

HEIDRICK & STRUGGLES INTERNATIONAL INC
Form 10-Q
October 27, 2015

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

FORM 10-Q

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

FOR THE QUARTERLY PERIOD ENDED SEPTEMBER 30, 2015

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 0-25837

HEIDRICK & STRUGGLES INTERNATIONAL, INC.
(Exact Name of Registrant as Specified in its Charter)

Delaware
(State or Other Jurisdiction of
Incorporation or Organization)
233 South Wacker Drive-Suite 4900
Chicago, Illinois
60606-6303
(Address of Principal Executive Offices)

36-2681268
(I.R.S. Employer
Identification Number)

(312) 496-1200
(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 of time 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 (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

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Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a small reporting company. See definitions of “large accelerated filer,” “accelerated filer” and “smaller reporting company” in Rule 12b-2 of the Exchange Act.

Large accelerated filer	<input type="checkbox"/>	Accelerated filer	<input checked="" type="checkbox"/>
Non-Accelerated filer	<input type="checkbox"/>	Smaller reporting company	<input type="checkbox"/>

(Do not check if a smaller reporting company)

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes No

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

As of October 23, 2015, there were 18,383,796 shares of the Company’s common stock outstanding.

HEIDRICK & STRUGGLES INTERNATIONAL, INC. AND SUBSIDIARIES
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PART I. FINANCIAL INFORMATION

ITEM 1. CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
HEIDRICK & STRUGGLES INTERNATIONAL, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS

(In thousands, except share amounts)

	September 30, 2015 (Unaudited)	December 31, 2014
Current assets:		
Cash and cash equivalents	\$128,960	\$211,352
Restricted cash	7,171	6,501
Accounts receivable, net	106,674	68,353
Prepaid expenses	15,715	14,536
Other current assets	13,464	12,205
Income taxes recoverable	5,669	5,288
Deferred income taxes	12,436	12,094
Total current assets	290,089	330,329
Non-current assets:		
Property and equipment, net	35,597	30,417
Assets designated for retirement and pension plans	17,949	19,426
Investments	14,185	13,989
Other non-current assets	12,169	8,012
Goodwill	120,150	122,176
Other intangible assets, net	17,327	20,939
Deferred income taxes	22,553	23,413
Total non-current assets	239,930	238,372
Total assets	\$530,019	\$568,701
Current liabilities:		
Current portion of debt	\$—	\$6,000
Accounts payable	4,056	5,493
Accrued salaries and employee benefits	120,023	130,434
Deferred revenue, net	33,739	30,452
Other current liabilities	28,697	26,835
Income taxes payable	4,388	6,684
Total current liabilities	190,903	205,898
Non-current liabilities:		
Non-current debt, less current maturities	—	23,500
Retirement and pension plans	38,186	39,892
Other non-current liabilities	46,835	54,747
Total non-current liabilities	85,021	118,139
Total liabilities	275,924	324,037
Commitments and contingencies (Note 18)		
Stockholders' equity:		
Preferred stock, \$0.01 par value, 10,000,000 shares authorized, no shares issued at September 30, 2015 and December 31, 2014	—	—
Common stock, \$0.01 par value, 100,000,000 shares authorized, 19,585,777 shares issued, 18,379,398 and 18,239,939 shares outstanding at September 30, 2015 and December 31, 2014, respectively	196	196

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Treasury stock at cost, 1,206,379 and 1,345,838 shares at September 30, 2015 and December 31, 2014, respectively	(39,583) (44,261)
Additional paid in capital	230,977	232,075	
Retained earnings	53,807	45,431	
Accumulated other comprehensive income	8,698	11,223	
Total stockholders' equity	254,095	244,664	
Total liabilities and stockholders' equity	\$530,019	\$568,701	

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

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HEIDRICK & STRUGGLES INTERNATIONAL, INC. AND SUBSIDIARIES
 CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(In thousands, except per share amounts)

(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2015	2014	2015	2014
Revenue:				
Revenue before reimbursements (net revenue)	\$ 138,421	\$ 125,829	\$ 386,619	\$ 373,030
Reimbursements	4,429	4,432	12,396	13,721
Total revenue	142,850	130,261	399,015	386,751
Operating expenses:				
Salaries and employee benefits	95,724	84,046	264,914	252,089
General and administrative expenses	29,764	32,226	92,928	98,092
Reimbursed expenses	4,429	4,432	12,396	13,721
Total operating expenses	129,917	120,704	370,238	363,902
Operating income	12,933	9,557	28,777	22,849
Non-operating expense:				
Interest, net	(54)	(152)	(300)	(232)
Other, net	(1,742)	(488)	(1,696)	(444)
Net non-operating expense	(1,796)	(640)	(1,996)	(676)
Income before income taxes	11,137	8,917	26,781	22,173
Provision for income taxes	3,647	5,925	10,909	16,138
Net income	7,490	2,992	15,872	6,035
Other comprehensive loss, net of tax:				
Foreign currency translation adjustment	(347)	(2,315)	(1,645)	(1,067)
Net unrealized (loss) gain on available-for-sale investments	(941)	(349)	(802)	160
Unrealized (loss) gain on cash flow hedge	—	77	(78)	8
Other comprehensive loss, net of tax	(1,288)	(2,587)	(2,525)	(899)
Comprehensive income	\$ 6,202	\$ 405	\$ 13,347	\$ 5,136
Basic weighted average common shares outstanding	18,372	18,233	18,318	18,200
Dilutive common shares	277	233	277	197
Diluted weighted average common shares outstanding	18,649	18,466	18,595	18,397
Basic net income per common share	\$ 0.41	\$ 0.16	\$ 0.87	\$ 0.33
Diluted net income per common share	\$ 0.40	\$ 0.16	\$ 0.85	\$ 0.33
Cash dividends paid per share	\$ 0.13	\$ 0.13	\$ 0.39	\$ 0.39

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

HEIDRICK & STRUGGLES INTERNATIONAL, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN STOCKHOLDERS' EQUITY
(In thousands)
(Unaudited)

	Common Stock		Treasury Stock		Additional Paid in Capital	Retained Earnings	Accumulated	Total
	Shares	Amount	Shares	Amount			Other Compre- hensive Income	
Balance at December 31, 2014	19,586	\$196	1,346	\$(44,261)	\$232,075	\$45,431	\$ 11,223	\$244,664
Net income	—	—	—	—	—	15,872	—	15,872
Other comprehensive loss, net of tax	—	—	—	—	—	—	(2,525)	(2,525)
Treasury and common stock transactions:								
Stock-based compensation	—	—	—	—	3,684	—	—	3,684
Vesting of equity, net of tax withholdings	—	—	(123)	4,094	(4,972)	—	—	(878)
Re-issuance of treasury stock	—	—	(17)	584	(134)	—	—	450
Cash dividends declared (\$0.39 per share)	—	—	—	—	—	(7,161)	—	(7,161)
Dividend equivalents on restricted stock units	—	—	—	—	—	(335)	—	(335)
Tax deficit related to stock-based compensation	—	—	—	—	324	—	—	324
Balance at September 30, 2015	19,586	\$196	1,206	\$(39,583)	\$230,977	\$53,807	\$ 8,698	\$254,095

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

HEIDRICK & STRUGGLES INTERNATIONAL, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands)

(Unaudited)

	Nine Months Ended September 30,	
	2015	2014
Cash flows—operating activities:		
Net income	\$15,872	\$6,035
Adjustments to reconcile net income to net cash used in operating activities:		
Depreciation and amortization	9,983	11,359
Deferred income taxes	(153)	) 5,633
Stock-based compensation expense	3,684	2,885
Accretion expense related to earnout payments	861	1,308
Changes in assets and liabilities:		
Account receivables	(40,582)	) (24,001)
Accounts payable	(1,311)	) (2,177)
Accrued expenses	(5,361)	) (1,774)
Deferred revenue	3,921	4,486
Income taxes payable, net	(3,101)	) (2,220)
Retirement and pension plan assets and liabilities	69	100
Prepaid expenses	(1,054)	) (557)
Other assets and liabilities, net	(2,868)	) (3,125)
Net cash used in operating activities	(20,040)	) (2,048)
Cash flows—investing activities:		
Restricted cash	—	(103)
Capital expenditures	(13,897)	) (2,609)
Purchases of available for sale investments	(1,402)	) (896)
Proceeds from sales of available for sale investments	630	966
Net cash used in investing activities	(14,669)	) (2,642)
Cash flows—financing activities:		
Debt repayment	(29,500)	) (4,500)
Debt issuance costs	(422)) —
Cash dividends paid	(7,496)	) (7,364)
Payment of employee tax withholdings on equity transactions	(878)	) (406)
Acquisition earnout payments	(5,496)	) (3,390)
Net cash used in financing activities	(43,792)	) (15,660)
Effect of exchange rates fluctuations on cash and cash equivalents	(3,891)	) (1,759)
Net decrease in cash and cash equivalents	(82,392)	) (22,109)
Cash and cash equivalents at beginning of period	211,352	181,646
Cash and cash equivalents at end of period	\$128,960	\$159,537
Supplemental Schedule of Non-cash Financing Activities:		
Term loan facility retirement (Note 12)	\$ (26,500)) \$—
Subsequent drawing on line of credit (Note 12)	\$26,500) \$—

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

HEIDRICK & STRUGGLES INTERNATIONAL, INC. AND SUBSIDIARIES
 NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
 (All tables in thousands, except share and per share figures)
 (Unaudited)

1. Basis of Presentation of Interim Financial Information

The accompanying unaudited Condensed Consolidated Financial Statements of Heidrick & Struggles International, Inc. and subsidiaries (the “Company”) have been prepared pursuant to the rules and regulations of the U.S. Securities and Exchange Commission (“SEC”). The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenue and expenses. Significant items subject to estimates and assumptions include revenue recognition, income taxes, interim effective tax rate, assessment of goodwill and other intangible assets for impairment, allowance for doubtful accounts and stock-based compensation. Estimates are subject to a degree of uncertainty and actual results could differ from these estimates. These financial statements and notes are to be read in conjunction with the Company’s Consolidated Financial Statements and Notes thereto included in the Company’s Annual Report on Form 10-K for the year ended December 31, 2014, as filed with the SEC on March 11, 2015.

2. Summary of Significant Accounting Policies

A complete listing of the Company’s significant accounting policies is discussed in Note 2, Summary of Significant Accounting Policies, in the Notes to Consolidated Financial Statements included in the Company’s Annual Report on Form 10-K for the year ended December 31, 2014.

Recent Financial Accounting Standards

In May 2014, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) No. 2014-09, Revenue from Contracts with Customers. The ASU requires that an entity recognizes revenue to depict the transfer of promised goods or services to customer in an amount that reflects the consideration to which the Company expects to be entitled in exchange for these goods or services. The effective date has been deferred for one year to the interim and annual reporting periods beginning after December 15, 2017. Early adoption is permitted as of the original effective date, which was interim and annual reporting periods beginning after December 15, 2016. The guidance permits the use of either of the following transition methods: (i) a full retrospective approach reflecting the application of the standard in each prior reporting period with the option to elect certain practical expedients or (ii) a retrospective approach with the cumulative effect upon initial adoption recognized at the date of adoption. The Company is currently evaluating the effect that this pronouncement will have on its financial statements and related disclosures. The effect is not known or reasonably estimable at this time.

3. Allowance for Doubtful Accounts

The activity of the allowance for doubtful accounts for the nine months ended September 30, 2015 is as follows:

Balance at December 31, 2014	\$3,942	
Provision charged to income	2,591	
Write-offs	(1,140)
Currency	(150)
Balance at September 30, 2015	\$5,243	

4. Property and Equipment, net

The components of the Company's property and equipment are as follows:

	September 30, 2015	December 31, 2014
Leasehold improvements	\$39,583	\$43,930
Office furniture, fixtures and equipment	16,320	18,693
Computer equipment and software	30,620	30,751
Property and equipment, gross	86,523	93,374
Accumulated depreciation	(50,926	) (62,957
Property and equipment, net	\$35,597	\$30,417

Depreciation expense for the three months ended September 30, 2015 and 2014 was \$2.2 million and \$2.3 million, respectively. Depreciation expense for the nine months ended September 30, 2015 and 2014 was \$6.5 million and \$7.2 million, respectively.

5. Restricted Cash

The components of the Company's restricted cash are as follows:

	September 30, 2015	December 31, 2014
Current restricted cash		
Retention escrow	\$6,500	\$6,501
Lease guarantees	671	—
Total current restricted cash	\$7,171	\$6,501
Non-current restricted cash		
Lease guarantees	\$482	\$1,316
Business licenses	91	95
Total non-current restricted cash	\$573	\$1,411

The retention escrow is associated with the Senn Delaney acquisition and will be paid to certain key executives of Senn Delaney if they remain with the Company for three years subsequent to the acquisition (See Note 8, Acquisitions). The Company has certain lease agreements and business licenses with terms that require the Company to restrict cash through the termination dates of the agreements, which extend through 2018. Non-current restricted cash is included in Other non-current assets on the Condensed Consolidated Balance Sheet.

6. Investments

The components of the Company's investments are as follows: