Hill-Rom Holdings, Inc.
Form 10-Q
April 27, 2018

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, 2018
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 No. 1-6651
HILL-ROM HOLDINGS, INC.
(Exact name of registrant as specified in its charter)

Indiana	35-1160484
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
130 E. Randolph St., Suite 1000 Chicago, IL	60601
(Address of principal executive offices)	(Zip Code)

(312) 819-7200
(Registrant's telephone number, including area code)
Not Applicable
(Former name, former address and former fiscal year, if changed since last report)
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 þ No o
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 þ No o
Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company (as defined in Rule 12b-2 of the Exchange Act).
Large accelerated filer þ Accelerated filer o Non-accelerated filer o Smaller reporting company o Emerging growth company o
If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. 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.
Common Stock, without par value – 66,277,670 shares as of April 23, 2018.

Table of Contents

HILL-ROM HOLDINGS, INC.

INDEX TO FORM 10-Q

Table of Contents

PART I – FINANCIAL INFORMATION

Item 1. FINANCIAL STATEMENTS

Hill-Rom Holdings, Inc. and Subsidiaries
Condensed Consolidated Statements of Income (Unaudited)
(In millions, except per share data)

	Quarter Ended March 31		Year to Date Ended March 31	
	2018	2017	2018	2017
Net Revenue				
Product sales and service	$610.7	$579.6	$1,185.9	$1,121.5
Rental revenue	99.8	99.3	194.3	194.8
Total revenue	710.5	678.9	1,380.2	1,316.3
Cost of Revenue				
Cost of goods sold	313.7	305.7	617.8	594.1
Rental expenses	46.4	48.8	92.4	95.2
Total cost of revenue	360.1	354.5	710.2	689.3
Gross Profit	350.4	324.4	670.0	627.0
Research and development expenses	34.7	35.3	67.0	67.3
Selling and administrative expenses	232.7	222.4	454.4	431.2
Special charges (Note 8)	36.9	3.1	50.4	8.9
Operating Profit	46.1	63.6	98.2	119.6
Interest expense	(24.2)	(21.9)	(47.3)	(41.4)
Investment income and other, net	(0.4)	(0.4)	1.4	(1.6)
Income Before Income Taxes	21.5	41.3	52.3	76.6
Income tax expense (benefit) (Note 9)	(7.0)	7.3	(64.5)	19.1
Net Income	28.5	34.0	116.8	57.5
Less: Net loss attributable to noncontrolling interests	—	(0.4)	—	(0.7)
Net Income Attributable to Common Shareholders	$28.5	$34.4	$116.8	$58.2
Net Income Attributable to Common Shareholders per Common Share - Basic	$0.43	$0.52	$1.77	$0.89
Net Income Attributable to Common Shareholders per Common Share - Diluted	$0.42	$0.51	$1.73	$0.87
Dividends per Common Share	$0.20	$0.18	$0.38	$0.35
Average Common Shares Outstanding - Basic (thousands) (Note 10)	66,192	65,462	66,040	65,473

Average Common Shares Outstanding - Diluted (thousands) (Note 10)	67,597	67,132	67,508	67,057

See Notes to Condensed Consolidated Financial Statements (unaudited)

3

Table of Contents

Hill-Rom Holdings, Inc. and Subsidiaries
Condensed Consolidated Statements of Comprehensive Income (Unaudited)
(In millions)

	Quarter Ended March 31		Year to Date Ended March 31	
	2018	2017	2018	2017
Net Income	$28.5	$34.0	$116.8	$57.5
Other Comprehensive Income (Loss), net of tax (Note 7):				
Derivative instruments and hedges	7.9	(0.2)	11.3	10.0
Foreign currency translation adjustment	16.5	14.0	22.6	(25.5)
Change in pension and postretirement defined benefit plans	0.8	0.8	1.6	2.1
Total Other Comprehensive Income (Loss), net of tax	25.2	14.6	35.5	(13.4)
Total Comprehensive Income	53.7	48.6	152.3	44.1
Less: Comprehensive loss attributable to noncontrolling interests	—	(0.4)	—	(0.7)
Total Comprehensive Income Attributable to Common Shareholders	$53.7	$49.0	$152.3	$44.8

See Notes to Condensed Consolidated Financial Statements (unaudited)

Table of Contents

Hill-Rom Holdings, Inc. and Subsidiaries
Condensed Consolidated Balance Sheets (Unaudited)
(In millions)

	March 31, 2018	September 30, 2017
ASSETS		
Current Assets		
Cash and cash equivalents	$239.0	$ 231.8
Trade accounts receivable, net of allowances (Note 2)	537.9	579.3
Inventories (Note 2)	315.1	284.5
Other current assets	109.0	70.6
Total current assets	1,201.0	1,166.2
Property, plant and equipment, net (Note 2)	341.8	355.4
Goodwill (Note 4)	1,754.2	1,759.6
Other intangible assets and software, net (Note 2)	1,088.1	1,144.0
Deferred income taxes (Notes 1 and 9)	41.5	40.9
Other assets	78.1	62.6
Total Assets	$4,504.7	$ 4,528.7
LIABILITIES		
Current Liabilities		
Trade accounts payable	$159.6	$ 167.9
Short-term borrowings (Note 5)	221.3	188.9
Accrued compensation	97.7	126.9
Accrued product warranties (Note 12)	25.0	25.5
Accrued rebates	38.0	39.7
Other current liabilities	108.9	109.8
Total current liabilities	650.5	658.7
Long-term debt (Note 5)	2,025.6	2,120.4
Accrued pension and postretirement benefits (Note 6)	78.7	78.1
Deferred income taxes (Notes 1 and 9)	180.0	266.2
Other long-term liabilities	59.5	39.7
Total Liabilities	2,994.3	3,163.1
Commitments and Contingencies (Note 14)		
SHAREHOLDERS' EQUITY		
Common Stock (Note 2)	4.4	4.4
Additional paid-in capital	596.7	584.4
Retained earnings	1,767.6	1,676.2
Accumulated other comprehensive loss (Note 7)	(74.5)	(110.0)
Treasury stock, at cost (Note 2)	(783.8)	(796.8)
Total Shareholders' Equity Attributable to Common Shareholders	1,510.4	1,358.2
Noncontrolling interests	—	7.4
Total Shareholders' Equity	1,510.4	1,365.6
Total Liabilities and Shareholders' Equity	$4,504.7	$ 4,528.7

See Notes to Condensed Consolidated Financial Statements (unaudited)

5

Table of Contents

Hill-Rom Holdings, Inc. and Subsidiaries
Condensed Consolidated Statements of Cash Flows (Unaudited)

(In millions)	Year to Date Ended March 31	
	2018	2017
Operating Activities		
Net income	$116.8	$57.5
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	39.2	40.6
Amortization	9.6	10.0
Acquisition-related intangible asset amortization	53.7	52.1
Provision for deferred income taxes	(89.2)	(14.6)
Gain on disposal of property, equipment leased to others, intangible assets, and impairments	(0.6)	(3.0)
(Gain) loss on disposition of businesses	22.4	(1.0)
Stock compensation	15.8	12.2
Change in working capital excluding cash, current debt, acquisitions and dispositions:		
Trade accounts receivable	45.7	25.4
Inventories	(29.0)	2.9
Other current assets	(37.9)	2.8
Trade accounts payable	(8.7)	(5.7)
Accrued expenses and other liabilities	(35.8)	(55.0)
Other, net	23.6	2.2
Net cash provided by operating activities	125.6	126.4
Investing Activities		
Capital expenditures and purchases of intangible assets	(51.4)	(47.3)
Proceeds on sale of property and equipment leased to others	3.7	10.6
Payment for acquisition of businesses, net of cash acquired	—	(314.3)
Proceeds on sale of businesses	1.0	4.5
Other	(1.0)	(0.4)
Net cash used in investing activities	(47.7)	(346.9)
Financing Activities		
Proceeds from borrowings on long-term debt	1.0	300.0
Payment of long-term debt	(54.9)	(36.6)
Borrowings on Revolving Credit Facility	75.0	53.0
Payments on Revolving Credit Facility	(95.0)	(60.8)
Borrowings on Securitization Program	51.4	—
Payments on Securitization Program	(37.3)	—
Debt issuance costs	—	(4.3)
Payment of cash dividends	(25.1)	(22.9)
Proceeds on exercise of stock options	10.5	14.6
Proceeds from stock issuance	3.0	2.3
Treasury stock acquired	(4.4)	(33.6)
Net cash provided by (used in) financing activities	(75.8)	211.7
Effect of exchange rate changes on cash	5.1	(4.7)
Net Cash Flows	7.2	(13.5)
Cash and Cash Equivalents:		
At beginning of period	231.8	232.2
At end of period	$239.0	$218.7

See Notes to Condensed Consolidated Financial Statements (unaudited)

Table of Contents

Hill-Rom Holdings, Inc. and Subsidiaries
Notes to Condensed Consolidated Financial Statements (Unaudited)
(Dollars in millions, except per share data)

Note 1. Summary of Significant Accounting Policies

Basis of Presentation and Principles of Consolidation

Unless the context otherwise requires, the terms “Hill-Rom,” “the Company,” “we,” “our,” and “us” refer to Hill-Rom Holding Inc. and its wholly-owned subsidiaries. The unaudited Condensed Consolidated Financial Statements appearing in this Quarterly Report on Form 10-Q should be read in conjunction with the audited Consolidated Financial Statements and notes thereto included in Hill-Rom’s latest Annual Report on Form 10-K for the fiscal year ended September 30, 2017 (“2017 Form 10-K”) as filed with the United States (“U.S.”) Securities and Exchange Commission. The September 30, 2017 Condensed Consolidated Balance Sheet was derived from audited Consolidated Financial Statements, but does not include all disclosures required by accounting principles generally accepted in the U.S. In the opinion of management, the Condensed Consolidated Financial Statements herein include all adjustments, consisting only of normal recurring adjustments, necessary to state fairly the financial position, results of operations and cash flows for the interim periods presented. Quarterly results are not necessarily indicative of annual results.

The Condensed Consolidated Financial Statements include the accounts of Hill-Rom and its wholly-owned subsidiaries. In addition, we also consolidate variable interest entities (“VIEs”) where Hill-Rom is deemed to have a controlling financial interest. Intercompany accounts and transactions have been eliminated in consolidation, including the intercompany transactions with consolidated VIEs. Where our ownership interest is less than 100%, the noncontrolling interests are reported in our Condensed Consolidated Financial Statements.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the U.S. requires management to make estimates and assumptions that affect the reported amounts of certain assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expense during the period. Actual results could differ from those estimates and such differences could be material. Examples of such estimates include, but are not limited to, income taxes (Notes 1 and 9), accounts receivable reserves (Note 2), accrued warranties (Note 12), the impairment of intangibles and goodwill (Note 4), pension expense (Note 6), and commitments and contingencies (Note 14).

Fair Value Measurements

Fair value measurements are classified and disclosed in one of the following three categories:

- Level 1: Financial instruments with unadjusted quoted prices in active markets that are accessible at the measurement date for identical, unrestricted assets and liabilities.
- Level 2: Financial instruments with observable inputs other than those included in Level 1 such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.
- Level 3: Financial instruments with unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. Unobservable inputs reflect our own assumptions that market participants would use in pricing the asset or liability (including assumptions about risk). Unobservable inputs are developed based on the best information available in the circumstances, which might include our own data.

We record cash and cash equivalents, as disclosed on our Condensed Consolidated Balance Sheets, as Level 1 instruments and certain other derivatives and investments as either Level 2 or 3 instruments. Investments measured at Net Asset Value as a practical expedient are not categorized in the fair value hierarchy. There have not been significant changes in our classification among assets and liabilities during the fiscal quarter. Refer to Note 5 for disclosure of our debt instrument and interest rate swap fair values.

Taxes Collected from Customers and Remitted to Governmental Units

Taxes assessed by a governmental authority that are directly imposed on a revenue producing transaction between us and our customers, including but not limited to sales taxes, use taxes and value added taxes, are accounted for on a net (excluded from revenue and costs) basis.

Table of Contents

Income Taxes

Hill-Rom and its eligible domestic subsidiaries file a consolidated U.S. income tax return. Foreign operations file income tax returns in a number of jurisdictions. Deferred income taxes are computed using an asset and liability approach to reflect the net tax effects of temporary differences between the financial reporting carrying amounts of assets and liabilities and the corresponding income tax amounts. We have a variety of deferred tax assets in numerous tax jurisdictions. These deferred tax assets are subject to periodic assessment as to recoverability. If it is determined that it is more likely than not that the benefits will not be realized, valuation allowances are recognized. In evaluating whether it is more likely than not that we would recover these deferred tax assets, future taxable income, the reversal of existing temporary differences and tax planning strategies are considered.

As of March 31, 2018, we had $60.0 million of valuation allowances on deferred tax assets, on a tax-effected basis, primarily related to certain foreign deferred tax attributes that are not expected to be utilized. The valuation allowance total was not materially impacted by the Tax Cuts and Jobs Act enacted in December 2017. We believe that our estimates for the valuation allowances recorded against deferred tax assets are appropriate based on current facts and circumstances.

We account for uncertain income tax positions using a threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. The difference between the tax benefit recognized in the financial statements for an uncertain income tax position and the tax benefit claimed in the tax return is referred to as an unrecognized tax benefit.

Dispositions

During the second quarter of fiscal 2018, we entered into an agreement to convey certain net assets related to the Company’s third-party rental business, which is comprised of purchased moveable medical equipment that can be rented to customers, to Universal Hospital Services, Inc. (“UHS”) in exchange for UHS's agreement to dismiss its previously disclosed litigation against the Company subject to satisfaction of customary closing conditions (“Settlement Agreement”). We recorded a loss of $23.4 million in special charges, which includes approximately $20.4 million related to the non-cash loss reserve for the assets to be conveyed, and other Settlement Agreement related costs of approximately $3.0 million. The third-party rental business is part of our Patient Support Systems segment. The transaction is expected to close during our fiscal third quarter.

During the fourth quarter of fiscal 2017, we sold our Völker business. During the first quarter of fiscal 2018, we recorded a gain of $1.0 million attributable to the final working capital settlement associated with the transaction.

Recently Issued Accounting Standards

In May 2014, the FASB issued ASU 2014-09, “Revenue from Contracts with Customers,” which provides guidance for revenue recognition. The standard’s core principle is that a company will recognize revenue when it transfers promised goods or services to customers in an amount that reflects the consideration to which the company expects to be entitled in exchange for those goods or services. In August 2015, the FASB issued ASU 2015-14 which delayed the effective date of the new revenue guidance by one year, while permitting companies to early adopt the new standard as of the original effective date. As a result, the provisions of ASU 2014-09 and subsequent amendments, are effective for us in the first quarter of fiscal 2019 using 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 modified retrospective approach with the cumulative effect of initially adopting ASU 2014-09 recognized at the date of adoption. We plan to adopt the new standard effective October 1, 2018 and are continuing to evaluate the impact of adoption on our Consolidated Financial Statements and the implementation approach to be used.

In February 2016, the FASB issued ASU 2016-02, Leases (Topic 842). From the lessee’s perspective, the new standard establishes a right-of-use (“ROU”) model that requires a lessee to record a ROU asset and a lease liability on the balance sheet for all leases with terms longer than 12 months. Leases will be classified as either finance or operating, with classification affecting the pattern of expense recognition in the income statement for a lessee. From the lessor’s perspective, the new standard requires a lessor to classify leases as either sales-type, finance or operating. A lease will be treated as a sale if it transfers all of the risks and rewards, as well as control of the underlying asset, to the lessee. If risks and rewards are conveyed without the transfer of control, the lease is treated as a financing lease. If the lessor does not convey risks and rewards or control, an operating lease results. ASU 2016-02 is effective for our first quarter of fiscal 2020. A modified retrospective transition approach is required for leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements, with certain practical expedients available. We are currently in the process of evaluating the impact of the amended guidance on our Consolidated Financial Statements.

Table of Contents

Except as noted above, there have been no significant changes to our assessment of the impact of recently issued accounting standards included in Note 1 of our Consolidated Financial Statements in our 2017 Form 10-K.

Note 2. Supplementary Balance Sheet Information

	March 31, 2018	September 30, 2017
Allowance for possible losses and discounts on trade receivables	$ 23.9	$ 25.1
Inventories:		
Finished products	$ 156.5	$ 147.5
Raw materials and work in process	158.6	137.0
Total inventory	$ 315.1	$ 284.5
Accumulated depreciation of property, plant and equipment	$ 659.3	$ 624.2
Accumulated amortization of software and other intangible assets	$ 553.2	$ 492.3

Preferred stock, without par value: