CARDINAL HEALTH INC
Form 10-Q
February 02, 2016
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
Form 10-Q

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

For the quarterly period ended December 31, 2015
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 Number: 1-11373
Cardinal Health, Inc.
(Exact name of registrant as specified in its charter)

Ohio	31-0958666
(State or other jurisdiction of incorporation or organization)	(IRS Employer Identification No.)
7000 Cardinal Place, Dublin, Ohio	43017
(Address of principal executive offices)	(Zip Code)

(614) 757-5000
(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 þ No o

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Website, 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, 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.

Large accelerated filer þ	Accelerated filer o
Non-accelerated filer o (Do not check if a smaller reporting company)	Smaller reporting company 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

The number of the registrant's common shares, without par value, outstanding as of January 27, 2016, was the following: 329,328,935.

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Forward-Looking Statements

This Form 10-Q (including information incorporated by reference) includes "forward-looking statements" addressing expectations, prospects, estimates and other matters that are dependent upon future events or developments. Many forward-looking statements appear in Management’s Discussion and Analysis of Financial Condition and Results of Operation ("MD&A"), but there are others in the document, which may be identified by the words such as "expect," "anticipate," "intend," "plan," "believe," "will," "should," "could," "would," "project," "continue," "likely," and similar expressions, and include statements reflecting future results, trends or guidance, statements of outlook and expense accruals. The matters discussed in these forward-looking statements are subject to risks, uncertainties and other factors that could cause actual results to differ materially from those made, projected or implied in the forward-looking statements. The most significant of these risks, uncertainties and other factors are described in Exhibit 99.1 to this Form 10-Q and in "Risk Factors" of our Annual Report on Form 10-K for the fiscal year ended June 30, 2015 (our “2015 Form 10-K”). Forward-looking statements in this document speak only as of the date of this document. Except to the extent required by applicable law, we undertake no obligation to update or revise any forward-looking statements, whether as a result of new information, future events, or otherwise.

About Cardinal Health

Cardinal Health, Inc. is an Ohio corporation formed in 1979. As used in this report, “we,” “our,” “us,” and similar pronouns refer to Cardinal Health, Inc. and its subsidiaries, unless the context requires otherwise. We are a healthcare services and products company that improves the cost-effectiveness of health care. We help pharmacies, hospitals, and other healthcare providers focus on patient care while reducing costs, enhancing efficiency, and improving quality. We also provide medical products to patients in the home. We manage our business and report our financial results in two segments: Pharmaceutical and Medical.

Non-GAAP Financial Measures

We use "non-GAAP financial measures" in the "Overview of Consolidated Results" section of MD&A. These measures are derived from our condensed consolidated financial data but are not presented in our financial statements prepared in accordance with U.S. generally accepted accounting principles ("GAAP"). The reasons we use these non-GAAP financial measures and the reconciliations to their most directly comparable GAAP financial measures are included in the “Explanation and Reconciliation of Non-GAAP Financial Measures” section following MD&A. The remaining sections of MD&A refer to GAAP measures only.

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

The discussion and analysis presented below is concerned with material changes in financial condition and results of operations between the periods specified in our condensed consolidated balance sheets at December 31, 2015 and June 30, 2015, and in our condensed consolidated statements of earnings for the three and six months ended December 31, 2015 and 2014. All comparisons presented are with respect to the prior-year period, unless stated otherwise. This discussion and analysis should be read in conjunction with MD&A included in our 2015 Form 10-K.

Significant Developments

Cordis

On October 2, 2015, we completed the acquisition of the Cordis business ("Cordis") from Ethicon, Inc., a wholly-owned subsidiary of Johnson and Johnson, for $1.9 billion using cash on hand and proceeds from our debt offering in June 2015. The acquisition of Cordis, a global manufacturer and distributor of interventional cardiology devices and endovascular solutions with operations in more than 50 countries, expands our Medical segment's portfolio of self-manufactured products and its geographic scope.

naviHealth

On August 26, 2015, we acquired a 71 percent ownership interest in naviHealth Group Holdings, L.P. ("naviHealth") for $238 million, net of cash acquired of $53 million. We funded the acquisition with cash on hand. The acquisition of naviHealth, a leader in post-acute care management solutions, expands our ability to serve health plans, health systems, and providers. We consolidate the results of naviHealth in our condensed consolidated financial statements and report its results in our Medical segment. The portion of naviHealth net earnings attributable to third-party interest holders is reported as a reduction to net earnings in the condensed consolidated statements of earnings.

Harvard Drug

On July 2, 2015, we completed the acquisition of The Harvard Drug Group ("Harvard Drug") for $1.1 billion using cash on hand and proceeds from our debt offering in June 2015. The acquisition of Harvard Drug, a distributor of generic pharmaceuticals, over-the-counter healthcare and related products to retail, institutional, and alternate care customers, enhances our Pharmaceutical segment's generic pharmaceutical distribution and related services businesses. Harvard Drug also manufactures and repackages generic pharmaceuticals and over-the-counter healthcare products.

Refer to Note 2 of the "Notes to Condensed Consolidated Financial Statements" for additional information on acquisitions.

Overview of Consolidated Results

Revenue (in billions)

Revenue for the three and six months ended December 31, 2015 was $31.4 billion and $59.5 billion, respectively, a 23 percent and 20 percent increase from the prior-year periods due primarily to sales growth from existing and new pharmaceutical distribution customers and from acquisitions.

GAAP and Non-GAAP Operating Earnings

GAAP and Non-GAAP Operating Earnings	Three Months Ended December 31			Six Months Ended December 31		
(in millions)	2015	2014	Change	2015	2014	Change
GAAP	$563	$546	3 %	$1,183	$1,012	17 %
LIFO charges/(credits)	39	—		39	—	
Restructuring and employee severance	2	7		14	26	
Amortization and other acquisition-related costs	114	60		219	112	
Impairments and (gain)/loss on disposal of assets	17	(18)		17	(18)	
Litigation (recoveries)/charges, net	(9)	44		(9)	72	
Non-GAAP	$726	$639	14 %	$1,463	$1,204	22 %

During the three and six months ended December 31, 2015, GAAP operating earnings increased 3 percent to $563 million and 17 percent to $1.2 billion, respectively. Non-GAAP operating earnings increased 14 percent to $726 million and 22 percent to $1.46 billion for the three and six months ended December 31, 2015, respectively. The increases in both GAAP and non-GAAP operating earnings were due to sales growth from existing and new pharmaceutical distribution customers, performance under our Pharmaceutical segment generics program, and acquisitions, offset in part by the adverse impact of customer pricing changes. GAAP operating earnings were also impacted by increased acquisition-related amortization, a last-in, first-out ("LIFO") charge, and prior-year litigation charges.

MD&A Results of Operations

GAAP and Non-GAAP Diluted EPS ($ per share)

GAAP and Non-GAAP Diluted EPS	Three Months Ended December 31			Six Months Ended December 31		
	2015	2014	Change	2015	2014	Change
GAAP	$0.98	$0.86	14 %	$2.14	$1.65	30 %
LIFO charges/(credits)	0.07	—		0.07	—	
Restructuring and employee severance	—	0.01		0.02	0.05	
Amortization and other acquisition-related costs	0.22	0.11		0.42	0.21	
Impairments and (gain)/loss on disposal of assets	0.03	(0.03)		0.03	(0.02)	
Litigation (recoveries)/charges, net	(0.01)	0.12		(0.01)	0.20	
Loss on extinguishment of debt	—	0.11		—	0.11	
Non-GAAP	$1.30	$1.20	8 %	$2.68	$2.19	22 %

The sum of the components may not equal the total due to rounding.

During the three and six months ended December 31, 2015, GAAP diluted earnings per share attributable to Cardinal Health, Inc. ("diluted EPS") increased 14 percent to $0.98 and 30 percent to $2.14, respectively. Non-GAAP diluted EPS increased 8 percent to $1.30 and 22 percent to $2.68 during the three and six months ended December 31, 2015, respectively. GAAP and non-GAAP diluted EPS increased primarily due to the factors impacting GAAP and non-GAAP operating earnings, partially offset by an increase in interest expense. GAAP and non-GAAP diluted EPS also increased due to a lower effective tax rate during the six months ended December 31, 2015. The increase in GAAP diluted EPS was also partially due to the prior-year loss on extinguishment of debt.

Cash and Equivalents

Our cash and equivalents balance was $2.3 billion at December 31, 2015 compared to $4.6 billion at June 30, 2015. The decrease in cash and equivalents during the six months ended December 31, 2015 was driven by $3.3 billion deployed for acquisitions and dividends of $259 million, offset in part by cash provided by operating activities of $1.4 billion.

Results of Operations

Revenue

(in millions)	Three Months Ended December 31			Six Months Ended December 31		
	2015	2014	Change	2015	2014	Change
Pharmaceutical	$28,287	$22,627	25 %	$53,427	$43,836	22 %
Medical	3,162	2,914	9 %	6,081	5,766	5 %
Total segment revenue	31,449	25,541	23 %	59,508	49,602	20 %
Corporate	(4)	(4)	N.M.	(9)	5	N.M.
Total revenue	$31,445	$25,537	23 %	$59,499	$49,607	20 %

Pharmaceutical Segment

Pharmaceutical segment revenue growth for the three and six months ended December 31, 2015 compared to the prior-year periods was primarily due to sales growth from existing and new pharmaceutical distribution customers, which increased revenue by $5.1 billion and $8.5 billion, respectively, including the impact of continued branded pharmaceutical price appreciation. Acquisitions also contributed to revenue growth ($622 million and $1.3 billion, respectively).

Medical Segment

Medical segment revenue growth for the three and six months ended December 31, 2015 compared to the prior-year periods was primarily due to acquisitions, net of divestitures, which contributed $205 million and $217 million, respectively.

Cost of Products Sold

As a result of the same factors affecting the change in revenue, consolidated cost of products sold increased $5.8 billion (24 percent) and $9.5 billion (20 percent) compared to the prior-year periods. In addition, we incurred a $39 million LIFO charge during the three months ended December 31, 2015. See the "Gross Margin" section for additional drivers impacting cost of products sold.

Gross Margin

(in millions)	Three Months Ended December 31			Six Months Ended December 31		
	2015	2014	Change	2015	2014	Change
Gross margin	$1,609	$1,454	11 %	$3,188	$2,794	14 %

Gross margin increased during the three and six months ended December 31, 2015 compared to the prior-year periods by $155 million (11 percent) and $394 million (14 percent), respectively.

Gross margin was positively impacted by sales growth from existing and new pharmaceutical distribution customers ($152 million and $269 million during the three and six months ended December 31, 2015, respectively) and acquisitions, net of divestitures ($147 million and $219 million, respectively).

Gross margin rate contracted during both the three and six months ended December 31, 2015, primarily due to the onboarding of a new mail order customer starting in October 2015. In addition, gross margin rate was favorably impacted by performance under our generics program and adversely impacted by customer pricing changes. Gross margin rate contraction includes the negative impact of a LIFO charge ($39 million) during the three months ended December 31, 2015. See Note 1 of the "Notes to Condensed Consolidated Financial Statements" for additional information on the LIFO inventory method.

Distribution, Selling, General, and Administrative ("SG&A") Expenses

(in millions)	Three Months Ended December 31			Six Months Ended December 31		
	2015	2014	Change	2015	2014	Change
SG&A expenses	$922	$815	13 %	$1,764	$1,590	11 %

The increase in SG&A expenses during the three and six months ended December 31, 2015 over the prior-year periods was driven by acquisitions, net of divestitures ($106 million and $136 million, respectively).

Segment Profit

We evaluate segment performance based on segment profit, among other measures. See Note 13 of the "Notes to Condensed Consolidated Financial Statements" for additional information on segment profit.

	Three Months Ended December 31			Six Months Ended December 31		
(in millions)	2015	2014	Change	2015	2014	Change
Pharmaceutical	$627	$542	16 %	$1,285	$992	29 %
Medical	106	115	(8)%	207	229	(10)%
Total segment profit	733	657	12 %	1,492	1,221	22 %
Corporate	(170)	(111)	N.M.	(309)	(209)	N.M.
Total consolidated operating earnings	$563	$546	3 %	$1,183	$1,012	17 %

Pharmaceutical Segment Profit

The increase in Pharmaceutical segment profit during the three and six months ended December 31, 2015 over the prior-year periods was due to sales growth from existing and new pharmaceutical distribution customers and performance under our generics program, partially offset by the adverse impact of customer pricing changes. Acquisitions also contributed to segment profit growth. Segment profit does not include LIFO charges/(credits) held at corporate as explained in Note 13 of the "Notes to Condensed Consolidated Financial Statements."

Medical Segment Profit

The decrease in Medical segment profit during the three and six months ended December 31, 2015 compared to the prior-year periods was primarily due to the negative impact of acquisitions and

divestitures, which included the unfavorable cost of products sold impact from the fair value step up of inventory acquired with Cordis. The decrease in Medical segment profit during the six months ended December 31, 2015 was also due to our Canada business.

Corporate

As discussed further in sections that follow, the principal drivers for the change in Corporate during the three and six months ended December 31, 2015 compared to the prior-year periods were increased amortization and other acquisition-related costs primarily due to amortization and costs incurred in connection with the acquisitions of Cordis and Harvard Drug. Corporate was also adversely impacted by the LIFO charge described under "Gross Margin" above.

MD&A Results of Operations

Other Components of Consolidated Operating Earnings

In addition to revenue, gross margin, and SG&A expenses discussed previously, consolidated operating earnings were impacted by the following:

	Three Months Ended December 31		Six Months Ended December 31	
(in millions)	2015	2014	2015	2014
Restructuring and employee severance	$2	$7	$14	$26
Amortization and other acquisition-related costs	114	60	219	112
Impairments and (gain)/loss on disposal of assets, net	17	(18)	17	(18)
Litigation (recoveries)/charges, net	(9)	44	(9)	72

Amortization and Other Acquisition-Related Costs

Amortization of acquisition-related intangible assets was $100 million and $47 million for the three months ended December 31, 2015 and 2014, respectively, and $167 million and $91 million for the six months ended December 31, 2015 and 2014, respectively. The increase in amortization of acquisition-related intangible assets during both periods is largely due to the acquisitions of Cordis and Harvard Drug. Transaction and integration costs associated with the acquisition of Cordis were $20 million and $41 million during the three and six months ended December 31, 2015, respectively.

Litigation (Recoveries)/Charges, Net

During the three months ended December 31, 2015, we received and recognized income of $13 million resulting from settlements of class action antitrust claims in which we were a class member.

During the three and six months ended December 31, 2014, we incurred litigation charges of $7 million and $61 million, respectively, related to the DEA and FTC investigations and related matters.

Earnings Before Income Taxes

In addition to the items discussed above, earnings before income taxes was impacted by the following:

	Three Months Ended December 31			Six Months Ended December 31		
(in millions)	2015	2014	Change	2015	2014	Change
Other (income)/expense, net	$(2)	$(1)	N.M.	$6	$(4)	N.M.
Interest expense, net	45	36	24%	90	70	28%
Loss on extinguishment of debt	—	60	N.M.	—	60	N.M.

Interest Expense, Net

Interest expense increased during both the three and six months ended December 31, 2015, primarily as a result of the additional $1.5 billion of debt issued in June 2015 to fund the Harvard Drug and Cordis acquisitions.

Loss on Extinguishment of Debt

In December 2014 we redeemed certain debt resulting in a loss on the extinguishment of debt of $60 million ($37 million, net of tax).

Provision for Income Taxes

During the three months ended December 31, 2015 and 2014, the effective tax rate was 37.3 percent and 36.0 percent, respectively. During the six months ended December 31, 2015 and 2014, the effective tax rate was 34.7 percent and 37.4 percent, respectively. The effective tax rate during the six months ended December 31, 2015 was impacted by net favorable discrete items of $28 million.

Due to the adoption of amended accounting guidance that simplifies the accounting for income taxes, current deferred tax assets of $20 million and current deferred tax liabilities of $1.1 billion in our December 31, 2015 condensed consolidated balance sheet were reclassified as non-current. In accordance with the adoption of this guidance, balances were not retrospectively adjusted. The adoption of this guidance had no impact on our condensed consolidated statements of earnings, comprehensive income or cash flows. Refer to Note 1 of the "Notes to Condensed Consolidated Financial Statements" for additional information.

Liquidity and Capital Resources

We currently believe that, based on available capital resources (cash on hand and committed credit facilities) and projected operating cash flow, we have adequate capital resources to fund working capital needs; currently anticipated capital expenditures; currently anticipated business growth and expansion; contractual obligations; tax payments; and current and projected debt service requirements, dividends, and share repurchases. If we decide to engage in one or more additional acquisitions, depending on the size and timing of such transactions, we may need to access capital markets for additional financing.

Cash and Equivalents

Our cash and equivalents balance was $2.3 billion at December 31, 2015 compared to $4.6 billion at June 30, 2015. The decrease in cash and equivalents during the six months ended December 31, 2015 was driven by $3.3 billion deployed for acquisitions and dividends of $259 million, offset in part by cash provided by operating activities of $1.4 billion. At December 31, 2015, our cash and equivalents were held in cash depository accounts with major banks or invested in high quality, short-term liquid investments.

The cash and equivalents balance at December 31, 2015 included $394 million of cash held by subsidiaries outside of the United States. Although the vast majority of this cash is available for repatriation, permanently bringing the money into the United States could trigger U.S. federal, state, and local income tax obligations. As a U.S. parent company, we may temporarily access cash held by our foreign subsidiaries without becoming subject to U.S. federal, state, and local income tax through intercompany loans.

Changes in working capital, which impact operating cash flow, can vary significantly depending on factors such as the timing of customer payments, inventory purchases and payments to vendors in the regular course of business, as well as fluctuating working capital needs driven by customer and product mix.

Financial Instruments and Other Financing Arrangements

Credit Facilities and Commercial Paper

Other sources of liquidity include a $1.5 billion revolving credit facility and a $950 million committed receivables sales facility program. We also have a commercial paper program of up to $1.5 billion, backed by the revolving credit facility. At December 31, 2015, we had no outstanding balances or borrowings under these facilities, except for standby letters of credit of $40 million under the committed receivables sales facility program.

Our revolving credit facility and committed receivables sales facility program require us to maintain a consolidated interest coverage ratio of at least 4-to-1 and consolidated leverage ratio of no more than 3.25-to-1. As of December 31, 2015, we were in compliance with these financial covenants.

Available-for-Sale Securities

At December 31, 2015, we held $198 million of marketable securities, which are classified as available-for-sale.

Capital Deployment

Capital Expenditures

Capital expenditures during the six months ended December 31, 2015 and 2014 were $175 million and $83 million, respectively.

Dividends

On November 4, 2015, our Board of Directors approved a quarterly dividend of $0.3870 per share, or $1.55 per share on an annualized basis, payable on January 15, 2016 to shareholders of record on January 4, 2016.

Share Repurchases

Our Board of Directors has approved a $2.0 billion share repurchase program, which expires on December 31, 2016. During the six months ended December 31, 2015, we did not repurchase common shares under this program. At December 31, 2015, we had $693 million remaining under this repurchase authorization.

Acquisitions

On July 2, 2015, August 26, 2015, and October 2, 2015, we acquired Harvard Drug, naviHealth, and Cordis for $1.1 billion, $238 million, and $1.9 billion, respectively.

Other Items

The MD&A in our 2015 Form 10-K addresses our contractual obligations, critical accounting policies and sensitive accounting estimates, and the absence of off-balance sheet arrangements, as of and for the fiscal year ended June 30, 2015. There have been no subsequent material changes outside of the ordinary course of business to those items.

Explanation and Reconciliation of Non-GAAP Financial Measures

Explanation and Reconciliation of Non-GAAP Financial Measures
The "Overview of Consolidated Results" section within MD&A in this Form 10-Q contains financial measures that are not calculated in accordance with GAAP. In general, the measures exclude items and charges that we do not believe reflect our core business and relate more to strategic, multi-year corporate activities, or the items and charges relate to activities or actions that may have occurred over multiple or in prior periods without predictable trends. We use these non-GAAP financial measures internally to evaluate our performance, evaluate our financial position, engage in financial and operational planning, and determine incentive compensation.
We provide these non-GAAP financial measures to investors as supplemental metrics to assist readers in assessing the effects of items and events on our financial and operating results and in comparing our performance to that of our competitors. However, the non-GAAP financial measures used by us may be calculated differently from, and therefore may not be comparable to, similarly titled measures used by other companies.
The non-GAAP financial measures disclosed by us should not be considered a substitute for, or superior to, financial measures calculated in accordance with GAAP, and the financial results calculated in accordance with GAAP and reconciliations to those financial measures should be carefully evaluated.
Following are definitions of the non-GAAP financial measures presented in this Form 10-Q and reconciliations of the differences between the non-GAAP financial measures and their most directly comparable GAAP financial measures. For all other definitions, refer to our 2015 Form 10-K.

Definitions
Non-GAAP operating earnings: operating earnings excluding (1) LIFO charges/(credits), (2) restructuring and employee severance, (3) amortization and other acquisition-related costs, (4) impairments and (gain)/loss on disposal of assets, and (5) litigation (recoveries)/charges, net.
Non-GAAP net earnings attributable to Cardinal Health, Inc.: net earnings attributable to Cardinal Health, Inc. excluding (1) LIFO charges/(credits), (2) restructuring and employee severance, (3) amortization and other acquisition-related costs, (4) impairments and (gain)/loss on disposal of assets, (5) litigation (recoveries)/charges, net, and (6) loss on extinguishment of debt, each net of tax.
Non-GAAP diluted EPS attributable to Cardinal Health, Inc. or "Non-GAAP diluted EPS": non-GAAP net earnings attributable to Cardinal Health, Inc. divided by diluted weighted-average shares outstanding.

MD&A

GAAP to Non-GAAP Reconciliations

(in millions, except per common share amounts)	Operating Earnings	Operating Earnings Growth Rate	Net Earnings attributable to Cardinal Health, Inc.	Net Earnings attributable to Cardinal Health, Inc. Growth Rate	Diluted EPS attributable to Cardinal Health, Inc.	Diluted EPS attributable to Cardinal Health, Inc. Growth Rate
	Three Months Ended December 31, 2015					
GAAP	$563	3 %	$326	13 %	$0.98	14 %
LIFO charges/(credits)	39		24		0.07	
Restructuring and employee severance	2		1		—	
Amortization and other acquisition-related costs	114		73		0.22	
Impairments and (gain)/loss on disposal of assets	17		10		0.03	
Litigation (recoveries)/charges, net	(9)		(4)		(0.01)	
Non-GAAP	$726	14 %	$430	7 %	$1.30	8 %
	Three Months Ended December 31, 2014					
GAAP	$546	5 %	$289	5 %	$0.86	9 %
Restructuring and employee severance	7		4		0.01	
Amortization and other acquisition-related costs	60		38		0.11	
Impairments and (gain)/loss on disposal of assets	(18)		(8)		(0.03)	
Litigation (recoveries)/charges, net	44		40		0.12	
Loss on extinguishment of debt	—		37		0.11	
Non-GAAP	$639	10 %	$400	28 %	$1.20	33 %
	Six Months Ended December 31, 2015					
GAAP	$1,183	17 %	$709	28 %	$2.14	30 %
LIFO charges/(credits)	39		24		0.07	
Restructuring and employee severance	14		9		0.02	
Amortization and other acquisition-related costs	219		141		0.42	
Impairments and (gain)/loss on disposal of assets	17		10		0.03	
Litigation (recoveries)/charges, net	(9)		(4)		(0.01)	
Non-GAAP	$1,463	22 %	$889	20 %	$2.68	22 %
	Six Months Ended December 31, 2014					
GAAP	$1,012	2 %	$555	(10)%	$1.65	(7)%
Restructuring and employee severance	26		17		0.05	
Amortization and other acquisition-related costs	112		71		0.21	
Impairments and (gain)/loss on disposal of assets	(18)		(8)		(0.02)	

Litigation (recoveries)/charges, net	72		68		0.20	
Loss on extinguishment of debt	—		37		0.11	
Non-GAAP	$1,204	8 %	$740	7 %	$2.19	10 %

The sum of the components may not equal the total due to rounding.
We apply varying tax rates depending on the item's nature and tax jurisdiction where it is incurred.

Other

Quantitative and Qualitative Disclosures About Market Risk

There have been no material changes in the quantitative and qualitative market risk disclosures included in our 2015 Form 10-K since the end of fiscal 2015 through December 31, 2015.

Controls and Procedures

Evaluation of Disclosure Controls and Procedures

We evaluated, with the participation of our principal executive officer and principal financial officer, the effectiveness of our disclosure controls and procedures (as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934 (the "Exchange Act")) as of December 31, 2015. Based on this evaluation, our principal executive officer and principal financial officer have concluded that as of December 31, 2015, our disclosure controls and procedures were effective to provide reasonable assurance that information required to be disclosed in our reports under the Exchange Act is recorded, processed, summarized, and reported within the time periods specified in the SEC rules and forms and that such information is accumulated and communicated to management as appropriate to allow timely decisions regarding required disclosure.

Changes in Internal Control Over Financial Reporting

There were no changes in our internal control over financial reporting during the quarter ended December 31, 2015 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Legal Proceedings

The legal proceedings described in Note 7 of the "Notes to Condensed Consolidated Financial Statements" are incorporated in this "Legal Proceedings" section by reference.

Risk Factors

You should carefully consider the information in this Form 10-Q and the risk factors discussed in "Risk Factors" and other risks discussed in our 2015 Form 10-K and our filings with the SEC since June 30, 2015. These risks could materially and adversely affect our results of operations, financial condition, liquidity, and cash flows. Our business also could be affected by risks that we are not presently aware of or that we currently consider immaterial to our operations.

Unregistered Sales of Equity Securities and Use of Proceeds

Issuer Purchases of Equity Securities

Period	Total Number of Shares Purchased (1)	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Program (2)	Approximate Dollar Value of Shares That May Yet be Purchased Under the Program (2) (in millions)
October 2015	266	$79.88	—	$693
November 2015	231	87.72	—	693
December 2015	221	88.83	—	693
Total	718	$85.16	—	$693

(1) Common shares purchased through a rabbi trust as investments of participants in our Deferred Compensation Plan.

(2) On October 29, 2013, our Board of Directors approved a $1.0 billion share repurchase program and on August 6, 2014, the Board of Directors authorized an additional $1.0 billion under the program, for a total of $2.0 billion. This program expires on December 31, 2016. We did not repurchase common shares under this program during the three months ended December 31, 2015.

Financial Statements

Condensed Consolidated Statements of Earnings
(Unaudited)

	Three Months Ended December 31		Six Months Ended December 31	
(in millions, except per common share amounts)	2015	2014	2015	2014
Revenue	$31,445	$25,537	$59,499	$49,607
Cost of products sold	29,836	24,083	56,311	46,813
Gross margin	1,609	1,454	3,188	2,794
Operating expenses:				
Distribution, selling, general, and administrative expenses	922	815	1,764	1,590
Restructuring and employee severance	2	7	14	26
Amortization and other acquisition-related costs	114	60	219	112
Impairments and (gain)/loss on disposal of assets, net	17	(18)	17	(18)
Litigation (recoveries)/charges, net	(9)	44	(9)	72
Operating earnings	563	546	1,183	1,012
Other (income)/expense, net	(2)	(1)	6	(4)
Interest expense, net	45	36	90	70
Loss on extinguishment of debt	—	60	—	60
Earnings before income taxes	520	451	1,087	886
Provision for income taxes	194	162	377	331
Net earnings	326	289	710	555
Less: Net earnings attributable to noncontrolling interests	—	—	(1)	—
Net earnings attributable to Cardinal Health, Inc.	$326	$289	$709	$555
Earnings per common share attributable to Cardinal Health, Inc.:				
Basic	$0.99	$0.87	$2.16	$1.66
Diluted	0.98	0.86	2.14	1.65
Weighted-average number of common shares outstanding:				
Basic	329	331	329	333
Diluted	332	334	332	337
Cash dividends declared per common share	$0.3870	$0.3425	$0.7740	$0.6850

See notes to condensed consolidated financial statements.

Financial Statements

Condensed Consolidated Statements of Comprehensive Income
(Unaudited)

	Three Months Ended December 31		Six Months Ended December 31	
(in millions)	2015	2014	2015	2014
Net earnings	$326	$289	$710	$555
Other comprehensive loss:				
Foreign currency translation adjustments	(28)	(40)	(73)	(64)
Net unrealized loss on derivative instruments, net of tax	(1)	(9)	(1)	(9)
Total other comprehensive loss, net of tax	(29)	(49)	(74)	(73)
Total comprehensive income	297	240	636	482
Less: Comprehensive income attributable to noncontrolling interests	—	—	(1)	—
Total comprehensive income attributable to Cardinal Health, Inc.	$297	$240	$635	$482

See notes to condensed consolidated financial statements.

Financial Statements

Condensed Consolidated Balance Sheets

(in millions)	December 31, 2015 (Unaudited)	June 30, 2015
Assets		
Current assets:		
Cash and equivalents	$ 2,324	$ 4,616
Trade receivables, net	6,980	6,523
Inventories, net	11,007	9,211
Prepaid expenses and other	1,518	1,402
Total current assets	21,829	21,752
Property and equipment, net	1,651	1,506
Goodwill and other intangibles, net	9,113	6,018
Other assets	914	866
Total assets	$ 33,507	$ 30,142
Liabilities, Redeemable Noncontrolling Interests, and Shareholders' Equity		
Current liabilities:		
Accounts payable	$ 16,919	$ 14,368
Current portion of long-term obligations and other short-term borrowings	354	281
Other accrued liabilities	1,606	2,594
Total current liabilities	18,879	17,243
Long-term obligations, less current portion	5,171	5,211
Deferred income taxes and other liabilities	2,609	1,432
Redeemable noncontrolling interests	120	—
Shareholders' equity:		
Preferred shares, without par value:		
Authorized—500 thousand shares, Issued—none	—	—
Common shares, without par value:		
Authorized—755 million shares, Issued—364 million shares at December 31, 2015 and June 30, 2015	2,973	3,003
Retained earnings	5,972	5,521
Common shares in treasury, at cost: 34 million shares and 36 million shares at December 31, 2015 and June 30, 2015, respectively	(2,137)	(2,245)
Accumulated other comprehensive loss	(97)	(23)
Total Cardinal Health, Inc. shareholders' equity	6,711	6,256
Noncontrolling interests	17	—
Total shareholders' equity	6,728	6,256
Total liabilities, redeemable noncontrolling interests, and shareholders' equity	$ 33,507	$ 30,142

See notes to condensed consolidated financial statements.

Financial Statements

Condensed Consolidated Statements of Cash Flows
(Unaudited)

	Six Months Ended December 31	
(in millions)	2015	2014
Cash flows from operating activities:		
Net earnings	$710	$555
Adjustments to reconcile net earnings to net cash provided by operating activities:		
Depreciation and amortization	306	220
Loss on extinguishment of debt	—	60
Gain on sale of other investments	—	(5)
Impairments and (gain)/loss on disposal of assets, net	17	(18)
Share-based compensation	56	53
Provision for bad debts	35	26
Change in fair value of contingent consideration obligation	(14)	—
Change in operating assets and liabilities, net of effects from acquisitions:		
Increase in trade receivables	(393)	(291)
Increase in inventories	(1,565)	(1,137)
Increase in accounts payable	2,431	1,438
Other accrued liabilities and operating items, net	(172)	113
Net cash provided by operating activities	1,411	1,014
Cash flows from investing activities:		
Acquisition of subsidiaries, net of cash acquired	(3,284)	(86)
Additions to property and equipment	(175)	(83)
Purchase of available-for-sale securities and other investments	(88)	(107)
Proceeds from sale of available-for-sale securities and other investments	57	107
Proceeds from maturities of available-for-sale securities	19	16
Proceeds from divestitures and disposal of held for sale assets	—	53
Net cash used in investing activities	(3,471)	(100)
Cash flows from financing activities:		
Payment of contingent consideration obligation	(23)	—
Net change in short-term borrowings	39	(18)
Reduction of long-term obligations	(4)	(1,220)
Proceeds from long-term obligations, net of issuance costs	—	1,182
Net proceeds/(tax withholdings) from share-based compensation	(7)	35
Tax proceeds from share-based compensation	32	42
Dividends on common shares	(259)	(233)
Purchase of treasury shares	—	(686)
Net cash used in financing activities	(222)	(898)
Effect of exchange rate changes on cash and equivalents	(10)	—
Net increase/(decrease) in cash and equivalents	(2,292)	16
Cash and equivalents at beginning of period	4,616	2,865
Cash and equivalents at end of period	$2,324	$2,881

See notes to condensed consolidated financial statements.

Notes to Financial Statements

Notes to Condensed Consolidated Financial Statements

1. Basis of Presentation and Summary of Significant Accounting Policies
Basis of Presentation
Our condensed consolidated financial statements include the accounts of all majority-owned or controlled subsidiaries, and all significant intercompany transactions and amounts have been eliminated. References to "we," "our," and similar pronouns in this Quarterly Report on Form 10-Q for the quarter ended December 31, 2015 (this "Form 10-Q") refer to Cardinal Health, Inc. and its majority-owned or controlled subsidiaries unless the context requires otherwise. The results of businesses acquired or disposed of are included in the condensed consolidated financial statements from the effective date of the acquisition or up to the date of disposal, respectively.
Our condensed consolidated financial statements have been prepared in accordance with the U.S. Securities and Exchange Commission ("SEC") instructions to Quarterly Reports on Form 10-Q and include all of the information and disclosures required by accounting principles generally accepted in the United States ("GAAP") for interim financial reporting. The preparation of financial statements in conformity with GAAP requires us to make estimates and assumptions that affect amounts reported in the condensed consolidated financial statements and accompanying notes. Actual amounts may differ from these estimated amounts. In addition, operating results presented for this fiscal 2016 interim period are not necessarily indicative of the results that may be expected for the full fiscal year ending June 30, 2016.
These condensed consolidated financial statements are unaudited and are presented pursuant to the rules and regulations of the SEC. Accordingly, the condensed consolidated financial statements included in this Form 10-Q should be read in conjunction with the audited consolidated financial statements and related notes contained in our Annual Report on Form 10-K for the fiscal year ended June 30, 2015 (the "2015 Form 10-K"). In our opinion, all adjustments necessary for a fair presentation of the condensed consolidated financial statements have been included. Except as disclosed elsewhere in this Form 10-Q, all such adjustments are of a normal and recurring nature.
Inventories
A substantial portion of our inventories are valued at the lower of cost, using the last-in, first-out ("LIFO") method, or market. These inventories are included within the core pharmaceutical distribution facilities of our Pharmaceutical segment ("distribution facilities") and are primarily merchandise inventories. The LIFO method presumes that the most recent inventory purchases are the first items sold, so LIFO helps us better match current costs and revenue. We believe that the average cost method of inventory valuation provides a reasonable approximation of the current cost of replacing inventory within these distribution facilities. As such, the LIFO reserve is the difference between (a) inventory at the lower of LIFO cost or market

and (b) inventory at replacement cost determined using the average cost method of inventory valuation.
Interim LIFO calculations are based on our estimates of expected year-end inventory levels and costs, as the actual valuation of inventory under the LIFO method is computed at the end of the fiscal year based on the inventory levels and costs at that time. Based upon the year-to-date balance and expectations for the remainder of the fiscal year, we recorded a LIFO charge of $39 million for the three months ended December 31, 2015, which is included in cost of products sold in the condensed consolidated financial statements.
Recent Financial Accounting Standards
In January 2016, the Financial Accounting Standards Board ("FASB") issued amended accounting guidance intended to improve the recognition and measurement of financial instruments as part of a larger simplification initiative. The amended guidance primarily changes the accounting for equity method investments, financial liabilities under the fair value option, the method for assessing the realizability of deferred tax assets related to available-for-sale securities, and the presentation and disclosure requirements for financial instruments. This classification and measurement guidance will be effective for us in the first quarter of fiscal 2019, with early adoption permitted. We are currently evaluating the impact of the adoption on our consolidated financial statements.

In November 2015, the FASB issued amended accounting guidance that simplifies the accounting for income taxes. Under this amended guidance, deferred tax assets and liabilities must be classified as noncurrent on the balance sheet instead of separating deferred tax items into current and noncurrent amounts. We adopted this guidance on a prospective basis in the second quarter of fiscal 2016. Upon adoption of this guidance, current deferred tax assets of $20 million and current deferred tax liabilities of $1.1 billion in our December 31, 2015 condensed consolidated balance sheet were reclassified as noncurrent. In accordance with the adoption of this guidance, balances were not retrospectively adjusted. The adoption of this guidance had no impact on our condensed consolidated statements of earnings, comprehensive income or cash flows.

In September 2015, the FASB issued amended accounting guidance that eliminates the requirement that an acquirer in a business combination account for measurement-period adjustments on a retrospective basis. Under this amended guidance, the acquirer will recognize a measurement-period adjustment during the period in which it determines the amount of the adjustment. We adopted this guidance in the second quarter of fiscal 2016. The adoption of this guidance did not materially impact our condensed consolidated financial statements.

In May 2014, the FASB issued amended accounting guidance related to revenue recognition. This guidance is based on the principle that revenue is recognized in an amount that reflects the consideration to which an entity expects to be entitled in exchange for the transfer of goods or services to customers. The guidance also requires additional disclosure about the nature, amount, timing, and

Notes to Financial Statements

uncertainty of revenue and cash flows arising from customer contracts, including significant judgments and changes in judgments and assets recognized from costs incurred to obtain or fulfill a contract. In July 2015, the FASB deferred the effective date for one year beyond the originally specified effective date. This amendment will be effective for us in the first quarter of fiscal 2019. We are continuing to evaluate the options for adoption and the impact on our consolidated financial statements.

In April 2014, the FASB issued amended accounting guidance related to the reporting of discontinued operations and disclosures of disposals of components of an entity. The amended guidance changes the thresholds for disposals to qualify as discontinued operations and requires additional disclosures. We adopted this guidance in the first quarter of fiscal 2016. The adoption of this guidance did not impact our condensed consolidated financial statements.

2. Acquisitions

During the six months ended December 31, 2015, we completed several acquisitions, the most significant of which are described in more detail below. The pro forma results of operations and the results of operations for acquired businesses since the acquisition dates have not been separately disclosed because the effects were not significant compared to the condensed consolidated financial statements, individually or in the aggregate.

Cordis

On October 2, 2015, we acquired the Cordis business ("Cordis") from Ethicon, Inc., a wholly-owned subsidiary of Johnson & Johnson, for $1.9 billion using cash on hand and proceeds from our debt offering in June 2015. The acquisition of Cordis, a global manufacturer and distributor of interventional cardiology devices and endovascular solutions with operations in more than 50 countries, expands our Medical segment's portfolio of self-manufactured products and its geographic scope. We closed the Cordis acquisition in 20 principal countries on October 2, 2015, and acquired the rights to the net economic benefit from the entire Cordis business in the other countries at that time. For the remaining non-principal countries, we will acquire legal ownership in the next 24 months. The results for the entire Cordis business in all countries are included in the condensed consolidated financial statements as of and for the six months ended December 31, 2015.

Transaction and integration costs associated with the acquisition of Cordis were $20 million and $41 million during the three and six months ended December 31, 2015, respectively, and are included in amortization and other acquisition-related costs in the condensed consolidated statements of earnings.

naviHealth

On August 26, 2015, we acquired a 71 percent ownership interest in naviHealth Group Holdings, L.P. ("naviHealth") for $238 million, net of cash acquired of $53 million. We funded the acquisition with cash on hand. The acquisition of naviHealth, a leader in post-acute care management solutions, expands our ability to serve health plans, health systems, and providers. We consolidate the results of naviHealth in our condensed consolidated financial statements and

report its consolidated results in our Medical segment. The terms of the agreement provide us with the option to acquire the remaining 29 percent noncontrolling interests at any time after the two-year anniversary of the closing. The third-party noncontrolling interests holders also hold an option, which allows them to sell their noncontrolling interests to us at any time after the two-year anniversary of the closing. Refer to Note 10 for further information on the redeemable noncontrolling interests.

Harvard Drug

On July 2, 2015, we completed the acquisition of The Harvard Drug Group ("Harvard Drug") for $1.1 billion using cash on hand and proceeds from our debt offering in June 2015. The acquisition of Harvard Drug, a distributor of generic pharmaceuticals, over-the-counter healthcare and related products to retail, institutional and alternate care customers, enhances our Pharmaceutical segment's generic pharmaceutical distribution and related services businesses. Harvard Drug also manufactures and repackages generic pharmaceuticals and over-the-counter healthcare products.

Fair Value of Assets Acquired and Liabilities Assumed

The allocation of the purchase price for the acquisitions of Cordis, naviHealth, and Harvard Drug are not yet finalized and are subject to adjustment as we complete the valuation analysis for these acquisitions. The purchase prices are also subject to adjustment based on working capital requirements as set forth in the acquisition agreements.

The valuation of identifiable intangible assets utilizes significant unobservable inputs and thus represents a Level 3 nonrecurring fair value measurement. The estimated fair value of the identifiable intangible assets was determined using an income-based approach, which includes market participant expectations of the cash flows that an asset could generate over its remaining useful life, discounted back to present value using an appropriate rate of return. The discount rates used to arrive at the present value of the identifiable intangible assets ranged from 12 percent to 14 percent, and reflect the internal rate of return and uncertainty in the cash flow projections.

Notes to Financial Statements

The following table summarizes the estimated fair values of the assets acquired and liabilities assumed as of the acquisition dates for Cordis, naviHealth, and Harvard Drug:

(in millions)	Cordis	naviHealth	Harvard Drug
Identifiable intangible assets:			
Customer relationships (1)	$230	$38	$470
Trade names (2)	130	16	130
Developed technology (3)	400	61	—
In-process research and development (4)	55	—	—
Total identifiable intangible assets acquired	815	115	600
Cash and equivalents	—	53	46
Trade receivables	—	38	67
Inventories	213	—	49
Prepaid expenses and other	4	14	12
Property and equipment	98	5	16
Other assets	10	1	1
Accounts payable	(81)	(2)	(48)
Other accrued liabilities	(11)	(95)	(39)
Deferred income taxes and other liabilities	(7)	(42)	(104)
Redeemable noncontrolling interests	—	(119)	—
Total identifiable net assets/(liabilities) acquired	1,041	(32)	600
Goodwill	832	323	551
Total net assets acquired	$1,873	$291	$1,151

(1) The weighted-average useful lives of customer relationships range from 4 to 13