

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

-----  
FORM 10-Q

(MARK ONE)

- ( X ) QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE  
SECURITIES EXCHANGE ACT OF 1934  
FOR THE QUARTERLY PERIOD ENDED MARCH 31, 1998
- ( ) TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE  
SECURITIES EXCHANGE ACT OF 1934  
FOR THE TRANSITION PERIOD FROM \_\_\_\_\_ TO \_\_\_\_\_

1-4462

-----  
COMMISSION FILE NUMBER

STEPAN COMPANY

-----  
(Exact name of registrant as specified in its charter)

Delaware

36 1823834

-----  
(State or other jurisdiction of  
incorporation or organization)

-----  
(I.R.S. Employer  
Identification Number)

Edens and Winnetka Road, Northfield, Illinois 60093

-----  
(Address of principal executive offices)

Registrant's telephone number

(847) 446-7500  
-----

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes      X      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 at April 30, 1998

-----  
Common Stock, \$1 par value

-----  
9,849,000 shares

Part I FINANCIAL INFORMATION

Item 1 - Financial Statements

STEPAN COMPANY  
 CONDENSED CONSOLIDATED BALANCE SHEETS  
 March 31, 1998 and December 31, 1997  
 Unaudited

(Dollars in Thousands)	3/31/98	12/31/97
	-----	-----
<b>ASSETS</b>		
-----		
<b>CURRENT ASSETS:</b>		
Cash and cash equivalents	\$ 5,245	\$ 5,507
Receivables, net	86,553	81,018
Inventories (Note 2)	46,598	48,999
Deferred income taxes	6,636	6,636
Other current assets	3,526	4,322
	-----	-----
Total current assets	148,558	146,482
	-----	-----
<b>PROPERTY, PLANT AND EQUIPMENT:</b>		
Cost	533,345	527,666
Less: Accumulated depreciation	329,627	321,065
	-----	-----
	203,718	206,601
	-----	-----
<b>OTHER ASSETS</b>		
	21,384	21,853
	-----	-----
Total assets	\$373,660	\$ 374,936
	=====	=====
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
-----		
<b>CURRENT LIABILITIES:</b>		
Current maturities of long-term debt	\$ 5,937	\$ 5,957
Accounts payable	42,839	42,894
Accrued liabilities	34,635	33,842
	-----	-----
Total current liabilities	83,411	82,693
	-----	-----
<b>DEFERRED INCOME TAXES</b>		
	31,803	32,258
	-----	-----
<b>LONG-TERM DEBT, less current maturities</b>		
	93,263	94,898
	-----	-----
<b>OTHER NON-CURRENT LIABILITIES</b>		
	23,909	27,489
	-----	-----
<b>STOCKHOLDERS' EQUITY:</b>		
5-1/2% convertible preferred stock, cumulative, voting without par value; authorized 2,000,000 shares; issued 786,827 shares in 1998 and 788,434 shares in 1997	19,671	19,711
Common stock, \$1 par value; authorized 15,000,000 shares; issued 10,353,786 shares in 1998 and 10,341,952 shares in 1997	10,354	10,342
Additional paid-in capital	8,707	8,091
Cumulative translation adjustments	(7,936)	(7,337)
Retained earnings (approximately \$38,830 unrestricted in 1998 and \$52,623 in 1997)	124,993	120,854
	-----	-----
	155,789	151,661
Less: Treasury stock, at cost	14,515	14,063
	-----	-----
Stockholders' equity	141,274	137,598
	-----	-----
Total liabilities and stockholders' equity	\$373,660	\$ 374,936

=====

=====

The accompanying Notes to Condensed Consolidated Financial Statements are an integral part of these condensed consolidated balance sheets.

STEPAN COMPANY  
CONSOLIDATED STATEMENTS OF INCOME  
For the Three Months Ended March 31, 1998 and 1997  
Unaudited

(In Thousands, except per share amounts)

	Three Months Ended March 31	
	1998	1997
NET SALES	\$150,388	\$139,670
Cost of Sales	122,559	115,625
	27,829	24,045
Gross Profit		
Operating Expenses:		
Marketing	5,953	4,866
Administrative	5,174	4,765
Research, Development and Technical Services	5,304	4,909
	16,431	14,540
Operating Income	11,398	9,505
Other Income (Expense):		
Interest, Net	(1,907)	(1,870)
Income (Loss) from Equity Joint Ventures	47	(96)
	(1,860)	(1,966)
Income Before Income Taxes	9,538	7,539
Provision for Income Taxes	3,816	3,062
NET INCOME	\$ 5,722	\$ 4,477
Net Income Per Common Share (Note 3)		
Basic	\$ 0.56	\$ 0.43
Diluted	\$ 0.52	\$ 0.41
Dividends per Common Share	\$ 0.1375	\$ 0.1250
Average Common Shares Outstanding	9,846	9,839

The accompanying Notes to Condensed Consolidated Financial Statements are an integral part of these statements.

STEPAN COMPANY  
CONSOLIDATED STATEMENTS OF CASH FLOWS  
For the Three Months Ended March 31, 1998 and 1997  
Unaudited

(Dollars In Thousands)	3/31/98	3/31/97
	-----	-----
<b>NET CASH FLOW FROM OPERATING ACTIVITIES</b>		
Net income	\$ 5,722	\$ 4,477
Depreciation and amortization	9,318	8,876
Deferred revenue recognition	(1,081)	(724)
Customer prepayments	-	2,000
Deferred income taxes	(406)	(599)
Non-current environmental and legal liabilities	(548)	(540)
Other non-cash items	87	284
Changes in Working Capital:		
Receivables, net	(5,535)	823
Inventories	2,401	5,202
Accounts payable and accrued liabilities	(1,213)	(5,308)
Other	796	50
	-----	-----
Net Cash Provided by Operating Activities	9,541	14,541
	-----	-----
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Expenditures for property, plant and equipment	(6,401)	(9,332)
Other non-current assets	125	228
	-----	-----
Net Cash Used for Investing Activities	(6,276)	(9,104)
	-----	-----
<b>CASH FLOWS FROM FINANCING AND OTHER RELATED ACTIVITIES</b>		
Revolving debt and notes payable to banks, net	(1,610)	(3,729)
Other debt repayments	(57)	(1,247)
Sales of treasury stock, net	(452)	(381)
Dividends paid	(1,583)	(1,500)
Other non-cash items	175	(325)
	-----	-----
Net Cash Used for Financing and Other Related Activities	(3,527)	(7,182)
	-----	-----
NET DECREASE IN CASH AND CASH EQUIVALENTS	(262)	(1,745)
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	5,507	4,778
	-----	-----
CASH AND CASH EQUIVALENTS AT END OF PERIOD	\$ 5,245	\$ 3,033
	=====	=====
<b>CASH PAID DURING THE PERIOD FOR:</b>		
Interest	\$ 887	\$ 855
Income taxes	\$ 896	\$ 1,872

The accompanying Notes to Condensed Consolidated Financial Statements are an integral part of these statements.

STEPAN COMPANY  
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS  
March 31, 1998 and December 31, 1997  
Unaudited

1. CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

The condensed consolidated financial statements included herein have been prepared by the company, without audit, pursuant to the rules and regulations of the Securities and Exchange Commission. Certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted pursuant to such rules and regulations, although management believes that the disclosures are adequate and make the information presented not misleading. It is suggested that these condensed consolidated financial statements be read in conjunction with the financial statements and the notes thereto included in the company's latest Annual Report to Stockholders and the Annual Report to the Securities and Exchange Commission on Form 10-K for the year ended December 31, 1997. In the opinion of management all adjustments, consisting only of normal recurring adjustments, necessary to present fairly the consolidated financial position of Stepan Company as of March 31, 1998, and the consolidated results of operations and cash flows for the three months then ended, have been included.

2. INVENTORIES

Inventories include the following amounts:

(Dollars in Thousands)	3/31/98	12/31/97
	-----	-----
Inventories valued primarily on LIFO basis -		
Finished products	\$ 29,286	\$ 31,110
Raw materials	17,312	17,889
	-----	-----
Total inventories	\$ 46,598	\$ 48,999
	=====	=====

If the first-in, first-out (FIFO) inventory valuation method had been used for all inventories, inventory balances would have been approximately \$11,700,000 and \$11,900,000 higher than reported at March 31, 1998, and December 31, 1997, respectively.

3. NET INCOME PER COMMON SHARE

In 1997, the company adopted Statement of Financial Accounting Standards No. 128 (SFAS No. 128), "Earnings per Share", effective December 15, 1997. Accordingly, basic net income per common share amounts are computed by dividing net income less the convertible preferred stock dividend requirement by the weighted average number of common shares outstanding. Diluted net income per share amounts are based on an increased number of common shares that would be outstanding assuming the exercise of

certain outstanding stock options and the conversion of the convertible preferred stock, when such conversion would have the effect of reducing net income per share. The adoption of SFAS No. 128 had no effect on the net income per common share amounts reported for the first quarter of 1997; therefore, no restatement was necessary. For computation of earnings per share, reference should be made to Exhibit 11.

#### 4. CONTINGENCIES

There are a variety of legal proceedings pending or threatened against the company. Some of these proceedings may result in fines, penalties, judgments or costs being assessed against the company at some future time. The company's operations are subject to extensive local, state and federal regulations, including the federal Comprehensive Environmental Response, Compensation and Liability Act of 1980 ("Superfund") and the Superfund amendments of 1986. The company, and others, have been named as potentially responsible parties at affected geographic sites. As discussed in Management's Discussion and Analysis of Financial Condition and Results of Operations included in this filing, the company believes that it has made adequate provisions for the costs it may incur with respect to these sites. The company has estimated a range of possible environmental and legal losses from \$4.1 million to \$25.7 million at March 31, 1998. At March 31, 1998, the company's reserve was \$20.1 million for legal and environmental matters compared to \$20.6 million at December 31, 1997.

For certain sites, estimates cannot be made of the total costs of compliance, or the company's share of such costs; accordingly, the company is unable to predict the effect thereof on future results of operations. In the event of one or more adverse determinations in any annual or interim period, the impact on results of operations for those periods could be material. However, based upon the company's present belief as to its relative involvement at these sites, other viable entities' responsibilities for cleanup and the extended period over which any costs would be incurred, the company believes that these matters will not have a material effect on the company's financial position. Certain of these matters are discussed in Item 3, Legal Proceedings, in the 1997 Form 10-K Annual Report and in other filings of the company with the Securities and Exchange Commission, which are available upon request from the company.

#### 5. COMPREHENSIVE INCOME

In 1997, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 130, "Reporting Comprehensive Income" (SFAS No. 130), which is effective for fiscal years beginning after December 15, 1997. SFAS No. 130 requires that comprehensive income be reported in a financial statement that is displayed with the same prominence as other financial statements (although for interim financial reporting footnote disclosure of comprehensive income is acceptable). Comprehensive income includes net income and all other nonowner changes in equity that are not reported in net income.

The company adopted SFAS No. 130 in 1998. For the quarters ended March 31, 1998 and 1997, the company's comprehensive income included net income and foreign currency translation losses. The foreign currency translation losses totaled \$599,000 and \$1,382,000 for the quarters ended March 31, 1998 and 1997, respectively. Therefore, total comprehensive income was \$5,123,000 for the quarter ended March 31, 1998, compared to \$3,095,000 for the same quarter of 1997.



STEPAN COMPANY  
Management's Discussion and Analysis of  
Financial Condition and Results of Operations

The following is management's discussion and analysis of certain significant factors which have affected the company's financial condition and results of operations during the interim period included in the accompanying condensed consolidated financial statements.

#### LIQUIDITY AND CAPITAL RESOURCES

For the first quarter of 1998, net cash from operations totaled \$9.5 million, a decrease of \$5.0 million from the same period in 1997. Net income was up by \$1.2 million for the current quarter while customer prepayments credited to deferred revenue fell to zero from \$2.0 million last year. During 1998, changes in working capital have resulted in a \$3.6 million use of cash compared to \$0.8 million source for the same period in 1997.

Capital expenditures totaled \$6.4 million for first quarter, down by \$2.9 million, or 31%, from \$9.3 million for the comparable period last year. However, it is projected that total year spending for 1998 will exceed last year's total of \$35.6 million.

Since last year-end, total company debt has decreased by \$1.7 million, to \$99.2 million. At March 31, 1998, the ratio of long-term debt to long-term debt plus shareholders' equity was 39.8 percent, down from 40.8 percent as of last year end.

The company maintains contractual relationships with its domestic banks which provide for \$45 million of revolving credit which may be drawn upon as needed for general corporate purposes. At March 31, 1998, the company had \$11.8 million outstanding under this revolving credit line. The company also meets short-term liquidity requirements through uncommitted bank lines of credit. The company's foreign subsidiaries maintain committed and uncommitted bank lines of credit in their respective countries to meet working capital requirements as well as to fund capital expenditure programs and acquisitions.

The company anticipates that cash from operations and from committed credit facilities will be sufficient to fund anticipated capital expenditures, dividends and other planned financial commitments for the foreseeable future.

#### RESULTS OF OPERATIONS

##### Three Months Ended March 31, 1998 and 1997

Net income for the first quarter ended March 31, 1998, was \$5.7 million, or \$.56 per share, up 28 percent from \$4.5 million, or \$.43 per share reported for the same quarter a year earlier. Net

sales increased eight percent to \$150.4 million from \$139.7 million reported last year. Net sales by product group were:

(Dollars in Thousands)

Three Months  
Ended March 31

	1998	1997	% Change
Net Sales:			
Surfactants	\$116,703	\$107,718	+8%
Polymers	25,729	24,928	+3%
Specialty Products	7,956	7,024	+13%
Total	\$150,388	\$139,670	+8%

Surfactants net sales increased eight percent between years. Domestic operations, which accounted for about 80 percent of total surfactant revenues, reported net sales that were \$6.3 million, or seven percent, greater than those of a year ago. An 11 percent increase in sales volume, due largely to stronger demand for personal care products, led to the improvement. The company continued to benefit from last year's second quarter acquisition of Lonza Inc.'s West Coast anionic surfactant business and from some consolidation in the surfactant marketplace. Foreign operations net sales grew \$2.7 million, or 13 percent, on a 28 percent increase in sales volume. The company's Mexican, Canadian and European subsidiaries posted volume increases of 86 percent, 24 percent and seven percent, respectively.

Surfactants gross profit increased 20 percent from \$17.3 million for the first quarter of 1997 to \$20.8 million for the first quarter of 1998. Both domestic and foreign operations contributed to the improvement. Domestic gross profit increased \$2.4 million, or 17 percent, on the strength of the sales volume noted earlier. Better margins, arising from an improved sales mix also contributed to the higher domestic gross profit. Foreign operations gross profit increased \$1.1 million, or 41 percent. Most of the increase was attributable to the greater sales volumes for the company's Mexican and Canadian subsidiaries. The European subsidiaries continued to be hurt by weak margins.

Polymers net sales increased three percent between years. Sales volume grew 15 percent. Volumes for polyurethane polyols and phthalic anhydride (PA) improved 18 percent and 15 percent, respectively, and volume for polyurethane systems decreased three percent. The polyurethane polyols volume growth led to a \$2.0 million, or 21 percent, increase in revenues. Despite its volume increase, PA's net sales fell by \$.6 million, or five percent. Lower average selling prices, due in part to competitive pressures arising from oversupply in the PA marketplace, led to the net sales decline. Polyurethane systems net sales decreased \$.6 million, or 14 percent, due to sales mix and lower sales volumes.

Polymers gross profit decreased 11 percent to \$5.0 million in the first quarter of 1998 from \$5.7 million in the first quarter of 1997. Reduced margins for PA, arising from the earlier noted competitive pressures, more than offset the polymer sales volume gain. Gross profit for polyurethane systems also fell due to sales mix and lower sales volumes. Improved gross profit for polyurethane polyols, attributable to increased volume and margins, partially offset the declines in PA and polyurethane systems.

Specialty products net sales were up 13 percent due to higher sales volumes. Gross profit increased to \$1.9 million for the first three months of 1998 from \$1.0 million for the first three months of 1997.

Operating expenses increased 13 percent between years. Marketing, administrative and research, development and technical services expenses increased 22 percent, nine percent and eight percent, respectively. Higher salary and fringe benefit costs led to the increases in each of the expense classifications.

#### 1998 OUTLOOK

The company is optimistic about achieving record sales and earnings in 1998. Surfactant sales volumes and profit are expected to remain strong, particularly in North America. Polymer earnings should improve on gains in the polyurethane polyol business even if PA pricing remains weak.

#### ENVIRONMENTAL AND LEGAL MATTERS

The company is subject to extensive federal, state and local environmental laws and regulations. Although the company's environmental policies and practices are designed to ensure compliance with these laws and regulations, future developments and increasingly stringent environmental regulation could require the company to make additional unforeseen environmental expenditures. The company will continue to invest in the equipment and facilities necessary to comply with existing and future regulations. During the first quarter of 1998, company expenditures for capital projects related to the environment were \$0.8 million and should approximate \$5.0 million to \$7.0 million for the full year 1998. These projects are capitalized and typically depreciated over 10 years. Recurring costs associated with the operation and maintenance of facilities for waste treatment and disposal and managing environmental compliance in ongoing operations at our manufacturing locations were \$2.0 million for the first three months of 1998. While difficult to project, it is not anticipated that these recurring expenses will increase significantly in the future.

The company has been named by the government as a potentially responsible party at 16 waste disposal sites where cleanup costs have been or may be incurred under the federal Comprehensive Environmental Response, Compensation and Liability Act and similar state statutes. In addition, damages are being claimed against the company in general liability actions for alleged personal injury or property damage in the case of some disposal and plant sites. The company believes that it has made adequate provisions for the costs it may incur with respect to these sites. The company has estimated a range of possible environmental and legal losses from \$4.1 million to \$25.7 million at March 31, 1998. At March 31, 1998, the company's reserve was \$20.1 million for legal and environmental matters compared to \$20.6 million at December 31, 1997. During the first three months of 1998, expenditures related to legal and environmental matters approximated \$0.7 million. For certain sites, estimates cannot be made of the total costs of compliance or the company's share of such costs; accordingly, the company is unable to predict the effect thereof on future results of operations. In the event of one or more adverse

determinations in any annual or interim period, the impact on results of operations for those periods could be material. However, based upon the company's present belief as to its relative involvement at these sites, other viable entities' responsibilities for cleanup and the extended period over which any costs would be incurred, the company believes that these matters will not have a material effect on the company's financial position. Certain of these matters are discussed in Item 3, Legal Proceedings, in the 1997 Form 10-K Annual Report and in other filings of the company with the Securities and Exchange Commission, which are available upon request from the company.

#### ACCOUNTING STANDARD

The company adopted Financial Accounting Standards No. 130, "Reporting Comprehensive Income" (SFAS No. 130), in 1998. The adoption of SFAS No. 130 has no effect on reported Net Income or Net Income per Common Share (see note 5 of the Notes to Condensed Consolidated Financial Statements for further information).

#### OTHER

Except for the historical information contained herein, the matters discussed in this document are forward looking statements that involve risks and uncertainties. The results achieved this quarter are not necessarily an indication of future prospects for the company. Actual results in future quarters may differ materially. Potential risks and uncertainties include, among others, fluctuations in the volume and timing of product orders, changes in demand for the company's products, changes in technology, continued competitive pressures in the marketplace, outcome of environmental contingencies, availability of raw materials, foreign currency fluctuations and the general economic conditions.

-----  
Item 1 - Legal Proceedings

Stepan Company is aware of the fact that three plaintiffs' law firms located in New Jersey have filed a complaint in the Superior Court of New Jersey, Middlesex County, annexing approximately 270 separate case captions, collectively referred to as Gilberg, et al. V. Stepan, et al. and Accurso, et al. v. Stepan, et al., Civil Action No. 98-139 (KSH), alleging personal and property injury as well as wrongful death, on behalf of certain citizens of Maywood, Rochelle Park and Lodi, New Jersey. Stepan Company has accepted service in Gilberg, et al. pursuant to a court request. The injuries and deaths are alleged to have been the result of radiological and chemical contamination from the company's Maywood, New Jersey site. The company has asserted in legal papers filed by it that plaintiffs did not follow proper procedure under State Court rules and that the multiple suits therefore were not properly filed. The complaint and annexed captions, consistent with applicable federal law, have been removed to the Federal District Court in Newark where the issue of jurisdiction will be determined. The company believes it did not cause the alleged contamination. In addition, the company believes it has other valid defenses. Moreover, as it is uncertain as of this date how many, if any, lawsuits have been properly filed or when the company will be served in any or all of the lawsuits, the company cannot estimate what its liability, if any, will be.

## Item 4 - Submission of Matters to a Vote of Security Holders

- (A) The company's 1997 Annual Meeting of Stockholders was held on May 5, 1998.
- (B) Proxies were solicited by management pursuant to Regulation 14 under the Securities Exchange Act of 1934, there was no solicitation in opposition to management's nominees as listed in the proxy statement, and all such nominees were elected.
- (C) A majority of the outstanding shares voted to ratify the appointment of Arthur Andersen LLP as independent auditors for the company for 1998.

9,224,658	For
65,793	Against
16,279	Abstentions
402	Broker Non-Vote

## Item 6 - Exhibits and Reports on Form 8-K

- (A) Exhibits
  - (11) Statement re computation of Per Share Earnings
  - (27) Financial Data Schedule
- (B) Reports on Form 8-K
  - None

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

STEPAN COMPANY

/s/ Walter J. Klein

Walter J. Klein  
Vice President - Finance  
Principal Financial and Accounting Officer

Date: May 13, 1998

STEPAN COMPANY  
 STATEMENT RE COMPUTATION OF PER SHARE EARNINGS  
 For the Three Months Ended March 31, 1998 and 1997  
 Unaudited

(In Thousands, except per share amounts)

	Three Months Ended March 31	
	1998	1997
	----	----
Computation of Basic Earnings per Share		
-----		
Net income	\$ 5,722	\$ 4,477
Deduct dividends on preferred stock	224	267
	-----	-----
Income applicable to common stock	\$ 5,498	\$ 4,210
	=====	=====
Weighted-average number of shares outstanding	9,846	9,839
Per share earnings*	\$ 0.558	\$ 0.428
	=====	=====
Computation of Diluted Earnings per Share		
-----		
Net income	\$ 5,722	\$ 4,477
	=====	=====
Weighted-average number of shares outstanding	9,846	9,839
Add net shares issuable from assumed exercise of options (under treasury stock method)	391	276
Add weighted-average shares issuable from assumed conversion of convertible preferred stock	746	887
	-----	-----
Shares applicable to diluted earnings	10,983	11,002
	=====	=====
Per share diluted earnings*	\$ 0.521	\$ 0.407
	=====	=====

---

\* Rounded

This calculation is submitted in accordance with Regulation S-K, item 601(b)(11).





This schedule contains summary financial information extracted from condensed consolidated balance sheet as of March 31, 1998 and consolidated statement of income for the three months then ended and is qualified in its entirety by reference to such financial statements.

1,000

3-MOS		
	DEC-31-1998	
	JAN-01-1998	
	MAR-31-1998	
		5,245
	0	
	86,553	
	0	
	46,598	
	148,558	533,345
	329,627	
	373,660	
83,411		0
0		
	19,671	
	10,354	
	111,249	
373,660		
	150,388	
150,388		122,559
	138,990	
	0	
	0	
1,907		
	9,538	
	3,816	
5,722		
	0	
	0	
		0
	5,722	
	0.56	
	0.52	