

HENRY SCHEIN INC
Form 10-Q
August 02, 2012

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 June 30, 2012

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

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company” in Rule 12b-2 of the Exchange Act.

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 July 23, 2012, there were 88,529,318 shares of the registrant’s common stock outstanding.

HENRY SCHEIN, INC.
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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)

	June 30, 2012 (unaudited)	December 31, 2011
ASSETS		
Current assets:		
Cash and cash equivalents	\$87,896	\$147,284
Accounts receivable, net of reserves of \$63,988 and \$65,853	972,292	888,248
Inventories, net	976,996	947,849
Deferred income taxes	60,693	54,970
Prepaid expenses and other	233,267	234,157
Total current assets	2,331,144	2,272,508
Property and equipment, net	255,715	262,088
Goodwill	1,523,446	1,497,108
Other intangibles, net	425,038	409,612
Investments and other	299,913	298,828
Total assets	\$4,835,256	\$4,740,144
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	\$619,936	\$621,468
Bank credit lines	83,454	55,014
Current maturities of long-term debt	17,129	22,819
Accrued expenses:		
Payroll and related	179,186	191,173
Taxes	126,703	121,234
Other	257,046	259,932
Total current liabilities	1,283,454	1,271,640
Long-term debt	434,417	363,524
Deferred income taxes	185,247	188,739
Other liabilities	82,980	80,568
Total liabilities	1,986,098	1,904,471
Redeemable noncontrolling interests	359,114	402,050
Commitments and contingencies		
Stockholders' equity:		
Preferred stock, \$.01 par value, 1,000,000 shares authorized, none outstanding	-	-
Common stock, \$.01 par value, 240,000,000 shares authorized,		

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88,904,637 outstanding on June 30, 2012 and 89,928,082 outstanding on December 31, 2011	889	899
Additional paid-in capital	398,819	401,262
Retained earnings	2,076,060	2,007,477
Accumulated other comprehensive income	12,880	22,584
Total Henry Schein, Inc. stockholders' equity	2,488,648	2,432,222
Noncontrolling interests	1,396	1,401
Total stockholders' equity	2,490,044	2,433,623
Total liabilities, redeemable noncontrolling interests and stockholders' equity	\$4,835,256	\$4,740,144

See accompanying notes.

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

	Three Months Ended		Six Months Ended	
	June 30, 2012	June 25, 2011	June 30, 2012	June 25, 2011
Net sales	\$2,201,452	\$2,130,640	\$4,300,471	\$4,078,401
Cost of sales	1,577,057	1,518,416	3,065,497	2,900,355
Gross profit	624,395	612,224	1,234,974	1,178,046
Operating expenses:				
Selling, general and administrative	466,333	461,009	931,785	902,531
Restructuring costs	3,360	-	15,192	-
Operating income	154,702	151,215	287,997	275,515
Other income (expense):				
Interest income	3,609	4,192	6,939	8,125
Interest expense	(7,711)	(7,902)	(15,351)	(15,987)
Other, net	830	758	1,355	1,081
Income before taxes and equity in earnings of affiliates	151,430	148,263	280,940	268,734
Income taxes	(47,201)	(47,340)	(89,041)	(86,493)
Equity in earnings of affiliates	3,073	4,133	4,464	5,786
Net income	107,302	105,056	196,363	188,027
Less: Net income attributable to noncontrolling interests	(9,216)	(10,581)	(17,525)	(17,057)
Net income attributable to Henry Schein, Inc.	\$98,086	\$94,475	\$178,838	\$170,970
Earnings per share attributable to Henry Schein, Inc.:				
Basic	\$1.11	\$1.04	\$2.03	\$1.88
Diluted	\$1.08	\$1.01	\$1.98	\$1.83
Weighted-average common shares outstanding:				
Basic	88,490	90,766	88,161	90,710
Diluted	90,553	93,446	90,431	93,330

See accompanying notes.

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

	Three Months Ended		Six Months Ended	
	June 30, 2012	June 25, 2011	June 30, 2012	June 25, 2011
Net income	\$107,302	\$105,056	\$196,363	\$188,027
Other comprehensive income, net of tax:				
Foreign currency translation gain (loss)	(42,004)	13,238	(10,343)	72,947
Unrealized gain (loss) from foreign currency hedging activities	(1,022)	(77)	(107)	1,810
Unrealized investment gain	55	61	88	197
Pension adjustment gain (loss)	481	163	46	(355)
Other comprehensive income (loss), net of tax	(42,490)	13,385	(10,316)	74,599
Comprehensive income	64,812	118,441	186,047	262,626
Comprehensive income attributable to noncontrolling interests:				
Net income	(9,216)	(10,581)	(17,525)	(17,057)
Foreign currency translation (gain) loss	1,626	(300)	612	(2,192)
Comprehensive income attributable to noncontrolling interests	(7,590)	(10,881)	(16,913)	(19,249)
Comprehensive income attributable to Henry Schein, Inc.	\$57,222	\$107,560	\$169,134	\$243,377

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 Shares	Amount	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income	Noncontrolling Interests	Total Stockholders' Equity
Balance, December 31, 2011	89,928,082	\$ 899	\$ 401,262	\$ 2,007,477	\$ 22,584	\$ 1,401	\$ 2,433,623
Net income (excluding \$17,311 attributable to Redeemable noncontrolling interests)	-	-	-	178,838	-	214	179,052
Foreign currency translation loss (excluding \$612 attributable to Redeemable noncontrolling interests)	-	-	-	-	(9,731)	-	(9,731)
Unrealized loss from foreign currency hedging activities, net of tax of \$17	-	-	-	-	(107)	-	(107)
Unrealized investment gain, net of tax of \$95	-	-	-	-	88	-	88
Pension adjustment gain, net of tax of \$286	-	-	-	-	46	-	46
Dividends paid	-	-	-	-	-	(219)	(219)
Initial noncontrolling interests and adjustments related to business acquisitions	-	-	(3,142)	-	-	-	(3,142)
Change in fair value of redeemable securities	-	-	742	-	-	-	742

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Repurchase and retirement of common stock	(2,119,494)	(21)	(46,615)	(110,255)	-	-	(156,891)
Stock issued upon exercise of stock options, including tax benefit of \$8,900	1,084,708	11	49,604	-	-	-	49,615
Stock-based compensation expense	320,259	3	20,046	-	-	-	20,049
Shares withheld for payroll taxes	(308,918)	(3)	(22,784)	-	-	-	(22,787)
Liability for cash settlement stock-based compensation awards	-	-	(294)	-	-	-	(294)
Balance, June 30, 2012	88,904,637	\$ 889	\$ 398,819	\$ 2,076,060	\$ 12,880	\$ 1,396	\$ 2,490,044

See accompanying notes.

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

	Six Months Ended	
	June 30, 2012	June 25, 2011
Cash flows from operating activities:		
Net income	\$ 196,363	\$ 188,027
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	61,389	57,469
Stock-based compensation expense	20,049	17,960
Provision for losses on trade and other accounts receivable	2,637	2,722
Benefit from deferred income taxes	(7,715)	(10,265)
Equity in earnings of affiliates	(4,464)	(5,786)
Distributions from equity affiliates	6,007	1,180
Other	3,859	2,242
Changes in operating assets and liabilities, net of acquisitions:		
Accounts receivable	(59,329)	(9,902)
Inventories	(11,340)	3,902
Other current assets	(8,078)	(11,100)
Accounts payable and accrued expenses	(69,485)	(49,977)
Net cash provided by operating activities	129,893	186,472
Cash flows from investing activities:		
Purchases of fixed assets	(21,372)	(20,764)
Payments for equity investments and business acquisitions, net of cash acquired	(120,348)	(143,636)
Proceeds from sales of available-for-sale securities	4,025	2,150
Other	(4,385)	1,897
Net cash used in investing activities	(142,080)	(160,353)
Cash flows from financing activities:		
Proceeds from bank borrowings	26,384	7,671
Proceeds from issuance of long-term debt	100,050	3,101
Debt issuance costs	(213)	(2,847)
Principal payments for long-term debt	(35,375)	(23,916)
Proceeds from issuance of stock upon exercise of stock options	40,715	27,938
Payments for repurchases of common stock	(156,891)	(32,098)
Excess tax benefits related to stock-based compensation	10,051	6,852
Distributions to noncontrolling shareholders	(8,595)	(6,417)
Acquisitions of noncontrolling interests in subsidiaries	(20,013)	(3,366)
Other	-	(90)
Net cash used in financing activities	(43,887)	(23,172)

Net change in cash and cash equivalents	(56,074)	2,947
Effect of exchange rate changes on cash and cash equivalents	(3,314)	8,494
Cash and cash equivalents, beginning of period	147,284	150,348
Cash and cash equivalents, end of period	\$87,896	\$161,789

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 31, 2011.

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 six months ended June 30, 2012 are not necessarily indicative of the results to be expected for any other interim period or for the year ending December 29, 2012.

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, medical and animal health 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, schools and other institutions. Our global medical group serves office-based medical practitioners, surgical centers, other alternate-care settings and other institutions. Our global animal health group serves animal health practices and clinics. Our global dental, medical and animal health groups serve practitioners in 24 countries outside of North America.

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.

Beginning with the first quarter of 2012, we are reporting net sales and prior-year sales comparisons for each of our global dental, medical, animal health and global technology and value-added services business groups.

This sales reporting is consistent with our new global business groups. These groups have been formed to provide distinct organizational focus for reaching and serving each practitioner segment with the benefits of a global perspective, as well as global product and service offerings and best practices.

We will continue to report financial results for our health care distribution and technology and value-added services reportable segments. The health care distribution segment now comprises three global operating segments (dental, medical and animal health) and the technology and value-added services segment remains unchanged.

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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)

In connection with this change in business groups, goodwill was reallocated to the new reporting units. We reviewed the newly allocated goodwill and determined that there was no impairment.

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

	Three Months Ended		Six Months Ended	
	June 30, 2012	June 25, 2011	June 30, 2012	June 25, 2011
Net Sales:				
Health care distribution (1):				
Dental	\$ 1,185,919	\$ 1,201,224	\$ 2,341,585	\$ 2,296,588
Medical	361,122	340,872	715,948	681,941
Animal health	586,258	526,487	1,111,848	982,169
Total health care distribution	2,133,299	2,068,583	4,169,381	3,960,698
Technology and value-added services (2)				
	68,153	62,057	131,090	117,703
Total	\$ 2,201,452	\$ 2,130,640	\$ 4,300,471	\$ 4,078,401

(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 services, including e-services and continuing education services for practitioners.

	Three Months Ended		Six Months Ended	
	June 30, 2012	June 25, 2011	June 30, 2012	June 25, 2011
Operating Income:				
Health care distribution	\$ 136,047	\$ 134,217	\$ 253,268	\$ 243,944
Technology and value-added services	18,655	16,998	34,729	31,571
Total	\$ 154,702	\$ 151,215	\$ 287,997	\$ 275,515

Note 3 – Debt

Credit Facilities

On September 5, 2008, we entered into a \$400 million revolving credit facility with a \$100 million expansion feature. The borrowings outstanding under this revolving credit facility were \$55.0 million as of June 30, 2012. The \$400 million credit line expires in September 2013. The interest rate, which was 0.70% during the six months ended June 30, 2012, is based on USD LIBOR plus a spread based on our leverage ratio at the end of each financial reporting quarter. The agreement provides, among other things, that we maintain certain interest coverage and maximum leverage ratios, and contains restrictions relating to subsidiary indebtedness, liens, employee and shareholder loans, disposal of businesses and certain changes in ownership. As of June 30, 2012, there were \$9.6 million of letters of credit provided to third parties.

As of June 30, 2012, we had various other short-term bank credit lines available, of which approximately \$28.5 million was outstanding. During the six months ended June 30, 2012, borrowings under all of our credit lines had a weighted average interest rate of 1.27%.

Certain of our subsidiaries, excluding Butler Animal Health Supply, LLC, or BAHS, maintain credit lines which are collateralized by assets of those subsidiaries with an aggregate net carrying value of \$84.8 million.

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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 agreement provides, among other things, that we maintain certain maximum leverage ratios, and contains restrictions relating to subsidiary indebtedness, liens, employee and shareholder loans, disposal of businesses and certain changes in ownership.

The components of our private placement facility borrowings as of June 30, 2012 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
	\$ 200,000		

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

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

Note 3 – Debt – (Continued)

Butler Animal Health Supply

Effective December 31, 2009, BAHS, a majority-owned subsidiary whose financial information is consolidated with ours, had incurred approximately \$320.0 million of debt (of which \$37.5 million was provided by Henry Schein, Inc.) in connection with our acquisition of a majority interest in BAHS.

On May 27, 2011, BAHS refinanced the terms and amount of its debt in an aggregate principal amount of \$366.0 million (of which \$55.0 million was provided by Henry Schein, Inc.). The refinanced debt consists of the following three components:

	Term Loan A	Term Loan B	Revolver
Original amount of debt (includes \$55.0 million of debt provided by Henry Schein, Inc.)	\$100,000	\$216,000	\$50,000
Number of remaining quarterly installments	9	13	
Quarterly payments from:			
September 30, 2012 through June 30, 2013	6,574		
September 30, 2013 through June 30, 2014	8,766		
July 1, 2014 through September 30, 2014	2,739		
September 30, 2012 through September 30, 2015		4,592	
Final installment due on December 31, 2014	65,196		
Final installment due on December 31, 2015		135,287	
Balance outstanding as of June 30, 2012	83,275	139,045	2,000
	LIBOR plus a margin of	LIBOR plus a margin of	LIBOR plus a margin of
Interest rate on debt	2.75%	3.25%	2.75%
Interest rate on debt - LIBOR floor		1.25	%

During 2011 and 2012, BAHS made prepayments on Term Loans A and B, which resulted in a reduction to the future quarterly and final installment amounts due. Future prepayments by BAHS, if any, will result in reductions to remaining quarterly and final installment amounts due.

The outstanding balance of \$224.3 million (net of unamortized debt discount) is reflected in our consolidated balance sheet as of June 30, 2012. Borrowings incurred as part of the acquisition of BAHS are collateralized by assets of BAHS with an aggregate net carrying value of \$759.1 million.

The debt agreement provides, among other things, that BAHS maintain certain interest coverage and maximum leverage ratios, and contains restrictions relating to subsidiary indebtedness, capital expenditures, liens, employee and shareholder loans, disposal of businesses and certain changes in ownership. In addition, the debt agreement contains provisions which, under certain circumstances, require BAHS to make prepayments based on excess cash flows of BAHS as defined in the debt agreement.

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

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 six months ended June 30, 2012 and the year ended December 31, 2011 are presented in the following table:

	June 30, 2012	December 31, 2011
Balance, beginning of period	\$402,050	\$304,140
Decrease in redeemable noncontrolling interests due to redemptions	(23,169)	(160,254)
Increase in redeemable noncontrolling interests due to business acquisitions	14,999	13,618
Net income attributable to redeemable noncontrolling interests	17,311	36,514
Dividends declared	(8,087)	(15,212)
Effect of foreign currency translation loss attributable to redeemable noncontrolling interests	(612)	(889)
Change in fair value of redeemable securities	(742)	224,133
Other adjustment to redeemable noncontrolling interests	(42,636)	-
Balance, end of period	\$359,114	\$402,050

Changes in the estimated redemption amounts of the noncontrolling interests subject to