

HENRY SCHEIN INC  
Form 10-Q  
May 06, 2014  
UNITED STATES

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

(Mark One)

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

For the quarterly period ended March 29, 2014

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: 0-27078

HENRY SCHEIN, INC.

(Exact name of registrant as specified in its charter)

Delaware  
(State or other jurisdiction of  
incorporation or organization)

11-3136595  
(I.R.S. Employer Identification No.)

135 Duryea Road  
Melville, New York  
(Address of principal executive offices)  
11747  
(Zip Code)

(631) 843-5500  
(Registrant's telephone number, including area code)

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

Yes

No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

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.

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Large accelerated filer

Accelerated filer

Non-accelerated filer

(Do not check if a smaller reporting company)

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

As of April 28, 2014, there were 85,364,454 shares of the registrant's common stock outstanding.

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PART I. FINANCIAL INFORMATION  
ITEM 1. CONSOLIDATED FINANCIAL STATEMENTS  
HENRY SCHEIN, INC.  
CONSOLIDATED BALANCE SHEETS  
(in thousands, except share and per share data)

	March 29, 2014 (unaudited)	December 28, 2013
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$ 129,115	\$ 188,616
Accounts receivable, net of reserves of \$80,286 and \$78,298	1,116,502	1,055,216
Inventories, net	1,246,873	1,250,403
Deferred income taxes	77,388	63,865
Prepaid expenses and other	307,028	276,565
Total current assets	2,876,906	2,834,665
Property and equipment, net	285,528	275,888
Goodwill	1,802,905	1,635,005
Other intangibles, net	587,202	417,133
Investments and other	327,569	461,945
Total assets	\$ 5,880,110	\$ 5,624,636
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Current liabilities:		
Accounts payable	\$ 685,915	\$ 824,495
Bank credit lines	144,042	29,508
Current maturities of long-term debt	105,984	5,441
Accrued expenses:		
Payroll and related	182,007	216,629
Taxes	165,814	145,161
Other	329,499	329,429
Total current liabilities	1,613,261	1,550,663
Long-term debt	541,687	450,233
Deferred income taxes	287,151	198,674
Other liabilities	136,253	139,526
Total liabilities	2,578,352	2,339,096
Redeemable noncontrolling interests	482,701	497,539
Commitments and contingencies		
Stockholders' equity:		
Preferred stock, \$.01 par value, 1,000,000 shares authorized, none outstanding	-	-

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Common stock, \$.01 par value, 240,000,000 shares  
authorized,

85,563,353 outstanding on March 29, 2014 and		
85,622,452 outstanding on December 28, 2013	856	856
Additional paid-in capital	297,057	318,225
Retained earnings	2,445,536	2,398,267
Accumulated other comprehensive income	72,862	67,849
Total Henry Schein, Inc. stockholders' equity	2,816,311	2,785,197
Noncontrolling interests	2,746	2,804
Total stockholders' equity	2,819,057	2,788,001
Total liabilities, redeemable noncontrolling interests and stockholders' equity	\$ 5,880,110	\$ 5,624,636

See accompanying notes.

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HENRY SCHEIN, INC.  
 CONSOLIDATED STATEMENTS OF INCOME  
 (in thousands, except per share data)  
 (unaudited)

	Three Months Ended	
	March 29, 2014	March 30, 2013
Net sales	\$2,430,159	\$2,293,511
Cost of sales	1,733,446	1,646,520
Gross profit	696,713	646,991
Operating expenses:		
Selling, general and administrative	539,445	493,362
Operating income	157,268	153,629
Other income (expense):		
Interest income	3,455	3,205
Interest expense	(5,258 )	(12,727 )
Other, net	3,580	(370 )
Income before taxes and equity in earnings of affiliates	159,045	143,737
Income taxes	(49,623 )	(45,852 )
Equity in earnings of affiliates	706	801
Net income	110,128	98,686
Less: Net income attributable to noncontrolling interests	(8,029 )	(7,208 )
Net income attributable to Henry Schein, Inc.	\$102,099	\$91,478
Earnings per share attributable to Henry Schein, Inc.:		
Basic	\$1.20	\$1.06
Diluted	\$1.18	\$1.03
Weighted-average common shares outstanding:		
Basic	84,808	86,654
Diluted	86,518	88,792

See accompanying notes.

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HENRY SCHEIN, INC.  
 CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME  
 (in thousands)  
 (unaudited)

	Three Months Ended	
	March 29, 2014	March 30, 2013
Net income	\$ 110,128	\$ 98,686
Other comprehensive income (loss), net of tax:		
Foreign currency translation gain (loss)	7,792	(40,441 )
Unrealized loss from foreign currency hedging activities	(948 )	(159 )
Unrealized investment gain (loss)	11	(9 )
Pension adjustment gain	268	738
Other comprehensive income (loss), net of tax	7,123	(39,871 )
Comprehensive income	117,251	58,815
Comprehensive income attributable to noncontrolling interests:		
Net income	(8,029 )	(7,208 )
Foreign currency translation loss (gain)	(2,110 )	1,478
Comprehensive income attributable to noncontrolling interests	(10,139 )	(5,730 )
Comprehensive income attributable to Henry Schein, Inc.	\$ 107,112	\$ 53,085

See accompanying notes.



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HENRY SCHEIN, INC.  
 CONSOLIDATED STATEMENT OF CHANGES IN STOCKHOLDERS' EQUITY  
 (in thousands, except share and per share data)

	Common Stock \$.01 Par Value		Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income	Noncontrolling Interests	Total Stockholders' Equity
	Shares	Amount					
Balance, December 28, 2013	85,622,452	\$ 856	\$ 318,225	\$ 2,398,267	\$ 67,849	\$ 2,804	\$ 2,788,001
Net income (excluding \$7,939 attributable to Redeemable noncontrolling interests)	-	-	-	102,099	-	90	102,189
Foreign currency translation gain (loss) (excluding gain of \$2,129 attributable to Redeemable noncontrolling interests)	-	-	-	-	5,682	(19 )	5,663
Unrealized loss from foreign currency hedging activities, including tax benefit of \$204	-	-	-	-	(948 )	-	(948 )
Unrealized investment gain, net of tax of \$7	-	-	-	-	11	-	11
Pension adjustment gain, net of tax of \$78	-	-	-	-	268	-	268
Dividends paid	-	-	-	-	-	(129 )	(129 )
Change in fair value of redeemable securities	-	-	(9,263 )	-	-	-	(9,263 )
Other adjustments	-	-	(31 )	-	-	-	(31 )
Repurchase and retirement of	(647,315 )	(6 )	(20,470 )	(54,830 )	-	-	(75,306 )

common stock							
Stock issued upon exercise of stock options, including tax benefit of \$4,270	335,935	3	20,717	-	-	-	20,720
Stock-based compensation expense	425,012	4	8,959	-	-	-	8,963
Shares withheld for payroll taxes	(172,731 )	(1 )	(20,939 )	-	-	-	(20,940 )
Liability for cash settlement stock-based compensation awards	-	-	(141 )	-	-	-	(141 )
Balance, March 29, 2014	85,563,353	\$ 856	\$ 297,057	\$ 2,445,536	\$ 72,862	\$ 2,746	\$ 2,819,057

See accompanying notes.

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HENRY SCHEIN, INC.  
CONSOLIDATED STATEMENTS OF CASH FLOWS  
(in thousands)  
(unaudited)

	Three Months Ended	
	March 29, 2014	March 30, 2013
<b>Cash flows from operating activities:</b>		
Net income	\$ 110,128	\$ 98,686
<b>Adjustments to reconcile net income to net cash used in operating activities:</b>		
Depreciation and amortization	36,136	32,393
Accelerated amortization of deferred financing costs	-	6,203
Stock-based compensation expense	8,963	5,310
Provision for losses on trade and other accounts receivable	1,323	840
Provision for deferred income taxes	15,744	6,371
Equity in earnings of affiliates	(706 )	(801 )
Distributions from equity affiliates	1,972	2,881
Other	1,973	3,291
<b>Changes in operating assets and liabilities, net of acquisitions:</b>		
Accounts receivable	(29,602 )	(25,392 )
Inventories	41,559	54,011
Other current assets	(23,446 )	14,003
Accounts payable and accrued expenses	(219,293 )	(235,843 )
Net cash used in operating activities	(55,249 )	(38,047 )
<b>Cash flows from investing activities:</b>		
Purchases of fixed assets	(18,484 )	(11,862 )
Payments for equity investments and business acquisitions, net of cash acquired	(144,679 )	(32,359 )
Other	(3,931 )	(68 )
Net cash used in investing activities	(167,094 )	(44,289 )
<b>Cash flows from financing activities:</b>		
Proceeds from bank borrowings	114,768	22,827
Proceeds from issuance of debt	190,387	328,000
Debt issuance costs	-	(236 )
Principal payments for long-term debt	(396 )	(232,905 )
Proceeds from issuance of stock upon exercise of stock options	16,450	11,799
Payments for repurchases of common stock	(75,306 )	(73,449 )
Excess tax benefits related to stock-based compensation	3,350	3,364
Distributions to noncontrolling shareholders	(3,763 )	(2,792 )
Acquisitions of noncontrolling interests in subsidiaries	(83,793 )	(535 )
Net cash provided by financing activities	161,697	56,073

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Effect of exchange rate changes on cash and cash equivalents	1,145	(5,255 )
Net change in cash and cash equivalents	(59,501 )	(31,518 )
Cash and cash equivalents, beginning of period	188,616	122,080
Cash and cash equivalents, end of period	\$ 129,115	\$ 90,562

See accompanying notes.

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HENRY SCHEIN, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
(in thousands, except per share data)  
(unaudited)

Note 1 – Basis of Presentation

Our consolidated financial statements include our accounts, as well as those of our wholly-owned and majority-owned subsidiaries. Certain prior period amounts have been reclassified to conform to the current period presentation.

Our accompanying unaudited consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States (“U.S. GAAP”) for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnote disclosures required by U.S. GAAP for complete financial statements.

The consolidated financial statements reflect all adjustments considered necessary for a fair presentation of the consolidated results of operations and financial position for the interim periods presented. All such adjustments are of a normal recurring nature. These unaudited interim consolidated financial statements should be read in conjunction with the audited consolidated financial statements and notes to the consolidated financial statements contained in our Annual Report on Form 10-K for the year ended December 28, 2013.

The preparation of financial statements in conformity with U.S. GAAP requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities, and disclosure of contingent assets and liabilities, at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. The results of operations for the three months ended March 29, 2014 are not necessarily indicative of the results to be expected for any other interim period or for the year ending December 27, 2014.

Note 2 – Segment Data

We conduct our business through two reportable segments: health care distribution and technology and value-added services. These segments offer different products and services to the same customer base. The health care distribution reportable segment aggregates our global dental, animal health and medical operating segments. This segment consists of consumable products, small equipment, laboratory products, large equipment, equipment repair services, branded and generic pharmaceuticals, vaccines, surgical products, diagnostic tests, infection-control products and vitamins.

Our global dental group serves office-based dental practitioners, dental laboratories, schools and other institutions. Our global animal health group serves animal health practices and clinics. Our global medical group serves office-based medical practitioners, ambulatory surgery centers, other alternate-care settings and other institutions. Our global dental, animal health and medical groups serve practitioners in 26 countries worldwide.

Our global technology and value-added services group provides software, technology and other value-added services to health care practitioners. Our technology group offerings include practice management software systems for dental and medical practitioners and animal health clinics. Our value-added practice solutions include financial services on a non-recourse basis, e-services and continuing education services for practitioners.

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HENRY SCHEIN, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)  
(in thousands, except per share data)  
(unaudited)

## Note 2 – Segment Data – (Continued)

The following tables present information about our reportable and operating segments:

	Three Months Ended	
	March 29, 2014	March 30, 2013
<b>Net Sales:</b>		
Health care distribution (1):		
Dental	\$ 1,296,928	\$ 1,190,795
Animal health	654,488	639,142
Medical	397,414	388,862
Total health care distribution	2,348,830	2,218,799
Technology and value-added services (2)	81,329	74,712
Total	\$ 2,430,159	\$ 2,293,511

(1) Consists of consumable products, small equipment, laboratory products, large equipment, equipment repair services, branded and generic pharmaceuticals, vaccines, surgical products, diagnostic tests, infection-control products and vitamins.

(2) Consists of practice management software and other value-added products, which are distributed primarily to health care providers, and financial and other services, including e-services and continuing education services for practitioners.

	Three Months Ended	
	March 29, 2014	March 30, 2013
<b>Operating Income:</b>		
Health care distribution	\$ 133,819	\$ 134,460
Technology and value-added services	23,449	19,169
Total	\$ 157,268	\$ 153,629

## Note 3 – Debt

## Bank Credit Lines

On September 12, 2012, we entered into a new \$500 million revolving credit agreement (the “Credit Agreement”) with a \$200 million expansion feature, which expires on September 12, 2017. There was \$115.0 million outstanding under this revolving credit facility as of March 29, 2014. The interest rate is based on USD LIBOR plus a spread based on our leverage ratio at the end of each financial reporting quarter. The Credit Agreement provides, among other things,

that we are required to maintain certain interest coverage and maximum leverage ratios, and contains customary representations, warranties and affirmative covenants. The Credit Agreement also contains customary negative covenants, subject to negotiated exceptions on liens, indebtedness, significant corporate changes (including mergers), dispositions and certain restrictive agreements. As of March 29, 2014, there were \$10.1 million of letters of credit provided to third parties under the credit facility.

As of March 29, 2014, we had various other short-term bank credit lines available, of which \$29.0 million was outstanding. At March 29, 2014, borrowings under all of our credit lines had a weighted average interest rate of 1.34%.

#### Term Loan Note

On January 9, 2014, we entered into a \$100 million term loan, of which \$100.0 million was outstanding as of March 29, 2014. The interest rate on this note is LIBOR plus 75 basis points. The note matures on July 9, 2014.

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HENRY SCHEIN, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)  
(in thousands, except per share data)  
(unaudited)

## Note 3 – Debt – (Continued)

## Private Placement Facilities

On August 10, 2010, we entered into \$400 million private placement facilities with two insurance companies. On April 30, 2012, we increased our available credit facilities by \$375 million by entering into a new agreement with one insurance company and amending our existing agreements with two insurance companies. These facilities are available on an uncommitted basis at fixed rate economic terms to be agreed upon at the time of issuance, from time to time during a three year issuance period, through April 26, 2015. The facilities allow us to issue senior promissory notes to the lenders at a fixed rate based on an agreed upon spread over applicable treasury notes at the time of issuance. The term of each possible issuance will be selected by us and can range from five to 15 years (with an average life no longer than 12 years). The proceeds of any issuances under the facilities will be used for general corporate purposes, including working capital and capital expenditures, to refinance existing indebtedness and/or to fund potential acquisitions. The agreements provide, among other things, that we maintain certain maximum leverage ratios, and contain restrictions relating to subsidiary indebtedness, liens, affiliate transactions, disposal of assets and certain changes in ownership. These facilities contain make-whole provisions in the event that we pay off the facilities prior to the applicable due dates.

The components of our private placement facility borrowings as of March 29, 2014 are presented in the following table:

Date of Borrowing	Amount of Borrowing Outstanding	Borrowing Rate	Due Date
September 2, 2010	\$ 100,000	3.79 %	September 2, 2020
January 20, 2012	50,000	3.45	January 20, 2024
January 20, 2012 (1)	50,000	3.09	January 20, 2022
December 24, 2012	50,000	3.00	December 24, 2024
	\$ 250,000		

(1) Annual repayments of approximately \$7.1 million for this borrowing will commence on January 20, 2016.

## U.S. Trade Accounts Receivable Securitization

On April 17, 2013, we entered into a facility agreement of up to \$300 million with a bank, as agent, based on the securitization of our U.S. trade accounts receivable. The new facility allowed us to replace public debt (approximately \$220 million), which had a higher interest rate at HSAH during February 2013 and provided funding for working capital and general corporate purposes. The financing was structured as an asset-backed securitization program with pricing committed for up to three years. The borrowings outstanding under this securitization facility were \$250.0 million as of March 29, 2014. At March 29, 2014, the interest rate on borrowings under this facility is based on the average asset-backed commercial paper rate of 20 basis points plus 75 basis points, for a combined rate of 0.95%.

We are required to pay a commitment fee of 30 basis points on the daily balance of the unused portion of the facility if our usage is greater than or equal to 50% of the facility limit or a commitment fee of 35 basis points on the daily



balance of the unused portion of the facility if our usage is less than 50% of the facility limit.

Borrowings under this facility are presented as a component of Long-term debt within our consolidated balance sheet.

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HENRY SCHEIN, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)  
(in thousands, except per share data)  
(unaudited)

## Note 3 – Debt – (Continued)

## Other Loans Payable

Certain of our subsidiaries have various collateralized and uncollateralized long-term loans payable with interest, with borrowings of \$39.6 million outstanding at March 29, 2014, in varying installments through 2018 at interest rates ranging from 2.4% to 5.41%.

## Henry Schein Animal Health

During the first quarter of 2013, we repaid the then outstanding debt related to the Henry Schein Animal Health (“HSAH”), formerly Butler Schein Animal Health, transaction using our existing Credit Agreement. As part of this transaction, we recorded a one-time interest expense charge of \$6.2 million related to the accelerated amortization of deferred financing costs.

## Note 4 – Redeemable Noncontrolling Interests

Some minority shareholders in certain of our subsidiaries have the right, at certain times, to require us to acquire their ownership interest in those entities at fair value. Accounting Standards Codification (“ASC”) Topic 480-10 is applicable for noncontrolling interests where we are or may be required to purchase all or a portion of the outstanding interest in a consolidated subsidiary from the noncontrolling interest holder under the terms of a put option contained in contractual agreements. The components of the change in the Redeemable noncontrolling interests for the three months ended March 29, 2014 and the year ended December 28, 2013 are presented in the following table:

	March 29, 2014	December 28, 2013
Balance, beginning of period	\$497,539	\$435,175
Decrease in redeemable noncontrolling interests due to redemptions	(83,793 )	(9,028 )
Increase in redeemable noncontrolling interests due to business acquisitions	53,133	11,542
Net income attributable to redeemable noncontrolling interests	7,939	39,430
Dividends declared	(3,509 )	(19,965 )
Effect of foreign currency translation gain (loss) attributable to redeemable noncontrolling interests	2,129	(654 )
Change in fair value of redeemable securities	9,263	41,039
Balance, end of period	\$482,701	\$497,539

Changes in the estimated redemption amounts of the noncontrolling interests subject to put options are adjusted at each reporting period with a corresponding adjustment to Additional paid-in capital. Future reductions in the carrying amounts are subject to a “floor” amount that is equal to the fair value of the redeemable noncontrolling interests at the time they were originally recorded. The recorded value of the redeemable noncontrolling interests cannot go below the floor level. These adjustments do not impact the calculation of earnings per share.



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HENRY SCHEIN, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)  
(in thousands, except per share data)  
(unaudited)

## Note 5 – Comprehensive Income

Comprehensive income includes certain gains and losses that, under U.S. GAAP, are excluded from net income as such amounts are recorded directly as an adjustment to stockholders' equity. Our comprehensive income is primarily comprised of net income, foreign currency translation gain (loss), unrealized gain (loss) on foreign currency hedging activities, unrealized investment gain (loss) and pension adjustment gain (loss).

The following table summarizes our Accumulated other comprehensive income, net of applicable taxes as of:

	March 29, 2014	December 28, 2013
<b>Attributable to Redeemable noncontrolling interests:</b>		
Foreign currency translation adjustment	\$626	\$(1,503 )
<b>Attributable to noncontrolling interests:</b>		
Foreign currency translation adjustment	\$(19 )	\$-
<b>Attributable to Henry Schein, Inc.:</b>		
Foreign currency translation gain	\$87,970	\$82,288
Unrealized gain from foreign currency hedging activities	334	1,282
Unrealized investment loss	(504 )	(515 )
Pension adjustment loss	(14,938 )	(15,206 )
Accumulated other comprehensive income	\$72,862	\$67,849
<b>Total Accumulated other comprehensive income</b>		