Report on Form 10-K. However, see expanded disclosure of lease accounting policies in Note 5 due to the adoption of new lease accounting guidance.

Recently Issued Accounting Standards

In August 2018, the Financial Accounting Standards Board (“FASB”) issued new accounting guidance related to the disclosure requirements for fair value measurements. The guidance removes, modifies and adds disclosures related to fair value. The amendments on changes in unrealized gains and losses, the range and weighted average of significant unobservable inputs used to develop Level 3 fair value measurements, and the narrative description of measurement uncertainty should be applied prospectively for only the most recent interim or annual period presented in the initial fiscal year of adoption. All other amendments should be applied retrospectively to all periods presented upon their effective date. This guidance will be effective for us in fiscal 2021, including interim periods. As the guidance only relates to disclosures, there will be no impact on our financial position or results of operations.

LANCASTER COLONY CORPORATION AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Tabular amounts in thousands, except per share data)

Recently Adopted Accounting Standards

In February 2016, the FASB issued new accounting guidance to require lessees to recognize a right-of-use asset and a lease liability for leases with terms of more than 12 months and issued subsequent clarifications of this new guidance. This guidance retains the two classifications of a lease as either an operating or finance lease (previously referred to as a capital lease). Both lease classifications require the lessee to record a right-of-use asset and a lease liability based upon the present value of the lease payments. Finance leases will reflect the financial arrangement by recognizing interest expense on the lease liability separately from the amortization expense of the right-of-use asset. Operating leases will recognize lease expense (with no separate recognition of interest expense) on a straight-line basis over the term of the lease. The guidance requires expanded qualitative and quantitative disclosures, including additional information about the amounts recorded in the consolidated financial statements. In July 2018, the FASB issued guidance that allows for an alternate transition method whereby companies can recognize a cumulative-effect adjustment to the opening balance of retained earnings in the period of adoption rather than restating comparative periods. We adopted the new guidance on July 1, 2019 using this alternate transition method, but we did not record a cumulative-effect adjustment from initially applying the standard. We elected the package of practical expedients that permits us not to reassess our prior conclusions about lease identification, lease classification and initial direct costs and made an accounting policy election to exclude short-term leases with an initial term of 12 months or less from our Consolidated Balance Sheets. We have completed the implementation of a lease accounting system to enable the preparation of financial information and have implemented relevant accounting policies and internal controls surrounding the lease accounting process. As a result of adoption, we recognized a lease liability and right-of-use asset of \$33.5 million and \$31.7 million, respectively. The right-of-use asset balance reflects the reclassification of deferred rent and prepaid rent against the initial asset. The adoption did not impact our results of operations or cash flows. See additional lease disclosures in Note 5.

Note 2 – Acquisitions

Omni Baking Company LLC

On November 16, 2018, we acquired substantially all of the assets of Omni Baking Company LLC (“Omni”). Omni has been a long-time supplier of products to our frozen garlic bread operations and is based in Vineland, New Jersey. The purchase price of \$22.3 million, which includes the post-closing working capital adjustment, was funded with cash on hand. Omni’s results of operations are allocated between our Retail and Foodservice segments in a manner consistent with our current segment allocations. These results have been included in our condensed consolidated financial statements from the date of acquisition.

Bantam Bagels, LLC

On October 19, 2018, we acquired all the assets of Bantam Bagels, LLC (“Bantam”). Bantam, a producer and marketer of frozen mini stuffed bagels and other frozen bread products sold to both the retail and foodservice channels, is based in New York, New York. The base purchase price of \$33.1 million, which includes the post-closing working capital adjustment, was funded with cash on hand. This purchase price excludes contingent consideration relating to an additional earn-out payment which is tied to performance-based conditions. In general, the terms of the acquisition specify that the sellers will receive an earn-out based upon a pre-determined multiple of the defined adjusted EBITDA of Bantam for the twelve months ending December 31, 2023. We are unable to provide a range for the amount of this earn-out because it is based on the future adjusted EBITDA of Bantam, and the earn-out does not contain a minimum or maximum value. See further discussion of the earn-out in Note 3. Bantam’s results of operations are allocated between our Retail and Foodservice segments in a manner consistent with our current segment allocations. These results have been included in our condensed consolidated financial statements from the date of acquisition.

Note 3 – Fair Value

Fair value is defined as the exit price, or the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants as of the measurement date. GAAP sets forth a three-level fair value hierarchy, which prioritizes the inputs used in measuring fair value. The three levels are as follows:

Level 1 – defined as observable inputs, such as quoted market prices in active markets.

Level 2 – defined as inputs other than quoted prices in active markets that are either directly or indirectly observable.

Level 3 – defined as unobservable inputs in which little or no market data exists, therefore, requiring an entity to develop its own assumptions.

LANCASTER COLONY CORPORATION AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Tabular amounts in thousands, except per share data)

Our financial assets and liabilities subject to the three-level fair value hierarchy consist principally of cash and equivalents, accounts receivable, accounts payable, contingent consideration payable and defined benefit pension plan assets. The estimated fair value of cash and equivalents, accounts receivable and accounts payable approximates their carrying value.

Our contingent consideration, which resulted from the earn-outs associated with our acquisitions of Bantam and Angelic Bakehouse, Inc. (“Angelic”), is measured at fair value on a recurring basis and is included in Other Noncurrent Liabilities on the Condensed Consolidated Balance Sheets. The following table summarizes our contingent consideration:

Fair Value Measurements at December 31, 2019				
	Level 1	Level 2	Level 3	Total
Contingent consideration - Bantam	\$ —	\$ —	\$ 9,027	\$ 9,027
Contingent consideration - Angelic	—	—	—	—
Total contingent consideration	\$ —	\$ —	\$ 9,027	\$ 9,027

Fair Value Measurements at June 30, 2019				
	Level 1	Level 2	Level 3	Total
Contingent consideration - Bantam	\$ —	\$ —	\$ 8,900	\$ 8,900
Contingent consideration - Angelic	—	—	—	—
Total contingent consideration	\$ —	\$ —	\$ 8,900	\$ 8,900

Bantam Contingent Consideration

This contingent consideration resulted from the earn-out associated with our October 19, 2018 acquisition of Bantam. In general, the terms of the acquisition specify the sellers will receive an earn-out based upon a pre-determined multiple of the defined adjusted EBITDA of Bantam for the twelve months ending December 31, 2023. The initial fair value of the contingent consideration was determined to be \$8.0 million, which included a refinement to the purchase price allocation in the prior-year third quarter related to a change in assumptions. The fair value is measured on a recurring basis using a Monte Carlo simulation that randomly changes revenue growth, forecasted adjusted EBITDA and other uncertain variables to estimate an expected value. We record the present value of this amount by applying a discount rate. As this fair value measurement is based on significant inputs not observable in the market, it represents a Level 3 measurement within the fair value hierarchy.

The following table represents our Level 3 fair value measurements using significant other unobservable inputs for Bantam’s contingent consideration:

	Three Months Ended December 31,		Six Months Ended December 31,	
	2019	2018	2019	2018
Contingent consideration at beginning of period	\$ 8,963	\$ —	\$ 8,900	\$ —
Initial fair value - additions	—	8,900	—	8,900
Change in contingent consideration included in operating income	64	95	127	95
Contingent consideration at end of period	\$ 9,027	\$ 8,995	\$ 9,027	\$ 8,995

Angelic Contingent Consideration

This contingent consideration resulted from the earn-out associated with our November 17, 2016 acquisition of Angelic. In general, the terms of the acquisition specify the sellers will receive an earn-out based upon a pre-determined multiple of the defined adjusted EBITDA of Angelic for fiscal 2021. The initial fair value of the contingent consideration was determined to be \$13.9 million. The fair value is measured on a recurring basis using a present value approach, which incorporates factors such as revenue growth and forecasted adjusted EBITDA, to estimate an expected value. We record the present value of this amount by applying a discount rate. As this fair value measurement is based on significant inputs not observable in the market, it represents a Level 3 measurement within the fair value hierarchy. Our 2019 fair value measurements resulted in a \$9.7 million reduction in the fair value of Angelic’s contingent consideration in the second quarter ended December 31, 2018 and a \$7.4 million reduction in the fourth quarter ended June 30, 2019 based on changes in Angelic’s forecasted adjusted EBITDA for fiscal 2021. These adjustments were recorded in our Retail segment.

LANCASTER COLONY CORPORATION AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Tabular amounts in thousands, except per share data)

The following table represents our Level 3 fair value measurements using significant other unobservable inputs for Angelic's contingent consideration:

	Three Months Ended December 31,		Six Months Ended December 31,	
	2019	2018	2019	2018
Contingent consideration at beginning of period	\$ —	\$ 17,080	\$ —	\$ 17,080
Change in contingent consideration included in operating income	—	(9,700)	—	(9,700)
Contingent consideration at end of period	\$ —	\$ 7,380	\$ —	\$ 7,380

Note 4 – Long-Term Debt

At December 31, 2019 and June 30, 2019, we had an unsecured credit facility ("Facility") under which we could borrow, on a revolving credit basis, up to a maximum of \$150 million at any one time, with potential to expand the total credit availability to \$225 million subject to us obtaining consent of the issuing banks and certain other conditions. The Facility expires on April 8, 2021, and all outstanding amounts are then due and payable. Interest is variable based upon formulas tied to LIBOR or an alternative base rate defined in the Facility, at our option. We must also pay facility fees that are tied to our then-applicable consolidated leverage ratio. Loans may be used for general corporate purposes. Due to the nature of its terms, when we have outstanding borrowings under the Facility, they will be classified as long-term debt.

At December 31, 2019 and June 30, 2019, we had no borrowings outstanding under the Facility. At December 31, 2019 and June 30, 2019, we had \$5.1 million of standby letters of credit outstanding, which reduced the amount available for borrowing on the Facility. We paid no interest for the three and six months ended December 31, 2019 and 2018.

The Facility contains certain restrictive covenants, including limitations on indebtedness, asset sales and acquisitions. There are two principal financial covenants: an interest expense test that requires us to maintain an interest coverage ratio not less than 2.5 to 1 at the end of each fiscal quarter; and an indebtedness test that requires us to maintain a consolidated leverage ratio not greater than 3 to 1 at all times. The interest coverage ratio is calculated by dividing Consolidated EBIT by Consolidated Interest Expense, and the leverage ratio is calculated by dividing Consolidated Debt by Consolidated EBITDA. All financial terms used in the covenant calculations are defined more specifically in the Facility.

Note 5 – Leases

General Lease Description

We have operating leases with initial noncancelable lease terms in excess of one year covering the rental of various facilities and equipment. Certain of these leases contain renewal options and some provide options to purchase during the lease term. Our operating leases include leases for real estate for some of our office and manufacturing facilities as well as manufacturing and non-manufacturing equipment used in our business. The remaining lease terms for these operating leases range from 1 year to 9 years.

We have finance leases with initial noncancelable lease terms in excess of one year covering the rental of various equipment. These leases are generally for manufacturing and non-manufacturing equipment used in our business. The remaining lease terms for these finance leases range from 3 years to 4 years.

Significant Assumptions and Judgments

Contract Contains a Lease

In evaluating our contracts to determine whether a contract is or contains a lease, we considered the following:

- Whether explicitly or implicitly identified assets have been deployed in the contract; and
- Whether we obtain substantially all of the economic benefits from the use of that underlying asset, and we can direct how and for what purpose the asset is used during the term of the contract.

Allocation of Consideration

In determining how to allocate consideration between lease and non-lease components in a contract that was deemed to contain a lease, we used judgment and consistent application of assumptions to reasonably allocate the consideration.

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Options to Extend or Terminate Leases

We have leases which contain options to extend or terminate the leases. On a lease-by-lease basis, we have determined if the extension should be considered reasonably certain to be exercised and thus a right-of-use asset and a lease liability should be recorded.

Discount Rate

The discount rate for leases, if not explicitly stated in the lease, is the incremental borrowing rate, which is the rate of interest that a lessee would have to pay to borrow on a collateralized basis over a similar term an amount equal to the lease payments in a similar economic environment.

We used a discount rate to calculate the present value of the lease liability at the date of adoption. In the development of the discount rate, we considered our internal borrowing rate, treasury security rates, collateral and credit risk specific to us, and our lease portfolio characteristics.

As of December 31, 2019, the weighted-average discount rate of our operating and finance leases was 3.1% and 4.1%, respectively.

Practical Expedients and Accounting Policy Elections

We elected the package of practical expedients that permits us not to reassess our prior conclusions about lease identification, lease classification and initial direct costs and made an accounting policy election to exclude short-term leases with an initial term of 12 months or less from our Consolidated Balance Sheets.

Amounts Recognized in the Financial Statements

The components of lease expense were as follows:

	Three Months Ended December 31, 2019	Six Months Ended December 31, 2019
Operating lease cost in Cost of Sales and Selling, General and Administrative Expenses	\$ 2,005	\$ 4,141
Finance lease cost:		
Amortization of assets in Cost of Sales	\$ 84	\$ 168
Interest on lease liabilities in Other, Net	19	39
Total finance lease cost	\$ 103	\$ 207
Short-term lease cost in Cost of Sales and Selling, General and Administrative Expenses	752	1,424
Total net lease cost	\$ 2,860	\$ 5,772

Supplemental balance sheet information related to leases is as follows:

	December 31, 2019
Operating Leases	
Operating Lease Right-Of-Use Assets	\$ 24,617
Current operating lease liabilities in Accrued Liabilities	\$ 6,693
Noncurrent Operating Lease Liabilities	19,704
Total operating lease liabilities	\$ 26,397
Finance Leases	
Finance lease right-of-use assets in Property, Plant and Equipment-Net	\$ 1,882
Current finance lease liabilities in Accrued Liabilities	\$ 441
Noncurrent finance lease liabilities in Other Noncurrent Liabilities	1,297
Total finance lease liabilities	\$ 1,738

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Supplemental cash flow information related to leases is as follows:

	Six Months Ended December 31, 2019
Cash paid for amounts included in the measurement of lease liabilities:	
Operating cash flows from operating leases	\$ 4,282
Operating cash flows from finance leases	\$ 39
Financing cash flows from finance leases	\$ 213
Supplemental noncash information on lease liabilities arising from obtaining right-of-use assets	\$ 2,882
Supplemental noncash information on lease liabilities removed due to purchase of leased asset	\$ 5,765

As of December 31, 2019, the maturities of lease liabilities were as follows:

	Operating Leases	Finance Leases
Six months ending June 30, 2020	\$ 4,079	\$ 253
2021	6,308	505
2022	5,451	505
2023	4,247	493
2024	3,761	121
Thereafter	4,694	—
Total minimum payments	\$ 28,540	\$ 1,877
Less amount representing interest	(2,143)	(139)
Present value of lease obligations	\$ 26,397	\$ 1,738

As of December 31, 2019, the weighted-average remaining term of our operating and finance leases was 5.1 years and 3.7 years, respectively.

As previously disclosed in our 2019 Annual Report on Form 10-K and under the previous lease accounting standard (Topic 840), as of June 30, 2019, future minimum lease payments under noncancelable leases with initial lease terms in excess of one year were as follows:

	Operating Leases	Capital Leases
2020	\$ 8,261	\$ 505
2021	7,136	505
2022	6,345	505
2023	4,992	493
2024	4,619	121
Thereafter	6,901	—
Total minimum payments	\$ 38,254	\$ 2,129
Less amount representing interest		(178)
Present value of capital lease obligations		\$ 1,951

Note 6 – Contingencies

At December 31, 2019, we were a party to various claims and litigation matters arising in the ordinary course of business. Such matters did not have a material effect on the current-year results of operations and, in our opinion, their ultimate disposition will not have a material effect on our consolidated financial statements.

Our acquisitions of Angelic and Bantam included provisions for contingent consideration for the earn-outs associated with these transactions. See further discussion in Note 3.

Note 7 – Goodwill and Other Intangible Assets

Goodwill attributable to the Retail and Foodservice segments was \$157.4 million and \$51.0 million, respectively, at December 31, 2019 and June 30, 2019.

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The following table summarizes our identifiable other intangible assets:

	December 31, 2019	June 30, 2019
Tradenames (20 to 30-year life)		
Gross carrying value	\$ 63,121	\$ 63,121
Accumulated amortization	(8,630)	(7,335)
Net carrying value	\$ 54,491	\$ 55,786
Customer Relationships (10 to 15-year life)		
Gross carrying value	\$ 17,507	\$ 17,507
Accumulated amortization	(10,367)	(9,641)
Net carrying value	\$ 7,140	\$ 7,866
Technology / Know-how (10-year life)		
Gross carrying value	\$ 8,950	\$ 8,950
Accumulated amortization	(2,949)	(2,501)
Net carrying value	\$ 6,001	\$ 6,449
Non-compete Agreements (5-year life)		
Gross carrying value	\$ 791	\$ 791
Accumulated amortization	(694)	(615)
Net carrying value	\$ 97	\$ 176
Total net carrying value	\$ 67,729	\$ 70,277

Amortization expense for our other intangible assets, which is reflected in Selling, General and Administrative Expenses, was as follows:

	Three Months Ended December 31,		Six Months Ended December 31,	
	2019	2018	2019	2018
Amortization expense	\$ 1,274	\$ 1,087	\$ 2,548	\$ 2,052

Total annual amortization expense for each of the next five years is estimated to be as follows:

2021	\$ 4,976
2022	\$ 4,902
2023	\$ 4,343
2024	\$ 4,343
2025	\$ 4,083

Note 8 – Income Taxes

Prepaid federal income taxes of \$1.7 million and \$5.2 million were included in Other Current Assets at December 31, 2019 and June 30, 2019, respectively. Prepaid state and local income taxes of \$0.4 million and \$0.1 million were included in Other Current Assets at December 31, 2019 and June 30, 2019, respectively.

Note 9 – Business Segment Information

Our financial results are presented as two reportable segments: Retail and Foodservice. Costs that are directly attributable to either Retail or Foodservice are charged directly to the appropriate segment. Costs that are deemed to be indirect, excluding corporate expenses and other unusual significant transactions, are allocated to the two reportable segments using a reasonable methodology that is consistently applied.

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Retail - The vast majority of the products we sell in the Retail segment are sold through sales personnel, food brokers and distributors in the United States. We have placement of products in grocery produce departments through our refrigerated salad dressings, vegetable dips and fruit dips. Our flatbread products and sprouted grain bakery products are generally placed in the specialty bakery/deli section of the grocery store. We also have products typically marketed in the shelf-stable section of the grocery store, which include salad dressing, slaw dressing and croutons. Within the frozen food section of the grocery store, we sell yeast rolls, garlic breads and mini stuffed bagels.

Foodservice - The vast majority of the products we sell in the Foodservice segment are sold through sales personnel, food brokers and distributors in the United States. Most of the products we sell in the Foodservice segment are custom-formulated and include salad dressings, sandwich and dipping sauces, frozen breads and yeast rolls. The majority of our Foodservice sales are products sold under private label to restaurants. We also manufacture and sell various branded Foodservice products to distributors. Finally, within this segment, we sell other roll products under a transitional co-packing arrangement resulting from the Omni acquisition.

As many of our products are similar between our two segments, our procurement, manufacturing, warehousing and distribution activities are substantially integrated across our operations in order to maximize efficiency and productivity. Consequently, we do not prepare, and our Chief Operating Decision Maker does not review, separate balance sheets for the reportable segments. As such, our external reporting does not include the presentation of identifiable assets by reportable segment. The composition of our identifiable assets at December 31, 2019 is generally consistent with that of June 30, 2019.

We evaluate our Retail and Foodservice segments based on net sales and operating income which follow:

	Three Months Ended December 31,		Six Months Ended December 31,	
	2019	2018	2019	2018
Net Sales				
Retail	\$ 186,210	\$ 186,302	\$ 352,287	\$ 349,050
Foodservice	168,907	163,279	339,884	317,185
Total	<u>\$ 355,117</u>	<u>\$ 349,581</u>	<u>\$ 692,171</u>	<u>\$ 666,235</u>
Operating Income				
Retail	\$ 39,017	\$ 44,785	\$ 74,452	\$ 78,733
Foodservice	23,416	19,405	47,205	38,266
Restructuring and Impairment Charges	—	—	(886)	—
Corporate Expenses	(8,355)	(3,035)	(14,989)	(6,724)
Total	<u>\$ 54,078</u>	<u>\$ 61,155</u>	<u>\$ 105,782</u>	<u>\$ 110,275</u>

The following table sets forth net sales disaggregated by class of similar products for the Retail and Foodservice segments:

	Three Months Ended December 31,		Six Months Ended December 31,	
	2019	2018	2019	2018
Retail				
Frozen breads	\$ 92,105	\$ 89,902	\$ 152,402	\$ 147,410
Refrigerated dressings, dips and other	51,405	55,204	114,042	117,073
Shelf-stable dressings and croutons	42,700	41,196	85,843	84,567
Total Retail net sales	<u>\$ 186,210</u>	<u>\$ 186,302</u>	<u>\$ 352,287</u>	<u>\$ 349,050</u>
Foodservice				
Dressings and sauces	\$ 114,970	\$ 115,925	\$ 234,733	\$ 231,837
Frozen breads and other	47,597	43,518	90,961	81,512
Other roll products	6,340	3,836	14,190	3,836
Total Foodservice net sales	<u>\$ 168,907</u>	<u>\$ 163,279</u>	<u>\$ 339,884</u>	<u>\$ 317,185</u>
Total net sales	<u>\$ 355,117</u>	<u>\$ 349,581</u>	<u>\$ 692,171</u>	<u>\$ 666,235</u>

LANCASTER COLONY CORPORATION AND SUBSIDIARIES
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The following table provides an additional disaggregation of Foodservice net sales by type of customer:

	Three Months Ended December 31,		Six Months Ended December 31,	
	2019	2018	2019	2018
Foodservice				
National accounts	\$ 122,050	\$ 120,652	\$ 245,808	\$ 236,227
Branded and other	40,517	38,791	79,886	77,122
Other roll products	6,340	3,836	14,190	3,836
Total Foodservice net sales	<u>\$ 168,907</u>	<u>\$ 163,279</u>	<u>\$ 339,884</u>	<u>\$ 317,185</u>

Note 10 – Stock-Based Compensation

There have been no changes to our stock-based compensation plans from those disclosed in our 2019 Annual Report on Form 10-K.

Our stock-settled stock appreciation rights (“SSSARs”) compensation expense was \$0.8 million and \$0.9 million for the three months ended December 31, 2019 and 2018, respectively. Year-to-date SSSARs compensation expense was \$1.5 million for the current-year period compared to \$1.6 million for the prior-year period. At December 31, 2019, there was \$3.7 million of unrecognized compensation expense related to SSSARs that we will recognize over a weighted-average period of 2 years.

Our restricted stock compensation expense was \$0.7 million and \$0.9 million for the three months ended December 31, 2019 and 2018, respectively. Year-to-date restricted stock compensation expense was \$1.4 million for the current-year period compared to \$1.7 million for the prior-year period. At December 31, 2019, there was \$3.3 million of unrecognized compensation expense related to restricted stock that we will recognize over a weighted-average period of 2 years.

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

Our fiscal year begins on July 1 and ends on June 30. Unless otherwise noted, references to "year" pertain to our fiscal year; for example, 2020 refers to fiscal 2020, which is the period from July 1, 2019 to June 30, 2020.

The following discussion should be read in conjunction with our condensed consolidated financial statements and the notes thereto, all included elsewhere in this report, and our 2019 Annual Report on Form 10-K. The forward-looking statements in this section and other parts of this report involve risks, uncertainties and other factors, including statements regarding our plans, objectives, goals, strategies, and financial performance. Our actual results could differ materially from the results anticipated in these forward-looking statements due to these factors. For more information, see the section below entitled "Forward-Looking Statements."

OVERVIEW

Business Overview

Lancaster Colony Corporation is a manufacturer and marketer of specialty food products for the retail and foodservice channels.

Our financial results are presented as two reportable segments: Retail and Foodservice. Costs that are directly attributable to either Retail or Foodservice are charged directly to the appropriate segment. Costs that are deemed to be indirect, excluding corporate expenses and other unusual significant transactions, are allocated to the two reportable segments using a reasonable methodology that is consistently applied.

Over 95% of our products are sold in the United States. Foreign operations and export sales have not been significant in the past and are not expected to be significant in the future based upon existing operations. We do not have any fixed assets located outside of the United States.

Our business has the potential to achieve future growth in sales and profitability due to attributes such as:

- leading Retail market positions in several product categories with a high-quality perception;
- recognized innovation in Retail products;
- a broad customer base in both Retail and Foodservice accounts;
- well-regarded culinary expertise among Foodservice customers;
- recognized leadership in Foodservice product development;
- experience in integrating complementary business acquisitions; and
- historically strong cash flow generation that supports growth opportunities.

Our goal is to grow both Retail and Foodservice segment sales over time by:

- introducing new products and expanding distribution;
- leveraging the strength of our Retail brands to increase current product sales;
- expanding Retail growth through strategic licensing agreements;
- continuing to rely upon the strength of our reputation in Foodservice product development and quality; and
- acquiring complementary businesses.

With respect to long-term growth, we continually evaluate the future opportunities and needs for our business specific to our plant infrastructure, IT platforms and other initiatives to support and strengthen our operations. Recent examples of resulting investments include a significant capacity expansion project for our Sister Schubert's frozen dinner roll facility in Horse Cave, Kentucky that was completed in January 2020; a new R&D center that was completed near the end of 2019; and the establishment of a Transformation Program Office in 2019 that will serve to coordinate our various capital and integration efforts, including our enterprise resource planning system ("ERP") that is now underway.

We also continue to review potential acquisitions that we believe will complement our existing product lines, enhance our profitability and/or offer good expansion opportunities in a manner that fits our overall strategic goals. Consistent with this acquisition strategy, on November 16, 2018, we acquired, using available cash on hand, substantially all of the assets of Omni Baking Company LLC ("Omni"), a long-time supplier of products to our frozen garlic bread operations. On October 19, 2018, we acquired, using available cash on hand, all the assets of Bantam Bagels, LLC ("Bantam"), a producer and marketer of frozen mini stuffed bagels and other frozen bread products sold to both the retail and foodservice channels. See further discussion of these acquisitions in Note 2 to the condensed consolidated financial statements.

RESULTS OF CONSOLIDATED OPERATIONS

(Dollars in thousands, except per share data)	Three Months Ended December 31,				Six Months Ended December 31,			
	2019	2018	Change		2019	2018	Change	
Net Sales	\$ 355,117	\$ 349,581	\$ 5,536	2 %	\$ 692,171	\$ 666,235	\$ 25,936	4 %
Cost of Sales	255,228	258,189	(2,961)	(1)%	500,174	493,644	6,530	1 %
Gross Profit	99,889	91,392	8,497	9 %	191,997	172,591	19,406	11 %
Gross Margin	28.1%	26.1%			27.7%	25.9%		
Selling, General and Administrative Expenses	45,747	39,842	5,905	15 %	85,202	71,921	13,281	18 %
Change in Contingent Consideration	64	(9,605)	9,669	(101)%	127	(9,605)	9,732	(101)%
Restructuring and Impairment Charges	—	—	—	N/M	886	—	886	N/M
Operating Income	54,078	61,155	(7,077)	(12)%	105,782	110,275	(4,493)	(4)%
Operating Margin	15.2%	17.5%			15.3%	16.6%		
Other, Net	877	1,039	(162)	(16)%	2,304	2,353	(49)	(2)%
Income Before Income Taxes	54,955	62,194	(7,239)	(12)%	108,086	112,628	(4,542)	(4)%
Taxes Based on Income	11,531	14,287	(2,756)	(19)%	23,917	25,693	(1,776)	(7)%
Effective Tax Rate	21.0%	23.0%			22.1%	22.8%		
Net Income	\$ 43,424	\$ 47,907	\$ (4,483)	(9)%	\$ 84,169	\$ 86,935	\$ (2,766)	(3)%
Diluted Net Income Per Common Share	\$ 1.58	\$ 1.73	\$ (0.15)	(9)%	\$ 3.06	\$ 3.15	\$ (0.09)	(3)%

Net Sales

Consolidated net sales for the three months ended December 31, 2019 increased 2% to a second quarter record \$355.1 million versus \$349.6 million last year. This growth was driven by an increase in Foodservice net sales. Consolidated net sales for the six months ended December 31, 2019 increased 4% due to higher sales for both segments. See discussion of net sales by segment following the discussion of “Earnings Per Share” below.

Gross Profit

Consolidated gross profit for the three months ended December 31, 2019 increased \$8.5 million, or 9%, to \$99.9 million compared to the prior-year period. The increase was driven by our cost savings programs, lower commodity costs, improved net price realization and a more favorable sales mix within the Foodservice segment.

Consolidated gross profit for the six months ended December 31, 2019 increased \$19.4 million, or 11%, to \$192.0 million compared to the prior-year period. The increase was driven by the higher sales volumes, our cost savings programs, lower commodity costs and improved net price realization.

Selling, General and Administrative Expenses

Selling, general and administrative (“SG&A”) expenses increased 15% for the three months ended December 31, 2019 and increased 18% for the year-to-date period. These increases were primarily driven by ERP expenses. The year-to-date period was also impacted by increased investments in consumer promotions and incremental expenses attributed to Bantam. ERP expenses are included within Corporate Expenses.

(Dollars in thousands)	Three Months Ended December 31,				Six Months Ended December 31,			
	2019	2018	Change		2019	2018	Change	
SG&A Expenses - Excluding ERP	\$ 40,854	\$ 39,842	\$ 1,012	3%	\$ 77,587	\$ 71,921	\$ 5,666	8%
ERP Expenses	4,893	—	4,893	N/M	7,615	—	7,615	N/M
Total SG&A Expenses	\$ 45,747	\$ 39,842	\$ 5,905	15%	\$ 85,202	\$ 71,921	\$ 13,281	18%

Change in Contingent Consideration

The change in contingent consideration resulted in expense of less than \$0.1 million and \$0.1 million for the three and six months ended December 31, 2019, respectively, compared to a net benefit of \$9.6 million for the three and six months ended December 31, 2018. The prior-year amount reflected a \$9.7 million benefit due to a reduction in the fair value of the contingent consideration liability for Angelic Bakehouse, Inc. (“Angelic”) as a result of our December 31, 2018 fair value measurement. See further discussion in Note 3 to the condensed consolidated financial statements.

Restructuring and Impairment Charges

In the fourth quarter of 2019, we committed to a plan to close our frozen bread manufacturing plant located in Saraland, Alabama. This decision was intended to provide greater production efficiency by consolidating most of this facility’s operations into other existing plants, outsourcing certain requirements and discontinuing less profitable frozen bread products. Production at the plant ceased in July 2019. The operations of this plant have not been classified as discontinued operations as the closure did not represent a strategic shift that would have a major effect on our operations or financial results.

We recorded restructuring and impairment charges of \$0.9 million for the six months ended December 31, 2019, which primarily consisted of plant clean-up expenses and contract termination costs. These charges were not allocated to our two reportable segments due to their unusual nature. All of these charges were recorded in the three months ended September 30, 2019, and we do not expect any additional charges attributed to this plant closure.

Operating Income

Operating income decreased 12% and 4% for the three and six months ended December 31, 2019, respectively, as the benefit from the gross profit growth was more than offset by the prior-year benefit from the reduction in the fair value of Angelic’s contingent consideration as well as the increase in SG&A expenses primarily related to the ERP. The year-to-date period was also unfavorably impacted by the restructuring and impairment charges. See discussion of operating results by segment following the discussion of “Earnings Per Share” below.

Taxes Based on Income

Our effective tax rate was 22.1% and 22.8% for the six months ended December 31, 2019 and 2018, respectively. For the six months ended December 31, 2019 and 2018, our effective tax rate varied from the statutory federal income tax rate as a result of the following factors:

	Six Months Ended December 31,	
	2019	2018
Statutory rate	21.0 %	21.0 %
State and local income taxes	2.7	2.7
Net windfall tax benefits - stock-based compensation	(1.0)	(0.9)
Other	(0.6)	—
Effective rate	22.1 %	22.8 %

We include the tax consequences related to stock-based compensation within the computation of income tax expense. We may experience increased volatility to our income tax expense and resulting net income dependent upon, among other variables, the price of our common stock and the timing and volume of share-based payment award activity such as employee exercises of stock-settled stock appreciation rights and vesting of restricted stock awards. For the six months ended December 31, 2019 and 2018, the impact of net windfall tax benefits from stock-based compensation reduced our effective tax rate by 1.0% and 0.9%, respectively.

Earnings Per Share

As influenced by the factors noted above, diluted net income per share for the second quarter of 2020 totaled \$1.58, as compared to \$1.73 per diluted share in the prior year. Year-to-date net income per share was \$3.06 per diluted share, as compared to \$3.15 per diluted share for the prior-year period. Diluted weighted average common shares outstanding have remained relatively stable for the current and prior-year periods ended December 31.

In 2020, spend for the ERP reduced diluted earnings per share by \$0.14 and \$0.21 for the second quarter and year-to-date periods, respectively. The restructuring and impairment charge had an unfavorable impact of \$0.02 per diluted share for the six months ended December 31, 2019. In 2019, the reduction in the fair value of Angelic’s contingent consideration liability increased diluted earnings per share by \$0.27 for the second quarter and year-to-date periods.

RESULTS OF OPERATIONS - SEGMENTS

Retail Segment

(Dollars in thousands)	Three Months Ended December 31,			Change	Six Months Ended December 31,			Change
	2019	2018			2019	2018		
Net Sales	\$ 186,210	\$ 186,302	\$ (92)	— %	\$ 352,287	\$ 349,050	\$ 3,237	1 %
Operating Income	\$ 39,017	\$ 44,785	\$ (5,768)	(13)%	\$ 74,452	\$ 78,733	\$ (4,281)	(5)%
Operating Margin	21.0%	24.0%			21.1%	22.6%		

For the three months ended December 31, 2019, Retail segment net sales were essentially flat. Retail segment net sales benefited from favorable net price realization in addition to increased sales of frozen garlic bread and continued volume gains for shelf-stable dressings and sauces sold under license agreements. Notable offsets to Retail segment growth included reduced sales of our Marzetti® caramel dips and produce dressings that were impacted by the timing of shipments between the first and second quarter.

Year-to-date net sales for the Retail segment reached \$352.3 million, a 1% increase from the prior-year total of \$349.1 million driven by higher sales of frozen garlic bread and croutons and continued volume gains for shelf-stable dressings and sauces sold under license agreements. These gains were partially offset by declines in flatbread wraps and our decision to selectively exit some low-margin private-label business.

For the three months ended December 31, 2019, Retail segment operating income decreased 13% as the prior-year results were favorably impacted by the \$9.7 million reduction in the fair value of Angelic's contingent consideration liability. Retail segment operating income benefited from our cost savings programs, improved net price realization, as well as lower trade and consumer promotional spending.

For the six months ended December 31, 2019, Retail segment operating income decreased 5% as the prior-year results were favorably impacted by the \$9.7 million reduction in the fair value of Angelic's contingent consideration liability. Retail segment operating income benefited from our cost savings programs and improved net price realization, as partially offset by higher trade and consumer promotional spending.

Foodservice Segment

(Dollars in thousands)	Three Months Ended December 31,			Change	Six Months Ended December 31,			Change
	2019	2018			2019	2018		
Net Sales	\$ 168,907	\$ 163,279	\$ 5,628	3%	\$ 339,884	\$ 317,185	\$ 22,699	7%
Operating Income	\$ 23,416	\$ 19,405	\$ 4,011	21%	\$ 47,205	\$ 38,266	\$ 8,939	23%
Operating Margin	13.9%	11.9%			13.9%	12.1%		

For the three months ended December 31, 2019, Foodservice segment net sales grew 3%. Excluding all sales attributed to Omni, Foodservice segment net sales improved 2% driven by higher sales of our branded products and continued growth for Bantam. Omni sales totaled \$6.3 million in the current year compared to \$3.8 million in the prior year. Note that Omni sales are attributed to a temporary supply agreement that is expected to end by December 2020 with declining sales projected through the end of the agreement.

For the six months ended December 31, 2019, Foodservice segment net sales increased 7%. Excluding all sales attributed to Omni, Foodservice segment net sales improved 4% with sales from the Bantam acquisition, national chain restaurant accounts, branded products and frozen pasta products all contributing to growth. Omni sales totaled \$14.2 million in the current year compared to \$3.8 million in the prior year.

The increase in Foodservice segment operating income and related margins for the three and six months ended December 31, 2019 was driven by the higher sales volumes, a more favorable sales mix and the benefits from our cost savings programs.

Corporate Expenses

For the three months ended December 31, 2019 and 2018, corporate expenses totaled \$8.4 million and \$3.0 million, respectively. For the six months ended December 31, 2019 and 2018, corporate expenses totaled \$15.0 million and \$6.7 million, respectively. The increase for both periods was primarily driven by ERP expenses which totaled \$4.9 million and \$7.6 million for the three and six months ended December 31, 2019, respectively. For the three months ended December 31, 2019, we also capitalized an additional \$0.9 million of ERP-related expenditures for application development stage activities.

LOOKING FORWARD

Looking forward to the back half of our fiscal year, we expect Retail segment sales will benefit from continued growth from shelf-stable dressings and sauces sold under license agreements, sales contributions from new product introductions and improved net price realization. In the Foodservice segment, we anticipate modest sales growth driven by select national chain restaurant accounts and sales of our branded products. We expect Foodservice sales to be unfavorably influenced by a second-sourcing initiative by one of our national chain restaurant accounts, slowing sales trends for the overall restaurant industry and sales declines attributed to the temporary supply agreement with Omni that is expected to end by December 2020. We foresee input costs to be increasingly inflationary through the second half of our fiscal year while SG&A expenses will continue to reflect incremental investments in our strategic initiatives, most notably the ERP. Our cost-savings and net price realization initiatives will help to offset these higher costs.

FINANCIAL CONDITION

For the six months ended December 31, 2019, net cash provided by operating activities totaled \$105.4 million, as compared to \$113.2 million in the prior-year period. This decrease was due to the year-over-year change in net working capital, as partially offset by the impact of the prior-year reduction in the fair value of Angelic's contingent consideration.

Cash used in investing activities for the six months ended December 31, 2019 was \$57.9 million, as compared to \$86.5 million in the prior year. This decrease primarily reflects the impact of the prior-year second quarter acquisitions of Bantam and Omni as partially offset by a higher level of capital expenditures paid in the current year. The year-over-year increase in our capital expenditures includes spending on a capacity expansion project at our frozen dinner roll facility in Horse Cave, Kentucky that was completed in January 2020 and the purchase of a manufacturing facility that was previously leased.

Cash used in financing activities for the six months ended December 31, 2019 of \$41.5 million increased from the prior-year total of \$38.0 million. This increase was primarily due to higher dividend payments and larger tax withholdings related to stock-based compensation.

Under our unsecured revolving credit facility ("Facility"), we may borrow up to a maximum of \$150 million at any one time. We had no borrowings outstanding under the Facility at December 31, 2019. At December 31, 2019, we had \$5.1 million of standby letters of credit outstanding, which reduced the amount available for borrowing on the Facility. The Facility expires in April 2021, and all outstanding amounts are then due and payable. Interest is variable based upon formulas tied to LIBOR or an alternative base rate defined in the Facility, at our option. We must also pay facility fees that are tied to our then-applicable consolidated leverage ratio. Loans may be used for general corporate purposes. Due to the nature of its terms, when we have outstanding borrowings under the Facility, they will be classified as long-term debt.

The Facility contains certain restrictive covenants, including limitations on indebtedness, asset sales and acquisitions, and financial covenants relating to interest coverage and leverage. At December 31, 2019, we were in compliance with all applicable provisions and covenants of this facility, and we exceeded the requirements of the financial covenants by substantial margins. At December 31, 2019, there were no events that would constitute a default under this facility.

We currently expect to remain in compliance with the Facility's covenants for the foreseeable future. However, a default under the Facility could accelerate the repayment of any then outstanding indebtedness and limit our access to \$75 million of additional credit available under the Facility. Such an event could require a reduction in or curtailment of cash dividends or share repurchases, reduce or delay beneficial expansion or investment plans, or otherwise impact our ability to meet our obligations when due.

We believe that cash provided by operating activities and our existing balances in cash and equivalents, in addition to that available under the Facility, should be adequate to meet our cash requirements through 2020, including the projected levels of capital expenditures and dividend payments. Based on our current plans and expectations, we continue to expect our capital expenditures for 2020 could total between \$80 and \$100 million. This range of projected expenditures includes approximately \$10 million for a significant expansion that is expected to begin soon at one of our dressing and sauce production facilities to support the continued growth of select national chain restaurant accounts. The total investment for this project is estimated to be \$95 million, most of which will be spent in fiscal 2021. If we were to borrow outside of the Facility under current market terms, our average interest rate may increase and have an adverse effect on our results of operations.

CONTRACTUAL OBLIGATIONS

We have various contractual obligations that are appropriately recorded as liabilities in our condensed consolidated financial statements. Certain other contractual obligations are not recognized as liabilities in our condensed consolidated financial statements. Examples of such items are commitments to purchase raw materials or packaging inventory that has not yet been received as of December 31, 2019. There have been no significant changes to the contractual obligations disclosed in our 2019 Annual Report on Form 10-K aside from expected changes in raw-material costs associated with changes in product demand or pricing.

CRITICAL ACCOUNTING POLICIES

There have been no changes in critical accounting policies from those policies disclosed in our 2019 Annual Report on Form 10-K. We adopted the new lease accounting guidance on July 1, 2019. See expanded disclosure of lease accounting policies in Note 5 to the condensed consolidated financial statements.

RECENT ACCOUNTING PRONOUNCEMENTS

Recent accounting pronouncements and their impact on our consolidated financial statements are disclosed in Note 1 to the condensed consolidated financial statements.

FORWARD-LOOKING STATEMENTS

We desire to take advantage of the “safe harbor” provisions of the Private Securities Litigation Reform Act of 1995 (the “PSLRA”). This Quarterly Report on Form 10-Q contains various “forward-looking statements” within the meaning of the PSLRA and other applicable securities laws. Such statements can be identified by the use of the forward-looking words “anticipate,” “estimate,” “project,” “believe,” “intend,” “plan,” “expect,” “hope” or similar words. These statements discuss future expectations; contain projections regarding future developments, operations or financial conditions; or state other forward-looking information. Such statements are based upon assumptions and assessments made by us in light of our experience and perception of historical trends, current conditions, expected future developments and other factors we believe to be appropriate. These forward-looking statements involve various important risks, uncertainties and other factors that could cause our actual results to differ materially from those expressed in the forward-looking statements. Actual results may differ as a result of factors over which we have no, or limited, control including, without limitation, the specific influences outlined below. Management believes these forward-looking statements to be reasonable; however, one should not place undue reliance on such statements that are based on current expectations. Forward-looking statements speak only as of the date they are made, and we undertake no obligation to update such forward-looking statements, except as required by law.

Items which could impact these forward-looking statements include, but are not limited to:

- the ability to successfully grow recently acquired businesses;
- the extent to which recent and future business acquisitions are completed and acceptably integrated;
- difficulties in designing and implementing our new enterprise resource planning system;
- cyber-security incidents, information technology disruptions, and data breaches;
- price and product competition;
- the lack of market acceptance of new products;
- the success and cost of new product development efforts;
- the potential for loss of larger programs or key customer relationships;
- fluctuations in the cost and availability of ingredients and packaging;
- the impact of customer store brands on our branded retail volumes;
- the reaction of customers or consumers to price increases we may implement;
- adverse changes in freight, energy or other costs of producing, distributing or transporting our products;
- dependence on contract manufacturers, distributors and freight transporters;
- stability of labor relations;
- changes in demand for our products, which may result from loss of brand reputation or customer goodwill;
- dependence on key personnel and changes in key personnel;
- the effect of consolidation of customers within key market channels;
- the possible occurrence of product recalls or other defective or mislabeled product costs;
- capacity constraints that may affect our ability to meet demand or may increase our costs;
- maintenance of competitive position with respect to other manufacturers;
- changes in estimates in critical accounting judgments;
- the impact of any regulatory matters affecting our food business, including any required labeling changes and their impact on consumer demand;
- the outcome of any litigation or arbitration;
- efficiencies in plant operations;
- adequate supply of skilled labor;
- the impact, if any, of certain contingent liabilities associated with our withdrawal from a multiemployer pension plan;
- the impact of fluctuations in our pension plan asset values on funding levels, contributions required and benefit costs; and
- certain other factors, including the information disclosed in our discussion of risk factors under Item 1A of our 2019 Annual Report on Form 10-K.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Our market risks have not changed materially from those disclosed in our 2019 Annual Report on Form 10-K.

Item 4. Controls and Procedures

(a) *Evaluation of Disclosure Controls and Procedures.* As of the end of the period covered by this Quarterly Report on Form 10-Q, our management, including our Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934, as amended (the “Exchange Act”). Based upon this evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective as of December 31, 2019 to ensure that information required to be disclosed in the reports that we file or submit under the Exchange Act is 1) recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission’s rules and forms and 2) accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, in a manner that allows timely decisions regarding required disclosure.

(b) *Changes in Internal Control Over Financial Reporting.* No changes were made to our internal control over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) of the Exchange Act) during our most recent fiscal quarter that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II – OTHER INFORMATION

Item 1A. Risk Factors

There have been no material changes to the risk factors disclosed under Item 1A in our 2019 Annual Report on Form 10-K.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

(c) In November 2010, our Board of Directors approved a share repurchase authorization of 2,000,000 common shares, of which 1,344,099 common shares remained authorized for future repurchases at December 31, 2019. This share repurchase authorization does not have a stated expiration date. In the second quarter, we made the following repurchases of our common stock:

<u>Period</u>	<u>Total Number of Shares Purchased</u>	<u>Average Price Paid Per Share</u>	<u>Total Number of Shares Purchased as Part of Publicly Announced Plans</u>	<u>Maximum Number of Shares that May Yet be Purchased Under the Plans</u>
October 1-31, 2019	—	\$ —	—	1,344,144
November 1-30, 2019 ⁽¹⁾	45	\$ 158.67	45	1,344,099
December 1-31, 2019	—	\$ —	—	1,344,099
Total	<u>45</u>	<u>\$ 158.67</u>	<u>45</u>	<u>1,344,099</u>

(1) Represents shares that were repurchased in satisfaction of tax withholding obligations arising from the vesting of restricted stock granted to employees under the Lancaster Colony Corporation 2015 Omnibus Incentive Plan.

Item 6. Exhibits

See Index to Exhibits following Signatures.

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.

LANCASTER COLONY CORPORATION

(Registrant)

Date: February 4, 2020

By: /s/ DAVID A. CIESINSKI

David A. Ciesinski

President, Chief Executive Officer

and Director

(Principal Executive Officer)

Date: February 4, 2020

By: /s/ THOMAS K. PIGOTT

Thomas K. Pigott

Chief Financial Officer and Assistant Secretary

(Principal Financial and Accounting Officer)

LANCASTER COLONY CORPORATION AND SUBSIDIARIES
FORM 10-Q
DECEMBER 31, 2019
INDEX TO EXHIBITS

Exhibit Number	Description	Located at
<u>31.1</u>	<u>Certification of CEO under Section 302 of the Sarbanes-Oxley Act of 2002</u>	<u>Filed herewith</u>
<u>31.2</u>	<u>Certification of CFO under Section 302 of the Sarbanes-Oxley Act of 2002</u>	<u>Filed herewith</u>
<u>32</u>	<u>Certification of CEO and CFO under Section 906 of the Sarbanes-Oxley Act of 2002</u>	<u>Furnished herewith</u>
101.INS	XBRL Instance Document - the instance document does not appear in the Interactive Data File because its XBRL tags are embedded within the Inline XBRL document	Filed herewith
101.SCH	Inline XBRL Taxonomy Extension Schema Document	Filed herewith
101.CAL	Inline XBRL Taxonomy Extension Calculation Linkbase Document	Filed herewith
101.DEF	Inline XBRL Taxonomy Extension Definition Linkbase Document	Filed herewith
101.LAB	Inline XBRL Taxonomy Extension Label Linkbase Document	Filed herewith
101.PRE	Inline XBRL Taxonomy Extension Presentation Linkbase Document	Filed herewith
104	The cover page of Lancaster Colony Corporation's Quarterly Report on Form 10-Q for the quarter ended December 31, 2019, formatted in Inline XBRL (included within Exhibit 101 attachments)	Filed herewith

Certification by Chief Executive Officer

I, David A. Ciesinski, certify that:

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

Date: February 4, 2020

By: /s/ DAVID A. CIESINSKI

David A. Ciesinski

Chief Executive Officer

Certification by Chief Financial Officer

I, Thomas K. Pigott, certify that:

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

Date: February 4, 2020

By: /s/ THOMAS K. PIGOTT

Thomas K. Pigott

Chief Financial Officer

**CERTIFICATION OF CHIEF EXECUTIVE OFFICER AND CHIEF FINANCIAL OFFICER
PURSUANT TO 18, UNITED STATES CODE, SECTION 1350,
AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report of Lancaster Colony Corporation (the "Company") on Form 10-Q for the quarter ending December 31, 2019, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), David A. Ciesinski, Chief Executive Officer of the Company, and Thomas K. Pigott, Chief Financial Officer of the Company, respectively, do each hereby certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 that:

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

By: /s/ DAVID A. CIESINSKI

David A. Ciesinski

Chief Executive Officer

February 4, 2020

By: /s/ THOMAS K. PIGOTT

Thomas K. Pigott

Chief Financial Officer

February 4, 2020

The foregoing certification is being furnished solely pursuant to 18 U.S.C. Section 1350 and is not being filed as part of the Report or as a separate disclosure document.