

HNI CORP  
Form 10-Q  
October 30, 2018

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

FORM 10-Q

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

For the quarterly period ended September 29, 2018

OR

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

Commission File Number: 1-14225

HNI Corporation  
Iowa 42-0617510  
(State of Incorporation) (I.R.S. Employer No.)

600 East Second Street  
P. O. Box 1109  
Muscatine, Iowa 52761-0071  
(563) 272-7400

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 every Interactive Data File required to be submitted 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 such files).

YES  NO

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,"

Edgar Filing: HNI CORP - Form 10-Q

"accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer  Accelerated filer  Non-accelerated filer  Smaller reporting company  Emerging growth company

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.

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

YES  NO

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

Common Stock, \$1 Par Value Outstanding as of September 29, 2018 43,819,664

---

HNI Corporation and Subsidiaries  
 Quarterly Report on Form 10-Q

Table of Contents

PART I. FINANCIAL INFORMATION

	Page
Item 1. Financial Statements (Unaudited)	
<u>Condensed Consolidated Statements of Comprehensive Income - Three Months and Nine Months Ended September 29, 2018 and September 30, 2017</u>	<u>3</u>
<u>Condensed Consolidated Balance Sheets - September 29, 2018 and December 30, 2017</u>	<u>4</u>
<u>Consolidated Statements of Equity - Three Months and Nine Months Ended September 29, 2018 and September 30, 2017</u>	<u>6</u>
<u>Condensed Consolidated Statements of Cash Flows - Nine Months Ended September 29, 2018 and September 30, 2017</u>	<u>8</u>
<u>Notes to Condensed Consolidated Financial Statements</u>	<u>9</u>
Item 2. <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	<u>25</u>
Item 3. <u>Quantitative and Qualitative Disclosures About Market Risk</u>	<u>34</u>
Item 4. <u>Controls and Procedures</u>	<u>34</u>
PART II. OTHER INFORMATION	
Item 1. <u>Legal Proceedings</u>	<u>35</u>
Item 1A. <u>Risk Factors</u>	<u>35</u>
Item 2. <u>Unregistered Sales of Equity Securities and Use of Proceeds</u>	<u>35</u>
Item 3. Defaults Upon Senior Securities - None	-
Item 4. Mine Safety Disclosures - Not Applicable	-
Item 5. Other Information - None	-
Item 6. <u>Exhibits</u>	<u>36</u>
<u>Signatures</u>	<u>37</u>



## PART I. FINANCIAL INFORMATION

## Item 1. Financial Statements

HNI Corporation and Subsidiaries  
Condensed Consolidated Statements of Comprehensive Income  
(In thousands, except share and per share data)  
(Unaudited)

	Three Months Ended		Nine Months Ended	
	September 30,	September 30,	September 29,	September 30,
	2018	2017	2018	2017
Net sales	\$611,120	\$ 599,455	\$1,659,803	\$ 1,591,607
Cost of sales	377,789	378,211	1,048,683	1,011,888
Gross profit	233,331	221,244	611,120	579,719
Selling and administrative expenses	179,577	169,547	524,445	495,897
Gain on sale and license of assets	—	(6,805	) —	(6,805
Restructuring and impairment charges	128	783	2,303	3,325
Operating income	53,626	57,719	84,372	87,302
Interest income	80	71	282	467
Interest expense	2,602	1,835	7,657	4,228
Income before income taxes	51,104	55,955	76,997	83,541
Income taxes	11,197	18,624	16,033	27,573
Net income	39,907	37,331	60,964	55,968
Less: Net income (loss) attributable to non-controlling interest	—	60	(50	) 12
Net income attributable to HNI Corporation	\$39,907	\$ 37,271	\$61,014	\$ 55,956
Average number of common shares outstanding – basic	43,822,757	43,682,805	43,616,046	43,970,377
Net income attributable to HNI Corporation per common share basic	\$0.91	\$ 0.85	\$1.40	\$ 1.27
Average number of common shares outstanding – diluted	44,678,824	44,479,117	44,349,456	45,078,719
Net income attributable to HNI Corporation per common share diluted	\$0.89	\$ 0.84	\$1.38	\$ 1.24
Foreign currency translation adjustments	\$(817	) \$ 320	\$(1,944	) \$ 779
Change in unrealized gains (losses) on marketable securities, net of tax	(6	) 7	(99	) 44
Change in derivative financial instruments, net of tax	106	38	1,459	(90
Other comprehensive income (loss), net of tax	(717	) 365	(584	) 733
Comprehensive income	39,190	37,696	60,380	56,701
Less: Comprehensive income (loss) attributable to non-controlling interest	—	60	(50	) 12
Comprehensive income attributable to HNI Corporation	\$39,190	\$ 37,636	\$60,430	\$ 56,689

See accompanying Notes to Condensed Consolidated Financial Statements (Unaudited).



HNI Corporation and Subsidiaries  
Condensed Consolidated Balance Sheets  
(In thousands)  
(Unaudited)

	September 29, 2018	December 30, 2017
Assets		
Current Assets:		
Cash and cash equivalents	\$ 43,738	\$ 23,348
Short-term investments	1,880	2,015
Receivables	254,898	258,551
Inventories	174,551	155,683
Prepaid expenses and other current assets	38,839	49,283
Total Current Assets	513,906	488,880
Property, Plant, and Equipment:		
Land and land improvements	28,120	28,593
Buildings	292,048	306,137
Machinery and equipment	553,236	556,571
Construction in progress	31,243	39,788
	904,647	931,089
Less accumulated depreciation	525,316	540,768
Net Property, Plant, and Equipment	379,331	390,321
Goodwill and Other Intangible Assets	480,812	490,892
Deferred Income Taxes	193	193
Other Assets	21,504	21,264
Total Assets	\$ 1,395,746	\$ 1,391,550

See accompanying Notes to Condensed Consolidated Financial Statements (Unaudited).

HNI Corporation and Subsidiaries  
Condensed Consolidated Balance Sheets  
(In thousands, except par value)  
(Unaudited)

	September 29, 2018	December 30, 2017
Liabilities and Equity		
Current Liabilities:		
Accounts payable and accrued expenses	\$ 430,723	\$ 450,128
Current maturities of long-term debt	720	36,648
Current maturities of other long-term obligations	4,518	2,927
Total Current Liabilities	435,961	489,703
Long-Term Debt	249,334	240,000
Other Long-Term Liabilities	77,628	70,409
Deferred Income Taxes	79,749	76,861
Equity:		
HNI Corporation shareholders' equity:		
Capital Stock:		
Preferred stock - \$1 par value, authorized 2,000 shares, no shares outstanding	—	—
Common stock - \$1 par value, authorized 200,000 shares, outstanding:		
September 29, 2018 – 43,820 shares		
December 30, 2017 – 43,354 shares	43,820	43,354
Additional paid-in capital	27,517	7,029
Retained earnings	485,432	467,296
Accumulated other comprehensive income (loss)	(4,195)	(3,611)
Total HNI Corporation shareholders' equity	552,574	514,068
Non-controlling interest	500	509
Total Equity	553,074	514,577
Total Liabilities and Equity	\$ 1,395,746	\$ 1,391,550

See accompanying Notes to Condensed Consolidated Financial Statements (Unaudited).



HNI Corporation and Subsidiaries  
Consolidated Statements of Equity  
(In thousands, except per share data)  
(Unaudited)

	Three Months Ended - September 29, 2018					
	Common Stock	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Non-controlling Interest	Total Shareholders' Equity
Balance, June 30, 2018	\$43,736	\$26,077	\$458,458	\$ (3,477 )	\$ 500	\$ 525,294
Comprehensive income:						
Net income (loss)	—	—	39,907	—	—	39,907
Other comprehensive income (loss), net of tax	—	—	—	(717 )	—	(717 )
Change in ownership of non-controlling interest	—	—	—	—	—	—
Cash dividends; \$0.295 per share	—	—	(12,933 )	—	—	(12,933 )
Common shares – treasury:						
Shares purchased	(163 )	(6,758 )	—	—	—	(6,921 )
Shares issued under Members' Stock Purchase Plan and stock awards, net of tax	247	8,198	—	—	—	8,445
Balance, September 29, 2018	\$43,820	\$27,517	\$485,432	\$ (4,195 )	\$ 500	\$ 553,074
	Nine Months Ended - September 29, 2018					
	Common Stock	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Non-controlling Interest	Total Shareholders' Equity
Balance, December 30, 2017	\$43,354	\$7,029	\$467,296	\$ (3,611 )	\$ 509	\$ 514,577
Comprehensive income:						
Net income (loss)	—	—	61,014	—	(50 )	60,964
Other comprehensive income (loss), net of tax	—	—	—	(584 )	—	(584 )
Change in ownership of non-controlling interest	—	—	(41 )	—	41	—
Cash dividends; \$0.875 per share	—	—	(38,201 )	—	—	(38,201 )
Common shares – treasury:						
Shares purchased	(369 )	(9,879 )	(4,636 )	—	—	(14,884 )
Shares issued under Members' Stock Purchase Plan and stock awards, net of tax	835	30,367	—	—	—	31,202
Balance, September 29, 2018	\$43,820	\$27,517	\$485,432	\$ (4,195 )	\$ 500	\$ 553,074

See accompanying Notes to Condensed Consolidated Financial Statements (Unaudited).



HNI Corporation and Subsidiaries  
Consolidated Statements of Equity  
(In thousands, except per share data)  
(Unaudited)

	Three Months Ended - September 30, 2017					
	Common Stock	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Non-controlling Interest	Total Shareholders' Equity
Balance, July 1, 2017	\$44,056	\$ 5,438	\$449,130	\$ (4,633 )	\$ 358	\$ 494,349
Comprehensive income:						
Net income (loss)	—	—	37,271	—	60	37,331
Other comprehensive income (loss), net of tax	—	—	—	365	—	365
Change in ownership of non-controlling interest	—	—	—	—	—	—
Cash dividends; \$0.285 per share	—	—	(12,448 )	—	—	(12,448 )
Common shares – treasury:						
Shares purchased	(779 )	(4,379 )	(23,864 )	—	—	(29,022 )
Shares issued under Members' Stock Purchase Plan and stock awards, net of tax	150	5,155	—	—	—	5,305
Balance, September 30, 2017	\$43,427	\$ 6,214	\$450,089	\$ (4,267 )	\$ 418	\$ 495,881

	Nine Months Ended - September 30, 2017					
	Common Stock	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Non-controlling Interest	Total Shareholders' Equity
Balance, December 31, 2016	\$44,079	\$ —	\$461,524	\$ (5,000 )	\$ 406	\$ 501,009
Comprehensive income:						
Net income (loss)	—	—	55,956	—	12	55,968
Other comprehensive income (loss), net of tax	—	—	—	733	—	733
Change in ownership of non-controlling interest	—	—	—	—	—	—
Cash dividends; \$0.845 per share	—	—	(37,175 )	—	—	(37,175 )
Common shares – treasury:						
Shares purchased	(1,301 )	(21,333 )	(30,216 )	—	—	(52,850 )
Shares issued under Members' Stock Purchase Plan and stock awards, net of tax	649	27,547	—	—	—	28,196
Balance, September 30, 2017	\$43,427	\$ 6,214	\$450,089	\$ (4,267 )	\$ 418	\$ 495,881

See accompanying Notes to Condensed Consolidated Financial Statements (Unaudited).



HNI Corporation and Subsidiaries  
Condensed Consolidated Statements of Cash Flows  
(In thousands)  
(Unaudited)

	Nine Months Ended	
	September 29, 2018	September 30, 2017
<b>Net Cash Flows From (To) Operating Activities:</b>		
Net income	\$60,964	\$ 55,968
Non-cash items included in net income:		
Depreciation and amortization	55,887	54,524
Other post-retirement and post-employment benefits	1,325	1,194
Stock-based compensation	6,215	6,759
Deferred income taxes	2,733	8,128
(Gain) loss on sale, retirement, license, and impairment of long-lived assets and intangibles, net	1,283	(5,085 )
Amortization of deferred gain on sale leaseback transaction	(285 )	—
Other – net	2,599	(1,649 )
Net increase (decrease) in operating assets and liabilities, net of divestitures	(16,533 )	(53,096 )
Increase (decrease) in other liabilities	849	(9,399 )
Net cash flows from (to) operating activities	115,037	57,344
<b>Net Cash Flows From (To) Investing Activities:</b>		
Capital expenditures	(39,887 )	(87,142 )
Proceeds from sale and license of property, plant, equipment, and intangibles	22,686	8,646
Capitalized software	(7,092 )	(16,749 )
Acquisition spending, net of cash acquired	(2,850 )	(898 )
Purchase of investments	(2,471 )	(2,874 )
Sales or maturities of investments	2,375	2,678
Other – net	1,135	1,511
Net cash flows from (to) investing activities	(26,104 )	(94,828 )
<b>Net Cash Flows From (To) Financing Activities:</b>		
Payments of long-term debt and other financing	(352,795)	(185,390 )
Proceeds from long-term debt	322,755	287,188
Dividends paid	(38,201 )	(37,175 )
Purchase of HNI Corporation common stock	(16,043 )	(52,850 )
Proceeds from sales of HNI Corporation common stock	15,896	12,024
Withholding related to net share settlements of equity based awards	(155 )	(209 )
Net cash flows from (to) financing activities	(68,543 )	23,588
Net increase (decrease) in cash and cash equivalents	20,390	(13,896 )
Cash and cash equivalents at beginning of period	23,348	36,312
Cash and cash equivalents at end of period	\$43,738	\$ 22,416

See accompanying Notes to Condensed Consolidated Financial Statements (Unaudited).



## HNI Corporation and Subsidiaries

Notes to Condensed Consolidated Financial Statements (Unaudited)  
September 29, 2018

## Note 1. Basis of Presentation

The accompanying unaudited, condensed consolidated financial statements have been prepared in accordance with generally accepted accounting principles 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 notes required by generally accepted accounting principles for complete financial statements. The December 30, 2017 consolidated balance sheet included in this Form 10-Q was derived from audited financial statements but does not include all disclosures required by generally accepted accounting principles. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair statement have been included. Operating results for the nine-month period ended September 29, 2018 are not necessarily indicative of the results expected for the fiscal year ending December 29, 2018. For further information, refer to the consolidated financial statements and accompanying notes included in HNI Corporation's (the "Corporation") Annual Report on Form 10-K for the fiscal year ended December 30, 2017.

## Note 2. Revenue from Contracts with Customers

The Corporation implemented ASU No. 2014-09, Revenue from Contracts with Customers (Topic 606), at the beginning of fiscal 2018 using the modified-retrospective method, which required the new guidance to be applied prospectively to revenue transactions completed on or after the effective date. Given the nature of the Corporation's revenue transactions, the new guidance did not have a material impact on the Corporation's results of operations or financial position. All necessary changes required by the new standard, including those to the Corporation's accounting policies, controls, and disclosures, have been identified and implemented as of the beginning of fiscal 2018.

## Disaggregation of Revenue

Revenue from contracts with customers disaggregated by sales channel and by segment is as follows (in thousands):

Segment	Three Months Ended		Nine Months Ended		
	September 29, 2018	September 30, 2017	September 29, 2018	September 30, 2017	
Supplies-driven channel	Office Furniture	\$ 265,971	\$ 238,542	\$ 680,656	\$ 620,602
Contract channel	Office Furniture	205,716	226,770	595,824	611,135
Hearth	Hearth Products	139,433	134,143	383,323	359,870
Net sales		\$ 611,120	\$ 599,455	\$ 1,659,803	\$ 1,591,607

The majority of revenue presented as "Net sales" in the Condensed Consolidated Statements of Comprehensive Income is the result of contracts with customers. All other sources of revenue are not material to the Corporation's results of operations.

Sales by channel type are subject to similar economic factors and market conditions regardless of the channel under which the product is sold. See "Note 17. Reportable Segment Information" in the Notes to Condensed Consolidated Financial Statements for further information about operating segments.

## Contract Assets and Contract Liabilities

In addition to trade receivables, the Corporation has contract assets consisting of funds paid to certain office furniture dealers in exchange for their multi-year commitment to market and sell the Corporation's product. These dealer investments are amortized over the term of the contract. For contracts less than one year, the Corporation has elected the practical expedient to recognize incremental costs to obtain a contract as an expense when incurred. The Corporation has contract liabilities consisting of deferred revenue and rebate and marketing program liabilities.

9

---



Contract assets and contract liabilities were as follows (in thousands):

	September 29, December 30,	
	2018	2017
Trade receivables (1)	\$ 257,191	\$ 260,455
Contract assets (current) (2)	\$ 483	\$ 300
Contract assets (long-term) (3)	\$ 3,905	\$ 2,350
Contract liabilities (4)	\$ 53,495	\$ 54,527

The index below indicates the line item in the Condensed Consolidated Balance Sheets where contract assets and contract liabilities are reported:

- (1) "Receivables"
- (2) "Prepaid expenses and other current assets"
- (3) "Other Assets"
- (4) "Accounts payable and accrued expenses"

Changes in contract asset and contract liability balances during the nine months ended September 29, 2018 were as follows (in thousands):

	Contract assets increase (decrease)	Contract liabilities (increase) decrease
Contract assets recognized	\$ 2,100	\$ —
Reclassification of contract assets to contra revenue	(362 )	—
Contract liabilities recognized and recorded to contra revenue as a result of performance obligations satisfied	—	(87,674 )
Contract liabilities paid	—	86,329
Cash received in advance and not recognized as revenue	—	(43,878 )
Reclassification of cash received in advance to revenue as a result of performance obligations satisfied	—	46,178
Impact of business combination	—	77
Net change	\$ 1,738	\$ 1,032

For the three months ended September 29, 2018, no revenue was recognized in the Condensed Consolidated Statements of Comprehensive Income related to contract liabilities as of December 30, 2017, as the entire liability was recognized as revenue during the three months ended March 31, 2018. For the nine months ended September 29, 2018, the Corporation recognized revenue of \$12.5 million in the Condensed Consolidated Statements of Comprehensive Income related to contract liabilities as of December 30, 2017.

#### Performance Obligations

The Corporation recognizes revenue for sales of office furniture and hearth products at a point in time following the transfer of control of such products to the customer, which typically occurs upon shipment of the product. In certain circumstances, transfer of control to the customer does not occur until the goods are received by the customer or upon installation and/or customer acceptance, depending on the terms of the underlying contracts. Contracts typically have a duration of less than one year and normally do not include a significant financing component. Generally, payment is due within 30 days of invoicing. See "Note 7. Product Warranties" in the Notes to Condensed Consolidated Financial Statements for additional information on warranty obligations.

#### Significant Judgments

The Corporation uses significant judgment throughout the year in estimating the reduction in net sales driven by rebate and marketing programs. Judgments made include expected sales levels and utilization of funds. However, this judgment factor is significantly reduced at the end of each year when sales volumes and the impact to rebate and marketing programs are known and recorded.

#### Accounting Policies and Practical Expedients Elected

The Corporation elected to use the modified-retrospective method of adopting the new standard on revenue recognition. The new standard has been applied to all contracts not completed as of December 30, 2017, the end of the Corporation's fiscal 2017. The impact of the Corporation's transition adjustment for the new revenue recognition guidance was not material to the Corporation's results of operations or financial position. The additional disclosures required as a result of adopting the new revenue recognition guidance were material to the Corporation's financial statements.

The Corporation elected the following accounting policies as a result of adopting the new standard on revenue recognition:

**Shipping and Handling Activities** - The Corporation has elected to apply the accounting policy election permitted in ASC 606-10-25-18B, which allows an entity to account for shipping and handling activities as fulfillment activities. The Corporation accrues for shipping and handling costs at the same time revenue is recognized, which is in accordance with the policy election. When shipping and handling activities occur prior to the customer obtaining control of the good(s), they are considered fulfillment activities rather than a performance obligation and the costs are accrued for as incurred.

**Sales Taxes** - The Corporation has elected to apply the accounting policy election permitted in ASC 606-10-32-2A, which allows an entity to exclude from the measurement of the transaction price all taxes assessed by a governmental authority associated with the transaction, including sales, use, excise, value-added, and franchise taxes (collectively referred to as sales taxes). This allows the Corporation to present revenue net of these certain types of taxes.

These policies have been applied consistently to all revenue transactions.

The Corporation has elected the following practical expedients as a result of adopting the new standard on revenue recognition:

**Incremental Costs of Obtaining a Contract** - The Corporation has elected the practical expedient permitted in ASC 340-40-25-4, which permits an entity to recognize incremental costs to obtain a contract as an expense when incurred if the amortization period will be less than one year. The Corporation will apply this practical expedient when the requirements to apply it are met.

**Significant Financing Component** - The Corporation has elected the practical expedient permitted in ASC 606-10-32-18, which allows an entity to not adjust the promised amount of consideration for the effects of a significant financing component if a contract has a duration of one year or less. As the Corporation's contracts are typically less than one year in length, consideration will not be adjusted.

These accounting policies and practical expedients have been applied consistently to all revenue transactions.

#### Note 3. Restructuring

Restructuring costs recorded in the Condensed Consolidated Statements of Comprehensive Income are as follows (in thousands):

	Three Months Ended		Nine Months Ended	
	September 30,	September 30,	September 30,	September 30,
	2018	2017	2018	2017
Cost of sales - accelerated depreciation	\$—	\$ 1,552	\$—	\$ 8,711
Restructuring and impairment charges	128	783	2,303	3,325

Total restructuring costs	\$ 128	\$ 2,335	\$2,303	\$ 12,036
---------------------------	--------	----------	---------	-----------

Restructuring costs in the third quarter of 2018 were primarily incurred as part of the previously announced closure of the hearth manufacturing facility in Paris, Kentucky. Restructuring costs in the year-to-date period for 2018 also include an impairment charge from the sale of the closed manufacturing facility in Paris, Kentucky and costs incurred as part of the previously announced closure of the office furniture manufacturing facility in Orleans, Indiana. Restructuring costs in both the quarter and year-to-date periods for 2017, which include accelerated depreciation recorded in "Cost of sales" in the Condensed Consolidated Statements of Comprehensive Income, were primarily incurred as part of the previously announced closures of the hearth manufacturing facilities in Paris, Kentucky and Colville, Washington and the office furniture manufacturing facility in Orleans, Indiana.

The accrued restructuring expenses are expected to be paid in the next twelve months and are included in "Accounts payable and accrued expenses" in the Condensed Consolidated Balance Sheets. The following is a summary of changes in restructuring accruals (in thousands):

	Severance Costs	Facility Exit Costs & Other	Total
Restructuring allowance as of December 30, 2017	\$ 1,343	\$ 516	\$ 1,859
Restructuring charges	350	1,953	2,303
Cash payments	(1,573 )	(2,469)	(4,042 )
Restructuring allowance as of September 29, 2018	\$ 120	\$ —	\$ 120

#### Real Estate Transaction

As part of the Corporation's continued efforts to drive efficiency and simplification, the Corporation entered into a sale-leaseback transaction in the first quarter of 2018, selling a manufacturing facility and subsequently leasing back a portion of the facility for a term of 10 years. The net proceeds from the sale of the facility of \$16.9 million are reflected in "Proceeds from sale and license of property, plant, equipment, and intangibles" in the Condensed Consolidated Statements of Cash Flows. In accordance with ASC 840, Leases, the \$5.1 million gain on the sale of the facility was deferred and is being amortized as a reduction to rent expense evenly over the term of the lease. As of September 29, 2018, the current portion of the deferred gain is \$0.5 million and included within "Accounts payable and accrued expenses" and the long-term portion of the deferred gain is \$4.4 million and included within "Other Long-Term Liabilities" in the Condensed Consolidated Balance Sheets. The transaction did not have a material impact to the Condensed Consolidated Statements of Comprehensive Income.

#### Note 4. Acquisitions and Divestitures

On September 21, 2018, the Corporation acquired a small hearth products company at a purchase price of approximately \$3 million, resulting in a preliminary goodwill valuation of \$3.4 million. The remaining assets and liabilities recorded in the third quarter of 2018 were not material to the Corporation's financial statements. The Corporation will finalize the allocation of the purchase price over the next few quarters based on the final purchase price and fair value adjustments.

As part of the Corporation's ongoing business strategy, it continues to acquire and divest small office furniture dealerships, for which the impact is not material to the Corporation's financial statements.

#### Note 5. Inventories

The Corporation values its inventory at the lower of cost or net realizable value with approximately 83 percent valued by the last-in, first-out ("LIFO") costing method. Inventories included in the Condensed Consolidated Balance Sheets consisted of the following (in thousands):

	September 29, 2018	December 30, 2017
Finished products	\$ 106,349	\$ 101,715
Materials and work in process	95,584	81,202
LIFO allowance	(27,382 )	(27,234 )
Total inventories	\$ 174,551	\$ 155,683



## Note 6. Goodwill and Other Intangible Assets

Goodwill and other intangible assets included in the Condensed Consolidated Balance Sheets consisted of the following (in thousands):

	September 29, 2018	December 30, 2017
Goodwill	\$ 282,939	\$ 279,505
Definite-lived intangible assets	168,692	182,186
Indefinite-lived intangible assets	29,181	29,201
Total goodwill and other intangible assets	\$ 480,812	\$ 490,892

## Goodwill

The changes in the carrying amount of goodwill, by reporting segment, are as follows (in thousands):

	Office Furniture	Hearth Products	Total
Balance as of December 30, 2017			
Goodwill	\$ 128,657	\$ 183,199	\$ 311,856
Accumulated impairment losses	(32,208 )	(143 )	(32,351 )
Net goodwill balance as of December 30, 2017	96,449	183,056	279,505
Goodwill acquired during the year	—	3,444	3,444
Foreign currency translation adjustment	(10 )	—	(10 )
Balance as of September 29, 2018			
Goodwill	128,647	186,643	315,290
Accumulated impairment losses	(32,208 )	(143 )	(32,351 )
Net goodwill balance as of September 29, 2018	\$ 96,439	\$ 186,500	\$ 282,939

## Definite-lived intangible assets

The table below summarizes amortizable definite-lived intangible assets, which are reflected in "Goodwill and Other Intangible Assets" in the Condensed Consolidated Balance Sheets (in thousands):

	September 29, 2018			December 30, 2017		
	Gross	Accumulated Amortization	Net	Gross	Accumulated Amortization	Net
Patents	\$40	\$ 32	\$8	\$40	\$ 26	\$14
Software	169,915	46,110	123,805	167,105	34,792	132,313
Trademarks and trade names	7,564	2,556	5,008	7,564	2,061	5,503
Customer lists and other	105,946	66,075	39,871	106,090	61,734	44,356
Net definite-lived intangible assets	\$283,465	\$ 114,773	\$ 168,692	\$280,799	\$ 98,613	\$ 182,186

Amortization expense is reflected in "Selling and administrative expenses" in the Condensed Consolidated Statements of Comprehensive Income and was as follows (in thousands):

	Three Months Ended		Nine Months Ended	
	September 2018	September 30, 2017	September 2018	September 30, 2017
Capitalized software	\$4,290	\$ 2,658	\$12,734	\$ 5,225
Other definite-lived intangibles	\$1,642	\$ 1,746	\$4,972	\$ 5,267

The occurrence of events such as acquisitions, dispositions, or impairments may impact future amortization expense. Based on the current amount of intangible assets subject to amortization, the estimated amortization expense for each of the following five fiscal years is as follows (in millions):

	2018	2019	2020	2021	2022
Amortization expense	\$23.6	\$22.9	\$22.0	\$20.7	\$18.5

#### Indefinite-lived intangible assets

The Corporation also owns certain intangible assets, which are deemed to have indefinite useful lives because they are expected to generate cash flows indefinitely. These indefinite-lived intangible assets are reflected in "Goodwill and Other Intangible Assets" in the Condensed Consolidated Balance Sheets (in thousands):

	September 29, 2018	December 30, 2017
Trademarks and trade names	\$ 29,181	\$ 29,201

#### Sale and License of an Intangible Asset

In the third quarter of 2017, the Corporation recorded a \$6.0 million nonrecurring gain from the sale and license of an intangible asset, which had a zero carrying value. This nonrecurring gain is reflected in "Gain on sale and license of assets" in the Condensed Consolidated Statements of Comprehensive Income.

#### Impairment Analysis

The Corporation evaluates its goodwill and indefinite-lived intangible assets for impairment on an annual basis during the fourth quarter or whenever indicators of impairment exist. During the third quarter of 2018, the Corporation determined a triggering event occurred for one of the Corporation's reporting units within the office furniture segment due to lower projected operating results for the year. Accordingly, interim quantitative impairment tests were performed for goodwill and an indefinite-lived intangible asset. The tests indicated no impairment. In conjunction with the interim impairment tests, the Corporation also tested the recoverability of the remaining long-lived assets for the reporting unit and found no impairments.

The projections used in the impairment model reflected management's assumptions regarding revenue growth rates, economic and market trends, cost structure, investments required for operational transformation, and other expectations about the anticipated short-term and long-term operating results of the reporting unit. The Corporation assumed a discount rate of 13.5 percent, near term growth rates ranging from 3 percent to 12 percent, and a terminal growth rate of 3 percent. Holding other assumptions constant, a 100 basis point increase in the discount rate would result in a \$3.8 million decrease in the estimated fair value of the reporting unit. Holding other assumptions constant, a 100 basis point decrease in the long-term growth rate would result in a \$1.8 million decrease in the estimated fair value of the reporting unit. Neither of these scenarios individually would result in an impairment of the reporting unit's goodwill. There is \$19.6 million of goodwill associated with this reporting unit as of September 29, 2018.





## Note 7. Product Warranties

The Corporation issues certain warranty policies on its office furniture and hearth products that provide for repair or replacement of any covered product or component that fails during normal use because of a defect in design, materials, or workmanship. Allowances have been established for the anticipated future costs associated with the Corporation's warranty programs.

A warranty allowance is determined by recording a specific allowance for known warranty issues and an additional allowance for unknown claims expected to be incurred based on historical claims experience. Actual claims incurred could differ from the original estimates, requiring adjustments to the allowance. Activity associated with warranty obligations was as follows (in thousands):

	Nine Months Ended	
	September 29, 2018	September 30, 2017
Balance at beginning of period	\$15,388	\$ 15,250
Accruals for warranties issued during period	22,130	15,197
Adjustments related to pre-existing warranties	116	(298 )
Settlements made during the period	(22,203 )	(15,424 )
Balance at end of period	\$15,431	\$ 14,725

The current and long-term portions of the allowance for estimated settlements are included within "Accounts payable and accrued expenses" and "Other Long-Term Liabilities", respectively, in the Condensed Consolidated Balance Sheets. The following table summarizes when these estimated settlements are expected to be paid (in thousands):

	September 29, December 30,	
	2018	2017
Current - in the next twelve months	\$ 9,372	\$ 9,524
Long-term - beyond one year	6,059	5,864
Total estimated settlements	\$ 15,431	\$ 15,388

## Note 8. Long-Term Debt

Long-term debt is as follows (in thousands):

	September 29, December 30,	
	2018	2017
Revolving credit facility with interest at a variable rate (September 29, 2018 - 3.4%; December 30, 2017 - 2.7%)	\$ 150,000	\$ 267,500
Fixed rate notes due in 2025 with an interest rate of 4.22%	50,000	—
Fixed rate notes due in 2028 with an interest rate of 4.40%	50,000	—
Other amounts	720	9,148
Deferred debt issuance costs	(666 )	—
Total debt	250,054	276,648
Less: Current maturities of long-term debt	720	36,648
Long-term debt	\$ 249,334	\$ 240,000

As of September 29, 2018, the Corporation's revolving credit facility borrowings were under the credit agreement entered into on April 20, 2018 with a scheduled maturity of April 20, 2023. The Corporation deferred the debt issuance costs related to the credit agreement, which are classified as assets, and is amortizing them over the term of the credit agreement. The current portion of \$0.4 million is the amount to be amortized over the next twelve months based on the current credit agreement and is reflected in "Prepaid expenses and other current assets" in the Condensed Consolidated Balance Sheets. The long-term portion of \$1.6 million is reflected in "Other Assets" in the Condensed Consolidated Balance Sheets.

As of September 29, 2018, there was \$150 million outstanding under the \$450 million revolving credit facility. The entire amount drawn under the revolving credit facility is considered long-term as the Corporation assumes no obligation to repay any of the amounts borrowed in the next twelve months.

In addition to the revolving credit facility, the Corporation also has \$100 million of borrowings outstanding under private placement note agreements entered into on May 31, 2018. Under the agreements, the Corporation issued \$50 million of seven-year fixed rate notes with an interest rate of 4.22 percent, due May 31, 2025, and \$50 million of ten-year fixed rate notes with an interest rate of 4.40 percent, due May 31, 2028. The Corporation deferred the debt issuance costs related to the private placement note agreements, which are classified as a reduction of long-term debt in accordance with ASU No. 2015-03, and is amortizing them over the terms of the private placement note agreements. The deferred debt issuance costs do not reduce the amount owed by the Corporation under the terms of the private placement note agreements. The current portion of \$0.1 million is the amount to be amortized over the next twelve months based on the private placement note agreements and is reflected in "Current maturities of long-term debt" in the Condensed Consolidated Balance Sheets. The long-term portion of \$0.6 million is reflected in "Long-Term Debt" in the Condensed Consolidated Balance Sheets.

In addition to cash flows from operations, the revolving credit facility under the credit agreement is the primary source of daily operating capital for the Corporation and provides additional financial capacity for capital expenditures and strategic initiatives, such as acquisitions and repurchases of common stock.

The credit agreement and private placement notes both contain financial and non-financial covenants. The covenants under both are substantially the same. Non-compliance with covenants under the agreements could prevent the Corporation from being able to access further borrowings, require immediate repayment of all amounts outstanding, and/or increase the cost of borrowing.

Covenants require maintenance of financial ratios as of the end of any fiscal quarter, including:

- a consolidated interest coverage ratio (as defined in the credit agreement) of not less than 4.0 to 1.0, based upon the ratio of (a) consolidated EBITDA for the last four fiscal quarters to (b) the sum of consolidated interest charges; and
- a consolidated leverage ratio (as defined in the credit agreement) of not greater than 3.5 to 1.0, based upon the ratio of (a) the quarter-end consolidated funded indebtedness to (b) consolidated EBITDA for the last four fiscal quarters.

The most restrictive of the financial covenants is the consolidated leverage ratio requirement of 3.5 to 1.0. Under the credit agreement, consolidated EBITDA is defined as consolidated net income before interest expense, income taxes, and depreciation and amortization of intangibles, as well as non-cash items that increase or decrease net income. As of September 29, 2018, the Corporation was below the maximum allowable ratio and was in compliance with all of the covenants and other restrictions in the credit agreement. The Corporation expects to remain in compliance with all of the covenants and other restrictions in the credit agreement over the next twelve months.



## Note 9. Income Taxes

The Corporation's tax provision for interim periods is determined using an estimate of its annual effective tax rate, adjusted for discrete items. The following table summarizes the Corporation's income tax provision (dollars in thousands):

	Three Months Ended		Nine Months Ended	
	September 29, 2018	September 30, 2017	September 29, 2018	September 30, 2017
Income before income taxes	\$51,104	\$ 55,955	\$76,997	\$ 83,541
Income taxes	\$11,197	\$ 18,624	\$16,033	\$ 27,573
Effective tax rate	21.9	% 33.3	% 20.8	% 33.0

The Corporation's effective tax rate was lower in the three and nine months ended September 29, 2018 compared to the same periods last year primarily due to the enactment of the Tax Cuts and Jobs Act in 2017 (the "Act"). An additional driver of the change in the effective tax rate for the first nine months of 2018 was the release of a valuation allowance for certain foreign jurisdictions.

On December 22, 2017, the Act was signed into law, making significant changes to the Internal Revenue Code. Changes include, but are not limited to, a federal corporate tax rate decrease from 35 percent to 21 percent effective for tax years beginning after December 31, 2017, the transition of U.S. international taxation from a worldwide tax system to a territorial system, and a one-time transition tax on the mandatory deemed repatriation of cumulative foreign earnings as of December 31, 2017.

Staff Accounting Bulletin No. 118 ("SAB 118") was issued to address the application of U.S. GAAP in the reporting period that includes December 22, 2017 in situations when a registrant does not have the necessary information available, prepared, or analyzed (including computations) in reasonable detail to complete the accounting for certain income tax effects of the Act. In accordance with SAB 118, the Corporation determined as of the end of fiscal 2017, the \$45.4 million of the deferred tax benefit recorded in connection with the remeasurement of certain deferred tax assets and liabilities and the \$0.1 million of current tax expense recorded in connection with the transition tax on the mandatory deemed repatriation of foreign earnings was a provisional amount and a reasonable estimate as of December 30, 2017. Additional work was necessary to complete a more detailed analysis of historical foreign earnings as well as potential correlative adjustments. Subsequent adjustments to these amounts, which were not material, were recorded to current tax expense in the third quarter of 2018 when the analysis was completed.

During the third quarter of 2018, the 2017 federal income tax return was completed resulting in a \$0.5 million detriment related to the reversal of net deferred tax liabilities based on the rates at which they are expected to reverse in the future as a result of tax reform rate changes. The Corporation finalized its calculation of the full impact of the Act on its 2017 federal income tax return during the third quarter of 2018.

## Note 10. Fair Value Measurements of Financial Instruments

For recognition purposes, on a recurring basis, the Corporation is required to measure at fair value its marketable securities, derivative financial instruments, variable-rate and fixed-rate debt obligations, and deferred stock-based compensation. The marketable securities are comprised of money market funds, government securities, and corporate bonds. When available, the Corporation uses quoted market prices to determine fair value and classifies such measurements within Level 1. Where market prices are not available, the Corporation makes use of observable market-based inputs (prices or quotes from published exchanges and indexes) to calculate fair value using the market approach, in which case the measurements are classified within Level 2.

Financial instruments measured at fair value were as follows (in thousands):

	Fair value as of measurement date	Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)
Balance as of September 29, 2018				
Cash and cash equivalents (including money market funds) (1)	\$ 43,738	\$ 43,738	\$ —	\$ —
Government securities (2)	\$ 7,094	\$ —	\$ 7,094	\$ —
Corporate bonds (2)	\$ 5,341	\$ —	\$ 5,341	\$ —
Derivative financial instruments (3)	\$ 5,286	\$ —	\$ 5,286	\$ —
Variable-rate debt obligations (4)	\$ 150,000	\$ —	\$ 150,000	\$ —
Fixed-rate debt obligations (4)	\$ 100,000	\$ —	\$ 100,000	\$ —
Deferred stock-based compensation (5)	\$ 10,665	\$ —	\$ 10,665	\$ —
Balance as of December 30, 2017				
Cash and cash equivalents (including money market funds) (1)	\$ 23,348	\$ 23,348	\$ —	\$ —
Government securities (2)	\$ 6,345	\$ —	\$ 6,345	\$ —
Corporate bonds (2)	\$ 6,149	\$ —	\$ 6,149	\$ —
Derivative financial instruments (3)	\$ 3,354	\$ —	\$ 3,354	\$ —
Variable-rate debt obligations (4)	\$ 267,500	\$ —	\$ 267,500	\$ —
Deferred stock-based compensation (5)	\$ 8,885	\$ —	\$ 8,885	\$ —

The index below indicates the line item in the Condensed Consolidated Balance Sheets where the financial instruments are reported:

- (1) "Cash and cash equivalents"
- (2) Current portion - "Short-term investments"; Long-term portion - "Other Assets"
- (3) Current portion - "Prepaid expenses and other current assets"; Long-term portion - "Other Assets"
- (4) Current portion - "Current maturities of long-term debt"; Long-term portion - "Long-Term Debt"
- (5) Current portion - "Current maturities of other long-term obligations"; Long-term portion - "Other Long-Term Liabilities"



## Note 11. Accumulated Other Comprehensive Income (Loss) and Shareholders' Equity

The following tables summarize the components of accumulated other comprehensive income (loss) and the changes in accumulated other comprehensive income (loss), net of tax, as applicable (in thousands):

	Foreign Currency Translation Adjustment	Unrealized Gains (Losses) on Marketable Securities	Pension and Post-retirement Liabilities	Derivative Financial Instruments	Accumulated Other Comprehensive Income (Loss)
Balance as of December 30, 2017	\$ 31	\$ (132 )	\$ (5,630 )	\$ 2,120	\$ (3,611 )
Other comprehensive income (loss) before reclassifications	(1,944 )	(125 )	—	2,593	524
Tax (expense) or benefit	—	26	—	(635 )	(609 )
Amounts reclassified from accumulated other comprehensive income (loss), net of tax	—	—	—	(499 )	(499 )
Balance as of September 29, 2018	\$ (1,913 )	\$ (231 )	\$ (5,630 )	\$ 3,579	\$ (4,195 )

Amounts in parentheses indicate reductions to equity.

	Foreign Currency Translation Adjustment	Unrealized Gains (Losses) on Marketable Securities	Pension and Post-retirement Liabilities	Derivative Financial Instruments	Accumulated Other Comprehensive Income (Loss)
Balance as of December 31, 2016	\$ (1,188 )	\$ (105 )	\$ (5,167 )	\$ 1,460	\$ (5,000 )
Other comprehensive income (loss) before reclassifications	779	68	—	(471 )	376
Tax (expense) or benefit	—	(24 )	—	174	150
Amounts reclassified from accumulated other comprehensive income (loss), net of tax	—	—	—	207	207
Balance as of September 30, 2017	\$ (409 )	\$ (61 )	\$ (5,167 )	\$ 1,370	\$ (4,267 )

Amounts in parentheses indicate reductions to equity.

## Interest Rate Swap

In March 2016, the Corporation entered into an interest rate swap transaction to hedge \$150 million of outstanding variable rate revolver borrowings against future interest rate volatility. Under the terms of the interest rate swap, the Corporation pays a fixed rate of 1.29 percent and receives one month LIBOR on a \$150 million notional value expiring January 2021. As of September 29, 2018, the fair value of the Corporation's interest rate swap was an asset of \$5.3 million, which is reflected in "Other Assets" in the Condensed Consolidated Balance Sheets. The unrecognized change in value of the interest rate swap is reported net of tax as \$3.6 million in "Accumulated other comprehensive income (loss)" in the Condensed Consolidated Balance Sheets.

The following table details the reclassifications from accumulated other comprehensive income (loss) (in thousands):

Details about Accumulated Other Comprehensive Income (Loss) Components	Affected Line Item in the Statement Where Net Income is Presented	Three Months Ended		Nine Months Ended	
		September 30, 2018	September 30, 2017	September 30, 2018	September 30, 2017



Edgar Filing: HNI CORP - Form 10-Q

Derivative financial instruments

Interest rate swap	Interest (expense) or income	\$ 305	\$ (27 )	\$ 661	\$ (328 )
	Tax (expense) or benefit	(75 )	10	(162 )	121
	Net of tax	\$ 230	\$ (17 )	\$ 499	\$ (207 )

Amounts in parentheses indicate reductions to profit.

## Stock Repurchase

The following table summarizes shares repurchased and settled by the Corporation (in thousands, except share data):

	Nine Months Ended	
	September 30, 2018	September 30, 2017
Shares repurchased	368,822	1,300,936
Cash purchase price	\$(14,884)	\$(52,850)
Purchases unsettled as of quarter end	222	—
Prior year purchases settled in current year	(1,381)	—
Shares repurchased per cash flow	\$(16,043)	\$(52,850)

As of September 29, 2018, approximately \$63.1 million of the Corporation's Board of Directors' ("Board") current repurchase authorization remained unspent.

## Dividend

The Corporation declared and paid cash dividends per share as follows (in dollars):

	Nine Months Ended	
	September 30, 2018	September 30, 2017
Common shares	\$0.875	\$ 0.845

## Note 12. Earnings Per Share

The following table reconciles the numerators and denominators used in the calculation of basic and diluted earnings per share ("EPS") (in thousands, except per share data):

	Three Months Ended		Nine Months Ended	
	September 30, 2018	September 30, 2017	September 30, 2018	September 30, 2017
Numerator:				
Numerator for both basic and diluted EPS attributable to HNI Corporation net income	\$39,907	\$ 37,271	\$61,014	\$ 55,956
Denominators:				
Denominator for basic EPS weighted-average common shares outstanding	43,823	43,683	43,616	43,970
Potentially dilutive shares from stock-based compensation plans	856	796	733	1,109
Denominator for diluted EPS	44,679	44,479	44,349	45,079
Earnings per share – basic	\$0.91	\$ 0.85	\$1.40	\$ 1.27
Earnings per share – diluted	\$0.89	\$ 0.84	\$1.38	\$ 1.24

The weighted-average common stock equivalents presented above do not include the effect of the common stock equivalents in the table below because their inclusion would be anti-dilutive.

	Three Months Ended		Nine Months Ended	
	September 30, 2018	September 30, 2017	September 30, 2018	September 30, 2017
Common stock equivalents excluded because their inclusion would be anti-dilutive (in thousands)	1,273	1,111	1,474	788



## Note 13. Stock-Based Compensation

The Corporation measures stock-based compensation expense at grant date, based on the fair value of the award, and recognizes expense over the employees' requisite service periods. Stock-based compensation expense is the cost of stock options and time-based restricted stock units issued under the shareholder approved stock-based compensation plans and shares issued under the shareholder approved member stock purchase plans. The following table summarizes expense associated with these plans (in thousands):

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2018	2017	2018	2017
Compensation cost	\$ 1,307	\$ 956	\$6,215	\$ 6,759

The options and units granted by the Corporation had fair values as follows (in thousands):

	Nine Months Ended	
	September 30,	
	2018	2017
Stock options	\$7,200	\$ 7,206
Restricted stock units	\$76	\$ —

The following table summarizes unrecognized compensation expense and the weighted-average remaining service period for non-vested stock options and restricted stock units as of September 29, 2018:

	Unrecognized Compensation Expense (in thousands)	Weighted-Average Remaining Service Period (years)
Non-vested stock options	\$ 4,419	1.2
Non-vested restricted stock units	\$ 980	1.1

## Note 14. Post-Retirement Health Care

The following table sets forth the components of net periodic benefit costs included in the Condensed Consolidated Statements of Comprehensive Income (in thousands):

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2018	2017	2018	2017
Service cost	\$ 213	\$ 185	\$639	\$ 556
Interest cost	197	206	591	619
Amortization of net (gain) loss	32	6	95	19
Net periodic post-retirement benefit cost	\$ 442	\$ 397	\$1,325	\$ 1,194

Note 15. Recently Adopted Accounting Standards

In May 2014, the FASB issued ASU No. 2014-09, Revenue from Contracts with Customers (Topic 606). The new standard replaces most existing revenue recognition guidance in U.S. GAAP. The core principle of the ASU requires companies to reevaluate when revenue is recorded on a transaction based upon newly defined criteria, either at a point in time or over time as goods or services are delivered. The ASU requires additional disclosure about the nature, amount, timing, and uncertainty of revenue and cash flows arising from customer contracts, including significant judgments and estimates, and changes in those estimates. The FASB has issued ASU No. 2016-08, Revenue from Contracts with Customers: Principal versus Agent Considerations, ASU No. 2016-10, Revenue from Contracts with Customers: Identifying Performance Obligations and Licensing, and ASU No. 2016-12, Revenue from Contracts with Customers: Narrow Scope Improvements and Practical Expedients to provide further clarification and guidance. The Corporation implemented the new standard in the first quarter of fiscal 2018 using the modified-retrospective method, which required the new guidance to be applied prospectively to revenue transactions completed on or after the effective date. Given the nature of the Corporation's revenue transactions, the new guidance did not have a material impact on the Corporation's results of operations or financial position. All necessary changes required by the new standard, including those to the Corporation's accounting policies, controls, and disclosures, have been identified and implemented as of the beginning of fiscal 2018. See "Note 2. Revenue from Contracts with Customers" in the Notes to Condensed Consolidated Financial Statements for further information.

In August 2016, the FASB issued ASU No. 2016-15, Statement of Cash Flows - Classification of Certain Cash Receipts and Cash Payments. The new standard provides classification guidance on eight cash flow issues including debt prepayment, settlement of zero-coupon bonds, contingent consideration payments made after a business combination, proceeds from the settlements of insurance claims, proceeds from the settlement of corporate-owned life insurance policies, and distributions received from equity method investees. The Corporation implemented the new standard in the first quarter of fiscal 2018. This standard did not have a material effect on the condensed consolidated financial statements or related disclosures.

In October 2016, the FASB issued ASU No. 2016-16, Intra-Entity Transfers of Assets Other Than Inventory. The new standard requires an entity to recognize the income tax consequences of intra-entity transfers of assets other than inventory when the transfer occurs. The Corporation implemented the new standard in the first quarter of fiscal 2018. This standard did not have a material effect on the condensed consolidated financial statements or related disclosures.

In March 2017, the FASB issued ASU No. 2017-07, Improving the Presentation of Net Periodic Pension Cost and Net Periodic Post-retirement Benefit Cost. The new standard requires an entity with defined benefit and post-retirement benefit plans to present the service cost component of the net periodic benefit cost in the same income statement line item or items as other compensation costs arising from services rendered by employees during the period. All other components of net periodic benefit cost will be presented outside of operating income, if a subtotal is presented. The Corporation implemented the new standard in the first quarter of fiscal 2018 and it was applied retrospectively to each period presented. This standard did not have a material effect on the condensed consolidated financial statements or related disclosures.

Note 16. Guarantees, Commitments, and Contingencies

The Corporation utilizes letters of credit and surety bonds in the amount of approximately \$19 million to back certain insurance policies and payment obligations. The Corporation utilizes trade letters of credit and banker's acceptances in the amount of approximately \$3 million to guarantee certain payments to overseas suppliers. The letters of credit, bonds, and banker's acceptances reflect fair value as a condition of their underlying purpose and are subject to competitively determined fees.

The Corporation initiated litigation in Iowa on August 15, 2017 against the purchasers of Artcobell for amounts owed in connection with the sale of Artcobell. Artcobell initiated litigation against the Corporation in Texas on June 14, 2017 regarding a dispute arising after the sale of Artcobell. On October 9, 2018, the Corporation resolved all claims related to the disputes. The Corporation is not required to make any payments and expects to record an immaterial recovery in the fourth quarter of 2018.

The Corporation has contingent liabilities which have arisen in the ordinary course of its business, including liabilities relating to pending litigation, environmental remediation, taxes, and other claims. It is the Corporation's opinion, after consultation with legal counsel, that liabilities, if any, resulting from these matters are not expected to have a material adverse effect on the Corporation's financial condition, cash flows, or on the Corporation's quarterly or annual operating results when resolved in a future period.

Note 17. Reportable Segment Information

Management views the Corporation as being in two reportable segments based on industries: office furniture and hearth products, with the former being the principal segment.

The aggregated office furniture segment manufactures and markets a broad line of commercial and home office furniture which includes storage products, desks, credenzas, chairs, tables, bookcases, freestanding office partitions and panel systems, and other related products. The hearth products segment manufactures and markets a broad line of gas, electric, wood, and biomass burning fireplaces, inserts, stoves, facings, and accessories, principally for the home.

For purposes of segment reporting, intercompany sales between segments are not material, and operating profit is income before income taxes exclusive of certain unallocated general corporate expenses. These unallocated general corporate expenses include the net costs of the Corporation's corporate operations. Management views interest income and expense as corporate financing costs and not as a reportable segment cost. In addition, management applies an effective income tax rate to its consolidated income before income taxes so income taxes are not reported or viewed internally on a segment basis. Identifiable assets by segment are those assets applicable to the respective industry segments. Corporate assets consist principally of cash and cash equivalents, short-term investments, long-term investments, IT infrastructure, and corporate office real estate and related equipment.

No geographic information for revenues from external customers or for long-lived assets is disclosed since the Corporation's primary market and capital investments are concentrated in the United States.

Edgar Filing: HNI CORP - Form 10-Q

Reportable segment data reconciled to the Corporation's condensed consolidated financial statements was as follows (in thousands):

	Three Months Ended		Nine Months Ended	
	September 30,	September 30,	September 29,	September 30,
	2018	2017	2018	2017
Net Sales:				
Office furniture	\$471,687	\$ 465,312	\$1,276,480	\$ 1,231,737
Hearth products	139,433	134,143	383,323	359,870
Total	\$611,120	\$ 599,455	\$1,659,803	\$ 1,591,607
Income Before Income Taxes:				
Office furniture	\$46,075	\$ 39,729	\$66,207	\$ 65,856
Hearth products	21,824	28,737	55,250	52,651
General corporate	(14,273 )	(10,747 )	(37,085 )	(31,205 )
Operating income	53,626	57,719	84,372	87,302
Interest expense, net	2,522	1,764	7,375	3,761
Total	\$51,104	\$ 55,955	\$76,997	\$ 83,541
Depreciation and Amortization Expense:				
Office furniture	\$11,012	\$ 12,132	\$33,202	\$ 37,515
Hearth products	2,026	1,973	6,080	8,167
General corporate	5,569	3,955	16,605	8,842
Total	\$18,607	\$ 18,060	\$55,887	\$ 54,524
Capital Expenditures (including capitalized software):				
Office furniture	\$10,324	\$ 27,102	\$35,321	\$ 64,467
Hearth products	2,150	5,606	6,317	12,818
General corporate	2,181	7,095	5,341	26,606
Total	\$14,655	\$ 39,803	\$46,979	\$ 103,891
Identifiable Assets:				
Office furniture			\$817,753	\$ 821,767
Hearth products			360,609	347,189
General corporate			217,384	222,594
Total			\$1,395,746	\$ 1,391,550



## Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

The following discussion of the Corporation's historical results of operations and of its liquidity and capital resources should be read in conjunction with the Unaudited Condensed Consolidated Financial Statements of the Corporation and related notes. Statements that are not historical are forward-looking and involve risks and uncertainties. See "Forward-Looking Statements" at the end of this section for further information.

### Overview

The Corporation has two reportable segments: office furniture and hearth products. The Corporation is a leading global office furniture manufacturer and the leading manufacturer and marketer of hearth products. The Corporation utilizes a split and focus with leverage, decentralized business model to deliver value to customers via various brands and selling models. The Corporation is focused on growing its existing businesses while seeking out and developing new opportunities for growth.

Net sales for the third quarter of 2018 were \$611.1 million, an increase of 1.9 percent, compared to net sales of \$599.5 million in the third quarter of 2017. The change was driven by an increase in both the office furniture and hearth products segments. The closure and divestitures of small office furniture companies resulted in a net decrease in sales of \$15.0 million compared to the third quarter of 2017.

Net income attributable to the Corporation in the third quarter of 2018 was \$39.9 million compared to net income of \$37.3 million in the third quarter of 2017. The increase was primarily driven by productivity gains, improved price realization, lower restructuring and transition costs, and a lower tax rate. These factors were partially offset by input cost inflation, lower volume in the contract office furniture business, higher incentive based compensation, and strategic investments. In the third quarter of 2017, the Corporation also recorded a \$6.0 million nonrecurring gain from the sale and license of an intangible asset and a \$0.8 million gain on the sale of a closed facility.

## Results of Operations

The following table presents certain key highlights from the results of operations (in thousands):

	Three Months Ended			Nine Months Ended		
	September 29, 2018	September 30, 2017	Change	September 29, 2018	September 30, 2017	Change
Net sales	\$611,120	\$599,455	1.9 %	\$1,659,803	\$1,591,607	4.3 %
Cost of sales	377,789	378,211	(0.1 %)	1,048,683	1,011,888	3.6 %
Gross profit	233,331	221,244	5.5 %	611,120	579,719	5.4 %
Selling and administrative expenses	179,577	169,547	5.9 %	524,445	495,897	5.8 %
Gain on sale and license of assets	—	(6,805 )	(100.0%)	—	(6,805 )	(100.0%)
Restructuring and impairment charges	128	783	(83.7 %)	2,303	3,325	(30.7 %)
Operating income	53,626	57,719	(7.1 %)	84,372	87,302	(3.4 %)
Interest expense, net	2,522	1,764	43.0 %	7,375	3,761	96.1 %
Income before income taxes	51,104	55,955	(8.7 %)	76,997	83,541	(7.8 %)
Income taxes	11,197	18,624	(39.9 %)	16,033	27,573	(41.9 %)
Net income (loss) attributable to non-controlling interest	—	60	(100.0%)	(50 )	12	(516.7%)
Net income attributable to HNI Corporation	\$39,907	\$37,271	7.1 %	\$61,014	\$55,956	9.0 %

## As a Percentage of Net Sales:

	2018	2017	Change	2018	2017	Change
Net sales	100.0 %	100.0 %		100.0 %	100.0 %	
Gross profit	38.2	36.9	130 bps	36.8	36.4	40 bps
Selling and administrative expenses	29.4	28.3	110 bps	31.6	31.2	40 bps
Gain on sale and license of assets	—	(1.1 )	110 bps	—	(0.4 )	40 bps
Restructuring and impairment charges	—	0.1	-10 bps	0.1	0.2	-10 bps
Operating income	8.8	9.6	-80 bps	5.1	5.5	-40 bps
Income taxes	1.8	3.1	-130 bps	1.0	1.7	-70 bps
Net income attributable to HNI Corporation	6.5	6.2	30 bps	3.7	3.5	20 bps

## Results of Operations - Three Months Ended

## Net Sales

Consolidated net sales for the third quarter of 2018 increased 1.9 percent or \$11.7 million compared to the same quarter last year. The change was driven by an increase in both the office furniture and hearth products segments. Office furniture segment sales increased in the supplies-driven business, but were partially offset by a decrease in the contract business and a decrease of \$15.0 million from the net impact of closing and divesting small office furniture companies. Hearth products segment sales increased in the new construction and retail businesses.

## Gross Profit

Gross profit as a percentage of net sales increased 130 basis points in the third quarter of 2018 compared to the same quarter last year primarily driven by productivity gains, improved price realization, and lower restructuring and

transition costs, partially offset by increased input costs and lower volume in the contract office furniture business.

26

---

Third quarter 2018 cost of sales included \$0.2 million of transition costs primarily related to the previously announced closure of the hearth manufacturing facility in Paris, Kentucky.

Third quarter 2017 cost of sales included \$1.6 million of restructuring costs and \$3.6 million of transition costs primarily related to the previously announced closures of the hearth manufacturing facilities in Paris, Kentucky and Colville, Washington and the office furniture manufacturing facility in Orleans, Indiana and structural realignments in China and between office furniture facilities in Muscatine, Iowa. Specific items incurred include accelerated depreciation and production move costs.

#### Selling and Administrative Expenses

Selling and administrative expenses as a percentage of net sales increased 110 basis points in the third quarter of 2018 compared to the same quarter last year primarily driven by higher incentive based compensation, strategic investments, amortization from the Business Systems Transformation investment, and the impact of the Corporation's stock price change on deferred compensation, partially offset by higher sales and the impact of closing and divesting small office furniture companies.

#### Restructuring Charges

Restructuring charges as a percentage of net sales decreased 10 basis points in the third quarter of 2018 compared to the same quarter last year primarily due to lower charges incurred in connection with previously announced closures.

In the third quarter of 2018, the Corporation recorded \$0.1 million of restructuring costs primarily associated with the previously announced closure of the hearth manufacturing facility in Paris, Kentucky.

In the third quarter of 2017, the Corporation recorded \$0.8 million of restructuring costs primarily associated with the previously announced closures of the hearth manufacturing facilities in Paris, Kentucky and Colville, Washington and the office furniture manufacturing facility in Orleans, Indiana. The Corporation also recorded a \$6.0 million nonrecurring gain from the sale and license of an intangible asset and a \$0.8 million gain on the sale of a closed facility in the third quarter of 2017.

#### Interest Expense

Interest expense for the third quarter of 2018 increased \$0.8 million compared to the same quarter last year. Higher average debt balances, higher variable interest rates, and incremental amortization of deferred debt issuance costs drove approximately \$0.5 million of the increase. During the third quarter of 2017, the Corporation capitalized approximately \$0.3 million of interest costs related to the Business Systems Transformation initiative. Capitalization of interest ceased during the third quarter of 2017, driving a relative increase in current year interest expense.

#### Income Taxes

The Corporation's tax provision for interim periods is determined using an estimate of its annual effective tax rate, adjusted for discrete items. The Corporation's income tax provision for the three months ended September 29, 2018 was an expense of \$11.2 million on pre-tax income of \$51.1 million, or an effective tax rate of 21.9 percent. The income tax provision reflects a lower rate in 2018 primarily due to the enactment of the Tax Cuts and Jobs Act in 2017 (the "Act"). For the three months ended September 30, 2017, the Corporation's income tax provision was an expense of \$18.6 million on pre-tax income of \$56.0 million, or an effective tax rate of 33.3 percent. Refer to "Note 9. Income Taxes" for further information.

Net Income Attributable to HNI Corporation

Net income attributable to the Corporation was \$39.9 million or \$0.89 per diluted share in the third quarter of 2018 compared to \$37.3 million or \$0.84 per diluted share in the third quarter of 2017.

Results of Operations - Nine Months Ended

Net Sales

For the first nine months of 2018, consolidated net sales increased 4.3 percent or \$68.2 million to \$1,659.8 million compared to \$1,591.6 million in the same period last year. The change was driven by an increase in both the office furniture and hearth products segments. Office furniture segment sales increased in the supplies-driven business, but were partially offset by a decrease in the contract business and a decrease of \$40.5 million from the net impact of closing and divesting small office furniture companies. Hearth products segment sales increased in the new construction and retail businesses.

## Gross Profit

Gross profit as a percentage of net sales increased 40 basis points in the first nine months of 2018 compared to the same period last year primarily driven by productivity gains, improved price realization, and lower restructuring and transition costs, partially offset by increased input costs and implementation costs from the Business Systems Transformation initiative.

During the first nine months of 2018, the Corporation recorded \$1.7 million of transition costs in cost of sales primarily related to structural realignment in China and the previously announced closure of the office furniture manufacturing facility in Orleans, Indiana. Specific items incurred include production move costs.

During the first nine months of 2017, the Corporation recorded \$8.7 million of restructuring costs and \$11.7 million of transition costs in cost of sales primarily related to the previously announced closures of the hearth manufacturing facilities in Paris, Kentucky and Colville, Washington and the office furniture manufacturing facility in Orleans, Indiana and structural realignments in China and between office furniture facilities in Muscatine, Iowa. Specific items incurred include severance, accelerated depreciation, and production move costs.

## Selling and Administrative Expenses

Selling and administrative expenses as a percentage of net sales increased 40 basis points in the first nine months of 2018 compared to the same period last year primarily driven by amortization and other impacts from the Business Systems Transformation initiative and strategic investments, partially offset by higher sales and the impact of closing and divesting small office furniture companies.

## Restructuring and Impairment Charges

Restructuring and impairment charges as a percentage of net sales decreased 10 basis points in the first nine months of 2018 compared to the same period last year primarily due to lower charges incurred in connection with previously announced closures.

During the first nine months of 2018, the Corporation recorded \$2.3 million of restructuring and impairment charges primarily associated with the previously announced closures of the office furniture manufacturing facility in Orleans, Indiana and the hearth manufacturing facility in Paris, Kentucky. These costs include an impairment charge from the sale of the closed manufacturing facility in Paris, Kentucky.

During the first nine months of 2017, the Corporation recorded \$3.3 million of restructuring costs primarily associated with the previously announced closures of the hearth manufacturing facilities in Paris, Kentucky and Colville, Washington and the office furniture manufacturing facility in Orleans, Indiana. The Corporation also recorded a \$6.0 million nonrecurring gain from the sale and license of an intangible asset and a \$0.8 million gain on the sale of a closed facility in the third quarter of 2017.

## Interest Expense

Interest expense for the first nine months of 2018 increased \$3.4 million compared to the first nine months of 2017. Higher average debt balances, higher variable interest rates, and incremental amortization of deferred debt issuance costs drove approximately \$1.9 million of the increase. During the first nine months of 2017, the Corporation capitalized approximately \$1.5 million of interest costs related to the Business Systems Transformation initiative. Capitalization of interest ceased during the third quarter of 2017, driving a relative increase in current year interest expense.

## Income Taxes

The Corporation's tax provision for interim periods is determined using an estimate of its annual effective tax rate, adjusted for discrete items. The Corporation's income tax provision for the nine months ended September 29, 2018 was an expense of \$16.0 million on pre-tax income of \$77.0 million, or an effective tax rate of 20.8 percent. The income tax provision reflects a lower rate in 2018 primarily due to the enactment of the Act and the impact of releasing a valuation allowance for certain foreign jurisdictions during the first quarter of 2018. For the nine months ended September 30, 2017, the Corporation's income tax provision was an expense of \$27.6 million on pre-tax income of \$83.5 million, or an effective tax rate of 33.0 percent. Refer to "Note 9. Income Taxes" for further information.

## Net Income Attributable to HNI Corporation

Net income attributable to the Corporation was \$61.0 million or \$1.38 per diluted share for the first nine months of 2018 compared to \$56.0 million or \$1.24 per diluted share for the first nine months of 2017.

## Office Furniture

The following table presents certain key highlights from the results of operations in the office furniture segment (in thousands):

	Three Months Ended			Nine Months Ended		
	September 29, 2018	September 30, 2017	Change	September 29, 2018	September 30, 2017	Change
Net sales	\$471,687	\$ 465,312	1.4 %	\$1,276,480	\$ 1,231,737	3.6 %
Operating profit	\$46,075	\$ 39,729	16.0 %	\$66,207	\$65,856	0.5 %
Operating profit %	9.8	% 8.5	% 130 bps	5.2	% 5.3	% -10 bps

## Three Months Ended

Third quarter 2018 net sales for the office furniture segment increased 1.4 percent or \$6.4 million compared to the same quarter last year. Sales increased in the supplies-driven business, but were partially offset by a decrease in the contract business and a decrease of \$15.0 million due to the net impact of closing and divesting small office furniture companies.

Operating profit as a percentage of net sales increased 130 basis points in the third quarter of 2018 compared to the same quarter last year primarily driven by productivity gains, improved price realization, lower restructuring and transition costs, and the impact of closing and divesting small office furniture companies, partially offset by increased input costs, lower volume in the contract business, strategic investments, and amortization from the Business Systems Transformation investment.

In the third quarter of 2018, the office furniture segment recorded a minimal amount of restructuring and transition costs primarily associated with structural realignment in China and the previously announced closure of the office furniture manufacturing facility in Orleans, Indiana.

In the third quarter of 2017, the office furniture segment recorded \$2.0 million of restructuring costs and \$2.8 million of transition costs primarily associated with the previously announced closure of the office furniture manufacturing facility in Orleans, Indiana and structural realignments in China and between office furniture facilities in Muscatine, Iowa. Specific items incurred include accelerated depreciation and production move costs. Of these charges, \$4.3 million was included in cost of sales.

## Nine Months Ended

Net sales for the first nine months of 2018 for the office furniture segment increased 3.6 percent or \$44.7 million compared to the same period last year. Sales increased in the supplies-driven business, but were partially offset by a decrease in the contract business and a decrease of \$40.5 million due to the net impact of closing and divesting small office furniture companies.

Operating profit as a percentage of net sales decreased 10 basis points in the first nine months of 2018 compared to the same period last year primarily driven by increased input costs, amortization and implementation costs from the Business Systems Transformation initiative, strategic investments, and unfavorable product and business mix, partially offset by improved price realization, lower restructuring and transition costs, productivity gains, cost management, and the impact of closing and divesting small office furniture companies.

During the first nine months of 2018, the office furniture segment recorded \$1.3 million of restructuring costs and \$1.2 million of transition costs primarily associated with the previously announced closure of the office furniture manufacturing facility in Orleans, Indiana and structural realignment in China. Specific items incurred include severance, production move costs, and final facility closing costs. Of these charges, \$1.2 million was included in cost



of sales.

During the first nine months of 2017, the office furniture segment recorded \$7.8 million of restructuring costs and \$9.0 million of transition costs primarily associated with the previously announced closure of the office furniture manufacturing facility in Orleans, Indiana and structural realignments in China and between office furniture facilities in Muscatine, Iowa. Specific items incurred include severance, accelerated depreciation, and production move costs. Of these charges, \$15.5 million was included in cost of sales.

29

---

## Hearth Products

The following table presents certain key highlights from the results of operations in the hearth products segment (in thousands):

	Three Months Ended			Nine Months Ended		
	September 29, 2018	September 30, 2017	Change	September 29, 2018	September 30, 2017	Change
Net sales	\$ 139,433	\$ 134,143	3.9 %	\$ 383,323	\$ 359,870	6.5 %
Operating profit	\$ 21,824	\$ 28,737	(24.1 %)	\$ 55,250	\$ 52,651	4.9 %
Operating profit %	15.7 %	21.4 %	-570 bps	14.4 %	14.6 %	-20 bps

## Three Months Ended

Third quarter 2018 net sales for the hearth products segment increased 3.9 percent or \$5.3 million compared to the same quarter last year. Sales increased in the new construction and retail businesses.

Operating profit as a percentage of net sales decreased 570 basis points in the third quarter of 2018 compared to the same quarter last year primarily driven by nonrecurring gains in the prior year quarter, increased input costs, higher incentive based compensation, and strategic investments, partially offset by productivity gains, higher sales volume, improved price realization, and lower restructuring and transition costs.

In the third quarter of 2018, the hearth products segment recorded \$0.1 million of restructuring costs and \$0.2 million of transition costs primarily associated with the previously announced closure of the hearth manufacturing facility in Paris, Kentucky. Specific items incurred include severance and final facility closing costs.

In the third quarter of 2017, the hearth products segment recorded \$0.3 million of restructuring costs and \$0.8 million of transition costs primarily associated with the previously announced closures of the hearth manufacturing facilities in Paris, Kentucky and Colville, Washington. Specific items incurred include accelerated depreciation and production move costs. Of these charges, \$0.8 million was included in cost of sales. The hearth products segment also recorded a \$6.0 million nonrecurring gain from the sale and license of an intangible asset and a \$0.8 million gain on the sale of a closed facility in the third quarter of 2017.

## Nine Months Ended

Net sales for the first nine months of 2018 for the hearth products segment increased 6.5 percent or \$23.5 million compared to the same period last year. Sales increased in the new construction and retail businesses.

Operating profit as a percentage of net sales decreased 20 basis points in the first nine months of 2018 compared to the same period last year primarily driven by increased input costs, nonrecurring gains in the prior year, higher incentive based compensation, and strategic investments, partially offset by higher sales volume, improved price realization, productivity gains, and lower restructuring and transition costs.

During the first nine months of 2018, the hearth products segment recorded \$1.0 million of restructuring and impairment charges and \$0.5 million of transition costs primarily associated with the previously announced closures of the hearth manufacturing facilities in Paris, Kentucky and Colville, Washington. Specific items incurred include an impairment charge from the sale of the closed manufacturing facility in Paris, Kentucky, production move costs, severance, and final facility closing costs. Of these charges, \$0.5 million was included in cost of sales.

During the first nine months of 2017, the hearth products segment recorded \$4.2 million of restructuring costs and \$2.6 million of transition costs primarily associated with the previously announced closures of the hearth manufacturing facilities in Paris, Kentucky and Colville, Washington. Specific items incurred include severance,

accelerated depreciation, and production move costs. Of these charges, \$4.9 million was included in cost of sales. The hearth products segment also recorded a \$6.0 million nonrecurring gain from the sale and license of an intangible asset and a \$0.8 million gain on the sale of a closed facility in the third quarter of 2017.

## Liquidity and Capital Resources

### Cash Flow – Operating Activities

Operating activities were a source of \$115.0 million of cash in the first nine months of 2018 compared to a source of \$57.3 million of cash in the first nine months of 2017. The higher cash generation compared to the prior year was primarily due to changes in working capital timing, driven by lower accounts receivable and higher accrued expenses.

### Cash Flow – Investing Activities

Capital expenditures, including capitalized software, for the first nine months of 2018 were \$47.0 million compared to \$103.9 million in the same period last year. These expenditures are primarily focused on machinery, equipment, and tooling required to support new products, continuous improvements, and cost savings initiatives in manufacturing processes. The decline compared to the prior year is primarily due to the completion of the Corporation's operational transformations and Business Systems Transformation integrated information system. For the full year 2018, capital expenditures are expected to be approximately \$65 to \$70 million.

**Real Estate Transaction** - In the first quarter of 2018, the Corporation entered into a sale-leaseback transaction, selling a manufacturing facility and subsequently leasing back a portion of the facility for a term of 10 years. The net proceeds from the sale of the facility of \$16.9 million are reflected in "Proceeds from sale and license of property, plant, equipment, and intangibles" in the Condensed Consolidated Statements of Cash Flows. In accordance with ASC 840, Leases, the gain on the sale of the facility is deferred and will be amortized as a reduction to rent expense evenly over the term of the lease. See "Note 3. Restructuring" in the Notes to Condensed Consolidated Financial Statements for further information.

### Cash Flow – Financing Activities

**Long-Term Debt** - The Corporation maintains a revolving credit facility as the primary source of committed funding from which the Corporation finances its planned capital expenditures, strategic initiatives, and seasonal working capital needs. Cash flows included in financing activities represent periodic borrowings and repayments under the revolving credit facility. During the second quarter of 2018, the Corporation issued \$100 million of private placement notes. The proceeds were used to repay outstanding borrowings under the revolving credit facility. See "Note 8. Long-Term Debt" in the Notes to Condensed Consolidated Financial Statements for further information.

**Dividend** - The Corporation is committed to maintaining or modestly growing the quarterly dividend. Cash dividends declared and paid per share were as follows (in dollars):

	Three Months Ended		Nine Months Ended	
	September 30,	September 30,	September 30,	September 30,
	2018	2017	2018	2017
Common shares	\$0.295	\$ 0.285	\$0.875	\$ 0.845

During the quarter, the Board declared the regular quarterly cash dividend on August 7, 2018. The dividend was paid on September 4, 2018 to shareholders of record on August 17, 2018. This was a 3.5 percent per share increase over the comparable prior year quarterly dividend paid on September 1, 2017.

**Stock Repurchase** - The Corporation's capital strategy related to stock repurchase is focused on offsetting the dilutive impact of issuances for various compensation related matters. The Corporation may elect to opportunistically purchase additional shares based on excess cash generation and/or share price considerations. During the nine months ended September 29, 2018, the Corporation repurchased 368,822 shares of its common stock at a cost of approximately \$14.9 million, or an average price of \$40.36 per share. During the nine months ended September 29, 2018, the Corporation also paid approximately \$1.4 million relating to shares repurchased but not yet settled as of December 30, 2017. As of September 29, 2018, there was a payable of \$0.2 million reflected in "Accounts payable and accrued

expenses" in the Condensed Consolidated Balance Sheets relating to shares repurchased but not yet settled. As of September 29, 2018, \$63.1 million of the Board's current repurchase authorization remained unspent.

Cash, cash equivalents, and short-term investments, coupled with cash flow from future operations, borrowing capacity under the existing credit agreement, and the ability to access capital markets, are expected to be adequate to fund operations and satisfy cash flow needs for at least the next twelve months.

#### Off-Balance Sheet Arrangements

The Corporation does not have any off-balance sheet arrangements that have or are reasonably likely to have a current or future material effect on the Corporation's financial condition, revenues or expenses, results of operations, liquidity, capital expenditures, or capital resources.

#### Contractual Obligations

Contractual obligations associated with ongoing business and financing activities will result in cash payments in future periods. A table summarizing the amounts and estimated timing of these future cash payments was provided in the Corporation's Annual Report on Form 10-K for the fiscal year ended December 30, 2017. There were no material changes outside the ordinary course of business in the Corporation's contractual obligations or the estimated timing of the future cash payments for the first nine months of 2018.

#### Commitments and Contingencies

See "Note 16. Guarantees, Commitments, and Contingencies" in the Notes to Condensed Consolidated Financial Statements for further information.

#### Critical Accounting Policies and Estimates

The preparation of the financial statements requires the Corporation to make estimates and judgments affecting the reported amount of assets, liabilities, revenues, and expenses, and related disclosure of contingent assets and liabilities. The Corporation continually evaluates its accounting policies and estimates. The Corporation bases its estimates on historical experience and on a variety of other assumptions believed by management to be reasonable in order to make judgments about the carrying value of assets and liabilities. Actual results may differ from these estimates under different assumptions or conditions. A summary of the more significant accounting policies requiring the use of estimates and judgments in preparing the financial statements is provided in the Corporation's Annual Report on Form 10-K for the fiscal year ended December 30, 2017.

During the third quarter of 2018, the Corporation determined a triggering event occurred for one of the Corporation's reporting units within the office furniture segment due to lower expectations of operating results for the year. The Corporation makes every effort to estimate future cash flows as accurately as possible with the information available at the time the forecast is developed. However, changes in estimates may affect the estimated fair value of the reporting unit, and could result in an impairment charge in future periods. Refer to "Note 6. Goodwill and Other Intangible Assets" for further information.

#### Recently Issued Accounting Standards Not Yet Adopted

In February 2016, the FASB issued ASU No. 2016-02, Leases. The new standard requires lessees to recognize most leases, including operating leases, on-balance sheet via a right of use asset and lease liability. Changes to the lessee accounting model may change key balance sheet measures and ratios, potentially affecting analyst expectations. The new standard becomes effective for the Corporation in fiscal 2019, but may be adopted at any time, and requires a modified-retrospective transition approach. The Corporation has completed a preliminary review of the impact of the new standard and expects right of use assets and lease liabilities to increase the assets and liabilities on the Consolidated Balance Sheets. The Corporation is also reviewing accounting policies and disclosures to determine changes needed to comply with this new standard, as well as identifying changes to the Corporation's business processes, systems, and controls needed to support adoption of this ASU. The Corporation has selected a technology tool to assist with the accounting and disclosure requirements of the new standard. The Corporation expects to adopt

the standard in fiscal 2019 using the modified-retrospective transition approach.

In June 2016, the FASB issued ASU No. 2016-13, Measurement of Credit Losses on Financial Instruments. The new standard replaces the incurred loss impairment methodology in current GAAP with a methodology that reflects expected credit losses by requiring consideration of a broader range of reasonable and supportable information and is intended to provide financial statement users with more useful information about expected credit losses on financial instruments. The new standard becomes effective for the Corporation in fiscal 2020 and requires a cumulative effect adjustment in retained earnings as of the beginning of the year of adoption. The Corporation is currently evaluating the effect the standard will have on consolidated financial statements and related disclosures.

In August 2017, the FASB issued ASU No. 2017-12, Targeted Improvements to Accounting for Hedging Activities. The new standard improves the financial reporting of hedging relationships to better portray the economic results of an entity's risk management activities in its financial statements and make certain targeted improvements to simplify the application of the hedge accounting guidance through changes to both the designation and measurement guidance for qualifying hedging relationships and the presentation of hedge results. The new standard becomes effective for the Corporation in fiscal 2019, with early adoption permitted. For cash flow and net investment hedges existing at the date of adoption, entities will apply the new guidance using a modified retrospective approach by recording a cumulative effect adjustment in retained earnings as of the beginning of the year of adoption. Presentation and disclosure requirements are applied prospectively. The Corporation is currently evaluating the effect the standard will have on consolidated financial statements and related disclosures.

In February 2018, the FASB issued ASU No. 2018-02, Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income. The new standard allows entities to reclassify certain stranded tax effects from accumulated other comprehensive income to retained earnings resulting from the Act. The standard also requires certain disclosures about stranded tax effects. The new standard becomes effective for the Corporation in fiscal 2019, with early adoption permitted. The standard should be applied either in the period of adoption or retrospectively to each period (or periods) in which the effect of the change in the U.S. federal corporate income tax rate in the Act is recognized. The Corporation is currently evaluating the effect the standard will have on consolidated financial statements and related disclosures.

#### Looking Ahead

Management remains optimistic about the long-term prospects in the office furniture and hearth products markets. Management believes the Corporation continues to compete well and remains confident the investments made in the business will continue to generate strong returns for shareholders.

#### Forward-Looking Statements

Statements in this report to the extent they are not statements of historical or present fact, including statements as to plans, outlook, objectives, and future financial performance, are "forward-looking" statements, within the meaning of Section 21 of the Securities Exchange Act of 1934, as amended, and the Private Securities Litigation Reform Act of 1995. Words such as "anticipate," "believe," "could," "confident," "estimate," "expect," "forecast," "hope," "intend," "likely," "may," "plan," "possible," "potential," "predict," "project," "should," "will," "would," and variations of such words and similar expressions identify forward-looking statements.

Forward-looking statements involve known and unknown risks and uncertainties, which may cause the Corporation's actual results in the future to differ materially from expected results. These risks and uncertainties include but are not limited to: the levels of office furniture needs and housing starts; overall demand for the Corporation's products; general economic and market conditions in the United States and internationally; industry and competitive conditions; the consolidation and concentration of the Corporation's customers; the Corporation's reliance on its network of independent dealers; changes in raw material, component, or commodity pricing; market acceptance and demand for the Corporation's new products; the Corporation's ability to successfully execute its business software system integration; the Corporation's ability to achieve desired results from closures and structural cost reduction initiatives; the Corporation's ability to achieve the anticipated benefits from integrating its acquired businesses and alliances; changing legal, regulatory, environmental, and healthcare conditions; the risks associated with international operations; the potential impact of product defects; the various restrictions on the Corporation's financing activities; an inability to protect the Corporation's intellectual property; the impact of recent tax legislation; force majeure events outside the Corporation's control; and other risks described in the Corporation's annual and quarterly reports filed with the Securities and Exchange Commission on Forms 10-K and 10-Q, as well as others the Corporation may consider



not material or does not anticipate at this time. The risks and uncertainties described in this report, as well as those described within Item 1A of the Corporation's Annual Report on Form 10-K for the fiscal year ended December 30, 2017, are not exclusive and further information concerning the Corporation's financial results or condition may emerge from time to time.

The Corporation cautions readers not to place undue reliance on any forward-looking statement, which speaks only as of the date made, and to recognize forward-looking statements are predictions of future results, which may not occur as anticipated. The Corporation assumes no obligation to update, amend, or clarify forward-looking statements, whether as a result of new information, future events, or otherwise, except as required by applicable law.

### Item 3. Quantitative and Qualitative Disclosures About Market Risk

As of September 29, 2018, there were no material changes to the financial market risks affecting the quantitative and qualitative disclosures presented in Item 7A of the Corporation's Annual Report on Form 10-K for the fiscal year ended December 30, 2017.

### Item 4. Controls and Procedures

#### Evaluation of Disclosure Controls and Procedures

Disclosure controls and procedures are designed to ensure information required to be disclosed by the Corporation in the reports it files or submits under the Securities Exchange Act of 1934 (the "Exchange Act") is recorded, processed, summarized, and reported within the time periods specified in the Securities and Exchange Commission's rules and forms. Disclosure controls and procedures are also designed to ensure information is accumulated and communicated to management, including the Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure.

Under the supervision and with the participation of the Chief Executive Officer and Chief Financial Officer of the Corporation, the Corporation's management carried out an evaluation of the Corporation's disclosure controls and procedures pursuant to Exchange Act Rules 13a – 15(e) and 15d – 15(e). As of September 29, 2018, based on this evaluation, the Chief Executive Officer and Chief Financial Officer have concluded these disclosure controls and procedures are effective.

#### Changes in Internal Controls

The Corporation has been engaged in a multi-year, broad-based program, which is referred to as business systems transformation ("BST"). The BST initiative includes the introduction of a new software system along with related process changes intended to simplify and streamline the Corporation's business processes. In the first quarter of 2018, the Corporation implemented BST in the majority of the domestic office furniture operations. The implementation resulted in business and operational changes in areas including order management, production scheduling, pricing, shipping, purchasing, and general accounting. These changes required some modifications to the Corporation's internal control over financial reporting during the first, second, and third quarters of 2018. Except for the BST implementation, there have been no changes in the Corporation's internal control over financial reporting during the fiscal quarter covered by this quarterly report on Form 10-Q that have materially affected, or are reasonably likely to materially affect, its internal control over financial reporting.

## PART II. OTHER INFORMATION

## Item 1. Legal Proceedings

For information regarding legal proceedings, see "Note 16. Guarantees, Commitments, and Contingencies" in the Notes to Condensed Consolidated Financial Statements, which information is incorporated herein by reference.

## Item 1A. Risk Factors

There have been no material changes from the risk factors disclosed in the "Risk Factors" section of the Corporation's Annual Report on Form 10-K for the fiscal year ended December 30, 2017.

## Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

## Issuer Purchases of Equity Securities:

The following is a summary of share repurchase activity during the quarter:

Period	Total Number of Shares (or Units) Purchased (1)	Average Price Paid per Share (or Unit)	Total Number of Shares (or Units) Purchased as Part of Publicly Announced Plans or Programs	Maximum Number (or Approximate Dollar Value) of Shares (or Units) that May Yet be Purchased Under the Plans or Programs
07/01/18 – 07/28/18	39,000	\$ 39.81	39,000	\$ 68,493,277
07/29/18 – 08/25/18	14,000	\$ 43.05	14,000	\$ 67,890,637
08/26/18 – 09/29/18	110,000	\$ 43.33	110,000	\$ 63,124,755
Total	163,000		163,000	

(1) No shares were purchased outside of a publicly announced plan or program.

The Corporation repurchases shares under previously announced plans authorized by the Board as follows:

Corporation's share purchase program ("Program") announced November 9, 2007, providing share repurchase authorization of \$200,000,000 with no specific expiration date, with an increase announced November 7, 2014, providing additional share repurchase authorization of \$200,000,000 with no specific expiration date.

No repurchase plans expired or were terminated during the third quarter of 2018, nor do any plans exist under which the Corporation does not intend to make further purchases. The Program does not obligate the Corporation to purchase any shares and the authorization for the Program may be terminated, increased, or decreased by the Board at any time.

Item 6. Exhibits

- (3.1) Second Amended and Restated By-laws of the Corporation (incorporated by reference to Exhibit 3.1 to the Registrant's Current Report on Form 8-K filed August 7, 2018)
- (31.1) Certification of the CEO Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002<sup>+</sup>
- (31.2) Certification of the CFO Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002<sup>+</sup>
- (32.1) Certification of CEO and CFO Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002<sup>+</sup>

The following materials from HNI Corporation's Quarterly Report on Form 10-Q for the fiscal quarter ended September 29, 2018 are formatted in XBRL (eXtensible Business Reporting Language) and filed electronically herewith: (i) Condensed Consolidated Statements of Comprehensive Income; (ii) Condensed Consolidated Balance Sheets; (iii) Consolidated Statements of Equity; (iv) Condensed Consolidated Statements of Cash Flows; and (v) Notes to Condensed Consolidated Financial Statements

<sup>+</sup> Filed or furnished herewith.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

HNI Corporation

Date: October 30, 2018 By: /s/ Marshall H. Bridges  
Marshall H. Bridges  
Senior Vice President and Chief Financial Officer