MERIDIAN BIOSCIENCE INC
Form 10-Q
May 10, 2006

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

þ **QUARTERLY REPORT PURSUANT TO SECTION 13 or 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the Quarterly Period Ended March 31, 2006

OR

o **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 þ No o

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

Large accelerated filer o Accelerated filer þ Non-accelerated filer o

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

Yes o No þ

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

Class	Outstanding April 30, 2006
Common Stock, no par value	26,095,554

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, which also may be identified by their context. Such statements 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, 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 U.S. 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 will be successfully integrated into Meridian s operations.*

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

	Three Months Ended March 31, 2006	Three Months Ended March 31, 2005	Six Months Ended March 31, 2006	Six Months Ended March 31, 2005
NET SALES	$28,272	$23,686	$53,180	$42,528
COST OF SALES	11,692	10,109	21,450	17,938
Gross profit	16,580	13,577	31,730	24,590
OPERATING EXPENSES:				
Research and development	1,203	861	2,355	1,694
Sales and marketing	4,053	4,056	8,271	7,372
General and administrative	4,347	3,462	7,957	6,859
Total operating expenses	9,603	8,379	18,583	15,925
Operating income	6,977	5,198	13,147	8,665
OTHER INCOME (EXPENSE):				
Interest income	238	8	487	14
Interest expense	(32)	(225)	(67)	(515)
Other, net	63	125	(29)	149
Total other income (expense)	269	(92)	391	(352)
Earnings before income taxes	7,246	5,106	13,538	8,313
INCOME TAX PROVISION	2,523	1,910	4,853	3,007
NET EARNINGS	$ 4,723	$ 3,196	$ 8,685	$ 5,306
BASIC EARNINGS PER COMMON SHARE	$ 0.18	$ 0.14	$ 0.33	$ 0.23
DILUTED EARNINGS PER COMMON SHARE	$ 0.18	$ 0.13	$ 0.32	$ 0.22
AVERAGE NUMBER OF COMMON SHARES OUTSTANDING BASIC	26,142	23,469	26,050	23,019
DILUTIVE COMMON STOCK OPTIONS	694	693	696	723

AVERAGE NUMBER OF COMMON SHARES OUTSTANDING DILUTED	26,836	24,162	26,746	23,742
ANTI-DILUTIVE SECURITIES:				
Common stock options	11	2	6	110
Shares from convertible debentures	190	819	190	819
DIVIDENDS DECLARED PER COMMON SHARE	$ 0.115	$ 0.08	$ 0.195	$ 0.15

All historical share and per share data has been adjusted for the September 2, 2005 three-for-two stock split.

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)

Six Months Ended March 31,	**2006**	**2005**
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net earnings	$ 8,685	$ 5,306
Non-cash items:		
Depreciation of property, plant and equipment	1,344	1,289
Amortization of intangible assets and deferred costs	913	742
Stock based compensation	319	63
Deferred income taxes	314	4
Loss on disposition of fixed assets	44	
Change in current assets, excluding cash and deferred taxes and net of effects of acquisition	(1,323)	(684)
Change in current liabilities, excluding debt obligations and net of effects of acquisition	(3,882)	(372)
Other	66	216
Net cash provided by operating activities	6,480	6,564
CASH FLOWS FROM INVESTING ACTIVITIES:		
Acquisitions of property, plant and equipment	(2,054)	(1,484)
Proceeds from sales of property, plant and equipment	34	
Viral Antigens earnout payments	(1,313)	(678)
Acquisition of OEM Concepts, Inc.	(181)	(6,226)
Net cash used for investing activities	(3,514)	(8,388)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Net activity on revolving credit facility		5,397
Repayment of debt obligations	(469)	(1,141)
Dividends paid	(5,089)	(3,386)
Proceeds from exercise of stock options	825	2,476
Other	(3)	(11)
Net cash provided by (used for) financing activities	(4,736)	3,335
Effect of Exchange Rate Changes on Cash	8	105
Net Increase (Decrease) in Cash	(1,762)	1,616
Cash at Beginning of Period	33,085	1,983

Cash at End of Period	$31,323	$ 3,599

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

CURRENT ASSETS:	March 31, 2006	September 30, 2005
Cash and equivalents	$ 31,323	$ 33,085
Accounts receivable, less allowances of $422 and $360 for doubtful accounts	17,699	17,366
Inventories	18,046	16,785
Prepaid expenses and other current assets	1,396	1,666
Deferred income taxes	804	1,258
Total current assets	69,268	70,160
PROPERTY, PLANT AND EQUIPMENT:		
Land	693	693
Buildings and improvements	15,525	15,510
Machinery, equipment and furniture	21,514	21,053
Construction in progress	1,586	433
Subtotal	39,318	37,689
Less-accumulated depreciation and amortization	21,226	20,229
Net property, plant and equipment	18,092	17,460
OTHER ASSETS:		
Goodwill	8,960	8,779
Other intangible assets, net	12,385	13,249
Other assets	860	921
Total other assets	22,205	22,949
TOTAL ASSETS	$ 109,565	$ 110,569

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

CURRENT LIABILITIES:	March 31, 2006	September 30, 2005
Current portion of long-term debt	$ 308	$ 556
Accounts payable	3,664	2,949
Accrued payroll costs	4,663	7,707
Purchase business combination liabilities		1,313
Other accrued expenses	3,747	3,993
Income taxes payable	1,961	3,273
Total current liabilities	14,343	19,791
LONG-TERM DEBT:		
Bank debt		233
Convertible subordinated debentures	1,833	2,451
DEFERRED INCOME TAXES	4,186	4,326
COMMITMENTS AND CONTINGENCIES		
SHAREHOLDERS EQUITY:		
Preferred stock, no par value, 1,500,000 shares authorized, none issued		
Common shares, no par value, 50,000,000 shares authorized, 26,077,713 and 25,940,080 shares issued, respectively		
Treasury stock, at cost, 0 and 12,450 shares, respectively		(32)
Additional paid-in capital	73,262	71,568
Retained earnings	16,283	12,687
Accumulated other comprehensive loss	(342)	(455)
Total shareholders equity	89,203	83,768
TOTAL LIABILITIES AND SHAREHOLDERS EQUITY	$ 109,565	$ 110,569

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 Shares Issued	Shares Held in Treasury	Treasury Stock	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Comprehensive Income (Loss)	Total Shareholders Equity
Balance at September 30, 2005	25,940	(12)	$ (32)	$ 71,568	$ 12,687	$ (455)	$	$ 83,768
Dividends paid					(5,089)			(5,089)
Exercise of stock options, net of tax	87			825				825
Stock based compensation				319				319
Bond conversion	63			582				582
Treasury shares retired	(12)	12	32	(32)				
Comprehensive income:								
Net income					8,685		8,685	8,685
Foreign currency translation adjustment						113	113	113
Comprehensive income							$ 8,798	
Balance at March 31, 2006	26,078		$	$ 73,262	$ 16,283	$ (342)		$ 89,203

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, although Meridian believes 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, 2005.

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

Meridian s revenues are derived primarily from product sales. Revenue is generally recognized 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. Rebate agreements are in place with certain independent national distributors and are designed to reimburse such distributors for their cost in handling Meridian s products. Management estimates rebate accruals based on historical statistics, current trends, and other factors. Changes to these rebate accruals are recorded in the period that they become known.

Life Science operating segment revenue for contract services may come from standalone arrangements for process development and/or optimization work (contract research and development services), or multiple-deliverable arrangements that include process development work followed by larger-scale manufacturing (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*. 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 are performed. For fixed fee arrangements, revenue is recognized upon completion and

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acceptance by the customer. For contract manufacturing services, revenue is recognized upon delivery of product and acceptance by the customer.

(b) Foreign Currency Translation

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 (loss). Revenues and expenses are translated using exchange rates prevailing during the period. Meridian also recognizes 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.

Foreign currency translation is the only component of accumulated other comprehensive income (loss). Comprehensive income for the interim periods ended March 31 was as follows (in thousands):

	Three Months Ended March 31,		Six Months Ended March 31,	
	2006	2005	2006	2005
Net income	$4,723	$3,196	$8,685	$5,306
Foreign currency translation	(13)	(326)	113	247
Comprehensive income	$4,710	$2,870	$8,798	$5,553

(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. Meridian prepares estimates of permanent and temporary differences between income for financial reporting purposes and income for tax purposes. These differences are adjusted to actual upon filing of Meridian s tax returns, which typically occurs in the third and fourth quarters of the current fiscal year for the preceding fiscal year s estimates.

(d) Stock-based Compensation

Meridian accounts for stock-based compensation pursuant to SFAS No. 123R, *Share-Based Payment*, which was adopted as of July 1, 2005. SFAS No. 123R requires recognition of compensation expense for all share-based awards made to employees, based upon the fair value of the share-based award on the date of the grant. Meridian elected to adopt the provisions of SFAS No. 123R, utilizing the modified prospective method, which required compensation expense be measured and recognized based on grant-date fair value for stock option awards granted after July 1, 2005 and portions of stock options awards granted prior to July 1, 2005, but not vested as of July 1, 2005.

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Prior to July 1, 2005, Meridian accounted for its stock based compensation plans pursuant to the intrinsic value method in APB No. 25. Had compensation cost for these plans been determined using the fair value method provided in SFAS No. 123R, Meridian s net earnings for the second quarter of fiscal 2005 and the first six months of fiscal 2005 would have been $3,102,000 and $5,157,000, respectively, compared to reported amounts of $3,196,000 and $5,306,000, respectively. Basic earnings per share for the second quarter of fiscal 2005 and the first six months of fiscal 2005 would have been $0.13 and $0.22, respectively, compared to reported amounts of $0.14 and $0.23, respectively. Diluted earnings per share would not have been impacted.

(e) Cash equivalents

Meridian considers short-term investments with original maturities of 90 days or less to be cash equivalents.

(f) 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):

	March 31, 2006	September 30, 2005
Raw materials	$ 4,144	$ 4,059
Work-in-process	6,299	4,888
Finished goods	7,603	7,838
	$ 18,046	$ 16,785

4. Segment Information:

Meridian s 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 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 consists of the Viral Antigens, BIODESIGN, and OEM Concepts businesses, including the contract manufacture of proteins and other biologicals for use by biopharmaceutical and biotechnology companies engaged in research for new drugs and vaccines.

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Segment information for the interim periods ended March 31, 2006 and 2005 is as follows (in thousands):

	US Diagnostics	European Diagnostics	Life Science	Eliminations[1]	Total
Three Months 2006					
Net sales					
Third-party	$ 17,012	$ 5,319	$ 5,941	$	$ 28,272
Inter-segment	1,930		298	(2,228)	
Operating income	4,748	933	1,319	(23)	6,977
Total assets (March 31, 2006)	99,185	12,134	39,296	(41,050)	109,565
Three Months 2005					
Net sales					
Third-party	$ 14,517	$ 4,671	$ 4,498	$	$ 23,686
Inter-segment	1,775		183	(1,958)	
Operating income	3,613	821	734	30	5,198
Total assets (September 30, 2005)	99,878	11,552	39,382	(40,243)	110,569
Six Months 2006					
Net sales					
Third-party	$ 33,006	$ 9,554	$ 10,620	$	$ 53,180
Inter-segment	3,627		422	(4,049)	
Operating income	9,818	1,539	1,805	(15)	13,147
Six Months 2005					
Net sales					
Third-party	$ 26,389	$ 8,925	$ 7,214	$	$ 42,528
Inter-segment	3,401		345	(3,746)	
Operating income	6,652	1,150	805	58	8,665

(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 US Diagnostics and Life Science include goodwill of $1,612,000 and $7,348,000, respectively, at March 31, 2006, and $1,612,000 and $7,167,000, respectively, at September 30, 2005.

5. Intangible Assets:

A summary of Meridian s acquired intangible assets subject to amortization, as of March 31, 2006 and September 30, 2005 is as follows (in thousands):

	March 31, 2006		**September 30, 2005**	
	Gross Carrying Value	**Accumulated Amortization**	**Gross Carrying Value**	**Accumulated Amortization**
Core products and cell lines	$ 4,698	$ 1,878	$ 4,698	$ 1,733
Manufacturing technologies	5,907	3,552	5,907	3,373
Trademarks, licenses and patents	1,941	1,503	1,941	1,450
Customer lists and supply agreements	11,396	4,624	11,396	4,137
	$23,942	$ 11,557	$23,942	$ 10,693

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The aggregate amortization expense for these intangible assets for the three months ended March 31, 2006 and 2005 was $432,000 and $377,000, respectively. The actual aggregate amortization expense for these intangible assets for the six months ended March 31, 2006 and 2005 was $864,000 and $671,000, respectively.

6. Debenture Conversion and Redemption Transactions:

As of September 30, 2005, Meridian had outstanding a total of $2,451,000 principal amount of convertible subordinated debentures due September 1, 2013, bearing interest at 5%. These debentures are convertible at the option of the holder into common shares at a price of $9.67. Holders converted $618,000 principal amount of debentures into 63,000 common shares during the first six months of fiscal 2006.

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.

Operating Segments:

Meridian s 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 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 consists of the Viral Antigens, BIODESIGN, and OEM Concepts businesses, including the contract manufacture of 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. Meridian believes that the overall breadth of its product lines serves to reduce the variability in consolidated sales from quarter to quarter. Meridian is also evaluating hedging strategies that are intended to reduce the effects of foreign currency translation on sales of the European Diagnostics operating segment.

Results of Operations:

Three Months Ended March 31, 2006 Compared to Three Months Ended March 31, 2005

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Net sales

Overall, net sales increased 19% to $28,272,000 for the second quarter of fiscal 2006 compared to the second quarter of fiscal 2005. Net sales for the US Diagnostics operating segment increased $2,495,000, or 17%, for the European Diagnostics operating segment increased $648,000, or 14%, and for the Life Science operating segment increased $1,443,000, or 32%.

For the US Diagnostics operating segment, the sales increase was primarily related to C. *difficile* products (increased $1,154,000). The increase in sales of C. *difficile* products was driven by the first quarter 2005 launch of the Immuno*Card*® C. *difficile* Toxins A & B rapid diagnostic test in domestic markets, as well as volume growth in Meridian s C. *difficile* Toxins A & B high-volume Premier format. Recent outbreaks of C. *difficile* infections and increased awareness within the marketplace for the need to test for both Toxins A and B have driven volume growth for C. *difficile* products. Two distributors accounted for 45% and 42% of total sales for the US Diagnostics operating segment for the second quarters of fiscal 2006 and fiscal 2005, respectively.

For the European Diagnostics operating segment, sales in local currency increased 24% for the second quarter of fiscal 2006, partially offset by currency translation losses in the amount of $485,000. The increase in local currency was primarily driven by sales of C. *difficile* products (increased $299,000), including Immuno*Card*® *C. difficile* Toxins A & B rapid diagnostic test and H. *pylori* products (increased $429,000).

For the Life Science operating segment, the sales increase for the second quarter of fiscal 2006 was primarily attributable to volume growth in make-to-order bulk antigens and antibodies and the addition of the OEM Concepts business for a full three months in fiscal 2006, compared to two months in fiscal 2005. Sales to one customer accounted for 14% and 21% of total sales for the Life Science operating segment for the second quarters of fiscal 2006 and fiscal 2005, respectively.

For all operating segments combined, international sales were $9,127,000, or 32% of total sales, for the second quarter of fiscal 2006, compared to $7,640,000, or 32% of total sales, for the second quarter of fiscal 2005. Combined domestic exports for the US Diagnostics and Life Science operating segments were $3,806,000 for the second quarter of fiscal 2006, compared to $2,969,000 for the second quarter of fiscal 2005. The remaining international sales were generated by the European Diagnostics operating segment.

Gross Profit

Gross profit increased 22% to $16,580,000 for the second quarter of fiscal 2006 compared to the second quarter of fiscal 2005. Gross profit margins were 59% for the second quarter of fiscal 2006 compared to 57% for the second quarter of fiscal 2005.

Meridian s 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, and 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. Favorable margins on new products and reductions in diagnostic manufacturing costs due to efficiencies and investments in automation also contributed to the improvement in gross profit margins for the second quarter of fiscal 2006.

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Operating Expenses

Operating expenses increased 15% to $9,603,000, for the second quarter of fiscal 2006 compared to the second quarter of fiscal 2005. The overall increase in operating expenses for the second quarter of fiscal 2006 is discussed below.

Research and development expenses increased 40% to $1,203,000 for the second quarter of fiscal 2006 compared to the second quarter of fiscal 2005, and as a percentage of sales, were 4% for both periods. Of this increase, $113,000 related to the US Diagnostics operating segment and $229,000 related to the Life Science operating segment. The increase for the US Diagnostics operating segment was primarily attributable to legal and professional costs associated with patent defense and development, as well as, incentive compensation pursuant to Meridian s corporate incentive plan and higher earnings levels. The increase for the Life Science operating segment was primarily related to the component of research and development scientists labor related to contract work for third-party customers, which is classified in cost of sales or inventory depending on the stage of completion. During the second quarter of fiscal 2006, such labor was primarily focused on internal research and development work, and therefore charged to research and development expense, rather than being classified in cost of sales or inventory.

Selling and marketing expenses remained flat at $4,053,000 for the second quarter of fiscal 2006 compared to the second quarter of fiscal 2005, and as a percentage of sales, decreased from 17% for the second quarter of fiscal 2005 to 14% for the second quarter of fiscal 2006. Selling and marketing expenses for the US Diagnostics operating segment decreased $353,000, partially offset by an increase of $119,000 related to the European Diagnostics operating segment and $231,000 related to the Life Science operating segment. The decrease for the US Diagnostics operating segment was primarily attributable to decreased costs associated with sales force incentive compensation due to the mild upper respiratory season. The increase for the Life Science operating segment was primarily attributable to a full three months of costs for the OEM Concepts business, acquired during the second quarter of fiscal 2005.

General and administrative expenses increased 26% to $4,347,000 for the second quarter of fiscal 2006 compared to the second quarter of fiscal 2005, and as a percentage of sales, were 15% for both periods. Of this increase, $804,000 related to the US Diagnostics operating segment, $47,000 related to the European Diagnostics operating segment, and $34,000 related to the Life Science operating segment. The increase for the US Diagnostics operating segment was primarily attributable to incentive compensation pursuant to Meridian s corporate incentive plan and higher earnings levels, and costs for stock-based compensation related to adoption of SFAS No. 123R. The increase for the Life Science operating segment was primarily attributable to a full three months of costs for the OEM Concepts business, including amortization of acquired intangibles.

Operating Income

Operating income increased 34% to $6,977,000 for the second quarter of fiscal 2006, as a result of the factors discussed above.

Other Income and Expense

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Interest income was $238,000 for the second quarter of fiscal 2006, and related primarily to interest earned on proceeds from the September 2005 common share offering that have been invested in both taxable and tax-exempt cash equivalent instruments.

Interest expense declined 86% to $32,000 for the second quarter of fiscal 2006 compared to the second quarter of fiscal 2005. This decrease was primarily attributable to lower overall debt levels outstanding for the bank term debt, as well as the effects of conversion and redemption transactions related to Meridian s 7% and 5% convertible debentures.

Income Taxes

The effective rate for income taxes was 35% for the second quarter of fiscal 2006 compared to 37% for the second quarter of fiscal 2005. The decrease in the effective tax rate was primarily attributable to the favorable effects of tax-exempt interest and the domestic producers activities deduction for US manufacturers. For the fiscal year ending September 30, 2006, Meridian expects the effective tax rate to approximate 36%.

Six Months Ended March 31, 2006 Compared to Six Months Ended March 31, 2005

Net sales

Overall, net sales increased 25% for the first six months of fiscal 2006 compared to the first six months of fiscal 2005. Net sales for the US Diagnostics operating segment increased $6,617,000, or 25%, for the European Diagnostics operating segment increased $629,000, or 7%, and for the Life Science operating segment increased $3,406,000, or 47%.

For the US Diagnostics operating segment, the sales increase was primarily related to C. *difficile* products (increased $3,483,000), respiratory products (increased $962,000), fungal products (increased $444,000), rotavirus products (increased $435,000), and parasitology products (increased $428,000). The increase in sales of C *difficile* products was driven by the first quarter 2005 launch of the Immuno*Card*® C. *difficile* Toxins A & B rapid diagnostic test in domestic markets, as well as volume growth in Meridian s C. *difficile* Toxins A & B high-volume Premier format. Recent outbreaks of C. *difficile* infections and increased awareness within the marketplace for the need to test for both Toxins A and B have driven volume growth for C. *difficile* products. The increase in sales for respiratory products related to volume growth in tests for Respiratory Syncytial Virus and Mycoplasma. Two distributors accounted for 48% and 44% of total sales for the US Diagnostics operating segment for the first six months of fiscal 2006 and fiscal 2005, respectively.

For the European Diagnostics operating segment, the sales increase includes currency translation losses in the amount of $864,000. Sales in local currency increased 17% for the first six months of fiscal 2006, following an 11% increase during full-year fiscal 2005. The increase in local currency was primarily driven by sales of H. *pylori* products (increased $634,000), C. *difficile* products (increased $373,000), and respiratory products (increased $230,000).

For the Life Science operating segment, the sales increase for the first quarter of fiscal 2006 was primarily attributable to volume growth in make-to-order bulk antigens and antibodies and the addition of the OEM Concepts business for a full six months in fiscal 2006. Sales to one customer accounted for 18% of total sales for the Life Science operating segment for the first six months of fiscal 2006 and fiscal 2005.

For all operating segments combined, international sales were $16,399,000, or 31% of total sales, for the first six months of fiscal 2006, compared to $14,101,000, or 33% of total sales, for the first six months of fiscal 2005. Combined domestic exports for the US Diagnostics and Life Science operating segments were $6,845,000 for the first six months of fiscal 2006, compared to $5,176,000 for the first six months of fiscal 2005. The remaining international sales were generated by the European Diagnostics operating segment.

Gross Profit

Gross profit increased 29% for the first six months of fiscal 2006 compared to the first six months of fiscal 2005. Gross profit margins were 60% for the first six months of fiscal 2006 compared to 58% for the first six months of fiscal 2005.

Meridian s 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, and 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. Favorable margins on new products and reductions in diagnostic manufacturing costs due to efficiencies and investments in automation also contributed to the improvement in gross profit margins for the first six months of fiscal 2006.

Operating Expenses

Operating expenses increased 17% for the first six months of fiscal 2006 compared to the first six months of fiscal 2005. The overall increase in operating expenses for the first six months of fiscal 2006 is discussed below.

Research and development expenses increased 39% for the first six months of fiscal 2006 compared to the first six months of fiscal 2005, and as a percentage of sales, were 4% for both periods. Of this increase, $185,000 related to the US Diagnostics operating segment and $476,000 related to the Life Science operating segment. The increase for the US Diagnostics operating segment was primarily attributable to legal and professional costs associated with patent defense and development, as well as, incentive compensation pursuant to Meridian s corporate incentive plan and higher earnings levels. The increase for the Life Science operating segment was primarily related to the component of research and development scientists labor related to contract work for third-party customers, which is classified in cost of sales or inventory depending on the stage of completion. During the second quarter of fiscal 2006, such labor was primarily focused on internal research and development work, and therefore charged to research and development expense, rather than being classified in cost of sales or inventory.

Selling and marketing expenses increased 12% for the first six months of fiscal 2006 compared to the first six months of fiscal 2005, and as a percentage of sales, decreased from 17% in fiscal 2005, to 16% in fiscal 2006. Of this increase, $383,000 related to the US Diagnostics operating segment, $81,000 related to the European Diagnostics operating segment and $435,000 related to the Life Science operating segment. The increase for the US Diagnostics operating segment was primarily attributable to distributor incentives associated with higher sales levels, product branding and

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advertising activities, and strategic sales and marketing activities, as well as higher salaries and benefits costs. The increase for the Life Science operating segment was primarily due to business development costs and a full six months of costs for the OEM Concepts business, acquired during the second quarter of fiscal 2005.

General and administrative expenses increased 16% for the first six months of fiscal 2006 compared to the first six months of fiscal 2005, and as a percentage of sales, decreased from 16% for the first six months of fiscal 2005, to 15% for the first six months of fiscal 2006. Of this increase, $958,000 related to the US Diagnostics operating segment and $254,000 related to the Life Science operating segment, partially offset by a decrease of $114,000 related to the European Diagnostics operating segment. The increase for the US Diagnostics operating segment was primarily attributable to incentive compensation pursuant to Meridian s corporate incentive plan and higher earnings levels, and costs for stock-based compensation related to adoption of SFAS No. 123R. The increase for the Life Science operating segment was primarily attributable to a full six months of costs for the OEM Concepts business, including amortization of acquired intangibles.

Operating Income

Operating income increased 52% for the first six months of fiscal 2006, as a result of the factors discussed above.

Other Income and Expense

Interest income was $487,000 for the first six months of fiscal 2006, and related primarily to interest earned on proceeds from the September 2005 common share offering that have been invested in both taxable and tax-exempt cash equivalent instruments.

Interest expense declined 87%, or $448,000, for the first six months of fiscal 2006 compared to the first six months of fiscal 2005. This decrease was primarily attributable to lower overall debt levels outstanding for the bank term debt, as well as the effects of conversion and redemption transactions related to Meridian s 7% and 5% convertible debentures.

Income Taxes

The effective rate for income taxes was 36% for the first six months of fiscal 2006 and fiscal 2005. For the fiscal year ending September 30, 2006, Meridian expects the effective tax rate to approximate 36%.

Liquidity and Capital Resources:

Comparative Cash Flow Analysis

Meridian s operating cash flow and financing requirements are determined by analyses of operating and capital spending budgets and consideration of acquisition plans. Meridian has historically maintained line of credit availability to respond quickly to acquisition opportunities. This line of credit has been supplemented by the proceeds from the September 2005 common share offering.

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Net cash provided by operating activities was $6,480,000 for the first six months of fiscal 2006 compared to $6,564,000 for the first six months of fiscal 2005. Higher earnings levels in fiscal 2006 have been offset by higher investments in accounts receivables due to higher sales levels, and timing of payment of income taxes in US jurisdictions.

Net cash used for investing activities decreased to $3,514,000 for the first six months of fiscal 2006 compared to $8,388,000 for the first six months of fiscal 2005. This decrease was primarily attributable to the acquisition of OEM Concepts ($6,045,000) in fiscal 2005, partially offset by a higher earnout payment for fiscal 2006 compared to fiscal 2005 for the Viral Antigens acquisition (see discussion below), and increased investment in capital assets.

Net cash used for financing activities was $4,736,000 for the first six months of 2006, compared to net cash provided by financing activities for the first six months of fiscal 2005 of $3,335,000. Borrowings under the revolving credit facility in fiscal 2005 were used to fund a portion of the purchase price for the acquisition of the OEM Concepts business. Proceeds and tax benefits from the exercise of stock options were $825,000 for the first six months of fiscal 2006, compared to $2,476,000 for the first six months of fiscal 2005. Dividends paid to shareholders were $5,089,000 for the first six months of 2006, compared to $3,386,000 for the first six months of 2005, reflecting increased numbers of shares outstanding related to stock option exercises, the September 2005 offering, and bond conversions, as well as higher dividends declared per share.

Net cash flows from operating activities are anticipated to fund working capital requirements, debt service, and dividends during fiscal 2006.

Capital Resources

Meridian has a $25,000,000 credit facility with a commercial bank. This facility includes $2,500,000 of term debt and capital lease capacity and a $22,500,000 revolving line of credit that expires in September 2007. As of April 30, 2006, there were no borrowings outstanding on the line of credit portion of this facility.

As of September 30, 2005, Meridian had outstanding a total of $2,451,000 principal amount of convertible subordinated debentures due September 1, 2013, bearing interest at 5%. These debentures are convertible at the option of the holder into common shares at a price of $9.67. Holders converted $618,000 principal amount of debentures into 63,000 common shares during the first six months of fiscal 2006. These conversion transactions are expected to reduce annual interest expense by approximately $31,000.

The Viral Antigens acquisition, completed in fiscal 2000, provides for additional purchase consideration up to a maximum remaining amount of $3,491,000, contingent upon Viral Antigens future earnings through September 30, 2006. Earnout consideration is payable each year, following the period earned. Earnout consideration in the amount of $1,313,000 related to fiscal 2005 was paid during the second quarter of fiscal 2006 from operating cash flows.

The OEM Concepts acquisition, completed in fiscal 2005, provides for additional purchase consideration up to a maximum remaining amount of $2,089,000, contingent upon OEM Concepts future calendar-year sales and gross profit through December 31, 2008. Earnout consideration is payable each year, following the period earned. Earnout consideration in the

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amount of $181,000 related to calendar 2005 was paid during the second quarter of fiscal 2006 from operating cash flows.

Meridian s capital expenditures are estimated to be $4,000,000 for fiscal 2006, and may be funded with operating cash flows, availability under the $25,000,000 credit facility, or proceeds from the September 2005 common share offering. Capital expenditures relate to manufacturing and other equipment of a normal and recurring nature, as well as capacity expansions for the Maine and Florida facilities.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Meridian has market risk exposure related to interest rate sensitive debt and foreign currency transactions.

Excluding its revolving line of credit, Meridian has debt obligations in the aggregate amount of $2,141,000 outstanding at March 31, 2006, of which $308,000 bears interest at variable rates. To date, Meridian has not employed a hedging strategy with respect to interest rate risk.

Meridian is exposed to foreign currency risk related to its European distribution operations, including foreign currency denominated intercompany receivables, as well as Euro denominated term debt. The Euro denominated term debt serves as a natural hedge against a portion of the Euro denominated intercompany receivables.

ITEM 4. CONTROLS AND PROCEDURES

As of March 31, 2006, an evaluation was completed under the supervision and with the participation of Meridian s management, including Meridian s Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of Meridian s 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, Meridian s management, including the CEO and CFO, concluded that Meridian s disclosure controls and procedures were effective as of March 31, 2006. There have been no changes in Meridian s internal control over financial reporting identified in connection with the evaluation of internal control that occurred during the second fiscal quarter that has materially affected, or is reasonably likely to materially affect, Meridian s internal control over financial reporting, or changes in other factors that could materially affect internal control subsequent to March 31, 2006.

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PART II. OTHER INFORMATION

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

Meridian s Annual Meeting of Shareholders was held on January 20, 2006. Each of the following matters was voted upon and approved by Meridian s shareholders as indicated below:

(1) Election of the following six directors:
James A. Buzard, 23,612,240 votes for, zero votes against, and 650,704 abstentions.
John A. Kraeutler, 17,796,834 votes for, zero votes against, and 6,466,110 abstentions.
Gary P. Kreider, 16,280,431 votes for, zero votes against, and 7,982,513 abstentions.
William J. Motto, 17,842,474 votes for, zero votes against, and 6,420,470 abstentions.
David C. Phillips, 23,783,374 votes for, zero votes against, and 479,570 abstentions.
Robert J. Ready, 23,355,158 votes for, zero votes against, and 907,786 abstentions.

(2) Ratification of appointment of Grant Thornton LLP as Meridian s independent public accountants for fiscal year 2006: 24,027,394 votes for, 200,132 votes against, and 35,419 abstentions.

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: May 10, 2006 /S/ Melissa Lueke

Melissa Lueke
Vice President and Chief Financial Officer

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