

JOHNSON & JOHNSON
Form 10-Q
November 10, 2010

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**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 October 3, 2010**
or

**Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
for the transition period from to
Commission file number 1-3215**
(Exact name of registrant as specified in its charter)

NEW JERSEY
(State or other jurisdiction of
incorporation or organization)

22-1024240
(I.R.S. Employer
Identification No.)

One Johnson & Johnson Plaza
New Brunswick, New Jersey 08933
(Address of principal executive offices)

Registrant's telephone number, including area code (732) 524-0400

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

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

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes No

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

On October 29, 2010 2,746,253,692 shares of Common Stock, \$1.00 par value, were outstanding.

JOHNSON & JOHNSON AND SUBSIDIARIES

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Part I FINANCIAL INFORMATION

Item 1 FINANCIAL STATEMENTS

JOHNSON & JOHNSON AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

(Unaudited; Dollars in Millions)

| | October 3, 2010 | January 3, 2010 |
|--|--------------------|--------------------|
| ASSETS | | |
| Current assets: | | |
| Cash and cash equivalents | \$ 14,338 | \$ 15,810 |
| Marketable securities | 7,788 | 3,615 |
| Accounts receivable, trade, less allowances for doubtful accounts \$360 (2009, \$333) | 10,290 | 9,646 |
| Inventories (Note 2) | 5,409 | 5,180 |
| Deferred taxes on income | 2,418 | 2,793 |
| Prepaid expenses and other receivables | 2,474 | 2,497 |
| Total current assets | 42,717 | 39,541 |
| Property, plant and equipment at cost | 29,927 | 29,251 |
| Less: accumulated depreciation | (15,567) | (14,492) |
| Property, plant and equipment, net | 14,360 | 14,759 |
| Intangible assets, net (Note 3) | 17,068 | 16,323 |
| Goodwill, net (Note 3) | 15,375 | 14,862 |
| Deferred taxes on income | 5,175 | 5,507 |
| Other assets | 3,552 | 3,690 |
| Total assets | \$ 98,247 | \$ 94,682 |

See Notes to Consolidated Financial Statements

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JOHNSON & JOHNSON AND SUBSIDIARIES
 CONSOLIDATED BALANCE SHEETS
 (Unaudited; Dollars in Millions)

| | October 3, 2010 | January 3, 2010 |
|---|--------------------|--------------------|
| LIABILITIES AND SHAREHOLDERS EQUITY | | |
| Current liabilities: | | |
| Loans and notes payable | \$ 2,843 | \$ 6,318 |
| Accounts payable | 5,477 | 5,541 |
| Accrued liabilities | 4,333 | 5,796 |
| Accrued rebates, returns and promotions | 2,666 | 2,028 |
| Accrued salaries, wages and commissions | 1,314 | 1,606 |
| Accrued taxes on income | 781 | 442 |
| Total current liabilities | 17,414 | 21,731 |
| Long-term debt | 9,182 | 8,223 |
| Deferred taxes on income | 1,725 | 1,424 |
| Employee related obligations | 6,409 | 6,769 |
| Other liabilities | 6,226 | 5,947 |
| Total liabilities | 40,956 | 44,094 |
| Shareholders' equity: | | |
| Common stock — par value \$1.00 per share (authorized 4,320,000,000 shares; issued 3,119,843,000 shares) | 3,120 | 3,120 |
| Accumulated other comprehensive income (Note 7) | (2,924) | (3,058) |
| Retained earnings | 77,272 | 70,306 |
| Less: common stock held in treasury, at cost (372,132,000 and 365,522,000 shares) | 20,177 | 19,780 |
| Total shareholders' equity | 57,291 | 50,588 |
| Total liabilities and shareholders' equity | \$ 98,247 | \$ 94,682 |

See Notes to Consolidated Financial Statements

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JOHNSON & JOHNSON AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF EARNINGS

(Unaudited; dollars & shares in millions

except per share amounts)

| | Oct. 3, 2010 | Fiscal Quarters Ended Percent to Sales | Sept. 27, 2009 | Percent to Sales |
|--|-----------------|--|-------------------|---------------------|
| Sales to customers (Note 9) | \$ 14,982 | 100.0% | \$ 15,081 | 100.0% |
| Cost of products sold | 4,594 | 30.7 | 4,434 | 29.4 |
| Gross profit | 10,388 | 69.3 | 10,647 | 70.6 |
| Selling, marketing and administrative expenses | 4,709 | 31.4 | 4,767 | 31.6 |
| Research expense | 1,657 | 11.1 | 1,617 | 10.7 |
| Interest income | (13) | (0.1) | (28) | (0.2) |
| Interest expense, net of portion capitalized | 108 | 0.7 | 142 | 0.9 |
| Other (income)expense, net | (292) | (2.0) | (96) | (0.6) |
| Earnings before provision for taxes on income | 4,219 | 28.2 | 4,245 | 28.2 |
| Provision for taxes on income (Note 5) | 802 | 5.4 | 900 | 6.0 |
| NET EARNINGS | \$ 3,417 | 22.8% | \$ 3,345 | 22.2% |
| NET EARNINGS PER SHARE (Note 8) | | | | |
| Basic | \$ 1.24 | | \$ 1.21 | |
| Diluted | \$ 1.23 | | \$ 1.20 | |
| CASH DIVIDENDS PER SHARE | \$ 0.54 | | \$ 0.49 | |
| AVG. SHARES OUTSTANDING | | | | |
| Basic | 2,751.6 | | 2,756.3 | |
| Diluted | 2,786.4 | | 2,793.0 | |

See Notes to Consolidated Financial Statements

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JOHNSON & JOHNSON AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF EARNINGS

(Unaudited; dollars & shares in millions
except per share amounts)

| | Oct. 3, 2010 | Fiscal Nine Months Ended Percent to Sales | Sept. 27, 2009 | Percent to Sales |
|--|-----------------|---|-------------------|---------------------|
| Sales to customers (Note 9) | \$ 45,943 | 100.0% | \$ 45,346 | 100.0% |
| Cost of products sold | 13,752 | 29.9 | 13,135 | 29.0 |
| Gross profit | 32,191 | 70.1 | 32,211 | 71.0 |
| Selling, marketing and administrative expenses | 14,244 | 31.0 | 14,172 | 31.3 |
| Research expense | 4,862 | 10.6 | 4,773 | 10.5 |
| Interest income | (83) | (0.2) | (78) | (0.2) |
| Interest expense, net of portion capitalized | 317 | 0.7 | 358 | 0.8 |
| Other (income)expense, net | (1,868) | (4.0) | (165) | (0.4) |
| Earnings before provision for taxes on income | 14,719 | 32.0 | 13,151 | 29.0 |
| Provision for taxes on income (Note 5) | 3,327 | 7.2 | 3,091 | 6.8 |
| NET EARNINGS | \$ 11,392 | 24.8% | \$ 10,060 | 22.2% |
| NET EARNINGS PER SHARE (Note 8) | | | | |
| Basic | \$ 4.14 | | \$ 3.64 | |
| Diluted | \$ 4.08 | | \$ 3.61 | |
| CASH DIVIDENDS PER SHARE | \$ 1.57 | | \$ 1.44 | |
| AVG. SHARES OUTSTANDING | | | | |
| Basic | 2,754.2 | | 2,760.0 | |
| Diluted | 2,792.0 | | 2,787.9 | |

See Notes to Consolidated Financial Statements

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JOHNSON & JOHNSON AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited; Dollars in Millions)

| | Fiscal Nine Months Ended | |
|--|--------------------------|-------------------|
| | Oct. 3, 2010 | Sept. 27, 2009 |
| CASH FLOW FROM OPERATING ACTIVITIES | | |
| Net earnings | \$ 11,392 | \$ 10,060 |
| Adjustments to reconcile net earnings to cash flows from operating activities: | | |
| Depreciation and amortization of property and intangibles | 2,170 | 2,030 |
| Stock based compensation | 474 | 499 |
| Decrease in deferred tax provision | 644 | 541 |
| Accounts receivable allowances | 30 | 39 |
| Changes in assets and liabilities, net of effects from acquisitions: | | |
| Increase in accounts receivable | (585) | (61) |
| Increase in inventories | (197) | (250) |
| Decrease in accounts payable and accrued liabilities | (1,552) | (1,830) |
| Increase in other current and non-current assets | (310) | (35) |
| Increase in other current and non-current liabilities | 495 | 291 |
| NET CASH FLOWS FROM OPERATING ACTIVITIES | 12,561 | 11,284 |
| CASH FLOWS FROM INVESTING ACTIVITIES | | |
| Additions to property, plant and equipment | (1,425) | (1,521) |
| Proceeds from the disposal of assets | 324 | 12 |
| Acquisitions, net of cash acquired | (1,269) | (2,337) |
| Purchases of investments | (10,679) | (5,922) |
| Sales of investments | 6,669 | 4,697 |
| Other | (70) | (163) |
| NET CASH USED BY INVESTING ACTIVITIES | (6,450) | (5,234) |
| CASH FLOWS FROM FINANCING ACTIVITIES | | |
| Dividends to shareholders | (4,323) | (3,974) |
| Repurchase of common stock | (1,512) | (1,172) |
| Proceeds from short-term debt | 1,896 | 3,903 |
| Retirement of short-term debt | (5,390) | (4,012) |
| Proceeds from long-term debt | 1,079 | 9 |
| Retirement of long-term debt | (21) | (224) |
| Proceeds from the exercise of stock options/excess tax benefits | 685 | 300 |
| NET CASH USED BY FINANCING ACTIVITIES | (7,586) | (5,170) |
| Effect of exchange rate changes on cash and cash equivalents | 3 | 208 |
| (Decrease)/Increase in cash and cash equivalents | (1,472) | 1,088 |
| Cash and Cash equivalents, beginning of period | 15,810 | 10,768 |
| CASH AND CASH EQUIVALENTS, END OF PERIOD | \$ 14,338 | \$ 11,856 |

| | | |
|---|----------|----------|
| Acquisitions | | |
| Fair value of assets acquired | \$ 1,321 | \$ 3,193 |
| Fair value of liabilities assumed and non-controlling interests | (52) | (856) |
| Net cash paid for acquisitions | \$ 1,269 | \$ 2,337 |

See Notes to Consolidated Financial Statements

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 The accompanying unaudited interim consolidated financial statements and related notes should be read in conjunction with the audited Consolidated Financial Statements of Johnson & Johnson and its Subsidiaries (the Company) and related notes as contained in the Company s Annual Report on Form 10-K for the fiscal year ended January 3, 2010. The unaudited interim financial statements include all adjustments (consisting only of normal recurring adjustments) and accruals necessary in the judgment of management for a fair statement of the results for the periods presented.

The Financial Accounting Standards Board (FASB) issued guidance and amendments to the criteria for separating consideration in multiple-deliverable revenue arrangements, which the Company adopted in the fiscal first quarter of 2010. The guidance also (a) provides principles and application guidance on whether multiple deliverables exist, how the arrangement should be separated, and the consideration allocated; (b) requires an entity to allocate revenue in an arrangement using estimated selling prices of deliverables if a vendor does not have vendor-specific objective evidence or third-party evidence of selling price; and(c) eliminates the use of the residual method and requires an entity to allocate the revenue using the relative selling price method. The adoption did not have a material impact on the Company s results of operations, cash flows or financial position however it will expand the disclosures for multiple-deliverable revenue arrangements.

During the fiscal first quarter of 2010 the Company adopted the FASB standard related to variable interest entities. The adoption of this standard did not have an impact on the Company s results of operations, cash flows or financial position.

During the fiscal first quarter of 2010 the Company adopted the new accounting guidance on fair value measurements and disclosures. This guidance requires the Company to disclose the amount of significant transfers between Level 1 and Level 2 inputs and the reasons for these transfers as well as the reasons for any transfers in or out of Level 3 of the fair value hierarchy. In addition, the guidance clarifies certain existing disclosure requirements. The adoption of this standard did not have a material impact on the Company s results of operations, cash flows or financial position.

During the fiscal second quarter of 2010 the FASB issued an accounting standard update related to revenue recognition under the milestone method. The objective of the accounting standard update is to provide guidance on defining a milestone and determining when it may be appropriate to apply the milestone

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method of revenue recognition for research or development transactions. This update is effective on a prospective basis for milestones achieved in fiscal years, and interim periods within those years, beginning on or after June 15, 2010. The adoption of this standard is not expected to have a material impact on the Company's results of operations, cash flows or financial position.

NOTE 2 INVENTORIES

| (Dollars in Millions) | October 3, 2010 | January 3, 2010 |
|----------------------------|--------------------|--------------------|
| Raw materials and supplies | \$ 1,123 | \$ 1,144 |
| Goods in process | 1,548 | 1,395 |
| Finished goods | 2,738 | 2,641 |
| Inventories | \$ 5,409 | \$ 5,180 |

NOTE 3 INTANGIBLE ASSETS AND GOODWILL

Intangible assets that have finite useful lives are amortized over their estimated useful lives. The latest impairment assessment of goodwill and indefinite lived intangible assets was completed in the fiscal fourth quarter of 2009.

Future impairment tests for goodwill and indefinite lived intangible assets will be performed annually in the fiscal fourth quarter, or sooner if warranted.

| (Dollars in Millions) | October 3, 2010 | January 3, 2010 |
|---|--------------------|--------------------|
| Intangible assets with definite lives: | | |
| Patents and trademarks - gross | \$ 6,729 | \$ 5,697 |
| Less accumulated amortization | 2,529 | 2,177 |
| Patents and trademarks - net | 4,200 | 3,520 |
| Other intangibles - gross | 7,748 | 7,808 |
| Less accumulated amortization | 2,810 | 2,680 |
| Other intangibles - net | 4,938 | 5,128 |
| Total intangible assets with definite lives - gross | 14,477 | 13,505 |
| Less accumulated amortization | 5,339 | 4,857 |
| Total intangible assets with definite lives - net | 9,138 | 8,648 |
| Intangible assets with indefinite lives: | | |
| Trademarks | 5,971 | 5,938 |
| Purchased in-process research and development* | 1,959 | 1,737 |
| Total intangible assets with indefinite lives | 7,930 | 7,675 |
| Total intangible assets - net | \$ 17,068 | \$ 16,323 |

* Purchased in-process research and development is accounted for as an indefinite-lived intangible asset until the underlying project is completed or abandoned.

Goodwill as of October 3, 2010 was allocated by segment of business as follows:

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| (Dollars in Millions) | Consumer | Pharm | Med Dev & Diag | Total |
|-------------------------------------|----------|---------|-------------------|----------|
| Goodwill, net at January 3, 2010 | \$8,074 | \$1,244 | \$5,544 | \$14,862 |
| Acquisitions | | | 400 | 400 |
| Currency translation/Other | 140 | (11) | (16) | 113 |
| Goodwill, net as of October 3, 2010 | \$8,214 | \$1,233 | \$5,928 | \$15,375 |

The weighted average amortization periods for patents and trademarks and other intangible assets are 17 years and 28 years, respectively. The amortization expense of amortizable intangible assets for the fiscal nine months ended October 3, 2010 was \$528 million, and the estimated amortization expense for the five succeeding years approximates \$700 million, per year.

NOTE 4 FAIR VALUE MEASUREMENTS

The Company uses forward exchange contracts to manage its exposure to the variability of cash flows, primarily related to the foreign exchange rate changes of future intercompany product and third-party purchases of raw materials denominated in foreign currency. The Company also uses cross currency interest rate swaps to manage currency risk primarily related to borrowings. Both types of derivatives are designated as cash flow hedges. The Company also uses forward exchange contracts to manage its exposure to the variability of cash flows for repatriation of foreign dividends. These contracts are designated as net investment hedges. Additionally, the Company uses forward exchange contracts to offset its exposure to certain foreign currency assets and liabilities. These forward exchange contracts are not designated as hedges and therefore, changes in the fair values of these derivatives are recognized in earnings, thereby offsetting the current earnings effect of the related foreign currency assets and liabilities. The Company does not enter into derivative financial instruments for trading or speculative purposes, or contain credit risk related contingent features or requirements to post collateral. On an ongoing basis the Company monitors counterparty credit ratings. The Company considers credit non-performance risk to be low, because the Company enters into agreements with commercial institutions that have at least an A (or equivalent) credit rating. As of October 3, 2010, the Company had notional amounts outstanding for forward foreign exchange contracts and cross currency interest rate swaps of \$23 billion and \$3 billion, respectively.

All derivative instruments are to be recorded on the balance sheet at fair value. Changes in the fair value of derivatives are recorded each period in current earnings or other comprehensive income, depending on whether the derivative is designated as part of a hedge transaction, and if so, the type of hedge transaction.

The designation as a cash flow hedge is made at the entrance date into the derivative contract. At inception, all derivatives are expected to be highly effective. Changes in the fair value of a derivative that is designated as a cash flow hedge and is highly

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effective are recorded in accumulated other comprehensive income until the underlying transaction affects earnings, and are then reclassified to earnings in the same account as the hedged transaction. Gains/losses on net investment hedges are accounted for through the currency translation account and are insignificant. On an ongoing basis, the Company assesses whether each derivative continues to be highly effective in offsetting changes in the cash flows of hedged items. If and when a derivative is no longer expected to be highly effective, hedge accounting is discontinued. Hedge ineffectiveness, if any, is included in current period earnings in other (income)/expense, net, and was not material for the fiscal quarters and fiscal nine months ended October 3, 2010 and September 27, 2009. Refer to Note 7 for disclosures of movements in Accumulated Other Comprehensive Income.

As of October 3, 2010, the balance of deferred net gains on derivatives included in accumulated other comprehensive income was \$51 million after-tax. For additional information, see Note 7. The Company expects that substantially all of the amounts related to foreign exchange contracts will be reclassified into earnings over the next 12 months as a result of transactions that are expected to occur over that period. The maximum length of time over which the Company is hedging transaction exposure is 18 months excluding interest rate swaps. The amount ultimately realized in earnings will differ as foreign exchange rates change. Realized gains and losses are ultimately determined by actual exchange rates at maturity of the derivative.

The following table is a summary of the activity related to designated derivatives for the fiscal third quarters in 2010 and 2009:*

| | Gain/(Loss) recognized in Accumulated OCI ⁽¹⁾ | | Gain/(Loss) reclassified from Accumulated OCI into income ⁽¹⁾ | | Gain/(Loss) recognized in other income/expense ⁽²⁾ | |
|---------------------------------------|---|------------------------------------|--|------------------------------------|--|------------------------------------|
| | Fiscal third quarter 2010 | Fiscal third quarter 2009 | Fiscal third quarter 2010 | Fiscal third quarter 2009 | Fiscal third quarter 2010 | Fiscal third quarter 2009 |
| (Dollars in Millions) | | | | | | |
| Cash Flow Hedges | | | | | | |
| Foreign exchange contracts | \$ 45 | \$ 27 | \$ (12) | \$ (6) _(A) | \$ 18 | \$ 2 |
| Foreign exchange contracts | (7) | (124) | (106) | 3 _(B) | 121 | (2) |
| Foreign exchange contracts | (46) | (23) | 20 | (C) | (11) | 1 |
| Cross currency interest rate swaps | | | | | | |