

THERMO FISHER SCIENTIFIC INC.

Form 10-Q

August 03, 2018

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

ý Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the Quarter Ended June 30, 2018

¨ Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

Commission File Number 1-8002

THERMO FISHER SCIENTIFIC INC.

(Exact name of Registrant as specified in its charter)

Delaware 04-2209186

(State of incorporation or organization) (I.R.S. Employer Identification No.)

168 Third Avenue

Waltham, Massachusetts 02451

(Address of principal executive offices) (Zip Code)

Registrant's telephone number, including area code: (781) 622-1000

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 and (2) has been subject to such filing requirements for the past 90 days. Yes ý 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 during the preceding 12 months (or for such shorter period that the Registrant was required to submit and post such files). Yes ý 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. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company" and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer ý 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 ý

Indicate the number of shares outstanding of each of the issuer's classes of Common Stock, as of the latest practicable date.

Class	Outstanding at June 30, 2018
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Common Stock, \$1.00 par value	402,796,251
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THERMO FISHER SCIENTIFIC INC.
QUARTERLY REPORT ON FORM 10-Q
FOR THE QUARTER ENDED JUNE 30, 2018
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THERMO FISHER SCIENTIFIC INC.

PART I FINANCIAL INFORMATION

Item 1. Financial Statements

CONSOLIDATED BALANCE SHEET

(Unaudited)

	June 30, 2018	December 31, 2017
(In millions except share and per share amounts)		
Assets		
Current Assets:		
Cash and cash equivalents	\$937	\$1,335
Accounts receivable, less allowances of \$115 and \$109	3,911	3,879
Inventories	2,866	2,971
Refundable income taxes	530	432
Other current assets	1,230	804
Total current assets	9,474	9,421
Property, Plant and Equipment, Net	3,952	4,047
Acquisition-related Intangible Assets, Net	15,680	16,684
Other Assets	1,177	1,227
Goodwill	25,120	25,290
Total Assets	\$55,403	\$56,669
Liabilities and Shareholders' Equity		
Current Liabilities:		
Short-term obligations and current maturities of long-term obligations	\$1,711	\$2,135
Accounts payable	1,359	1,428
Accrued payroll and employee benefits	755	918
Contract liabilities	816	—
Deferred revenue	—	719
Other accrued expenses	1,339	1,848
Total current liabilities	5,980	7,048
Deferred Income Taxes	2,599	2,766
Other Long-term Liabilities	2,670	2,569
Long-term Obligations	17,709	18,873
Shareholders' Equity:		
Preferred stock, \$100 par value, 50,000 shares authorized; none issued		
Common stock, \$1 par value, 1,200,000,000 shares authorized; 429,925,100 and 428,327,873 shares issued	430	428
Capital in excess of par value	14,408	14,177
Retained earnings	17,226	15,914
Treasury stock at cost, 27,128,849 and 27,013,311 shares	(3,128)	(3,103)
Accumulated other comprehensive items	(2,491)	(2,003)

Total shareholders' equity	26,445	25,413
Total Liabilities and Shareholders' Equity	\$55,403	\$ 56,669

The accompanying notes are an integral part of these consolidated financial statements.

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THERMO FISHER SCIENTIFIC INC.

CONSOLIDATED STATEMENT OF INCOME
(Unaudited)

	Three Months Ended June 30, 2018		Six Months Ended June 30, 2018	
	July 1, 2017		July 1, 2017	
(In millions except per share amounts)				
Revenues				
Product revenues	\$4,708	\$4,298	\$9,236	\$8,400
Service revenues	1,370	692	2,695	1,355
Total revenues	6,078	4,990	11,931	9,755
Costs and Operating Expenses:				
Cost of product revenues	2,390	2,244	4,715	4,373
Cost of service revenues	950	462	1,898	905
Selling, general and administrative expenses	1,542	1,291	3,057	2,625
Research and development expenses	242	222	476	437
Restructuring and other costs, net	17	22	62	46
Total costs and operating expenses	5,141	4,241	10,208	8,386
Operating Income	937	749	1,723	1,369
Other Expense, Net	(131)	(123)	(283)	(240)
Income from Continuing Operations Before Income Taxes	806	626	1,440	1,129
(Provision for) Benefit from Income Taxes	(54)	(13)	(109)	35
Income from Continuing Operations	752	613	1,331	1,164
Loss from Discontinued Operations (net of income tax benefit of \$0, \$0, \$0 and \$0)	—	(1)	—	(1)
Net Income	\$752	\$612	\$1,331	\$1,163
Earnings per Share from Continuing Operations				
Basic	\$1.87	\$1.57	\$3.31	\$2.98
Diluted	\$1.85	\$1.56	\$3.28	\$2.96
Earnings per Share				
Basic	\$1.87	\$1.57	\$3.31	\$2.98
Diluted	\$1.85	\$1.56	\$3.28	\$2.95
Weighted Average Shares				
Basic	403	390	402	390
Diluted	406	393	406	394
Cash Dividends Declared per Common Share	\$0.17	\$0.15	\$0.34	\$0.30

The accompanying notes are an integral part of these consolidated financial statements.

THERMO FISHER SCIENTIFIC INC.

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME
(Unaudited)

(In millions)	Three Months Ended		Six Months Ended	
	June 30, 2018	July 1, 2017	June 30, 2018	July 1, 2017
Comprehensive Income				
Net Income	\$752	\$612	\$1,331	\$1,163
Other Comprehensive Items:				
Currency translation adjustment (net of tax provision of \$94, \$0, \$47 and \$0)	(462)	219	(415)	379
Unrealized gains and losses on available-for-sale investments:				
Unrealized holding gains arising during the period (net of tax provision of \$0, \$1, \$0 and \$1)	—	1	—	2
Reclassification adjustment for (gains) losses included in net income (net of tax (provision) benefit of \$0, (\$1), \$0 and (\$1))	—	(1)	—	(1)
Unrealized gains and losses on hedging instruments:				
Reclassification adjustment for losses included in net income (net of tax benefit of \$1, \$1, \$2 and \$2)	2	2	4	4
Pension and other postretirement benefit liability adjustments:				
Pension and other postretirement benefit liability adjustments arising during the period (net of tax provision (benefit) of \$2, (\$2), \$1 and (\$3))	5	(7)	3	(9)
Amortization of net loss and prior service benefit included in net periodic pension cost (net of tax benefit of \$2, \$1, \$3 and \$2)	6	3	8	5
Total other comprehensive items	(449)	217	(400)	380
Comprehensive Income	\$303	\$829	\$931	\$1,543

The accompanying notes are an integral part of these consolidated financial statements.

THERMO FISHER SCIENTIFIC INC.

CONSOLIDATED STATEMENT OF CASH FLOWS
(Unaudited)

(In millions)	Six Months Ended	
	June 30, 2018	July 1, 2017
Operating Activities		
Net income	\$1,331	\$1,163
Loss from discontinued operations	—	1
Income from continuing operations	1,331	1,164
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	1,146	942
Change in deferred income taxes	(99)	(299)
Non-cash stock-based compensation	91	71
Non-cash charges for sale of inventories revalued at the date of acquisition	8	31
Other non-cash expenses, net	55	46
Changes in assets and liabilities, excluding the effects of acquisitions and dispositions:		
Accounts receivable	(97)	(127)
Inventories	(195)	(146)
Other assets	(247)	(178)
Accounts payable	(20)	49
Other liabilities	(408)	(161)
Contributions to retirement plans	(43)	(181)
Net cash provided by continuing operations	1,522	1,211
Net cash used in discontinued operations	—	(1)
Net cash provided by operating activities	1,522	1,210
Investing Activities		
Acquisitions, net of cash acquired	(59)	(307)
Purchase of property, plant and equipment	(301)	(181)
Proceeds from sale of property, plant and equipment	3	2
Other investing activities, net	(7)	9
Net cash used in investing activities	\$(364)	\$(477)

THERMO FISHER SCIENTIFIC INC.

CONSOLIDATED STATEMENT OF CASH FLOWS (Continued)
(Unaudited)

	Six Months Ended	
	June	July
	30,	1,
(In millions)	2018	2017
Financing Activities		
Net proceeds from issuance of debt	\$—	\$519
Repayment of debt	(1,353)	(1,329)
Proceeds from issuance of commercial paper	2,761	4,487
Repayments of commercial paper	(2,655)	(3,991)
Purchases of company common stock	—	(750)
Dividends paid	(129)	(118)
Net proceeds from issuance of company common stock under employee stock plans	78	99
Other financing activities	(50)	—
Net cash used in financing activities	(1,348)	(1,083)
Exchange Rate Effect on Cash	(215)	168
Decrease in Cash, Cash Equivalents and Restricted Cash	(405)	(182)
Cash, Cash Equivalents and Restricted Cash at Beginning of Period	1,361	811
Cash, Cash Equivalents and Restricted Cash at End of Period	\$956	\$629

See Note 12 for supplemental cash flow information.

The accompanying notes are an integral part of these consolidated financial statements.

THERMO FISHER SCIENTIFIC INC.

CONSOLIDATED STATEMENT OF SHAREHOLDERS' EQUITY
(Unaudited)

(In millions)	Common Stock Shares	Amount	Capital in Excess of Par Value	Retained Earnings	Treasury Stock Shares	Amount	Accumulated Other Comprehensive Items	Total Shareholders' Equity
Balance at December 31, 2016	415	\$ 415	\$ 12,140	\$ 13,927	22	\$(2,306)	\$ (2,636)	) \$ 21,540
Issuance of shares under employees' and directors' stock plans	2	2	120	—	—	(14)	) —	108
Stock-based compensation	—	—	71	—	—	—	—	71
Purchases of company common stock	—	—	—	—	5	(750)	) —	(750)
Dividends declared	—	—	—	(118)	) —	—	—	(118)
Net income	—	—	—	1,163	—	—	—	1,163
Other comprehensive items	—	—	—	—	—	—	380	380
Other	—	—	(3)	) —	—	—	—	(3)
Balance at July 1, 2017	417	\$ 417	\$ 12,328	\$ 14,972	27	\$(3,070)	\$ (2,256)	) \$ 22,391
Balance at December 31, 2017	428	\$ 428	\$ 14,177	\$ 15,914	27	\$(3,103)	\$ (2,003)	) \$ 25,413
Cumulative effect of accounting changes	—	—	—	118	—	—	(88)	) 30
Issuance of shares under employees' and directors' stock plans	2	2	113	—	—	(25)	) —	90
Stock-based compensation	—	—	91	—	—	—	—	91
Dividends declared	—	—	—	(137)	) —	—	—	(137)
Net income	—	—	—	1,331	—	—	—	1,331
Other comprehensive items	—	—	—	—	—	—	(400)	) (400)
Other	—	—	27	—	—	—	—	27
Balance at June 30, 2018	430	\$ 430	\$ 14,408	\$ 17,226	27	\$(3,128)	\$ (2,491)	) \$ 26,445

The accompanying notes are an integral part of these consolidated financial statements.

THERMO FISHER SCIENTIFIC INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

Note 1. Nature of Operations and Summary of Significant Accounting Policies

Nature of Operations

Thermo Fisher Scientific Inc. (the company or Thermo Fisher) enables customers to make the world healthier, cleaner and safer by providing analytical instruments, equipment, reagents and consumables, software and services for research, manufacturing, analysis, discovery and diagnostics. Markets served include pharmaceutical and biotech, academic and government, industrial and applied, as well as healthcare and diagnostics.

Interim Financial Statements

The interim consolidated financial statements presented herein have been prepared by the company, are unaudited and, in the opinion of management, reflect all adjustments of a normal recurring nature necessary for a fair statement of the financial position at June 30, 2018, the results of operations for the three- and six-month periods ended June 30, 2018 and July 1, 2017, and the cash flows for the six-month periods ended June 30, 2018 and July 1, 2017. Interim results are not necessarily indicative of results for a full year.

The consolidated balance sheet presented as of December 31, 2017, has been derived from the audited consolidated financial statements as of that date. The consolidated financial statements and notes are presented as permitted by Form 10-Q and do not contain all information that is included in the annual financial statements and notes thereto of the company. The consolidated financial statements and notes included in this report should be read in conjunction with the 2017 financial statements and notes included in the company's Annual Report on Form 10-K filed with the Securities and Exchange Commission (SEC).

Note 1 to the consolidated financial statements for 2017 describes the significant accounting estimates and policies used in preparation of the consolidated financial statements. Except for the accounting for revenue arising from contracts with customers, as noted below, there have been no material changes in the company's significant accounting policies during the six months ended June 30, 2018.

Revenue Recognition

The company recognizes revenue for the transfer of 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. Consumables revenues consist of single-use products and are recognized at a point in time following the transfer of control of such products to the customer, which generally occurs upon shipment. Instruments revenues typically consist of longer-lived assets that, for the substantial majority of sales, are recognized at a point in time in a manner similar to consumables. Service revenues (clinical trial logistics, pharmaceutical development and manufacturing services, asset management, diagnostic testing, training, service contracts, and field services including related time and materials) are recognized over time as customers receive and consume the benefits of such services. For revenues recognized over time, the company generally uses costs accumulated as inputs to measure progress. For contracts that contain multiple performance obligations, the company allocates the consideration to which it expects to be entitled to each performance obligation based on relative standalone selling prices and recognizes the related revenue when or as control of each individual performance obligation is transferred to customers. The company exercises judgment in determining the timing of revenue by analyzing the point in time or the period over which the customer has the ability to direct the use of and obtain substantially all of the remaining benefits of the asset. The company immediately expenses contract costs that would otherwise be capitalized and amortized over a period of less than one year. Payments from customers for most instruments, consumables and services are typically due in a fixed number of days after shipment or delivery of the product. Service arrangements commonly call for payments in advance of performing the work (e.g. extended service contracts), upon completion of the service (e.g. pharmaceutical development and manufacturing) or a mix of both.

See Note 3 for revenue disaggregated by type and by geographic region as well as further information about remaining performance obligations.

Contract-related Balances

Contract assets include revenues recognized in advance of billings and are recorded net of estimated losses resulting from the inability to invoice customers. Contract assets are classified as current or noncurrent based on the amount of time expected

THERMO FISHER SCIENTIFIC INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

to lapse until the company's right to consideration becomes unconditional. Current contract assets and noncurrent contract assets are included within other current assets and other assets, respectively, in the accompanying balance sheet.

Contract liabilities include billings in excess of revenues recognized, such as those resulting from customer advances and deposits and unearned revenue on service contracts. Contract liabilities are classified as current or noncurrent based on the periods over which remaining performance obligations are expected to be transferred to customers. Noncurrent contract liabilities are included within other long-term liabilities in the accompanying balance sheet.

Contract asset and liability balances are as follows:

	June 30, 2018	January 1, 2018
(In millions)		

Current Contract Assets, Net	\$471	\$ 396
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Current Contract Liabilities	816	805
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Noncurrent Contract Liabilities	337	302
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Noncurrent contract assets were immaterial in 2018. In the first six months of 2018, the company recognized revenue of \$483 million that was included in the contract liabilities balance at January 1, 2018.

Warranty Obligations

The liability for warranties is included in other accrued expenses in the accompanying balance sheet. The changes in the carrying amount of standard product warranty obligations are as follows:

	Six Months Ended June 30, 2018	July 1, 2017
(In millions)		

Beginning Balance	\$87	\$78
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Provision charged to income	58	54
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Usage	(53)	(51)
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Acquisitions	—	1
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Adjustments to previously provided warranties, net	(2)	(1)
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Currency translation	(2)	2
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Ending Balance	\$88	\$83
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Inventories

The components of inventories are as follows:

	June 30, 2018	December 31, 2017
(In millions)		

Raw Materials	\$776	\$ 708
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Work in Process	415	505
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Finished Goods	1,675	1,758
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Inventories	\$2,866	\$ 2,971
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THERMO FISHER SCIENTIFIC INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

Property, Plant and Equipment

Property, plant and equipment consists of the following:

	June 30, 2018	December 31, 2017
(In millions)		
Land	\$ 398	\$ 401
Buildings and Improvements	1,668	1,662
Machinery, Equipment and Leasehold Improvements	4,408	4,276
Property, Plant and Equipment, at Cost	6,474	6,339
Less: Accumulated Depreciation and Amortization	2,522	2,292

Property, Plant and Equipment, Net \$3,952 \$ 4,047

Acquisition-related Intangible Assets

Acquisition-related intangible assets are as follows:

	Balance at June 30, 2018			Balance at December 31, 2017		
(In millions)	Gross	Accumulated Amortization	Net	Gross	Accumulated Amortization	Net
Definite Lived:						
Customer relationships	\$ 17,129	\$ (6,336)	) \$ 10,793	\$ 17,356	\$ (5,902)	) \$ 11,454
Product technology	6,012	(3,024)	) 2,988	6,046	(2,811)	) 3,235
Tradenames	1,516	(884)	) 632	1,538	(817)	) 721
Other	33	(33)	) —	34	(34)) —
	24,690	(10,277)	) 14,413	24,974	(9,564)	) 15,410
Indefinite Lived:						
Tradenames	1,235	N/A	1,235	1,235	N/A	1,235
In-process research and development	32	N/A	32	39	N/A	39
	1,267	N/A	1,267	1,274	N/A	1,274

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