

MERIDIAN BIOSCIENCE INC

Form 10-Q

August 08, 2008

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**SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549  
Form 10-Q**

**QUARTERLY REPORT PURSUANT TO SECTION 13 or 15(d) OF THE SECURITIES  
EXCHANGE ACT OF 1934  
For the Quarterly Period Ended June 30, 2008**

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 0-14902  
MERIDIAN BIOSCIENCE, INC.**

Incorporated under the laws of Ohio

31-0888197

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

3471 River Hills Drive  
Cincinnati, Ohio 45244  
(513) 271-3700

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

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

(Do not check if a smaller reporting company)

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

Yes  No

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

| Class                      | Outstanding July 31, 2008 |
|----------------------------|---------------------------|
| Common Stock, no par value | 40,220,808                |

**MERIDIAN BIOSCIENCE, INC. AND SUBSIDIARIES  
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*The Private Securities Litigation Reform Act of 1995 provides a safe harbor from civil litigation for forward-looking statements accompanied by meaningful cautionary statements. Except for historical information, this report contains forward-looking statements which may be identified by words such as "estimates", "anticipates", "projects", "plans", "seeks", "may", "will", "expects", "intends", "believes", "should" and similar expressions or the negative versions thereof and which also may be identified by their context. Such statements, whether expressed or implied, are based upon current expectations of the Company and speak only as of the date made. The Company assumes no obligation to publicly update any forward-looking statements. These statements are subject to various risks, uncertainties and other factors that could cause actual results to differ materially, including, without limitation, the following: Meridian's continued growth depends, in part, on its ability to introduce into the marketplace enhancements of existing products or new products that incorporate technological advances, meet customer requirements and respond to products developed by Meridian's competition. While Meridian has introduced a*

*number of internally developed products, there can be no assurance that it will be successful in the future in introducing such products on a timely basis. Ongoing consolidations of reference laboratories and formation of multi-hospital alliances may cause adverse changes to pricing and distribution. Costs and difficulties in complying with laws and regulations administered by the United States Food and Drug Administration can result in unanticipated expenses and delays and interruptions to the sale of new and existing products. Changes in the relative strength or weakness of the US dollar can change expected results. One of Meridian's main growth strategies is the acquisition of companies and product lines. There can be no assurance that additional acquisitions will be consummated or that, if consummated, will be successful and the acquired businesses successfully integrated into Meridian's operations. In addition to the factors described in this paragraph, Part I, Item 1A Risk Factors of our Form 10-K contains a list of uncertainties and risks that may affect the financial performance of the Company.*

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**MERIDIAN BIOSCIENCE, INC. AND SUBSIDIARIES**  
**Consolidated Statements of Operations (Unaudited)**  
(in thousands, except per share data)

|   | <b>Three Months<br/>Ended June 30,</b> |             | <b>Nine Months<br/>Ended June 30,</b> |             |
|---|--|-------------|---------------------------------------|-------------|
|   | <b>2008</b>                            | <b>2007</b> | <b>2008</b>                           | <b>2007</b> |
| NET SALES   | \$33,068                               | \$29,763    | \$103,164                             | \$90,577    |
| COST OF SALES                                     | 11,781                                 | 10,462      | 39,010                                | 34,826      |
| Gross profit                                      | 21,287                                 | 19,301      | 64,154                                | 55,751      |
| <b>OPERATING EXPENSES:</b>                        |  |             |                                       |             |
| Research and development                          | 1,322                                  | 1,306       | 4,372                                 | 4,339       |
| Sales and marketing                               | 4,459                                  | 4,072       | 13,697                                | 12,331      |
| General and administrative                        | 4,507                                  | 4,435       | 13,155                                | 12,686      |
| Total operating expenses                          | 10,288                                 | 9,813       | 31,224                                | 29,356      |
| Operating income                                  | 10,999                                 | 9,488       | 32,930                                | 26,395      |
| <b>OTHER INCOME (EXPENSE):</b>                    |  |             |                                       |             |
| Interest income                                   | 297                                    | 409         | 1,148                                 | 1,161       |
| Interest expense                                  |  |             |                                       | (38)        |
| Other, net  | 183                                    | (45)        | 156                                   | 46          |
| Total other income (expense)                      | 480                                    | 364         | 1,304                                 | 1,169       |
| Earnings before income taxes                      | 11,479                                 | 9,852       | 34,234                                | 27,564      |
| INCOME TAX PROVISION                              | 3,716                                  | 1,038       | 11,716                                | 7,287       |
| NET EARNINGS                                      | \$ 7,763                               | \$ 8,814    | \$ 22,518                             | \$20,277    |
| BASIC EARNINGS PER COMMON SHARE                   | \$ 0.19                                | \$ 0.22     | \$ 0.56                               | \$ 0.51     |
| DILUTED EARNINGS PER COMMON SHARE                 | \$ 0.19                                | \$ 0.22     | \$ 0.55                               | \$ 0.50     |
| AVERAGE NUMBER OF COMMON SHARES OUTSTANDING BASIC | 40,150                                 | 39,729      | 40,043                                | 39,462      |

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|  |         |         |         |         |
|--|---------|---------|---------|---------|
| DILUTIVE COMMON STOCK OPTIONS                          | 900     | 991     | 975     | 968     |
| AVERAGE NUMBER OF COMMON<br>SHARES OUTSTANDING DILUTED | 41,050  | 40,720  | 41,018  | 40,430  |
| ANTI-DILUTIVE SECURITIES:                              |         |         |         |         |
| Common stock options                                   | 100     | 5       | 52      | 3       |
| DIVIDENDS DECLARED PER COMMON<br>SHARE                 | \$ 0.14 | \$ 0.11 | \$ 0.39 | \$ 0.29 |

The accompanying notes are an integral part of these consolidated financial statements.

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**MERIDIAN BIOSCIENCE, INC. AND SUBSIDIARIES**  
**Consolidated Statements of Cash Flows (Unaudited)**  
**(dollars in thousands)**

| <b>Nine Months Ended June 30,</b>                                      | <b>2008</b> | <b>2007</b> |
|--|-------------|-------------|
| <b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>                           |             |             |
| Net earnings   | \$ 22,518   | \$ 20,277   |
| Non-cash items:  |             |             |
| Depreciation of property, plant and equipment                          | 2,142       | 2,065       |
| Amortization of intangible assets and deferred costs                   | 1,206       | 1,227       |
| Stock based compensation   | 1,190       | 1,231       |
| Discrete tax contingency reserve adjustment                            |             | (2,425)     |
| Deferred income taxes  | 649         | 1,073       |
| Loss on disposition of fixed assets                                    | 52          | 2           |
| Change in accounts receivable, inventory, and prepaid expenses         | (1,073)     | 369         |
| Change in accounts payable, accrued expenses, and income taxes payable | (4,274)     | (5,300)     |
| Other  | (276)       | (92)        |
| Net cash provided by operating activities                              | 22,134      | 18,427      |
| <b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>                           |             |             |
| Acquisitions of property, plant and equipment                          | (2,905)     | (2,168)     |
| Proceeds from sales of property, plant and equipment                   | 12          | 4           |
| Purchase of intangibles and other assets                               | (1,108)     | (265)       |
| Acquisition earnout payments   | (157)       | (971)       |
| (Purchases) proceeds from sales of short-term investments              | (7,750)     | 4,000       |
| Net cash provided by (used for) investing activities                   | (11,908)    | 600         |
| <b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>                           |             |             |
| Repayment of debt obligations  |             | (29)        |
| Dividends paid   | (15,624)    | (11,461)    |
| Proceeds and tax benefits from exercises of stock options              | 2,780       | 2,017       |
| Net cash used for financing activities                                 | (12,844)    | (9,473)     |
| Effect of Exchange Rate Changes on Cash and Equivalents                | 268         | 104         |
| Net Increase (Decrease) in Cash and Equivalents                        | (2,350)     | 9,658       |
| Cash and Equivalents at Beginning of Period                            | 49,400      | 36,348      |
| Cash and Equivalents at End of Period                                  | \$ 47,050   | \$ 46,006   |

The accompanying notes are an integral part of these consolidated financial statements.

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**MERIDIAN BIOSCIENCE, INC. AND SUBSIDIARIES**  
**Consolidated Balance Sheets (Unaudited)**  
**(dollars in thousands)**

ASSETS

|   | <b>June 30,<br/>2008</b> | <b>September<br/>30,<br/>2007</b> |
|---|--------------------------|-----------------------------------|
| <b>CURRENT ASSETS:</b>                                  |                          |                                   |
| Cash and equivalents                                    | \$ 47,050                | \$ 49,400                         |
| Accounts receivable, less allowances of \$229 and \$258 | 22,134                   | 22,651                            |
| Inventories   | 21,034                   | 18,171                            |
| Prepaid expenses and other current assets               | 2,251                    | 2,147                             |
| Deferred income taxes                                   | 1,791                    | 1,376                             |
| <br>  |                          |                                   |
| Total current assets                                    | 94,260                   | 93,745                            |
| <br>  |                          |                                   |
| <b>PROPERTY, PLANT AND EQUIPMENT:</b>                   |                          |                                   |
| Land  | 908                      | 890                               |
| Buildings and improvements                              | 17,045                   | 16,907                            |
| Machinery, equipment and furniture                      | 26,141                   | 24,619                            |
| Construction in progress                                | 2,482                    | 1,290                             |
| <br>  |                          |                                   |
| Subtotal  | 46,576                   | 43,706                            |
| Less: accumulated depreciation and amortization         | 27,502                   | 25,395                            |
| <br>  |                          |                                   |
| Net property, plant and equipment                       | 19,074                   | 18,311                            |
| <br>  |                          |                                   |
| <b>OTHER ASSETS:</b>                                    |                          |                                   |
| Goodwill  | 9,965                    | 9,964                             |
| Other intangible assets, net                            | 9,197                    | 9,457                             |
| Restricted cash   | 1,000                    | 1,000                             |
| Investments in auction rate securities                  | 7,518                    |                                   |
| Other assets  | 216                      | 221                               |
| <br>  |                          |                                   |
| Total other assets                                      | 27,896                   | 20,642                            |
| <br>  |                          |                                   |
| <b>TOTAL ASSETS</b>                                     | <b>\$141,230</b>         | <b>\$132,698</b>                  |

The accompanying notes are an integral part of these consolidated financial statements.

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**MERIDIAN BIOSCIENCE, INC. AND SUBSIDIARIES**  
**Consolidated Balance Sheets (Unaudited)**  
**(dollars in thousands)**  
LIABILITIES AND SHAREHOLDERS' EQUITY

|   | <b>June 30,<br/>2008</b> | <b>September<br/>30,<br/>2007</b> |
|---|--------------------------|-----------------------------------|
| <b>CURRENT LIABILITIES:</b>   |                          |                                   |
| Accounts payable  | \$ 3,266                 | \$ 4,704                          |
| Accrued employee compensation costs   | 4,640                    | 7,541                             |
| Purchase business combination liability   |                          | 152                               |
| Other accrued expenses  | 4,768                    | 4,008                             |
| Income taxes payable  | 1,665                    | 662                               |
| <br>  |                          |                                   |
| Total current liabilities   | 14,339                   | 17,067                            |
| <br>  |                          |                                   |
| DEFERRED INCOME TAXES   | 2,517                    | 2,683                             |
| <br>  |                          |                                   |
| <b>COMMITMENTS AND CONTINGENCIES</b>  |                          |                                   |
| <br>  |                          |                                   |
| <b>SHAREHOLDERS' EQUITY:</b>  |                          |                                   |
| <br>  |                          |                                   |
| Preferred stock, no par value, 1,000,000 shares authorized, none issued   |                          |                                   |
| <br>  |                          |                                   |
| Common shares, no par value, 71,000,000 shares authorized, 40,156,082 and<br>39,847,391 shares issued, respectively |                          |                                   |
| Additional paid-in capital  | 86,614                   | 82,209                            |
| Retained earnings   | 36,964                   | 30,375                            |
| Accumulated other comprehensive income  | 796                      | 364                               |
| <br>  |                          |                                   |
| Total shareholders' equity  | 124,374                  | 112,948                           |
| <br>  |                          |                                   |
| <b>TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY</b>   | <b>\$ 141,230</b>        | <b>\$ 132,698</b>                 |

The accompanying notes are an integral part of these consolidated financial statements.

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**MERIDIAN BIOSCIENCE, INC. AND SUBSIDIARIES**  
**Consolidated Statement of Changes in Shareholders' Equity (Unaudited)**  
**(dollars and shares in thousands)**

|  | Common<br>Shares<br><br>Issued | Additional<br>Paid-in<br>Capital | Retained<br>Earnings | Accumulated<br>Other<br>Comprehensive<br>Income<br>(Loss) | Comprehensive<br>Income<br>(Loss) | Total<br>Shareholders'<br>Equity |
|--|--------------------------------|----------------------------------|----------------------|---|-----------------------------------|----------------------------------|
| <b>Balance at<br/>September 30, 2007</b>   | 39,847                         | \$ 82,209                        | \$ 30,375            | \$ 364  |                                   | \$ 112,948                       |
| Adoption of FASB<br>Interpretation No. 48  |                                |                                  | (305)                |   |                                   | (305)                            |
| Dividends paid                             |                                |                                  | (15,624)             |   |                                   | (15,624)                         |
| Exercise of stock<br>options, net of tax   | 309                            | 3,215                            |                      |   |                                   | 3,215                            |
| Stock based<br>compensation                |                                | 1,190                            |                      |   |                                   | 1,190                            |
| Comprehensive income:                      |                                |                                  |                      |   |                                   |                                  |
| Net earnings                               |                                |                                  | 22,518               |   | \$ 22,518                         | 22,518                           |
| Hedging activity                           |                                |                                  |                      | (144)   | (144)                             | (144)                            |
| Unrealized loss on<br>investments          |                                |                                  |                      | (233)   | (233)                             | (233)                            |
| Other comprehensive<br>income taxes        |                                |                                  |                      | (235)   | (235)                             | (235)                            |
| Foreign currency<br>translation adjustment |                                |                                  |                      | 1,044   | 1,044                             | 1,044                            |
| Comprehensive income                       |                                |                                  |                      |   | \$ 22,950                         |                                  |
| <br><b>Balance at June 30,<br/>2008</b>    | <br>40,156                     | <br>\$ 86,614                    | <br>\$ 36,964        | <br>\$ 796  |                                   | <br>\$ 124,374                   |

The accompanying notes are an integral part of these consolidated financial statements.

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**MERIDIAN BIOSCIENCE, INC. AND SUBSIDIARIES**  
**Notes to Consolidated Financial Statements**  
**(Unaudited)**

**1. Basis of Presentation:**

The consolidated financial statements included herein have not been audited by an independent registered public accounting firm, but include all adjustments (consisting of normal recurring entries), which are, in the opinion of management, necessary for a fair presentation of the results for such periods.

Certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been omitted pursuant to the requirements of the Securities and Exchange Commission. We believe that the disclosures included in these financial statements are adequate to make the information not misleading.

It is suggested that these consolidated interim financial statements be read in conjunction with the consolidated annual financial statements and notes thereto, included in Meridian's Annual Report on Form 10-K for the Year Ended September 30, 2007.

The results of operations for the interim periods are not necessarily indicative of the results to be expected for the year.

**2. Significant Accounting Policies:**

***(a) Revenue Recognition***

Revenue is generally recognized from sales when product is shipped and title has passed to the buyer. Revenue for the US Diagnostics operating segment is reduced at the date of sale for estimated rebates that will be claimed by customers. We estimate accruals for rebate agreements based on historical statistics, current trends, and other factors. Changes to the accruals are recorded in the period that they become known. Our rebate accruals were \$2,980,000 at June 30, 2008 and \$2,415,000 at September 30, 2007.

Life Science revenue for contract services may come from standalone arrangements for process development and/or optimization work (contract research and development services) or custom manufacturing, or multiple-deliverable arrangements that include process development work followed by larger-scale manufacturing (both contract research and development services and contract manufacturing services). Revenue is recognized based on the nature of the arrangements, using the principles in EITF 00-21, *Revenue Arrangements with Multiple Deliverables*. The framework in EITF 00-21 is based on each of the multiple deliverables in a given arrangement having distinct and separate fair values. Fair values are determined via consistent pricing between standalone arrangements and multiple deliverable arrangements, as well as a competitive bidding process. Contract research and development services may be performed on a time and materials basis or fixed fee basis. For time and materials arrangements, revenue is recognized as services

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are performed and billed. For fixed fee arrangements, revenue is recognized upon completion and acceptance by the customer.

For contract manufacturing services, revenue is generally recognized upon delivery of product and acceptance by the customer. In some cases, customers may request that we store on their behalf, clinical grade biologicals that we produce under contract manufacturing agreements. These cases arise when customers do not have clinical grade storage facilities or do not want to risk contamination during transport. For such cases, revenue may be recognized on a bill-and-hold basis pursuant to the satisfaction of criteria in SEC Staff Accounting Bulletins Nos. 101 and 104 related to bill-and-hold revenue recognition.

**(b) Comprehensive Income**

Comprehensive income represents the net change in shareholders' equity during a period from sources other than transactions with shareholders. Our comprehensive income is comprised of net earnings, foreign currency translation, changes in the fair value of forward exchange contracts accounted for as cash flow hedges, and changes in the fair value of available-for-sale fixed income securities.

Assets and liabilities of foreign operations are translated using period-end exchange rates with gains or losses resulting from translation included in accumulated other comprehensive income or loss. Revenues and expenses are translated using exchange rates prevailing during the period. We also recognize foreign currency transaction gains and losses on certain assets and liabilities that are denominated in the Euro currency. These gains and losses are included in other income and expense in the accompanying consolidated statements of operations.

Comprehensive income for the interim periods was as follows (in thousands):

|   | <b>Three Months<br/>Ended June 30,</b> |             | <b>Nine Months<br/>Ended June 30,</b> |             |
|---|--|-------------|---------------------------------------|-------------|
|   | <b>2008</b>                            | <b>2007</b> | <b>2008</b>                           | <b>2007</b> |
| Net earnings                            | \$7,763                                | \$8,814     | \$22,518                              | \$20,277    |
| Hedging activity                        | 230                                    | 5           | (144)                                 | (28)        |
| Unrealized loss on investments          |  |             | (233)                                 |             |
| Income taxes                            | (84)                                   | (34)        | (235)                                 | (151)       |
| Foreign currency translation adjustment | 10                                     | 91          | 1,044                                 | 455         |
| Comprehensive income                    | \$7,919                                | \$8,876     | \$22,950                              | \$20,553    |

**(c) Income Taxes**

The provision for income taxes includes federal, foreign, state, and local income taxes currently payable and those deferred because of temporary differences between income for financial reporting and income for tax purposes. We prepare estimates of permanent and temporary differences between income for financial reporting purposes and income for tax purposes which are adjusted to actual upon filing of our tax returns, which typically occurs in the third and fourth quarters of the current fiscal year for the preceding fiscal year's estimates.

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On October 1, 2007, we adopted FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes* (FIN 48). FIN 48 prescribes a comprehensive model for the recognition, measurement, presentation and disclosure of uncertain tax positions, assuming full knowledge of all relevant facts by the applicable tax authorities. The cumulative effect of adopting FIN 48, \$305,000, was charged to opening retained earnings. As of October 1, 2007, Meridian's liability for uncertain tax positions was \$856,000, including estimated penalties and interest. Meridian's liability for uncertain tax positions was reduced to \$736,000 as of June 30, 2008, related to activity during the first three quarters of fiscal 2008, as well as currency translation. This liability is included in current income taxes payable in the accompanying consolidated balance sheet. Penalties and interest are a component of the income tax provision. The full amount of \$736,000 would favorably affect our effective tax rate if recognized. The amount of Meridian's liability for uncertain tax positions expected to be paid or settled in the next 12 months is uncertain.

We are subject to examination by the tax authorities in the US (both federal and state) and the countries of Belgium, France, Holland and Italy. In the US, open tax years are for fiscal 2005 and forward, although, we recently completed an examination by the IRS for fiscal 2006. In countries outside the US, open tax years generally range from fiscal 2002 and forward. However, in Belgium, the utilization of local net operating loss carryforwards extends the statute of limitations for examination well into the foreseeable future.

In fiscal 2000, Meridian recorded a tax benefit related to the insolvency of a foreign subsidiary that has since been liquidated and dissolved. At that time, a reserve was also provided for future resolution of tax uncertainties related to this matter. During June 2007, the statute of limitations expired on the tax returns affected by this matter, and consequently, the adjustment to tax reserves resulted in a tax benefit of \$2,425,000. This tax benefit reduced the effective tax rate by 25 points and 9 points, respectively, for the three and nine-month periods ended June 30, 2007.

***(d) Share-based Compensation***

Meridian accounts for share-based compensation pursuant to SFAS No. 123R, *Share-Based Payment*. SFAS No. 123R requires recognition of compensation expense for all share-based awards made to employees and outside directors, based upon the fair value of the share-based award on the date of the grant.

***(e) Cash, Cash Equivalents and Investments***

We consider short-term investments in debt securities with original maturities or put features of 90 days or less to be cash equivalents. Our investments in debt securities are accounted for as available-for-sale under SFAS No. 115, *Accounting for Certain Investments in Debt and Equity Securities*. As such, unrealized holding gains and losses are reported as a component of other comprehensive income within shareholders' equity until realized, except where losses are considered to be other-than-temporary, in which case they would be recorded to other income and expense, net. As of June 30, 2008, accumulated other comprehensive income included \$233,000 of unrealized holding losses related to student loan auction-rate securities.

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Our investment portfolio includes the following components:

|                                      | June 30, 2008           |                 | September 30, 2007      |                 |
|--------------------------------------|-------------------------|-----------------|-------------------------|-----------------|
|                                      | Cash and<br>Equivalents | Other<br>Assets | Cash and<br>Equivalents | Other<br>Assets |
| Taxable investments                  |                         |                 |                         |                 |
| Repurchase agreements                | \$ 6,889                | \$              | \$ 7,751                | \$              |
| Money market funds                   | 2,483                   |                 |                         |                 |
| Tax-exempt investments               |                         |                 |                         |                 |
| Money market funds                   | 8,122                   |                 | 2,536                   |                 |
| Variable rate demand notes           | 24,277                  |                 | 36,069                  |                 |
| Student loan auction-rate securities |                         | 7,518           |                         |                 |
| Cash on hand                         |                         |                 |                         |                 |
| Restricted                           |                         | 1,000           |                         | 1,000           |
| Unrestricted                         | 5,279                   |                 | 3,044                   |                 |
| Total                                | \$47,050                | \$8,518         | \$49,400                | \$1,000         |

The primary objectives of our investment activities are to preserve capital and provide sufficient liquidity to meet operating requirements and fund strategic initiatives such as acquisitions. We maintain a written investment policy that governs the management of our investments in fixed income securities. This policy, among other things, provides that we may purchase only high credit-quality securities, that have short-term ratings of at least A-1 and P-1 or better, and long-term ratings of at least A-2 and A or better, by Moody's and Standard & Poor's, respectively, at the time of purchase.

Our investments in repurchase agreements are with our commercial bank pursuant to an overnight sweep/liquidity arrangement with our operating cash accounts. Our investments in variable rate demand notes contain a seven-day put feature.

Our investment portfolio also includes student loan auction-rate securities, which are long-term student loan revenue bonds whose interest rates are reset every 35 days via a Dutch auction process. All of our auction-rate securities are backed by pools of student loans originated under the Federal Family Education Loan Program (FFELP). FFELP student loans are guaranteed by State guarantors who have reinsurance agreements with the US Department of Education. All of our student loan auction-rate securities were rated Aaa and AAA by Moody's and Standard & Poor's, respectively, at the time of purchase, and have continued to maintain these credit ratings through the present time.

The Dutch auction process historically provided the necessary liquidity mechanism to either purchase or sell these securities. Beginning in mid-February 2008, liquidity issues in the US credit markets resulted in the failure of auctions across a broad spectrum of tax-exempt securities, including student loan revenue bonds. Auctions for the student loan revenue bonds that we hold have continued to fail through the present time.

The consequence of a failed auction is that we do not have access to the principal amount of our investments. Such principal amounts will not be accessible until successful auctions occur, issuers establish a different form of financing to replace these securities, scheduled

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maturities of the student loan revenue bonds occur, or a buyer is found outside of the auction process. Issuers are still required to make interest payments when due in the event of failed auctions. We have not experienced any missed interest payments. We understand that issuers, financial markets, the US Treasury, and the US Department of Education are working on potential alternatives that may improve liquidity; although, it is unclear at the present time when or if such efforts will be successful.

We continue to believe the credit quality of our student loan auction-rate securities remains high due to the FFELP reinsurance with the US Department of Education. We also have the intent and ability to hold these securities into the foreseeable future and expect to receive 100% of the principal amount of our investments via one of the alternatives mentioned above. As of June 30, 2008, the carrying value of these securities was adjusted by \$233,000. We consider this adjustment to be temporary under SFAS No. 115, and accordingly, it has been recorded as a component of other comprehensive income in shareholders' equity. This adjustment was based upon discounted pricing from a proprietary discounted cash flow model developed by the broker-dealer from whom we purchased these securities. Our investments in student loan auction-rate securities are included in other long-term assets in the accompanying consolidated balance sheet based on the maturities of the student loan revenue bonds (2029 to 2037) and our intent and ability to hold these securities.

We do not believe that the recent auction failures and our inability to liquidate these investments for some period of time will have any material impact on our ability to fund our operating requirements, capital expenditures, dividend payments, acquisitions, if any, or other business requirements.

***(f) New Accounting Pronouncements***

In December 2007, the FASB issued SFAS No. 141(R), *Business Combinations*, as part of a joint project with the International Accounting Standards Board. Statement 141(R) provides for several significant changes to existing accounting practices for business combinations. Most notably, (i) acquisition-related transaction costs, such as legal and professional fees, shall be expensed rather than accounted for as part of the acquisition cost; (ii) acquired in-process research and development shall be capitalized rather than expensed at the acquisition date; and (iii) contingent consideration shall be recorded at fair value at the acquisition date rather than the points in time that payment becomes probable. Statement 141(R) is effective for fiscal years beginning after December 15, 2008. Thus, for Meridian, it will affect any acquisitions after October 1, 2009.

In April 2008, the FASB issued Staff Position No. 142-3, *Determination of the Useful Life of Intangible Assets*. This statement provides guidance on the determination of the useful life of intangible assets in accordance with FASB Statement 142, *Goodwill and Other Intangible Assets*. FSP 142-3 is effective for fiscal years beginning after December 15, 2008 and for interim periods within those fiscal years, which, for Meridian, would be fiscal 2010. Early adoption is prohibited.

In June 2008, the FASB issued SFAS No. 161, *Disclosures about Derivative Instruments and Hedging Activities* — an amendment of FASB Statement No. 133. This statement



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requires additional disclosures regarding the effect of hedging activities on a company's results. This statement is effective for financial statements issued for fiscal years and interim periods beginning after November 15, 2008, which for Meridian would be the second quarter of fiscal 2009. We have elected to early-adopt this statement, as permitted. See Note 6.

**(g) Reclassifications**

Certain reclassifications have been made to the prior period financial statements to conform to the current year presentation.

**3. Inventories:**

Inventories are comprised of the following (in thousands):

|                 | June 30,<br>2008 | September<br>30,<br>2007 |
|-----------------|------------------|--------------------------|
| Raw materials   | \$ 5,445         | \$ 4,816                 |
| Work-in-process | 5,268            | 5,141                    |
| Finished goods  | 10,321           | 8,214                    |
|                 | \$21,034         | \$ 18,171                |

Effective July 1, 2007, we changed our method of accounting for certain inventories from the LIFO method to the FIFO method, so that substantially all of our inventories are reflected at the lower of cost or market with cost determined by the FIFO method. We changed to the FIFO method for these inventories because: it conformed substantially all of our worldwide inventories to a consistent basis of accounting; and it provides better comparability to our industry peers, many of whom use the FIFO method of accounting for inventories. In accordance with SFAS No. 154, *Accounting Changes and Error Corrections*, this change in accounting has been retrospectively applied to the three and nine-month periods ended June 30, 2007. The effect of this change was to increase gross profit and net earnings by \$15,000 and \$10,000, respectively, for the three months ended June 30, 2007 and to increase gross profit and net earnings by \$45,000 and \$28,000, respectively, for the nine months ended June 30, 2007.

**4. Major Customers and Segment Information:**

Our reportable operating segments are US Diagnostics, European Diagnostics, and Life Science. The US Diagnostics operating segment consists of manufacturing operations in Cincinnati, Ohio, and the sale and distribution of diagnostic test kits in the US and countries outside of Europe, Africa and the Middle East. The European Diagnostics operating segment consists of the sale and distribution of diagnostic test kits in Europe, Africa and the Middle East. The Life Science operating segment consists of manufacturing operations in Memphis, Tennessee, Saco, Maine, and Boca Raton, Florida; and the sale and distribution of bulk antigens, antibodies, and bioresearch reagents domestically and abroad. The Life Science operating segment also includes the contract development and manufacture of cGMP clinical grade proteins and other biologicals for use by biopharmaceutical and biotechnology companies engaged in research for new drugs and vaccines.

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Two customers accounted for 48% of the US Diagnostics operating segment third-party sales during the three months ended June 30, 2008 and 2007, and 53% and 51% during the nine months ended June 30, 2008 and 2007, respectively. Two customers accounted for 20% and 44% of the Life Science operating segment third-party sales during the three months ended June 30, 2008 and 2007, respectively, and 34% and 38% during the nine months ended June 30, 2008 and 2007, respectively.

Segment information for the interim periods is as follows (in thousands):

|                                   | US<br>Diagnostics | European<br>Diagnostics | Life<br>Science | Eliminations <sup>(1)</sup> | Total     |
|-----------------------------------|-------------------|-------------------------|-----------------|-----------------------------|-----------|
| <b>Three Months June 30, 2008</b> |                   |                         |                 |                             |           |
| Net sales -                       |                   |                         |                 |                             |           |
| Third-party                       | \$ 19,406         | \$ 8,016                | \$ 5,646        | \$                          | \$ 33,068 |
| Inter-segment                     | 3,355             |                         | 162             | (3,517)                     |           |
| Operating income                  | 8,890             | 1,720                   | 774             | (385)                       | 10,999    |
| Total assets (June 30, 2008)      | 119,846           | 18,236                  | 48,516          | (45,368)                    | 141,230   |
| <b>Three Months June 30, 2007</b> |                   |                         |                 |                             |           |
| Net sales -                       |                   |                         |                 |                             |           |
| Third-party                       | \$ 17,065         | \$ 6,279                | \$ 6,419        | \$                          | \$ 29,763 |
| Inter-segment                     | 2,619             |                         | 117             | (2,736)                     |           |
| Operating income                  | 6,842             | 1,517                   | 1,297           | (168)                       | 9,488     |
| Total assets (September 30, 2007) | 115,297           | 13,600                  | 45,410          | (41,609)                    | 132,698   |
| <b>Nine Months June 30, 2008</b>  |                   |                         |                 |                             |           |
| Net sales -                       |                   |                         |                 |                             |           |
| Third-party                       | \$ 64,878         | \$21,709                | \$16,577        | \$                          | \$103,164 |
| Inter-segment                     | 8,926             | 2                       | 440             | (9,368)                     |           |
| Operating income                  | 26,669            | 4,470                   | 2,117           | (326)                       | 32,930    |
| <b>Nine Months June 30, 2007</b>  |                   |                         |                 |                             |           |
| Net sales -                       |                   |                         |                 |                             |           |
| Third-party                       | \$ 55,885         | \$17,808                | \$16,884        | \$                          | \$ 90,577 |
| Inter-segment                     | 6,880             |                         | 475             | (7,355)                     |           |
| Operating income                  | 20,653            | 3,793                   | 2,194           | (245)                       | 26,395    |

(1) Eliminations consist of intersegment transactions.

Transactions between operating segments are accounted for at established intercompany prices for internal and management purposes with all intercompany amounts eliminated in consolidation. Total assets for the US Diagnostics and Life Science operating segments include goodwill of \$1,492,000 and \$8,473,000, respectively, at June 30, 2008, and \$1,492,000 and \$8,472,000, respectively, at September 30, 2007.

**Table of Contents****5. Intangible Assets:**

A summary of our acquired intangible assets subject to amortization, as of June 30, 2008 and September 30, 2007 is as follows (in thousands):

|                                      | Wtd<br>Avg<br>Amort<br>Period<br>(Yrs) | June 30, 2008              |                             | September 30, 2007         |                             |
|--------------------------------------|--|----------------------------|-----------------------------|----------------------------|-----------------------------|
|                                      |  | Gross<br>Carrying<br>Value | Accumulated<br>Amortization | Gross<br>Carrying<br>Value | Accumulated<br>Amortization |
| Core products and cell lines         | 15                                     | \$ 4,698                   | \$ 2,530                    | \$ 4,698                   | \$ 2,313                    |
| Manufacturing technologies           | 14                                     | 6,057                      | 4,356                       | 5,907                      | 4,089                       |
| Trademarks, licenses and patents     | 8                                      | 2,663                      | 1,811                       | 2,270                      | 1,694                       |
| Customer lists and supply agreements | 13                                     | 11,046                     | 6,570                       | 10,641                     | 5,963                       |
|                                      |  | \$24,464                   | \$15,267                    | \$23,516                   | \$14,059                    |

The actual aggregate amortization expense for these intangible assets for the three months ended June 30, 2008 and 2007 was \$343,000 and \$408,000, respectively. The actual aggregate amortization expense for these intangible assets for the nine months ended June 30, 2008 and 2007 was \$1,208,000 and \$1,222,000, respectively.

**6. Hedging Transactions:**

The Company is subjected to certain risks in the normal course of business. From time to time, we manage exchange rate risk related to forecasted intercompany sales denominated in the Euro currency through the use of forward exchange contracts.

SFAS No. 133 requires companies to recognize all derivative instruments as either assets or liabilities at fair value in the statement of financial position. In accordance with SFAS No. 133, we designate forward contracts as cash flow hedges. As such, the effective portion of the gain or loss on the derivative instrument is reported as a component of other comprehensive income and reclassified into earnings in the same period or periods during which the hedged transaction affects earnings. Gains and losses on the derivative instruments representing either hedge ineffectiveness or hedge components excluded from the assessment of effectiveness are recognized in current earnings.

The following table presents our hedging portfolio as of June 30, 2008 (in thousands).

| Notional<br>Amount | Contract<br>Value | Estimated<br>Fair<br>Value | Average<br>Exchange<br>Rate | Maturity   |
|--------------------|-------------------|----------------------------|-----------------------------|------------|
| 1,200              | \$1,654           | \$ 1,883                   | 1.3783                      | FY<br>2008 |
| 900                | \$1,289           | \$ 1,403                   | 1.4322                      | FY<br>2009 |

At June 30, 2008, \$415,000 of unrealized losses were included in accumulated other comprehensive income in the consolidated balance sheet, compared to unrealized losses of \$270,000 at September 30, 2007. This amount is expected to be reclassified into net earnings during the next 12 months.

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The following table presents the fair value of our hedging portfolio as of June 30, 2008 and September 30, 2007 (in thousands).

|  | Liability Derivatives  |            |                        |            |
|--|------------------------|------------|------------------------|------------|
|  | June 30, 2008          |            | September 30, 2007     |            |
|  | Balance Sheet Location | Fair Value | Balance Sheet Location | Fair Value |
| Derivatives designated as hedging instruments under SFAS No. 133       |                        |            |                        |            |
| Foreign exchange contracts   | Accrued expenses       | \$ 343     | Accrued expenses       | \$ 256     |
| Total derivatives designated as hedging instruments under SFAS No. 133 |                        | \$ 343     |                        | \$ 256     |
| Total derivatives  |                        | \$ 343     |                        | \$ 256     |

The effect of derivative instruments on the Consolidated Statements of Operations is shown below for the three and nine-month periods ended June 30, 2008 and June 30, 2007 (in thousands).

|                            | Amount of Gain or (Loss) Recognized in OCI on Derivative (Effective Portion) |        |                            |          | Location of Gain or (Loss) Reclassified from Accumulated OCI into Income (Effective Portion) | Amount of Gain or (Loss) Reclassified from Accumulated OCI into Income (Effective Portion <sup>1</sup> ) |        |                            |         |
|----------------------------|--|--------|----------------------------|----------|--|--|--------|----------------------------|---------|
|                            | Three months ended June 30,  |        | Nine months ended June 30, |          |  | Three months ended June 30,  |        | Nine months ended June 30, |         |
|                            | 2008   | 2007   | 2008                       | 2007     |  | 2008   | 2007   | 2008                       | 2007    |
| Foreign exchange contracts | \$9  | \$ (5) | \$ (544)                   | \$ (100) | Net Sales  | \$ (221)   | \$ (9) | \$ (400)                   | \$ (71) |

<sup>1</sup> No portion of the gain/loss was excluded from other

comprehensive  
income due to  
effectiveness  
testing.

The estimated fair value of forward contracts outstanding at June 30, 2008 and September 30, 2007 is based on quoted amounts provided by the counterparties to these contracts.

**7. Asset purchase:**

On June 18, 2008, we completed the purchase of certain assets related to a product line of infectious disease recombinant proteins and cardiac antigens from Vybion, Inc. The purchase agreement provided for consideration of \$653,000 in cash, plus future royalties based on net sales of the acquired products. The assets acquired included a portfolio of recombinant viral proteins and cardiac antigens, customer lists, supply agreements, patent and technology rights, equipment, and on-hand inventory. This transaction did not meet the criteria for a business combination. The consideration paid was allocated to the assets acquired based on their relative fair values.

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**Table of Contents****ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

Refer to *Forward Looking Statements* following the Index in front of this Form 10-Q.

**Overview:**

In fiscal 2008, we have continued our consistency in delivering double-digit sales and earnings growth, driven by new product launches and market share expansions in our diagnostics operating segments. Our diagnostics operating segments continue to provide the largest share of consolidated revenues, 84% for the first nine months of fiscal 2008 and 81% for the same period of fiscal 2007. Demand and buying patterns for certain of our bulk viral protein and reagent customers have led to a 2% reduction in year-to-date sales for our Life Science operating segment. We expect these conditions to continue into the fourth quarter of fiscal 2008 and the first quarter of fiscal 2009.

Net earnings and earnings per share for the three and nine-month periods ended June 30, 2007 include the effects of a tax benefit in the amount of \$2,425,000, or \$0.06 per basic and diluted share, related to a discrete adjustment to tax reserves that was recorded upon the expiration of the statute of limitations on certain income tax returns (see Note 2(c) to the consolidated financial statements herein). The tables below provide information on net earnings, basic earnings per share, and diluted earnings per share, excluding this tax benefit, as well as reconciliations to amounts reported under US GAAP. We believe that this information is useful to those who read our financial statements and evaluate our operating results because:

1. These measures help to appropriately evaluate and compare the results of operations from period to period by removing the favorable impact of a discrete material item that is not expected to recur in the future; and
2. These measures are used by our management for various purposes, including evaluating performance against incentive bonus achievement targets, comparing performance from period to period in presentations to our Board of Directors, and as a basis for strategic planning and forecasting.

|   | <b>Three Months June 30,</b> |             | <b>Nine Months June 30,</b> |             |
|---|------------------------------|-------------|-----------------------------|-------------|
|   | <b>2008</b>                  | <b>2007</b> | <b>2008</b>                 | <b>2007</b> |
| Net Earnings -                                  |                              |             |                             |             |
| US GAAP basis                                   | \$7,763                      | \$ 8,814    | \$22,518                    | \$20,277    |
| Tax benefit not expected to recur in the future |                              | (2,425)     |                             | (2,425)     |
| Excluding tax benefit                           | \$7,763                      | \$ 6,389    | \$22,518                    | \$17,852    |

|   | <b>Three Months June 30,</b> |             | <b>Nine Months June 30,</b> |             |
|---|------------------------------|-------------|-----------------------------|-------------|
|   | <b>2008</b>                  | <b>2007</b> | <b>2008</b>                 | <b>2007</b> |
| Net Earnings per Basic Common Share -           |                              |             |                             |             |
| US GAAP basis                                   | \$0.19                       | \$ 0.22     | \$0.56                      | \$ 0.51     |
| Tax benefit not expected to recur in the future |                              | (0.06)      |                             | (0.06)      |
| Excluding tax benefit                           | \$0.19                       | \$ 0.16     | \$0.56                      | \$ 0.45     |

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|  | <b>Three Months June 30,</b> |             | <b>Nine Months June 30,</b> |             |
|--|------------------------------|-------------|-----------------------------|-------------|
|  | <b>2008</b>                  | <b>2007</b> | <b>2008</b>                 | <b>2007</b> |
| Net Earnings per Diluted Common Share -<br>US GAAP basis | \$0.19                       | \$ 0.22     | \$0.55                      | \$ 0.50     |
| Tax benefit not expected to recur in the future          |                              | (0.06)      |                             | (0.06)      |
| Excluding tax benefit                                    | \$0.19                       | \$ 0.16     | \$0.55                      | \$ 0.44     |

*Diagnostics*

Sales for our US and European Diagnostics operating segments grew 14% and 28%, respectively, during the third quarter of fiscal 2008. Growth for the US Diagnostics operating segment during the third quarter was driven by continued market penetration of our food borne products and growth in *C. difficile* and *H. pylori* product families. For the European Diagnostics operating segment, organic growth in local currency was 13% for the third quarter, driven by volume increases in *C. difficile* products.

Our food borne products contributed to growth during the third quarter of fiscal 2008, led by ImmunoCard STAT!<sup>®</sup> EHEC. This product is a rapid test developed in collaboration with Merck for detection of toxin-producing *E. coli* in patients that may have ingested contaminated produce or meat products, which was launched during fiscal 2007.

We also recently launched two Epstein-Barr virus (Mononucleosis) tests in Europe using our proprietary TRU<sup>®</sup> rapid test technology. These products began contributing to sales during the third quarter of fiscal 2008. We expect continued sales growth for these new products.

For the first nine months of fiscal 2008, we have continued to see growth in the *C. difficile* and *H. pylori* testing markets where we hold market leadership positions, leading to sales volume increases for both product families. The *C. difficile* market has experienced more virulent strains of this toxin and heightened focus by hospitals on this dangerous pathogen. New AGA guidelines are creating increased focus on direct antigen testing for *H. pylori*, as this infection is a known cause of ulcers. Our managed care efforts are also contributing to volume growth in *H. pylori* products. Our line of patented *H. pylori* products includes both rapid and batch method noninvasive direct testing formats.

*Life Science*

Sales for our Life Science operating segment declined 12% for the third quarter of fiscal 2008. This decline was caused by lower demand from two major viral protein customers and a defense contract in fiscal 2007 that was not renewed for fiscal 2008. Sales to these two major viral protein customers accounted for 20% and 44% of total sales for this segment for the third quarters of fiscal 2008 and 2007, respectively.

**Operating Segments:**

Our reportable operating segments are US Diagnostics, European Diagnostics, and Life Science. The US Diagnostics operating segment consists of manufacturing operations in Cincinnati, Ohio, and the sale and distribution of diagnostics test kits in the US and countries outside of Europe, Africa and the Middle East. The European Diagnostics operating segment consists of the sale and distribution of diagnostics test kits in Europe, Africa and the Middle East. The Life Science

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distribution of diagnostics test kits in Europe, Africa and the Middle East. The Life Science operating segment consists of manufacturing operations in Memphis, Tennessee, Saco, Maine, and Boca Raton, Florida; and the sale and distribution of bulk antigens, antibodies, and bioresearch reagents domestically and abroad. The Life Science operating segment also includes the contract development and manufacture of cGMP clinical grade proteins and other biologicals for use by biopharmaceutical and biotechnology companies engaged in research for new drugs and vaccines.

Revenues for the Diagnostics operating segments, in the normal course of business, may be affected from quarter to quarter by buying patterns of major distributors, seasonality and strength of certain diseases and foreign currency exchange rates. Revenues for the Life Science operating segment, in the normal course of business, may be affected from quarter to quarter by the timing and nature of arrangements for contract services work, which may have longer production cycles than bioresearch reagents and bulk antigens and antibodies, as well as buying patterns of major customers. We believe that the overall breadth of our product lines serves to reduce the variability in consolidated sales from quarter to quarter.

**Results of Operations:****Net sales**

|                         | Three Months Ended June 30 |               |              | Nine Months Ended June 30 |               |              |
|-------------------------|----------------------------|---------------|--------------|---------------------------|---------------|--------------|
|                         | 2008                       | 2007          | Inc<br>(Dec) | 2008                      | 2007          | Inc<br>(Dec) |
| US Diagnostics          | \$ 19,406,000              | \$ 17,065,000 | 14%          | \$ 64,878,000             | \$ 55,885,000 | 16%          |
| European<br>Diagnostics | 8,016,000                  | 6,279,000     | 28%          | 21,709,000                | 17,808,000    | 22%          |
| Life Science            | 5,646,000                  | 6,419,000     | (12)%        | 16,577,000                | 16,884,000    | (2)%         |
| Consolidated            | \$ 33,068,000              | \$ 29,763,000 | 11%          | \$ 103,164,000            | \$ 90,577,000 | 14%          |
| International           |                            |               |              |                           |               |              |
| US Export               | \$ 4,405,000               | \$ 3,603,000  | 22%          | \$ 11,654,000             | \$ 10,294,000 | 13%          |
| European<br>Diagnostics | 8,016,000                  | 6,279,000     | 28%          | 21,709,000                | 17,808,000    | 22%          |
| Total                   | \$ 12,421,000              | \$ 9,882,000  | 26%          | \$ 33,363,000             | \$ 28,102,000 | 19%          |
| % of total sales        | 38%                        | 33%           |              | 32%                       | 31%           |              |

Sales growth for US Diagnostics was primarily related to volume increases across key product families. For the third quarter of fiscal 2008, the volume increases were in food borne products, *C. difficile* products and *H. pylori* products. In addition, for the nine-month period, we have also seen growth in respiratory products. Volume increases for food borne products were driven by the fiscal 2007 launch of ImmunoCard STAT!<sup>®</sup> EHEC. Volume increases in *C. difficile* products were driven by increased sales of our rapid diagnostic test, ImmunoCard<sup>®</sup> Toxins A & B. Volume increases for *H. pylori* products, driven by increased managed care efforts and issuance of AGA guidelines recommending direct antigen testing, also contributed to sales growth. Volume increases in respiratory products were driven by a strong Influenza season, increased market share, and a relatively ineffective Influenza vaccine. Two national distributors accounted for 48% of total sales for the US Diagnostics operating segment for each of the third quarters of fiscal 2008 and 2007, respectively, and 53% and 51% of total sales for the US Diagnostics operating segment for the first nine months of fiscal 2008 and 2007, respectively.





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For the European Diagnostics operating segment, the sales increase includes currency translation gains in the amount of \$928,000 and \$2,296,000 for the three and nine-month periods ending June 30, 2008, respectively. Organic sales growth, which excludes the effects of currency translation, was 13% and 9% for the three and nine-month periods, respectively. Organic sales growth was primarily driven by sales of *C. difficile* products, including the ImmunoCard® Toxins A & B rapid diagnostic test.

For the Life Science operating segment, the fluctuations in sales for both the quarter and the nine-month period reflect changes in demand and buying patterns of certain of our major diagnostic manufacturing customers and non-renewal of a supply contract with the US Department of Defense. Changes in the US Department of Defense's Critical Reagents program led to non-renewal of this contract after fiscal 2007. We sell three main products to a major diagnostic manufacturing customer, who accounted for 8% and 26% of total sales for the Life Science operating segment for the third quarters of fiscal 2008 and 2007, and 19% and 22% of total sales for the Life Science operating segment for the nine-month periods, respectively. During the first quarter of fiscal 2008, this customer reduced their forecasted requirements for two antigen products due to their internal inventory management initiatives and their market factors. The impact of this reduction was partially offset by the customer's increased purchases of a bulk reagent product. For the three and nine-month periods, these demand changes and buying patterns resulted in net revenue reductions of approximately \$1,200,000 and \$500,000, respectively. We expect our sales to this customer to continue to be lumpy on a quarter-to-quarter basis. This matter does not affect our fiscal 2008 guidance regarding expectations for net sales of \$140 to \$142 million and diluted earnings per share of \$0.72 to \$0.75.

**Gross Profit**

|                        | Three Months Ended June 30 |              |              | Nine Months Ended June 30 |              |              |
|------------------------|----------------------------|--------------|--------------|---------------------------|--------------|--------------|
|                        | 2008                       | 2007         | Inc<br>(Dec) | 2008                      | 2007         | Inc<br>(Dec) |
| Gross Profit           | \$21,287,000               | \$19,301,000 | 10%          | \$64,154,000              | \$55,751,000 | 15%          |
| Gross Profit<br>Margin | 64.4%                      | 64.8%        | (0.4)%       | 62.2%                     | 61.6%        | 0.6%         |

Our overall operations consist of the sale of diagnostic test kits for various disease states and in alternative test formats, as well as bioresearch reagents, bulk antigens and antibodies, proficiency panels, contract research and development and contract manufacturing services. Product sales mix shifts, in the normal course of business, can cause the consolidated gross profit margin to fluctuate by several points.

**Table of Contents****Operating Expenses**

|                      | Three Months Ended June 30 |                    |                          | Nine Months Ended June 30 |                     |                          |
|----------------------|----------------------------|--------------------|--------------------------|---------------------------|---------------------|--------------------------|
|                      | Research & Development     | Sales & Marketing  | General & Administrative | Research & Development    | Sales & Marketing   | General & Administrative |
| <b>2007 Expenses</b> | <b>\$1,306,000</b>         | <b>\$4,072,000</b> | <b>\$4,435,000</b>       | <b>\$4,339,000</b>        | <b>\$12,331,000</b> | <b>\$12,686,000</b>      |
| % of Sales           | 4%                         | 14%                | 15%                      | 5%                        | 14%                 | 14%                      |
| Fiscal 2008          |                            |                    |                          |                           |                     |                          |
| Increases            |                            |                    |                          |                           |                     |                          |
| (Decreases):         |                            |                    |                          |                           |                     |                          |
| US Diagnostics       | 146,000                    | 300,000            | (183,000)                | 252,000                   | 1,237,000           | 114,000                  |
| European             |                            |                    |                          |                           |                     |                          |
| Diagnostics          |                            | 203,000            | 59,000                   |                           | 320,000             | 152,000                  |
| Life Science         | (130,000)                  | (116,000)          | 196,000                  | (219,000)                 | (191,000)           | 203,000                  |
| <b>2008 Expenses</b> | <b>\$1,322,000</b>         | <b>\$4,459,000</b> | <b>\$4,507,000</b>       | <b>\$4,372,000</b>        | <b>\$13,697,000</b> | <b>\$13,155,000</b>      |
| % of Sales           | 4%                         | 13%                | 14%                      | 4%                        | 13%                 | 13%                      |
| % Increase           |                            |                    |                          |                           |                     |                          |
| (Decrease)           | 1%                         | 10%                | 2%                       | 1%                        | 11%                 | 4%                       |

Total operating expenses increased 5% to \$10,288,000, for the third quarter of fiscal 2008 compared to the third quarter of fiscal 2007 and 6% to \$31,224,000 for the first nine months of fiscal 2008 compared to the first nine months of fiscal 2007. The overall increase in operating expenses is discussed below.

Research and development expenses for the US Diagnostics operating segment increased for the third quarter primarily due to planned headcount additions. For the nine-month period, these increases were partially offset by clinical trial and other costs associated with the recently launched TRU<sup>®</sup> Influenza, RSV and Epstein-Barr Virus products that were incurred during fiscal 2007. The decrease for the Life Science operating segment related to retirements of senior personnel that occurred during fiscal 2007.

Sales and marketing expenses for the US Diagnostics operating segment increased primarily due to expenses for new product launches and increased salaries and benefits related to planned headcount additions. The increase for the European Diagnostics operating segment primarily related to currency translation in both the three and nine-month periods. The decrease for the Life Science operating segment primarily related to bonus expense related to decreased sales and earnings levels.

General and administrative expenses for the US Diagnostics operating segment for the third quarter reflected decreased property tax expense related to the phase-out of personal property taxes in Ohio and decreased insurance expense related to a favorable adjustment from a workers' compensation audit, and for the nine-month period, reflected increased salaries and benefits related to planned headcount additions, partially offset by decreased corporate incentive bonus accruals. The increases for the European Diagnostics operating segment primarily related to currency translation in both the three and nine-month periods. The increases for the Life Science operating segment reflect severance costs for certain personnel changes and the write-off of certain computer software costs.

**Operating Income**

Operating income increased 16% to \$10,999,000 for the third quarter of fiscal 2008 and 25% to \$32,930,000 for the first nine months of fiscal 2008, as a result of the factors discussed above.

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***Other Income and Expense***

Interest income decreased 27% to \$297,000 for the third quarter of fiscal 2008 compared to the third quarter of fiscal 2007 and 1% to \$1,148,000 for the first nine months of fiscal 2008 compared to the first nine months of fiscal 2007. This decrease was driven by lower interest yields in the current interest rate environment, somewhat offset by higher average investment balances during fiscal 2008. See Note 2(e) to the consolidated financial statements herein for discussion of our investment portfolio.

***Income Taxes***

The effective rate for income taxes was 32% for the third quarter of fiscal 2008 compared to 11% for the third quarter of fiscal 2007. The effective rate for income taxes was 34% for the first nine months of fiscal 2008 compared to 26% for the first nine months of fiscal 2007. The increase in the effective tax rate for the third quarter was primarily attributable to a discrete adjustment to tax reserves in the amount of \$2,425,000 in fiscal 2007. This discrete adjustment reduced the effective tax rate by 25 points and 9 points for the three and nine-month periods, respectively. See Note 2(c) to the consolidated financial statements included herein for a complete discussion of this matter. The current quarter reflected additional favorable benefits from manufacturing incentives under the American Jobs Creation Act. For the fiscal year ending September 30, 2008, Meridian expects the effective tax rate to be in the range of 34% to 35%.

Effective October 1, 2007, we adopted FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes*. FIN 48 prescribes a comprehensive model for the recognition, measurement, presentation and disclosure of uncertain tax positions, assuming full knowledge of all relevant facts by the applicable tax authorities. The cumulative effect of adopting FIN 48, \$305,000, was charged to opening retained earnings. See Note 2(c) to the consolidated financial statements herein.

**Liquidity and Capital Resources:**

***Comparative Cash Flow Analysis***

Our cash flow and financing requirements are determined by analyses of operating and capital spending budgets, consideration of acquisition plans, and consideration of common share dividends. We have historically maintained a credit facility to augment working capital requirements and to respond quickly to acquisition opportunities. This credit facility has been supplemented by the proceeds from a September 2005 common share offering, which are invested in fixed income securities such as overnight repurchase agreements, institutional money-market mutual funds, municipal variable rate demand notes with a seven-day put feature and tax-exempt auction rate securities. We do not expect current conditions in the financial markets, or overall economic conditions to have a significant effect on our financial condition, results of operations, or cash flows.

Net cash provided by operating activities increased 20% for the first nine months of fiscal 2008 compared to the first nine months of fiscal 2007. This increase was driven primarily by growth in net earnings for the first nine months.

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Net cash used in investing activities was \$11,908,000 for the first nine months of fiscal 2008 compared to net cash provided by investing activities of \$600,000 for the first nine months of fiscal 2007. This change was primarily attributable to purchases and sales of investments in both periods, acquisitions of property, plant and equipment, and purchases of intangibles and other assets.

Net cash used for financing activities was \$12,844,000 for the first nine months of fiscal 2008, compared to \$9,473,000 for the first nine months of fiscal 2007. The increase primarily related to increased dividends paid on common shares and increased tax benefits related to stock option exercises.

Net cash flows from operating activities are anticipated to fund working capital requirements and dividends during the next twelve months.

*Capital Resources*

Meridian has a \$30,000,000 credit facility with a commercial bank which expires on September 15, 2012. As of July 31, 2008, there were no borrowings outstanding on this facility.

The OEM Concepts acquisition, completed in fiscal 2005, provides for additional purchase consideration up to a maximum remaining amount of \$1,815,000, contingent upon future calendar-year sales and gross profit of OEM Concepts products through December 31, 2008. Earnout consideration is payable each year, following the period earned. Earnout consideration in the amount of \$157,000 related to calendar 2007 was paid from operating cash flows during the second quarter of fiscal 2008.

Our capital expenditures are estimated to be \$4,000,000 to \$5,000,000 for fiscal 2008 and may be funded with operating cash flows, availability under the \$30,000,000 credit facility, or cash equivalents on-hand. Capital expenditures relate to manufacturing equipment to further automation initiatives, computer system improvements, and capacity expansion for the Maine facility.

We do not utilize any special-purpose financing vehicles or have any similar off balance sheet type arrangements.

*Student Loan Auction-Rate Securities*

Our investment portfolio includes student loan auction-rate securities, which are long-term student loan revenue bonds whose interest rates are reset every 35 days via a Dutch auction process. All of our auction-rate securities are backed by pools of student loans originated under the Federal Family Education Loan Program (FFELP). FFELP student loans are guaranteed by State guarantors who have reinsurance agreements with the US Department of Education. All of our student loan auction-rate securities were rated Aaa and AAA by Moody's and Standard & Poor's, respectively, at the time of purchase, and have continued to maintain these credit ratings through the present time.

The Dutch auction process historically provided the necessary liquidity mechanism to either purchase or sell these securities. Beginning in mid-February 2008, liquidity issues in the US credit markets resulted in the failure of auctions across a broad spectrum of tax-exempt securities, including student loan revenue bonds. Auctions for the student loan revenue bonds that we hold have continued to fail through the present time.

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The consequence of a failed auction is that we do not have access to the principal amount of our investments. Such principal amounts will not be accessible until successful auctions occur, issuers establish a different form of financing to replace these securities, scheduled maturities of the student loan revenue bonds occur, or a buyer is found outside of the auction process. Issuers are still required to make interest payments when due in the event of failed auctions. We have not experienced any missed interest payments. We understand that issuers, financial markets, the US Treasury, and the US Department of Education are working on potential alternatives that may improve liquidity; although, it is unclear at the present time when or if such efforts will be successful.

We continue to believe the credit quality of our student loan auction-rate securities remains high due to the FFELP reinsurance with the US Department of Education. We also have the intent and ability to hold these securities into the foreseeable future and expect to receive 100% of the principal amount of our investments via one of the alternatives mentioned above. As of June 30, 2008, the carrying value of these securities was adjusted by \$233,000. We consider this adjustment to be temporary under SFAS No. 115, and accordingly, it has been recorded as a component of other comprehensive income in shareholders' equity. This adjustment was based upon discounted pricing from a proprietary discounted cash flow model developed by the broker-dealer from whom we purchased these securities. Our investments in student loan auction-rate securities are included in other long-term assets in the accompanying consolidated balance sheet based on the maturities of the student loan revenue bonds (2029 to 2037) and our intent and ability to hold these securities.

We do not believe that the recent auction failures and our inability to liquidate these investments for some period of time will have any material impact on our ability to fund our operating requirements, capital expenditures, dividend payments, acquisitions, if any, or other business requirements.

**ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

Other than auction-rate securities matters discussed under ITEM 2, there have been no material changes in the Company's exposure to market risk since September 30, 2007.

**ITEM 4. CONTROLS AND PROCEDURES**

As of June 30, 2008, an evaluation was completed under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures pursuant to Rule 13a-15(b) and 15d-15(b) promulgated under the Securities Exchange Act of 1934, as amended. Based on that evaluation, our management, including the CEO and CFO, concluded that our disclosure controls and procedures were effective as of June 30, 2008. There have been no changes in our internal controls over financial reporting identified in connection with the evaluation of internal controls that occurred during the third fiscal quarter that has materially affected, or is reasonably likely to materially affect, our internal controls over financial reporting, or in other factors that could materially affect internal controls subsequent to June 30, 2008.

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**PART II. OTHER INFORMATION**

**ITEM 1A. RISK FACTORS**

There have been no material changes from risk factors as previously disclosed in the Registrant's Form 10-K in response to Item 1A of Part I of Form 10-K.

**ITEM 6. EXHIBITS**

31.1 Certification of Principal Executive Officer Pursuant to Securities Exchange Act Rule 13a-14(a)/15d-14(a)

31.2 Certification of Principal Financial Officer Pursuant to Securities Exchange Act Rule 13a-14(a)/15d-14(a)

32 Certification of Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

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Signature:

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 there-unto duly authorized.

**MERIDIAN BIOSCIENCE, INC.**

Date: August 8, 2008

/s/ Melissa Lueke

Melissa Lueke

Vice President and Chief Financial Officer

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