

J&J SNACK FOODS CORP  
Form 10-Q  
August 02, 2018

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 period ended June 30, 2018

or

Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

Commission File Number: 0-14616

J & J SNACK FOODS CORP.

(Exact name of registrant as specified in its charter)

New Jersey

22-1935537

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

6000 Central Highway, Pennsauken, NJ 08109

(Address of principal executive offices)

Telephone (856) 665-9533

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.

X 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 (§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).

X Yes No

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

Large Accelerated filer (X) Accelerated filer ( )

Non-accelerated filer ( ) (Do not check if a smaller reporting company)  
Smaller reporting company ( )  
Emerging growth company ( )

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

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

Yes  No

As July 26, 2018 there were 18,716,140 shares of the Registrant's Common Stock outstanding.

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**J & J SNACK FOODS CORP. AND SUBSIDIARIES**  
**CONSOLIDATED BALANCE SHEETS**  
(in thousands, except share amounts)

|  | <b>June 30,</b>    | <b>September</b>  |
|--|--------------------|-------------------|
|  | <b>2018</b>        | <b>30,</b>        |
|  | <b>(unaudited)</b> | <b>2017</b>       |
| <b>Assets</b>                                  |                    |                   |
| Current assets                                 |                    |                   |
| Cash and cash equivalents                      | \$ 95,628          | \$ 90,962         |
| Marketable securities held to maturity         | 30,271             | 59,113            |
| Accounts receivable, net                       | 131,776            | 124,553           |
| Inventories                                    | 116,194            | 103,268           |
| Prepaid expenses and other                     | 6,857              | 3,936             |
| Total current assets                           | 380,726            | 381,832           |
| Property, plant and equipment, at cost         |                    |                   |
| Land   | 2,494              | 2,482             |
| Buildings                                      | 26,582             | 26,741            |
| Plant machinery and equipment                  | 279,077            | 257,172           |
| Marketing equipment                            | 285,689            | 278,860           |
| Transportation equipment                       | 8,648              | 8,449             |
| Office equipment                               | 27,948             | 25,302            |
| Improvements                                   | 38,657             | 38,003            |
| Construction in progress                       | 13,174             | 16,880            |
| Total Property, plant and equipment, at cost   | 682,269            | 653,889           |
| Less accumulated depreciation and amortization | 445,001            | 426,308           |
| Property, plant and equipment, net             | 237,268            | 227,581           |
| Other assets                                   |                    |                   |
| Goodwill                                       | 102,511            | 102,511           |
| Other intangible assets, net                   | 58,646             | 61,272            |
| Marketable securities held to maturity         | 103,548            | 60,908            |
| Marketable securities available for sale       | 28,908             | 30,260            |
| Other  | 2,625              | 2,864             |
| Total other assets                             | 296,238            | 257,815           |
| <b>Total Assets</b>                            | <b>\$ 914,232</b>  | <b>\$ 867,228</b> |
| <b>Liabilities and Stockholders' Equity</b>    |                    |                   |
| Current Liabilities                            |                    |                   |
| Current obligations under capital leases       | \$ 336             | \$ 340            |
| Accounts payable                               | 79,489             | 72,729            |
| Accrued insurance liability                    | 11,929             | 10,558            |
| Accrued liabilities                            | 7,770              | 7,753             |
| Accrued compensation expense                   | 15,147             | 19,826            |

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|  |                   |                   |
|--|-------------------|-------------------|
| Dividends payable  | 8,415             | 7,838             |
| Total current liabilities  | 123,086           | 119,044           |
| Long-term obligations under capital leases   | 833               | 904               |
| Deferred income taxes  | 50,228            | 62,705            |
| Other long-term liabilities  | 2,010             | 2,253             |
| <b>Stockholders' Equity</b>  |                   |                   |
| Preferred stock, \$1 par value; authorized 10,000,000 shares; none issued  | -                 | -                 |
| Common stock, no par value; authorized, 50,000,000 shares; issued and outstanding 18,697,000 and 18,705,000 respectively | 23,047            | 17,382            |
| Accumulated other comprehensive loss   | (13,770 )         | (8,875 )          |
| Retained Earnings  | 728,798           | 673,815           |
| Total stockholders' equity   | 738,075           | 682,322           |
| <b>Total Liabilities and Stockholders' Equity</b>  | <b>\$ 914,232</b> | <b>\$ 867,228</b> |

The accompanying notes are an integral part of these statements.

**J & J SNACK  
FOODS CORP.  
AND  
SUBSIDIARIES  
CONSOLIDATED  
STATEMENTS  
OF EARNINGS  
(Unaudited)  
(in thousands,  
except per share  
amounts)**

|   | Three months ended |                  | Nine months ended |                  |
|---|--------------------|------------------|-------------------|------------------|
|   | June 30,<br>2018   | June 24,<br>2017 | June 30,<br>2018  | June 24,<br>2017 |
| Net Sales                                 | \$306,239          | \$295,415        | \$837,550         | \$767,498        |
| Cost of goods sold <sup>(1)</sup>         | 211,764            | 200,651          | 592,518           | 534,022          |
| Gross Profit                              | 94,475             | 94,764           | 245,032           | 233,476          |
| Operating expenses                        |                    |                  |                   |                  |
| Marketing <sup>(2)</sup>                  | 25,589             | 25,571           | 69,672            | 67,435           |
| Distribution <sup>(3)</sup>               | 24,325             | 21,865           | 67,901            | 58,537           |
| Administrative <sup>(4)</sup>             | 9,654              | 9,588            | 28,014            | 26,404           |
| Other general expense (income)            | 38                 | (60 )            | (193 )            | (138 )           |
| Total operating expenses                  | 59,606             | 56,964           | 165,394           | 152,238          |
| Operating Income                          | 34,869             | 37,800           | 79,638            | 81,238           |
| Other income (expense)                    |                    |                  |                   |                  |
| Investment income                         | 1,705              | 1,422            | 4,687             | 3,824            |
| Interest expense & other                  | (209 )             | (80 )            | 267               | (651 )           |
| Earnings before income taxes              | 36,365             | 39,142           | 84,592            | 84,411           |
| Income taxes                              | 10,236             | 13,838           | 4,381             | 29,580           |
| NET EARNINGS                              | \$26,129           | \$25,304         | \$80,211          | \$54,831         |
| Earnings per diluted share                | \$1.39             | \$1.34           | \$4.27            | \$2.91           |
| Weighted average number of diluted shares | 18,822             | 18,846           | 18,801            | 18,818           |
| Earnings per basic share                  | \$1.40             | \$1.35           | \$4.29            | \$2.93           |

Weighted average number of basic shares      18,698      18,727      18,683      18,708

- (1) Includes share-based compensation expense of \$225 and \$642 for the three months and nine months ended June 30, 2018, respectively and \$192 and \$529 for the three months and nine months ended June 24, 2017.
- (2) Includes share-based compensation expense of \$349 and \$998 for the three months and nine months ended June 30, 2018, respectively and \$277 and \$763 for the three months and nine months ended June 24, 2017.
- (3) Includes share-based compensation expense of \$20 and \$56 for the three months and nine months ended June 30, 2018,, respectively and \$19 and \$52 for the three months and nine months ended June 24, 2017.
- (4) Includes share-based compensation expense of \$412 and \$1,178 for the three months and nine months ended June 30, 2018, respectively and \$323 and \$896 for the three months and nine months ended June 24, 2017.

The accompanying notes are an integral part of these statements.



**J&J SNACK FOODS CORP. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME**  
**(Unaudited)**  
**(in thousands)**

|   | Three months<br>ended |                  | Nine months<br>ended |                  |
|---|-----------------------|------------------|----------------------|------------------|
|   | June 30,<br>2018      | June 24,<br>2017 | June 30,<br>2018     | June 24,<br>2017 |
| Net Earnings  | \$26,129              | \$25,304         | \$80,211             | \$54,831         |
| Foreign currency translation adjustments                | (2,359 )              | 1,095            | (4,348 )             | 1,885            |
| Unrealized holding (loss) gain on marketable securities | (253 )                | 204              | (547 )               | 699              |
| Total Other Comprehensive (Loss) Income                 | (2,612 )              | 1,299            | (4,895 )             | 2,584            |
| Comprehensive Income                                    | \$23,517              | \$26,603         | \$75,316             | \$57,415         |

The accompanying notes are an integral part of these statements.

**J & J SNACK FOODS CORP. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
**(Unaudited) (in thousands)**

|   | Nine months ended |                  |
|---|-------------------|------------------|
|   | June 30,<br>2018  | June 24,<br>2017 |
| Operating activities:   |                   |                  |
| Net earnings  | \$80,211          | \$54,831         |
| Adjustments to reconcile net earnings to net cash provided by operating activities: |                   |                  |
| Depreciation of property, plant and equipment                                       | 31,929            | 28,060           |
| Amortization of intangibles and deferred costs                                      | 2,639             | 3,336            |
| Share-based compensation  | 2,874             | 2,240            |
| Deferred income taxes   | (12,502)          | (347 )           |
| Loss(gain)on sale and redemption of marketable securities                           | 32                | (13 )            |
| Other   | (3 )              | 712              |
| Changes in assets and liabilities net of effects from purchase of companies         |                   |                  |
| Increase in accounts receivable   | (7,530 )          | (23,385 )        |
| Increase in inventories   | (13,020)          | (12,154 )        |
| (Increase)decrease in prepaid expenses  | (2,949 )          | 10,035           |
| Increase in accounts payable and accrued liabilities                                | 3,606             | 20,023           |
| Net cash provided by operating activities   | 85,287            | 83,338           |
| Investing activities:   |                   |                  |
| Payment for purchases of companies, net of cash acquired                            | -                 | (42,058 )        |
| Purchases of property, plant and equipment  | (43,344)          | (57,151 )        |
| Purchases of marketable securities  | (65,227)          | (27,269 )        |
| Proceeds from redemption and sales of marketable securities                         | 51,417            | 14,681           |
| Proceeds from disposal of property, plant and equipment                             | 1,895             | 1,385            |
| Other   | 171               | (404 )           |
| Net cash used in investing activities   | (55,088)          | (110,816)        |
| Financing activities:   |                   |                  |
| Payments to repurchase common stock   | (2,794 )          | (3,374 )         |
| Proceeds from issuance of stock   | 5,561             | 4,745            |
| Payments on capitalized lease obligations   | (278 )            | (273 )           |
| Payment of cash dividend  | (24,652)          | (22,992 )        |
| Net cash used in financing activities   | (22,163)          | (21,894 )        |
| Effect of exchange rate on cash and cash equivalents                                | (3,370 )          | 1,334            |
| Net increase (decrease) in cash and cash equivalents                                | 4,666             | (48,038 )        |
| Cash and cash equivalents at beginning of period                                    | 90,962            | 140,652          |
| Cash and cash equivalents at end of period  | \$95,628          | \$92,614         |

The accompanying notes are an integral part of these statements.



J & J SNACK FOODS CORP. AND SUBSIDIARIES

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(unaudited)

Note 1  
The accompanying unaudited Consolidated Financial Statements have been prepared in accordance with accounting principles generally accepted in the United States for interim financial information and with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. They do not include all information and notes required by generally accepted accounting principles for complete financial statements. However, except as disclosed herein, there has been no material change in the information disclosed in the Notes to Consolidated Financial Statements included in the Company's Annual Report on Form 10-K for the year ended September 30, 2017.

In the opinion of management, the accompanying unaudited consolidated financial statements contain all adjustments (consisting of only normal recurring adjustments) necessary to present fairly the financial position and the results of operations and cash flows.

The results of operations for the nine months ended June 30, 2018 and June 24, 2017 are not necessarily indicative of results for the full year. Sales of our frozen beverages and frozen juices and ices are generally higher in the third and fourth quarters due to warmer weather.

While we believe that the disclosures presented are adequate to make the information not misleading, it is suggested that these consolidated financial statements be read in conjunction with the consolidated financial statements and the notes included in the Company's Annual Report on Form 10-K for the fiscal year ended September 30, 2017.

Note 2  
We recognize revenue from our products when the products are shipped to our customers. Repair and maintenance equipment service revenue is recorded when it is performed provided the customer terms are that the customer is to be charged on a time and material basis or on a straight-line basis over the term of the contract when the customer has signed a service contract. Revenue is recognized only where persuasive evidence of an arrangement exists, our price is fixed or determinable and collectability is reasonably assured. We record offsets to revenue for allowances, end-user pricing adjustments, trade spending, coupon redemption costs and returned product. Customers generally do not have the right to return product unless it is damaged or defective. We provide an allowance for doubtful receivables after taking into consideration historical experience and other factors. The allowance for doubtful receivables was \$420,000 and \$359,000 at June 30, 2018 and September 30, 2017, respectively.



Note 3 Depreciation of equipment and buildings is provided for by the straight-line method over the assets' estimated useful lives. Amortization of improvements is provided for by the straight-line method over the term of the lease or the assets' estimated useful lives, whichever is shorter. Licenses and rights, customer relationships and non-compete agreements arising from acquisitions are amortized by the straight-line method over periods ranging from 2 to 20 years. Depreciation expense was \$10,569,000 and \$9,629,000 for the three months ended June 30, 2018 and June 24, 2017, respectively, and \$31,929,000 and \$28,060,000 for the nine months ended June 30, 2018 and June 24, 2017, respectively.

Note 4 Basic earnings per common share (EPS) excludes dilution and is computed by dividing income available to common shareholders by the weighted average common shares outstanding during the period. Diluted EPS takes into consideration the potential dilution that could occur if securities (stock options) or other contracts to issue common stock were exercised and converted into common stock. Our calculation of EPS is as follows:

|  | Three Months Ended June 30,<br>2018      |        |                        |
|--|--|--------|------------------------|
|  | Income                                   | Shares | Per<br>Share<br>Amount |
|  | (Numerator)                              |        | (Denominator)          |
|  | (in thousands, except per share amounts) |        |                        |
| <b>Basic EPS</b>   |  |        |                        |
| Net Earnings available to common stockholders                          | \$26,129                                 | 18,698 | \$ 1.40                |
| <b>Effect of Dilutive Securities</b>                                   |  |        |                        |
| Options  | -  | 124    | (0.01 )                |
| <b>Diluted EPS</b>   |  |        |                        |
| Net Earnings available to common stockholders plus assumed conversions | \$26,129                                 | 18,822 | \$ 1.39                |

1,000 anti-dilutive shares have been excluded in the computation of EPS for the three months ended June 30, 2018.

|                  | Nine Months Ended June 30, 2018          |        |                        |
|------------------|--|--------|------------------------|
|                  | Income                                   | Shares | Per<br>Share<br>Amount |
|                  | (Numerator)                              |        | (Denominator)          |
|                  | (in thousands, except per share amounts) |        |                        |
| <b>Basic EPS</b> |  |        |                        |

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|  |          |        |         |
|--|----------|--------|---------|
| Net Earnings available to common stockholders                          | \$80,211 | 18,683 | \$ 4.29 |
| <b>Effect of Dilutive Securities</b>                                   |          |        |         |
| Options  | -        | 118    | (0.02 ) |
| <b>Diluted EPS</b>   |          |        |         |
| Net Earnings available to common stockholders plus assumed conversions | \$80,211 | 18,801 | \$ 4.27 |

1,000 anti-dilutive shares have been excluded in the computation of EPS for the nine months ended June 30, 2018.

|  | Three Months Ended June 24,<br>2017         |               |              |
|--|---|---------------|--------------|
|  | Income                                      | Shares        | Per<br>Share |
|  | (Numerator)                                 | (Denominator) | Amount       |
|  | (in thousands, except per share<br>amounts) |               |              |
| <b>Basic EPS</b>   |   |               |              |
| Net Earnings available to common stockholders                          | \$25,304                                    | 18,727        | \$ 1.35      |
| <b>Effect of Dilutive Securities</b>                                   |   |               |              |
| Options  | -   | 119           | (0.01 )      |
| <b>Diluted EPS</b>   |   |               |              |
| Net Earnings available to common stockholders plus assumed conversions | \$25,304                                    | 18,846        | \$ 1.34      |

500 anti-dilutive shares have been excluded in the computation of EPS for the three months ended June 24, 2017.

|  | Nine Months Ended June 24, 2017             |               |              |
|--|---|---------------|--------------|
|  | Income                                      | Shares        | Per<br>Share |
|  | (Numerator)                                 | (Denominator) | Amount       |
|  | (in thousands, except per share<br>amounts) |               |              |
| <b>Basic EPS</b>   |   |               |              |
| Net Earnings available to common stockholders                          | \$54,831                                    | 18,708        | \$ 2.93      |
| <b>Effect of Dilutive Securities</b>                                   |   |               |              |
| Options  | -   | 110           | (0.02 )      |
| <b>Diluted EPS</b>   |   |               |              |
| Net Earnings available to common stockholders plus assumed conversions | \$54,831                                    | 18,818        | \$ 2.91      |

158,494 anti-dilutive shares have been excluded in the computation of EPS for the nine months ended June 24, 2017



Note 5 At June 30, 2018, the Company has three stock-based employee compensation plans. Share-based compensation expense (benefit) was recognized as follows:

|   | Three months ended |               | Nine months ended |               |
|---|--------------------|---------------|-------------------|---------------|
|   | June 30, 2018      | June 24, 2017 | June 30, 2018     | June 24, 2017 |
| Stock Options                                 | \$473              | \$(20 )       | \$1,559           | \$(165 )      |
| Stock purchase plan                           | 89                 | 65            | 355               | 300           |
| Stock issued to an outside director           | 16                 | 14            | 48                | 42            |
| Restricted stock issued to an employee        | 1                  | 1             | 3                 | 3             |
| Total share-based compensation                | \$579              | \$60          | \$1,965           | \$180         |
| The above compensation is net of tax benefits | \$427              | \$751         | \$909             | \$2,060       |

The fair value of each option grant is estimated on the date of grant using the Black-Scholes options-pricing model with the following weighted average assumptions used for grants in fiscal 2018 first nine months: expected volatility of 16.8%; risk-free interest rate of 2.6%; dividend rate of 1.3% and expected lives of 5 years.

During the fiscal year 2018 nine month period, the Company granted 159,878 stock options. The weighted-average grant date fair value of these options was \$23.67.

During the fiscal year 2017 nine month period, the Company granted 159,294 stock options. The weighted-average grant date fair value of these options was \$18.85.

Expected volatility is based on the historical volatility of the price of our common shares over the past 50 months for 5 year options and 10 years for 10 year options. We use historical information to estimate expected life and forfeitures within the valuation model. The expected term of awards represents the period of time that options granted are expected to be outstanding. The risk-free rate for periods within the expected life of the option is based on the U.S. Treasury yield curve in effect at the time of grant. Compensation cost is recognized using a straight-line method over the vesting or service period and is net of estimated forfeitures.

We account for our income taxes under the liability method. Under the liability method, deferred tax assets and Note liabilities are determined based on the difference between the financial statement and tax bases of assets and 6 liabilities as measured by the enacted tax rates that will be in effect when these differences reverse. Deferred tax expense is the result of changes in deferred tax assets and liabilities.

Additionally, we recognize a liability for income taxes and associated penalties and interest for tax positions taken or expected to be taken in a tax return which are more likely than not to be overturned by taxing authorities (“uncertain tax positions”). We have not recognized a tax benefit in our financial statements for these uncertain tax positions.

The total amount of gross unrecognized tax benefits is \$389,000 and \$374,000 on June 30, 2018 and September 30, 2017, respectively, all of which would impact our effective tax rate over time, if recognized. We recognize interest and penalties related to uncertain tax positions as a part of the provision for income taxes. As of June 30, 2018, and September 30, 2017, respectively, the Company has \$254,000 and \$239,000 of accrued interest and penalties.

In addition to our federal tax return and tax returns for Mexico and Canada, we file tax returns in all states that have a corporate income tax with virtually all open for examination for three to four years.

Net earnings for the nine months ended June 30, 2018 benefited from a \$20.9 million, or \$1.11 per diluted share, gain on the remeasurement of deferred tax liabilities and a \$7.4 million, or \$0.40 per diluted share, reduction in income taxes related primarily to the lower corporate tax rate enacted under the Tax Cuts and Jobs Act in December 2017. Net earnings for the nine months were impacted by a \$1.2 million, or \$.06 per diluted share, provision for the one time repatriation tax required under the new tax law. For the three months ended June 30, 2018, net earnings benefited by a \$3.5 million, or \$.18 per diluted share, reduction in income taxes primarily related to the lower corporate tax rate. Excluding the deferred tax gain and the one-time repatriation tax, our effective tax rate decreased to 28.1% from 35.4% in the prior year quarter and to 28.4% from 35.0% in prior year nine months reflecting the reduction in the federal statutory rate to 21% from 35% on January 1, 2018. Last year’s nine months’ effective tax rate benefited from an unusually high tax benefit on share based compensation of \$2,060,000 which compares to this year’s nine month’s tax benefit of \$909,000. We are presently estimating an effective tax rate of 28-29% for the last quarter of our fiscal year 2018 and 26-27% for our fiscal year 2019.

On December 22, 2017, the SEC issued guidance under Staff Accounting Bulletin No. 118, Income Tax Accounting Implications of the Tax Cuts and Jobs Act (“SAB 118”) directing taxpayers to consider the impact of the U.S. legislation as “provisional” when it does not have the necessary information available, prepared or analyzed (including computations) in reasonable detail to complete its accounting for the change in tax law. In accordance with SAB 118, the estimated income tax net benefit of \$3.5 million for the three months and \$27.1 million for the nine months represents our best estimate based on interpretation of the U.S. legislation as we are still accumulating data to finalize the underlying calculations, or in certain cases, the U.S. Treasury is expected to issue further guidance on the application of certain provisions of the U.S. legislation. In accordance with SAB 118, the additional estimated income tax net benefit of \$3.5 million for the three months and \$27.1 million for the nine months are considered provisional and will be finalized before December 22, 2018.

In May 2014 and in subsequent updates, the FASB issued guidance on revenue recognition which requires that we recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration which we expect to be entitled in exchange for those goods or services. We have performed a review of the requirements of the new revenue standard and are in the process of reviewing customer contracts and applying the five-step model of this new guidance to each contract category we have identified and will compare the results to our current accounting practices. We plan to adopt this guidance on the first day of our fiscal 2019 year. We will apply the modified retrospective transition method, which would result in an adjustment to retained earnings for the cumulative effect, if any, of applying the standard to contracts in process as of the adoption date. Under this method, we would not restate the prior financial statements presented. Therefore, this guidance would require additional disclosures of the amount by which each financial statement line item is affected in the fiscal year 2019 reporting period. Our analysis indicates that the impact of this guidance on our consolidated financial statements will not be material.

In January 2016, the FASB issued guidance which requires an entity to measure equity investments at fair value with changes in fair value recognized in net income, to use the price that would be received by a seller when measuring the fair value of financial instruments for disclosure purposes, and which eliminates the requirement to disclose the method(s) and significant assumptions used to estimate the fair value that is required to be disclosed for financial instruments measured at amortized cost on the balance sheet. Under present guidance, changes in fair value of equity investments are recognized in Stockholders' Equity. This guidance is effective for our fiscal year ended September 2019. Early adoption is not permitted. We do not anticipate that the adoption of this new guidance will have a material impact on our consolidated financial statements.

In February 2016, the FASB issued guidance on lease accounting which requires that an entity recognize most leases on its balance sheet. The guidance retains a dual lease accounting model for purposes of income statement recognition, continuing the distinction between what are currently known as "capital" and "operating" leases for lessees. This guidance is effective for our fiscal year ended September 2020. While we continue to evaluate the effect of adopting this guidance on our consolidated financial statements and related disclosures, we expect our operating leases will be subject to the new standard. We will recognize right-of-use assets and operating lease liabilities on our consolidated balance sheets upon adoption, which will increase our total assets and liabilities. We anticipate that the impact of this guidance on our financial statements will be material.

Note 8 Inventories consist of the following:

|                         | June 30,<br>2018<br>(unaudited)<br>(in thousands) | September<br>30,<br>2017 |
|-------------------------|---|--------------------------|
| Finished goods          | \$54,183  | \$45,394                 |
| Raw Materials           | 25,082  | 22,682                   |
| Packaging materials     | 10,744  | 8,833                    |
| Equipment parts & other | 26,185  | 26,359                   |
| Total Inventories       | \$116,194   | \$103,268                |

We principally sell our products to the food service and retail supermarket industries. Sales and results of our Note frozen beverages business are monitored separately from the balance of our food service business because of 9 different distribution and capital requirements. We maintain separate and discrete financial information for the three operating segments mentioned above which is available to our Chief Operating Decision Makers.

Our three reportable segments are Food Service, Retail Supermarkets and Frozen Beverages. All inter-segment net sales and expenses have been eliminated in computing net sales and operating income. These segments are described below.

#### Food Service

The primary products sold by the food service group are soft pretzels, frozen juice treats and desserts, churros, dough enrobed handheld products and baked goods. Our customers in the food service industry include snack bars and food stands in chain, department and discount stores; malls and shopping centers; fast food outlets; stadiums and sports arenas; leisure and theme parks; convenience stores; movie theatres; warehouse club stores; schools, colleges and other institutions. Within the food service industry, our products are purchased by the consumer primarily for consumption at the point-of-sale.

#### Retail Supermarkets

The primary products sold to the retail supermarket channel are soft pretzel products – including SUPERPRETZEL, frozen juice treats and desserts including LUIGI'S Real Italian Ice, MINUTE MAID Juice Bars and Soft Frozen Lemonade, WHOLE FRUIT frozen fruit bars and sorbet, PHILLY SWIRL cups and sticks, ICEE Squeeze-Up Tubes and dough enrobed handheld products including PATIO burritos. Within the retail supermarket channel, our frozen and prepackaged products are purchased by the consumer for consumption at home.

## Frozen Beverages

We sell frozen beverages and related products to the food service industry primarily under the names ICEE, SLUSH PUPPIE and PARROT ICE in the United States, Mexico and Canada. We also provide repair and maintenance service to customers for customers' owned equipment.

The Chief Operating Decision Maker for Food Service and Retail Supermarkets and the Chief Operating Decision Maker for Frozen Beverages monthly review detailed operating income statements and sales reports in order to assess performance and allocate resources to each individual segment. Sales and operating income are key variables monitored by the Chief Operating Decision Makers and management when determining each segment's and the company's financial condition and operating performance. In addition, the Chief Operating Decision Makers review and evaluate depreciation, capital spending and assets of each segment on a quarterly basis to monitor cash flow and asset needs of each segment. Information regarding the operations in these three reportable segments is as follows:

|                                | Three months ended |                  | Nine months ended |                  |
|--------------------------------|--------------------|------------------|-------------------|------------------|
|                                | June 30,<br>2018   | June 24,<br>2017 | June 30,<br>2018  | June 24,<br>2017 |
| Sales to External Customers:   |                    |                  |                   |                  |
| Food Service                   |                    |                  |                   |                  |
| Soft pretzels                  | \$53,880           | \$45,069         | \$151,649         | \$129,556        |
| Frozen juices and ices         | 12,825             | 16,281           | 29,448            | 33,453           |
| Churros                        | 16,739             | 17,536           | 46,603            | 46,693           |
| Handhelds                      | 9,974              | 8,574            | 30,667            | 24,155           |
| Bakery                         | 93,082             | 89,712           | 278,828           | 248,795          |
| Other                          | 5,201              | 5,938            | 16,235            | 14,833           |
| Total Food Service             | \$191,701          | \$183,110        | \$553,430         | \$497,485        |
| Retail Supermarket             |                    |                  |                   |                  |
| Soft pretzels                  | \$7,332            | \$7,496          | \$27,925          | \$25,626         |
| Frozen juices and ices         | 28,785             | 27,317           | 53,950            | 50,359           |
| Handhelds                      | 2,960              | 3,548            | 8,749             | 10,374           |
| Coupon redemption              | (1,278 )           | (1,092 )         | (2,647 )          | (3,246 )         |
| Other                          | 733                | 873              | 1,715             | 2,260            |
| Total Retail Supermarket       | \$38,532           | \$38,142         | \$89,692          | \$85,373         |
| Frozen Beverages               |                    |                  |                   |                  |
| Beverages                      | \$50,343           | \$48,714         | \$118,932         | \$108,812        |
| Repair and maintenance service | 19,693             | 18,549           | 58,005            | 54,327           |
| Machines sales                 | 5,644              | 6,496            | 16,652            | 20,547           |
| Other                          | 326                | 404              | 839               | 954              |
| Total Frozen Beverages         | \$76,006           | \$74,163         | \$194,428         | \$184,640        |

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|                                     |           |           |           |           |
|-------------------------------------|-----------|-----------|-----------|-----------|
| Consolidated Sales                  | \$306,239 | \$295,415 | \$837,550 | \$767,498 |
| Depreciation and Amortization:      |           |           |           |           |
| Food Service                        | \$6,237   | \$6,028   | \$19,376  | \$18,155  |
| Retail Supermarket                  | 332       | 221       | 980       | 859       |
| Frozen Beverages                    | 4,860     | 4,437     | 14,212    | 12,382    |
| Total Depreciation and Amortization | \$11,429  | \$10,686  | \$34,568  | \$31,396  |
| Operating Income:                   |           |           |           |           |
| Food Service                        | \$19,663  | \$22,005  | \$54,098  | \$58,695  |
| Retail Supermarket                  | 3,203     | 4,890     | 8,295     | 8,390     |
| Frozen Beverages                    | 12,003    | 10,905    | 17,245    | 14,153    |
| Total Operating Income              | \$34,869  | \$37,800  | \$79,638  | \$81,238  |
| Capital Expenditures:               |           |           |           |           |
| Food Service                        | \$10,172  | \$16,923  | \$25,872  | \$35,536  |
| Retail Supermarket                  | 273       | 15        | 376       | 228       |
| Frozen Beverages                    | 6,618     | 7,230     | 17,096    | 21,387    |
| Total Capital Expenditures          | \$17,063  | \$24,168  | \$43,344  | \$57,151  |
| Assets:                             |           |           |           |           |
| Food Service                        | \$672,861 | \$631,131 | \$672,861 | \$631,131 |
| Retail Supermarket                  | 24,215    | 25,212    | 24,215    | 25,212    |
| Frozen Beverages                    | 217,156   | 209,441   | 217,156   | 209,441   |
| Total Assets                        | \$914,232 | \$865,784 | \$914,232 | \$865,784 |



Note 10 Our three reporting units, which are also reportable segments, are Food Service, Retail Supermarkets and Frozen Beverages.

The carrying amounts of acquired intangible assets for the Food Service, Retail Supermarkets and Frozen Beverage segments as of June 30, 2018 and September 30, 2017 are as follows:

|                                    | <b>June 30, 2018</b>   |                     | <b>September 30, 2017</b> |                     |
|------------------------------------|------------------------|---------------------|---------------------------|---------------------|
|                                    | <b>Gross</b>           | <b>Accumulated</b>  | <b>Gross</b>              | <b>Accumulated</b>  |
|                                    | <b>Carrying Amount</b> | <b>Amortization</b> | <b>Carrying Amount</b>    | <b>Amortization</b> |
|                                    | <b>(in thousands)</b>  |                     |                           |                     |
| <b>FOOD SERVICE</b>                |                        |                     |                           |                     |
| Indefinite lived intangible assets |                        |                     |                           |                     |
| Trade Names                        | \$16,628               | \$ -                | \$16,628                  | \$ -                |
| Amortized intangible assets        |                        |                     |                           |                     |
| Non compete agreements             | 980                    | 462                 | 980                       | 263                 |
| Customer relationships             | 20,510                 | 8,070               | 20,510                    | 6,476               |
| License and rights                 | 1,690                  | 1,122               | 1,690                     | 1,058               |
| <b>TOTAL FOOD SERVICE</b>          | <b>\$39,808</b>        | <b>\$ 9,654</b>     | <b>\$39,808</b>           | <b>\$ 7,797</b>     |
| <b>RETAIL SUPERMARKETS</b>         |                        |                     |                           |                     |
| Indefinite lived intangible assets |                        |                     |                           |                     |
| Trade Names                        | \$6,557                | \$ -                | \$6,557                   | \$ -                |
| Amortized Intangible Assets        |                        |                     |                           |                     |
| Trade Names                        | 649                    | 227                 | 649                       | 130                 |
| Customer relationships             | 7,979                  | 3,423               | 7,979                     | 2,822               |
| <b>TOTAL RETAIL SUPERMARKETS</b>   | <b>\$15,185</b>        | <b>\$ 3,650</b>     | <b>\$15,185</b>           | <b>\$ 2,952</b>     |
| <b>FROZEN BEVERAGES</b>            |                        |                     |                           |                     |
| Indefinite lived intangible assets |                        |                     |                           |                     |
| Trade Names                        | \$9,315                | \$ -                | \$9,315                   | \$ -                |
| Distribution rights                | 6,900                  | -                   | 6,900                     | -                   |
| Amortized intangible assets        |                        |                     |                           |                     |
| Customer relationships             | 257                    | 69                  | 257                       | 50                  |
| Licenses and rights                | 1,400                  | 846                 | 1,400                     | 794                 |
| <b>TOTAL FROZEN BEVERAGES</b>      | <b>\$17,872</b>        | <b>\$ 915</b>       | <b>\$17,872</b>           | <b>\$ 844</b>       |

CONSOLIDATED                      \$72,865   \$ 14,219                      \$72,865   \$ 11,593

Amortized intangible assets are being amortized by the straight-line method over periods ranging from 2 to 20 years and amortization expense is reflected throughout operating expenses. In last year's fiscal year, intangible assets of \$6,957,000 were acquired in an ICEE distributor acquisition in our frozen beverage segment, intangible assets of \$15,760,000 were acquired in the Hill & Valley acquisition in our food service segment and intangible assets of \$576,000 were acquired in the Labriola Baking acquisition, also in our food service segment. Aggregate amortization expense of intangible assets for the three months ended June 30, 2018 and June 24, 2017 was \$876,000 and \$828,000, respectively and for the nine months ended June 30, 2018 and June 24, 2017 was \$2,626,000 and \$2,957,000, respectively.

Estimated amortization expense for the next five fiscal years is approximately \$3,500,000 in 2018, \$3,300,000 in 2019, \$3,000,000 in 2020, \$2,400,000 in 2021 and \$2,300,000 in 2022. The weighted amortization period of the intangible assets is 10.8 years.

## Goodwill

The carrying amounts of goodwill for the Food Service, Retail Supermarket and Frozen Beverage segments are as follows:

|                               | Food<br>Service<br>(in thousands) | Retail<br>Supermarket | Frozen<br>Beverages | Total     |
|-------------------------------|-----------------------------------|-----------------------|---------------------|-----------|
| Balance at June 30, 2018      | \$61,665                          | \$ 3,670              | \$ 37,176           | \$102,511 |
| Balance at September 30, 2017 | \$61,665                          | \$ 3,670              | \$ 37,176           | \$102,511 |

In last year's fiscal year, goodwill of \$1,236,000 was acquired in an ICEE distributor acquisition in our frozen beverage segment, goodwill of \$14,175,000 was acquired in the Hill & Valley acquisition in our food service segment and goodwill of \$658,000 was acquired in our Labriola Baking acquisition, also in our food service segment.

We have classified our investment securities as marketable securities held to maturity and available for sale. The FASB defines fair value as the price that would be received from selling an asset or paid to transfer a liability in Note an orderly transaction between market participants. As such, fair value is a market-based measurement that 11 should be determined based on assumptions that market participants would use in pricing an asset or liability. As a basis for considering such assumptions, the FASB has established three levels of inputs that may be used to measure fair value:

Level 1 Observable inputs such as quoted prices in active markets for identical assets or liabilities;

Level 2 Observable inputs, other than Level 1 inputs in active markets, that are observable either directly or indirectly; and

Level 3 Unobservable inputs for which there is little or no market data, which require the reporting entity to develop its own assumptions.

Marketable securities held to maturity and available for sale consist primarily of investments in mutual funds, preferred stock and corporate bonds. The fair values of mutual funds are based on quoted market prices in active markets and are classified within Level 1 of the fair value hierarchy. The fair values of preferred stock, corporate bonds and certificates of deposit are based on quoted prices for identical or similar instruments in markets that are not active. As a result, preferred stock, corporate bonds and certificates of deposit are classified within Level 2 of the fair value hierarchy.

The amortized cost, unrealized gains and losses, and fair market values of our investment securities held to maturity at June 30, 2018 are summarized as follows:

|  | <b>Amortized Cost</b> | <b>Gross Unrealized Gains</b> | <b>Gross Unrealized Losses</b> | <b>Fair Market Value</b> |
|--|-----------------------|-------------------------------|--------------------------------|--------------------------|
|  | <b>(in thousands)</b> |                               |                                |                          |
| Corporate Bonds                              | \$126,939             | \$ 8                          | \$ 1,600                       | \$125,347                |
| Certificates of Deposit                      | 6,880                 | -                             | 8                              | 6,872                    |
| Total marketable securities held to maturity | \$133,819             | \$ 8                          | \$ 1,608                       | \$132,219                |

The amortized cost, unrealized gains and losses, and fair market values of our investment securities available for sale at June 30, 2018 are summarized as follows:

|  | <b>Gross<br/>Amortized<br/>Cost<br/>(in thousands)</b> | <b>Gross<br/>Unrealized<br/>Gains</b> | <b>Gross<br/>Unrealized<br/>Losses</b> | <b>Fair<br/>Market<br/>Value</b> |
|--|--|---------------------------------------|--|----------------------------------|
| Mutual Funds                                   | \$12,954   | \$ -                                  | \$ 385                                 | \$12,569                         |
| Preferred Stock                                | 16,035   | 344                                   | 40                                     | 16,339                           |
| Total marketable securities available for sale | \$28,989   | \$ 344                                | \$ 425                                 | \$28,908                         |

The mutual funds seek current income with an emphasis on maintaining low volatility and overall moderate duration. The Fixed-to-Floating Perpetual Preferred Stock generate fixed income to call dates in 2018, 2019 and 2025 and then income is based on a spread above LIBOR if the securities are not called. The mutual funds and Fixed-to-Floating Perpetual Preferred Stock do not have contractual maturities; however, we classify them as long term assets as it is our intent to hold them for a period of over one year, although we may sell some or all of them depending on presently unanticipated needs for liquidity or market conditions. The corporate bonds generate fixed income to maturity dates in 2018 through 2021, with \$124 million maturing within 3 years. Our expectation is that we will hold the corporate bonds to their maturity dates and redeem them at our amortized cost.

The amortized cost, unrealized gains and losses, and fair market values of our investment securities held to maturity at September 30, 2017 are summarized as follows:

|  | <b>Amortized Cost</b> | <b>Gross Unrealized Gains</b> | <b>Gross Unrealized Losses</b> | <b>Fair Market Value</b> |
|--|-----------------------|-------------------------------|--------------------------------|--------------------------|
|  | (in thousands)        |                               |                                |                          |
| Corporate Bonds                              | \$114,101             | \$ 424                        | \$ 155                         | \$114,370                |
| Certificates of Deposit                      | 5,920                 | 18                            | 1                              | 5,937                    |
| Total marketable securities held to maturity | \$120,021             | \$ 442                        | \$ 156                         | \$120,307                |

The amortized cost, unrealized gains and losses, and fair market values of our investment securities available for sale at September 30, 2017 are summarized as follows:

|  | <b>Amortized Cost</b> | <b>Gross Unrealized Gains</b> | <b>Gross Unrealized Losses</b> | <b>Fair Market Value</b> |
|--|-----------------------|-------------------------------|--------------------------------|--------------------------|
|  | (in thousands)        |                               |                                |                          |
| Mutual Funds                                   | \$13,003              | \$ 77                         | \$ 240                         | \$12,840                 |
| Preferred Stock                                | 16,791                | 711                           | 82                             | 17,420                   |
| Total marketable securities available for sale | \$29,794              | \$ 788                        | \$ 322                         | \$30,260                 |

The amortized cost and fair value of the Company's held to maturity securities by contractual maturity at June 30, 2018 and September 30, 2017 are summarized as follows:

| <b>June 30, 2018</b> | <b>September 30, 2017</b> |
|----------------------|---------------------------|
| <b>Fair</b>          | <b>Fair</b>               |

|  | <b>AmortizedMarket</b> |              | <b>AmortizedMarket</b> |              |
|--|------------------------|--------------|------------------------|--------------|
|  | <b>Cost</b>            | <b>Value</b> | <b>Cost</b>            | <b>Value</b> |
|  | <b>(in thousands)</b>  |              |                        |              |
| Due in one year or less                | \$30,271               | \$30,200     | \$59,113               | \$59,194     |
| Due after one year through five years  | 103,548                | 102,019      | 60,908                 | 61,113       |
| Due after five years through ten years | -                      | -            | -                      | -            |
| Total held to maturity securities      | \$133,819              | \$132,219    | \$120,021              | \$120,307    |
| Less current portion                   | 30,271                 | 30,200       | 59,113                 | 59,194       |
| Long term held to maturity securities  | \$103,548              | \$102,019    | \$60,908               | \$61,113     |

Proceeds from the redemption and sale of marketable securities were \$21,964,000 and \$51,417,000 in the three and nine months ended June 30, 2018, and \$9,577,000 and \$14,681,000 in the three and nine months ended June 24, 2017, respectively. Losses of \$35,000 and \$32,000 were recorded in the three and nine months ended June 30, 2018, respectively and gains of \$13,000 were recorded in the three and nine months ended June 24, 2017. We use the specific identification method to determine the cost of securities sold.

Note 12 Changes to the components of accumulated other comprehensive loss are as follows:

|  | Three Months Ended<br>June 30, 2018<br>(unaudited)<br>(in thousands) |   |            | Nine Months Ended<br>June 30, 2018<br>(unaudited)<br>(in thousands) |   |            |
|--|--|---|------------|---|---|------------|
|  | Foreign<br>Currency<br>Translation<br>Adjustment                     | Unrealized<br>Holding<br>Gain<br>(Loss)<br>on<br>Marketable<br>Securities | Total      | Foreign<br>Currency<br>Translation<br>Adjustment                    | Unrealized<br>Holding<br>Gain<br>(Loss)<br>on<br>Marketable<br>Securities | Total      |
| Beginning Balance  | \$(11,330)   | \$ 172  | \$(11,158) | \$(9,341 )  | \$ 466  | \$(8,875 ) |
| Other comprehensive loss before reclassifications                | (2,359 )   | (328 )  | (2,687 )   | (4,348 )  | (622 )  | (4,970 )   |
| Amounts reclassified from accumulated other comprehensive income | -  | 75  | 75         | -   | 75  | 75         |
| Ending Balance   | \$(13,689)   | \$ (81 )  | \$(13,770) | \$(13,689)  | \$ (81 )  | \$(13,770) |



|  | Three Months Ended<br>June 24, 2017<br>(unaudited)<br>(in thousands) |  |            | Nine Months Ended<br>June 24, 2017<br>(unaudited)<br>(in thousands) |  |            |
|--|--|--|------------|---|--|------------|
|  | Foreign<br>Currency<br>Translation<br>Adjustment                     | Unrealized<br>Holding<br>Gain on<br>Marketable<br>Securities | Total      | Foreign<br>Currency<br>Translation<br>Adjustment                    | Unrealized<br>Holding<br>Loss<br>(Gain) on<br>Marketable<br>Securities | Total      |
| Beginning Balance  | \$(12,296)   | \$ 166   | \$(12,130) | \$(13,086)  | \$ (329 )  | \$(13,415) |
| Other comprehensive income before reclassifications              | 1,095  | 204  | 1,299      | 1,885   | 699  | 2,584      |
| Amounts reclassified from accumulated other comprehensive income | -  | -  | -          | -   | -  | -          |
| Ending Balance   | \$(11,201)   | \$ 370   | \$(10,831) | \$(11,201)  | \$ 370   | \$(10,831) |

Note 13 On December 30, 2016, we acquired Hill & Valley Inc., a premium bakery located in Rock Island, IL, for approximately \$31 million. Hill & Valley, with sales of over \$45 million annually, is a manufacturer of a variety of pre-baked cakes, cookies, pies, muffins and other desserts to retail in-store bakeries. Hill & Valley is a leading brand of Sugar Free and No Sugar Added pre-baked in-store bakery items. Additionally, Hill & Valley sustains strategic private labeling partnerships with retailers nationwide.

On May 22, 2017, we acquired an ICEE distributor doing business in Georgia and Tennessee for approximately \$11 million.

On August 16, 2017, we acquired Labriola Baking Company, a bakery of breads and artisan soft pretzels located in Alsip, IL for approximately \$6 million. Labriola Bakery, with sales of approximately \$17 million annually, is a manufacturer of pre-baked breads, rolls and soft pretzels for retail in-store bakery and foodservice outlets nationwide.

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

### Liquidity and Capital Resources

Our current cash and cash equivalents balances, investments and cash expected to be provided by future operations are our primary sources of liquidity. We believe that these sources, along with our borrowing capacity, are sufficient to fund future growth and expansion. See Note 11 to these financial statements for a discussion of our investment securities.

The Company's Board of Directors declared a regular quarterly cash dividend of \$.45 per share of its common stock payable on July 5, 2018, to shareholders of record as of the close of business on June 14, 2018.

In our fiscal year ended September 30, 2017, we purchased and retired 142,665 shares of our common stock at a cost of \$18,228,763. In the three and nine months ended June 30, 2018, we purchased and retired 20,604 shares of our common stock at a cost of \$2,794,027. On August 4, 2017 the Company's Board of Directors authorized the purchase and retirement of 500,000 shares of the Company's common stock; 384,446 shares remain to be purchased under this authorization.

In the three months ended June 30, 2018 and June 24, 2017 fluctuations in the valuation of the Mexican and Canadian currencies and the resulting translation of the net assets of our Mexican and Canadian subsidiaries caused an increase of \$2,359,000 in accumulated other comprehensive loss in the 2018 third quarter and a decrease of \$1,095,000 in accumulated other comprehensive loss in the 2017 third quarter. In the nine-month period, fluctuations in the valuation of the Mexican and Canadian currencies and the resulting translation of the net assets of our Mexican and Canadian subsidiaries caused an increase of \$4,348,000 in accumulated other comprehensive loss in the 2018 nine-month period and decrease of \$1,885,000 in accumulated other comprehensive loss in the 2017 nine-month period.

Our general-purpose bank credit line which expires in November 2021 provides for up to a \$50,000,000 revolving credit facility. The agreement contains restrictive covenants and requires commitment fees in accordance with standard banking practice. There were no outstanding balances under this facility at June 30, 2018.

## Results of Operations

Net sales increased \$10,824,000 or 4% to \$306,239,000 for the three months and \$70,052,000 or 9% to \$837,550,000 for the nine months ended June 30, 2018 compared to the three and nine months ended June 24, 2017. Excluding first twelve months' sales from Hill & Valley, Inc., acquired in January 2017, an ICEE distributor located in the Southeast acquired in June 2017 and Labriola Bakery which was acquired in August 2017, sales for the three months increased \$6,329,000 or 2% from last year and sales for the nine months increased \$38,365,000, or 5% from last year.

## FOOD SERVICE

Sales to food service customers increased \$8,591,000 or 5% in the third quarter to \$191,701,000 and increased \$55,945,000 or 11% for the nine months. Excluding first twelve months' sales of Hill & Valley and Labriola, sales

increased \$4,596,000 or 3% for the third quarter and \$26,161,000 or 5% for the nine months. Soft pretzel sales to the food service market increased 20% to \$53,880,000 in the three months and 17% to \$151,649,000 in the nine months and about 11% and 10% in the three and nine months without Labriola sales. In addition to Labriola sales, soft pretzel sales increased significantly due to increased distribution to restaurant chains and movie theatres and we had strong sales of our recently introduced BRAUHAUS pretzels.

Frozen juices and ices sales decreased 21% to \$12,825,000 in the three months and decreased 12% to \$29,448,000 in the nine months due entirely to lower sales to warehouse club stores because of a loss of a promotion and because of reduced distribution.

Churro sales to food service customers were down 5% in the third quarter to \$16,739,000 and were essentially unchanged at \$46,603,000 in the nine months, with sales increases and decreases across our customer base but with particularly lower sales to one warehouse club store in the third quarter which last year had sales of a new product since discontinued.

Sales of bakery products increased \$3,370,000 or 4% in the third quarter to \$93,082,000 and increased \$30,033,000 or 12% for the nine months. Excluding sales of Hill & Valley and Labriola, bakery sales were up 3% for the quarter and 4% for the year primarily due to increased sales to several customers.

Sales of handhelds increased \$1,400,000 or 16% in the third quarter and \$6,512,000 or 27% for the nine months with the increase in both periods coming primarily from sales to two customers. Sales of funnel cake decreased \$535,000 or 10% in the quarter to \$5,094,000 and increased \$1,512,000 or 11% for the nine months to \$15,435,000 as we continue to increase sales to school food service. Sales of a limited time only funnel cake sold for distribution into independent fast food restaurant chains were down approximately \$350,000 in both periods compared to a year ago and lower sales to one fast food restaurant chain accounted for the balance of the decrease in this year's quarter's sales.

Sales of new products in the first twelve months since their introduction were approximately \$4 million in this quarter and \$17 million in the nine months. Price increases accounted for approximately \$2.4 million of sales in the quarter and \$6.0 million of sales in the nine months and net volume increases, including new product sales as defined above and Hill & Valley and Labriola sales, accounted for approximately \$6 million of sales in the quarter and \$50 million of sales in the nine months.

Operating income in our Food Service segment decreased from \$22,005,000 to \$19,663,000 in the third quarter and decreased from \$58,695,000 to \$54,098,000 in the nine months. Last year's operating income in the third quarter and nine months benefited from a \$1.8 million gain on an insurance recovery related to product quality issues in our 2016 fiscal year which was recorded as a reduction of cost of goods sold. This year's quarter and nine months was impacted by approximately \$1.3 million and \$3.3 million, respectively, of higher distribution expenses primarily due to higher fuel costs and the recent implementation of the electronic logging device mandate. Additionally, lower sales of our MARY B's biscuits and related costs due to our recall in early January impacted our operating income by approximately \$500,000 in the third quarter and \$1.0 million in the nine months. Hill & Valley contributed improved operating income of \$364,000 in the third quarter and \$2.1 million in the nine months. For the third quarter and nine months, operating income in the balance of our food service business was impacted by generally higher costs for payroll and insurance, added personnel in the selling function, product mix changes and significantly lower volume concentrated in specific facilities and higher ingredients costs. Operating income in the first quarter was impacted by inefficiencies at our recently acquired Labriola production facility (compounded by the integration of products previously manufactured at other facilities) and shutdown costs of our Chambersburg facility; both of which had little impact beyond the first quarter.

## RETAIL SUPERMARKETS

Sales of products to retail supermarkets increased \$390,000 or 1% to \$38,532,000 in the third quarter and increased \$4,319,000 or 5% in the nine months. Soft pretzel sales for the third quarter were down 2% to \$7,332,000 and up 9% to \$27,925,000 for the nine months. The nine month increase was primarily due to sales of AUNTIE ANNE'S\* soft pretzels under a license agreement entered into in 2017. Sales of frozen juices and ices increased \$1,468,000 or 5% to \$28,785,000 in the third quarter and were up \$3,591,000 or 7% to \$53,950,000 for the nine months primarily due to sales of SOUR PATCH KIDS\*\* frozen novelties under a new license agreement. Handheld sales to retail supermarket customers decreased 17% to \$2,960,000 in the third quarter and decreased 16% to \$8,749,000 for the nine months as the sales of this product line in retail supermarkets continues their long term decline.

Sales of new products in the third quarter were approximately \$3 million and were \$7 million for the nine months. Price increases had no impact on sales in the quarter and nine months and net volume increases, including new product sales as defined above accounted for \$390,000 of sales in the quarter and \$4.3 million of sales in the nine months.

Operating income in our Retail Supermarkets segment was \$3,203,000 in this year's third quarter compared to \$4,890,000 in last year's quarter and was \$8,295,000 in this year's nine months compared to \$8,390,000 in last year's nine months. Contributions to the lower operating income in this year's quarter were lower sales of soft pretzels and LUIGI'S Real Italian Ice and increases in trade spending, coupon redemptions and distribution costs.

\* AUNTIE ANNE'S is a registered trademark of Auntie Anne's LLC.

\*\*SOUR PATCH KIDS is a registered trademark of Mondelez International Group

## FROZEN BEVERAGES

Frozen beverage and related product sales increased 2% to \$76,006,000 in the third quarter and increased 5% to \$194,428,000 in the nine month period. Excluding sales of the acquired ICEE distributor, frozen beverages and related product sales were up about 2% for the third quarter and 4% for the nine month period. Beverage sales alone were up 3% to \$50,343,000 in the third quarter and up 9% to \$118,932,000 for the nine months. Without the acquired ICEE distributor, beverage sales alone were up about 2% for the quarter and 8% for the nine months. Gallon sales were up 7% for the third quarter and 7% for the nine months with higher sales to movie theatres and across our customer base. Service revenue increased 6% to \$19,693,000 in the third quarter and 7% to \$58,005,000 for the nine months with sales increases concentrated to several customers.

Sales of beverage machines, which tend to fluctuate from year to year while following no specific trend, were \$5,644,000, a decrease of 13% for the quarter, and \$16,652,000, a decrease of 19% for the nine month period.

Operating income in our Frozen Beverage segment increased to \$12,003,000 in this year's quarter and to \$17,245,000 for this year's nine months compared to \$10,905,000 and \$14,153,000 in last years' quarter and nine months, respectively, as a result of higher beverage sales and service revenue.

## CONSOLIDATED

Gross profit as a percentage of sales was 30.85% in the third quarter and 32.08% last year. Gross profit as a percentage of sales was 29.26% in the nine month period this year and 30.42% last year. Without the gain on insurance recovery of \$1.8 million recorded in last year's third quarter related to certain product quality issues in our 2016 fiscal year, gross profit as a percentage of sales would have been 31.48% in last year's third quarter and 30.19% in the nine months last year. For the nine months, the decrease was caused by higher costs for payroll and insurance, inefficiencies in our recently acquired Labriola production facility (compounded by the integration of products previously manufactured at other facilities), product mix changes, significantly lower volume concentrated in specific facilities, lower sales of our MARY B'S biscuits and related costs due to our recall in early January, shutdown costs of our Chambersburg, PA production facility and higher ingredients costs. Of these, the inefficiencies at Labriola and shutdown costs of our Chambersburg facility had little impact in our third quarter.

Total operating expenses increased \$2,642,000 in the third quarter and as a percentage of sales increased to 19.5% from 19.3% last year. For the nine months, operating expenses increased \$13,156,000, and as a percentage of sales decreased from 19.8% to 19.7%. Marketing expenses decreased to 8.4% of sales in this year's quarter from 8.7% last year primarily because of lower spending to support warehouse club store sales in our foodservice business and lower marketing expenses of the acquired Labriola business. Marketing expenses were 8.3% in this year's nine months



compared to 8.8% of sales in last year's nine months primarily because of lower media spending in our retail supermarket business in the first six months of the year, lower spending to support warehouse club store sales in our foodservice business and lower marketing expenses of the acquired Hill & Valley and Labriola businesses. Distribution expenses were 7.9% of sales in the third quarter and 7.4% of sales in last year's quarter and were 8.1% in this year's nine months compared to 7.6% of sales in last year's nine months. Distribution expenses have increased due to higher fuel costs and the recent implementation of the electronic logging device mandate. We expect distribution expenses to remain higher for at least the remainder of our 2018 fiscal year. Administrative expenses were 3.2% of sales in the third quarter compared to 3.2% of sales last year in the third quarter and were 3.3% in this year's nine months compared to 3.4% of sales in last year's nine months.

Operating income decreased \$2,931,000 or 8% to \$34,869,000 in the third quarter and decreased \$1,600,000 or 2% to \$79,638,000 in the nine months as a result of the aforementioned items.

Investment income increased by \$283,000 and \$863,000 in the third quarter and nine months, respectively, resulting from higher amounts invested and higher interest rates.

Other income for this year's nine months includes a \$520,000 gain on a sale of property; other expense in last year's quarter and nine months includes \$53,000 and \$567,000, respectively, of acquisition costs for the Hill & Valley and ICEE distributor purchases.

Net earnings increased \$825,000, or 3%, in the current three month period to \$26,129,000 and were \$80,211,000 for the nine month period this year compared to \$54,831,000 for the nine month period last year.

Net earnings for the nine months ended June 30, 2018 benefited from a \$20.9 million, or \$1.11 per diluted share, gain on the remeasurement of deferred tax liabilities and a \$7.4 million, or \$0.40 per diluted share, reduction in income taxes related primarily to the lower corporate tax rate enacted under the Tax Cuts and Jobs Act in December 2017. Net earnings for the nine months were impacted by a \$1.2 million, or \$.06 per diluted share, provision for the one time repatriation tax required under the new tax law. For the three months ended June 30, 2018, net earnings benefited by a \$3.5 million, or \$.18 per diluted share, reduction in income taxes primarily related to the lower corporate tax rate. Excluding the deferred tax gain and the one-time repatriation tax, our effective tax rate decreased to 28.1% from 35.4% in the prior year quarter and to 28.4% from 35.0% in prior year nine months reflecting the reduction in the federal statutory rate to 21% from 35% on January 1, 2018. Last year's nine months' effective tax rate benefited from an unusually high tax benefit on share based compensation of \$2,060,000 which compares to this year's nine month's tax benefit of \$909,000. We are presently estimating an effective tax rate of 28-29% for the last quarter of our fiscal year 2018 and 26-27% for our fiscal year 2019.

There are many factors which can impact our net earnings from year to year and in the long run, among which are the supply and cost of raw materials and labor, insurance costs, factors impacting sales as noted above, the continuing consolidation of our customers, our ability to manage our manufacturing, marketing and distribution activities, our ability to make and integrate acquisitions and changes in tax laws and interest rates.

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

There has been no material change in the Company's assessment of its sensitivity to market risk since its presentation set forth, in item 7a. "Quantitative and Qualitative Disclosures About Market Risk," in its 2017 annual report on Form 10-K filed with the SEC.

### Item 4. Controls and Procedures

The Chief Executive Officer and the Chief Financial Officer of the Company (its principal executive officer and principal financial officer, respectively) have concluded, based on their evaluation as of June 30, 2018, that the Company's disclosure controls and procedures are effective to ensure that information required to be disclosed by the Company in the reports filed or submitted by it under the Securities Exchange Act of 1934, as amended, is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and include controls and procedures designed to ensure that information required to be disclosed by the Company in such reports is accumulated and communicated to the Company's management, including the Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

There has been no change in the Company's internal control over financial reporting during the quarter ended June 30, 2018, that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II. OTHER INFORMATION

Item 6. Exhibits

Exhibit  
No.

31.1 & Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

31.2

99.5 Certification Pursuant to the 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the  
& Sarbanes-Oxley Act of 2002

99.6

- 101.1 The following financial information from J&J Snack Foods Corp.'s Quarterly Report on Form 10-Q for the quarter ended June 30, 2018, formatted in XBRL (extensible Business Reporting Language):
- (i) Consolidated Balance Sheets,
  - (ii) Consolidated Statements of Earnings,
  - (iii) Consolidated Statements of Comprehensive Income,
  - (iv) Consolidated Statements of Cash Flows and
  - (v) the Notes to the Consolidated Financial Statements

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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.

J & J SNACK FOODS CORP.

Dated: August 2, 2018

/s/ Gerald B. Shreiber

Gerald B. Shreiber

Chairman of the Board,

President, Chief Executive

Officer and Director

(Principal Executive Officer)

Dated: August 2, 2018

/s/ Dennis G. Moore

Dennis G. Moore, Senior Vice

President, Chief Financial

Officer and Director

(Principal Financial Officer)

(Principal Accounting Officer)