

Edgar Filing: H&E Equipment Services, Inc. - Form 10-Q

H&E Equipment Services, Inc.  
Form 10-Q  
October 25, 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 30, 2018

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: 000-51759

H&E Equipment Services, Inc.

(Exact Name of Registrant as Specified in Its Charter)

Delaware (State or Other Jurisdiction of Incorporation or Organization)	81-0553291 (I.R.S. Employer Identification No.)
7500 Pecue Lane, Baton Rouge, Louisiana (Address of Principal Executive Offices)	70809 (ZIP Code)

(225) 298 5200

(Registrant's Telephone Number, Including Area Code)

None

(Former Name, Former Address and Former Fiscal Year, if Changed Since Last Report)

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Sections 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 (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes 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,” “accelerated filer,” “smaller reporting company” and “emerging growth company” in Rule 12b-2 of the Exchange Act. (Check one):

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

As of October 18, 2018, there were 35,734,421 shares of H&E Equipment Services, Inc. common stock, \$0.01 par value, outstanding.

H&E EQUIPMENT SERVICES, INC. AND SUBSIDIARIES

TABLE OF CONTENTS

September 30, 2018

	Page
<u>PART I. FINANCIAL INFORMATION</u>	4
<u>Item 1. Financial Statements:</u>	4
<u>Condensed Consolidated Balance Sheets as of September 30, 2018 (Unaudited) and December 31, 2017</u>	4
<u>Condensed Consolidated Statements of Income (Unaudited) for the Three and Nine Months Ended September 30, 2018 and 2017</u>	5
<u>Condensed Consolidated Statements of Cash Flows (Unaudited) for the Nine Months Ended September 30, 2018 and 2017</u>	6
<u>Notes to Condensed Consolidated Financial Statements (Unaudited)</u>	8
<u>Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	33
<u>Item 3. Quantitative and Qualitative Disclosures About Market Risk</u>	48
<u>Item 4. Controls and Procedures</u>	48
<u>PART II. OTHER INFORMATION</u>	50
<u>Item 1. Legal Proceedings</u>	50
<u>Item 1A. Risk Factors</u>	50
<u>Item 2. Unregistered Sales of Equity Securities and Use of Proceeds</u>	50
<u>Item 3. Defaults upon Senior Securities</u>	50
<u>Item 4. Mine Safety Disclosures</u>	50
<u>Item 5. Other Information</u>	50
<u>Item 6. Exhibits</u>	51
<u>Signatures</u>	52

## Forward-Looking Statements

This Quarterly Report on Form 10-Q contains forward-looking statements within the meaning of the federal securities laws. Statements that are not historical facts, including statements about our beliefs and expectations, are forward-looking statements. Forward-looking statements include statements preceded by, followed by or that include the words “may”, “could”, “would”, “should”, “believe”, “expect”, “anticipate”, “plan”, “estimate”, “target”, “project”, “intend” or similar expressions. These statements include, among others, statements regarding our expected business outlook, anticipated financial and operating results, our business strategy and means to implement the strategy, our objectives, the amount and timing of capital expenditures, the likelihood of our success in expanding our business, financing plans, budgets, working capital needs and sources of liquidity. By their nature, forward-looking statements involve risks and uncertainties because they relate to events and depend on circumstances that may or may not occur in the future.

Forward-looking statements are only predictions and are not guarantees of performance. These statements are based on our management’s beliefs and assumptions, which in turn are based on currently available information. Important assumptions relating to the forward-looking statements include, among others, assumptions regarding demand for our products, the expansion of product offerings geographically or through new marketing applications, the timing and cost of planned capital expenditures, competitive conditions and general economic conditions. These assumptions could prove inaccurate. Forward-looking statements also involve known and unknown risks and uncertainties, which could cause actual results to differ materially from those contained in any forward-looking statement. In addition, even if our actual results are consistent with the forward-looking statements contained in this Quarterly Report on Form 10-Q, those results may not be indicative of results or developments in subsequent periods. Many of these factors are beyond our ability to control or predict. Such factors include, but are not limited to, the following:

- general economic conditions and construction and industrial activity in the markets where we operate in North America;
- our ability to forecast trends in our business accurately, and the impact of economic downturns and economic uncertainty on the markets we serve;
- the impact of conditions in the global credit and commodity markets and their effect on construction spending and the economy in general;
- relationships with equipment suppliers;
- increased maintenance and repair costs as we age our fleet and decreases in our equipment’s residual value;
- our indebtedness;
- risks associated with the expansion of our business and any potential acquisitions we may make, including any related capital expenditures, or our ability to consummate such acquisitions;
- our possible inability to integrate any businesses we acquire;
- competitive pressures;
- security breaches and other disruptions in our information technology systems;
- adverse weather events or natural disasters;
- compliance with laws and regulations, including those relating to environmental matters and corporate governance matters; and
- other factors discussed under “Risk Factors” in our Annual Report on Form 10-K for the year ended December 31, 2017.

Except as required by applicable law, including the securities laws of the United States and the rules and regulations of the Securities and Exchange Commission (“SEC”), we are under no obligation to publicly update or revise any forward-looking statements after we file this Quarterly Report on Form 10-Q, whether as a result of any new information, future events or otherwise. Investors, potential investors and other readers are urged to consider the above mentioned factors carefully in evaluating the forward looking statements and are cautioned not to place undue reliance on such forward looking statements. Although we believe that the expectations reflected in the

forward-looking statements are reasonable, we cannot guarantee future results or performance.

For a more detailed discussion of some of the foregoing risks and uncertainties, see Item 1A — “Risk Factors” in our Annual Report on Form 10-K for the year ended December 31, 2017, as well as other reports and registration statements filed by us with the SEC. These factors should not be construed as exhaustive and should be read with other cautionary statements in this Quarterly Report on Form 10-Q and our other public filings. All of our annual, quarterly and current reports, and any amendments thereto, filed with or furnished to the SEC are available on our Internet website under the Investor Relations link. For more information about us and the announcements we make from time to time, visit our Internet website at [www.he-equipment.com](http://www.he-equipment.com).

## PART I—FINANCIAL INFORMATION

## Item 1. Financial Statements.

## H&amp;E EQUIPMENT SERVICES, INC. AND SUBSIDIARIES

## CONDENSED CONSOLIDATED BALANCE SHEETS

(Amounts in thousands, except share amounts)

	Balances at	
	September 30,	December 31,
	2018	2017
	(Unaudited)	
<b>ASSETS</b>		
Cash	\$5,088	\$ 165,878
Receivables, net of allowance for doubtful accounts of \$3,692 and \$3,774, respectively	191,305	176,081
Inventories, net of reserves for obsolescence of \$377 and \$947, respectively	113,252	75,004
Prepaid expenses and other assets	9,368	9,172
Rental equipment, net of accumulated depreciation of \$562,647 and \$495,940, respectively	1,153,244	904,824
Property and equipment, net of accumulated depreciation and amortization of \$142,316 and \$131,500, respectively	113,403	101,789
Deferred financing costs, net of accumulated amortization of \$13,530 and \$12,946, respectively	3,188	3,772
Intangible assets, net	29,285	—
Goodwill	105,843	31,197
<b>Total assets</b>	<b>\$1,723,976</b>	<b>\$ 1,467,717</b>
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
<b>Liabilities:</b>		
Amounts due on senior secured credit facility	\$219,018	\$ —
Accounts payable	84,765	89,781
Manufacturer flooring plans payable	26,472	22,002
Accrued expenses payable and other liabilities	61,591	65,095
Dividends payable	104	150
Senior unsecured notes, net of unaccreted discount of \$3,287 and \$3,644 and deferred financing costs of \$2,129 and \$2,267, respectively	944,584	944,088
Capital leases payable	778	1,486
Deferred income taxes	144,288	126,419

Edgar Filing: H&E Equipment Services, Inc. - Form 10-Q

Deferred compensation payable	1,968	1,903
Total liabilities	1,483,568	1,250,924
Commitments and Contingencies		
Stockholders' equity:		
Preferred stock, \$0.01 par value, 25,000,000 shares authorized; no shares issued	—	—
Common stock, \$0.01 par value, 175,000,000 shares authorized; 39,749,549 and 39,623,773 shares issued at September 30, 2018 and December 31, 2017, respectively, and 35,735,432 and 35,646,585 shares outstanding at September 30, 2018 and December 31, 2017, respectively	396	395
Additional paid-in capital	229,958	227,070
Treasury stock at cost, 4,014,117 and 3,977,188 shares of common stock held at September 30, 2018 and December 31, 2017, respectively	(63,072 )	(61,749 )
Retained earnings	73,126	51,077
Total stockholders' equity	240,408	216,793
Total liabilities and stockholders' equity	\$1,723,976	\$ 1,467,717

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

## H&amp;E EQUIPMENT SERVICES, INC. AND SUBSIDIARIES

## CONDENSED CONSOLIDATED STATEMENTS OF INCOME

(Unaudited)

(Amounts in thousands, except per share amounts)

	Three Months Ended		Nine Months Ended	
	September 30, 2018	September 30, 2017	September 30, 2018	September 30, 2017
<b>Revenues:</b>				
Equipment rentals	\$ 156,037	\$ 125,616	\$ 429,227	\$ 351,303
New equipment sales	68,233	48,940	183,265	128,883
Used equipment sales	30,294	22,250	87,287	75,219
Parts sales	31,484	29,534	89,916	86,259
Services revenues	16,426	16,097	48,250	47,121
Other	19,667	16,725	55,042	46,568
<b>Total revenues</b>	<b>322,141</b>	<b>259,162</b>	<b>892,987</b>	<b>735,353</b>
<b>Cost of revenues:</b>				
Rental depreciation	55,060	43,255	152,700	125,996
Rental expense	22,936	19,988	66,281	58,524
New equipment sales	60,394	43,609	162,465	114,440
Used equipment sales	20,512	15,116	59,221	51,979
Parts sales	23,129	21,577	65,677	62,735
Services revenues	5,628	5,567	16,430	15,898
Other	19,752	16,024	54,795	46,743
<b>Total cost of revenues</b>	<b>207,411</b>	<b>165,136</b>	<b>577,569</b>	<b>476,315</b>
<b>Gross profit</b>	<b>114,730</b>	<b>94,026</b>	<b>315,418</b>	<b>259,038</b>
Selling, general and administrative expenses	70,346	55,203	205,272	172,328
Merger costs (net of merger breakup fee proceeds)	219	(6,506 )	439	(6,506 )
Gain on sales of property and equipment, net	1,153	2,325	6,040	4,431
<b>Income from operations</b>	<b>45,318</b>	<b>47,654</b>	<b>115,747</b>	<b>97,647</b>
<b>Other income (expense):</b>				
Interest expense	(16,715 )	(15,060 )	(47,061 )	(41,665 )
Loss on early extinguishment of debt	—	(25,363 )	—	(25,363 )
Other, net	368	346	1,222	1,156
<b>Total other expense, net</b>	<b>(16,347 )</b>	<b>(40,077 )</b>	<b>(45,839 )</b>	<b>(65,872 )</b>
<b>Income before provision (benefit) for income taxes</b>	<b>28,971</b>	<b>7,577</b>	<b>69,908</b>	<b>31,775</b>
Provision (benefit) for income taxes	7,657	(885 )	18,345	8,045
<b>Net income</b>	<b>\$ 21,314</b>	<b>\$ 8,462</b>	<b>\$ 51,563</b>	<b>\$ 23,730</b>
<b>Net income per common share:</b>				
Basic	\$ 0.60	\$ 0.24	\$ 1.45	\$ 0.67
Diluted	\$ 0.59	\$ 0.24	\$ 1.44	\$ 0.67
<b>Weighted average common shares outstanding:</b>				
Basic	35,719	35,543	35,649	35,494



Edgar Filing: H&E Equipment Services, Inc. - Form 10-Q

Diluted	35,926	35,715	35,904	35,656
Dividends declared per common share outstanding	\$0.275	\$0.275	\$0.825	\$0.825

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

## H&amp;E EQUIPMENT SERVICES, INC. AND SUBSIDIARIES

## CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

(Amounts in thousands)

	Nine Months Ended	
	September 30, 2018	2017
<b>Cash flows from operating activities:</b>		
Net income	\$51,563	\$23,730
<b>Adjustments to reconcile net income to net cash provided by operating activities:</b>		
Depreciation and amortization of property and equipment	18,367	18,092
Depreciation of rental equipment	152,700	125,996
Amortization of intangible assets	2,415	—
Amortization of deferred financing costs	819	785
Accretion of note discount, net of premium amortization	357	239
Provision for losses on accounts receivable	2,056	3,048
Provision for inventory obsolescence	74	151
Change in deferred income taxes	17,869	7,752
Stock-based compensation expense	2,998	2,614
Loss on early extinguishment of debt	—	25,363
Gain from sales of property and equipment, net	(6,040 )	(4,431 )
Gain from sales of rental equipment, net	(27,641 )	(22,196 )
<b>Changes in operating assets and liabilities, net of acquisitions:</b>		
Receivables	(6,825 )	(15,811 )
Inventories	(56,355 )	(38,930 )
Prepaid expenses and other assets	175	(1,606 )
Accounts payable	(10,081 )	42,122
Manufacturer flooring plans payable	4,470	(7,494 )
Accrued expenses payable and other liabilities	(8,961 )	(3,075 )
Deferred compensation payable	65	44
Net cash provided by operating activities	138,025	156,393
<b>Cash flows from investing activities:</b>		
Acquisition of businesses, net of cash acquired	(196,027 )	—
Purchases of property and equipment	(27,038 )	(16,002 )
Purchases of rental equipment	(350,646 )	(183,754 )
Proceeds from sales of property and equipment	7,958	6,765
Proceeds from sales of rental equipment	78,947	66,316
Net cash used in investing activities	(486,806 )	(126,675 )
<b>Cash flows from financing activities:</b>		
Purchases of treasury stock	(1,323 )	(753 )
Borrowings on senior secured credit facility	1,142,811	732,840
Payments on senior secured credit facility	(923,793 )	(818,285 )

Edgar Filing: H&E Equipment Services, Inc. - Form 10-Q

Dividends paid	(29,447 )	(29,369 )
Principal payments on senior unsecured notes due 2022	—	(630,000)
Costs paid to tender and redeem senior unsecured notes due 2022	—	(23,336 )
Proceeds from issuance of senior unsecured notes due 2025	—	750,000
Payments of deferred financing costs	(97 )	(12,152 )
Payments of capital lease obligations	(160 )	(162 )
Net cash provided by (used in) financing activities	187,991	(31,217 )
Net decrease in cash	(160,790 )	(1,499 )
Cash, beginning of period	165,878	7,683
Cash, end of period	\$5,088	\$6,184

H&E EQUIPMENT SERVICES, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (Continued)

(Unaudited)

(Amounts in thousands)

	Nine Months Ended September 30,	
	2018	2017
<b>Supplemental schedule of noncash investing and financing activities:</b>		
Accrued acquisition purchase price consideration	\$3,432	\$—
<b>Noncash asset purchases:</b>		
Assets transferred from new and used inventory to rental fleet	\$23,860	\$9,621
Purchases of property and equipment included in accrued expenses payable and other liabilities	\$(226 )	\$(127 )
<b>Supplemental disclosures of cash flow information:</b>		
<b>Cash paid during the period for:</b>		
Interest	\$59,475	\$50,931
Income taxes paid, net of refunds received	\$1,949	\$453

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

H&E EQUIPMENT SERVICES, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

(1) Organization and Nature of Operations

Basis of Presentation

Our condensed consolidated financial statements include the financial position and results of operations of H&E Equipment Services, Inc. and its wholly-owned subsidiaries H&E Finance Corp., GNE Investments, Inc., Great Northern Equipment, Inc., H&E California Holding, Inc., H&E Equipment Services (California), LLC and H&E Equipment Services (Mid-Atlantic), Inc., collectively referred to herein as “we” or “us” or “our” or the “Company.”

The accompanying unaudited interim condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted pursuant to such regulations. In the opinion of management, all adjustments (consisting of all normal and recurring adjustments) considered necessary for a fair presentation have been included. Operating results for the three and nine months ended September 30, 2018 are not necessarily indicative of the results that may be expected for the year ending December 31, 2018, and therefore, the results and trends in these interim condensed consolidated financial statements may not be the same for the entire year. These interim condensed consolidated financial statements should be read in conjunction with the annual audited consolidated financial statements and related notes in our Annual Report on Form 10-K for the year ended December 31, 2017, from which the consolidated balance sheet amounts as of December 31, 2017 were derived.

All significant intercompany accounts and transactions have been eliminated in these condensed consolidated financial statements. Business combinations accounted for as purchases are included in the condensed consolidated financial statements from their respective dates of acquisition.

The nature of our business is such that short-term obligations are typically met by cash flows generated from long-term assets. Consequently, and consistent with industry practice, the accompanying condensed consolidated balance sheets are presented on an unclassified basis.

Nature of Operations

As one of the largest integrated equipment services companies in the United States focused on heavy construction and industrial equipment, we rent, sell and provide parts and services support for four core categories of specialized equipment: (1) hi-lift or aerial work platform equipment; (2) cranes; (3) earthmoving equipment; and (4) industrial lift trucks. By providing equipment rental, sales, on-site parts, repair and maintenance functions under one roof, we are a one-stop provider for our customers' varied equipment needs. This full service approach provides us with multiple points of customer contact, enables us to maintain a high quality rental fleet, as well as an effective distribution channel for fleet disposal and provides cross selling opportunities among our new and used equipment sales, rental,

parts sales and services operations.

## (2) Significant Accounting Policies

We describe our significant accounting policies in note 2 of the notes to consolidated financial statements in our Annual Report on Form 10-K for the year ended December 31, 2017. During the three and nine month periods ended September 30, 2018, there were no significant changes to those accounting policies, other than those policies impacted by the new revenue recognition guidance, which is further described below in “Recent Accounting Pronouncements Adopted in Fiscal 2018”.

### Use of Estimates

We prepare our consolidated financial statements in accordance with accounting principles generally accepted in the United States of America, which requires management to use its judgment to make estimates and assumptions that affect the reported amounts of assets and liabilities and related disclosures at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reported period. These assumptions and estimates could have a material effect on our condensed consolidated financial statements. Actual results may differ materially from those estimates. We review our estimates on an ongoing basis based on information currently available, and changes in facts and circumstances may cause us to revise these estimates.

## Recent Accounting Pronouncements

### Pronouncements Not Yet Adopted

In February 2016, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) 2016-02, Leases (Topic 842) (“ASU 2016-02”). The new standard is intended to provide enhanced transparency and comparability by requiring lessees to record right-of-use assets and corresponding lease liabilities on the balance sheet, with the exception of leases with a term of 12 months or less, which permits a lessee to make an accounting policy election by class of underlying asset not to recognize lease assets and liabilities. At inception, lessees must classify leases as either finance or operating based on five criteria. Balance sheet recognition of finance and operating leases is similar, but the pattern of expense recognition in the income statement, as well as the effect on the classification of cash flows within the statement of cash flows, differs depending on the lease classification. Also, certain qualitative and quantitative disclosures are required to enable users of financial statements to assess the amount, timing and uncertainty of cash flows arising from leases. ASU 2016-02 is effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years, and early adoption is permitted.

We will adopt ASU 2016-02 as of January 1, 2019. Originally, Topic 842 required all entities to use a modified retrospective transition approach that is intended to maximize comparability and be less complex than a full retrospective approach. Under the modified retrospective approach, Topic 842 is effectively implemented as of the beginning of the earliest comparative period presented in an entity’s financial statements. ASU 2018-11 amends Topic 842 so that entities may elect not to recast their comparative periods in transition and allows entities to change their date of initial application to the beginning of the period of adoption. In doing so, the entity would (1) apply Topic 840 in the comparative periods; (2) provide the disclosures required by Topic 840 for all periods that continue to be presented in accordance with Topic 840; and (3) recognize the effects of applying Topic 842 as a cumulative-effect adjustment to retained earnings as of January 1, 2019. ASU 2018-11 also amends certain narrow-scope aspects of Topic 842.

Our operating leases under current guidance (Topic 840) include the real estate where all but 12 of our 89 branch locations are located as of September 30, 2018. Additionally, the Company leases various types of non-rental equipment. Given the size of our lease portfolio, we expect that the new standard will have a material effect on our consolidated balance sheets as a result of recognizing new right-of-use assets and lease liabilities for our existing operating leases. We have begun accumulating the information related to these leases but have not completed our comprehensive analysis of those leases and are unable to quantify the impact to our consolidated financial statements at this time. We are concurrently evaluating our internal processes and controls over financial reporting with respect to the impact that the new lease standard will have on our lease administration and financial reporting activities. We are also in the process of implementing a new software tool to help facilitate compliance with the new guidance.

As mentioned in the Topic 606 discussion below, our equipment rental business involves rental agreements with customers whereby we are the lessor in the transaction and therefore, we believe that such transactions are subject to the pending lessor accounting guidance of Topic 842. Topic 842, as originally issued, required lessors to separate lease and nonlease components in all circumstances. Under this requirement, once separate components are identified, lessors are required to use the relative stand-alone selling price allocation method in Topic 606 to allocate the consideration in the contract to the separated components. ASU 2018-11 also amends Topic 842 to include a practical expedient under which lessors are not required to separate lease and nonlease components. While our evaluation of Topic 842 is ongoing with respect to our equipment rental activities, we have tentatively concluded that no significant changes are expected to the accounting for our rental equipment revenues, as substantially all of our rental agreements with customers will continue to be treated as operating leases under the new standard. Accordingly, we do not expect

material changes to our related rental agreement accounting processes or internal controls upon adoption of Topic 842.

In June 2016, the FASB issued ASU 2016-13, “Financial Instruments - Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments” (“ASU 2016-13”). This standard adds to U.S. GAAP an impairment model (known as the current expected credit loss (“CECL”) model) that is based on expected losses rather than incurred losses. Under the new guidance, an entity recognizes as an allowance its estimate of expected credit losses, which is intended to result in the more timely recognition of losses. Under the CECL model, entities will estimate credit losses over the entire contractual term of the instrument (considering estimated prepayments, but not expected extensions or modifications) from the date of initial recognition of the financial instrument. Measurement of expected credit losses are to be based on relevant forecasts that affect collectability. The scope of financial assets within the CECL methodology is broad and includes trade receivables from revenue transactions and certain off-balance sheet credit exposures. Different components of the guidance require modified retrospective or prospective adoption. ASU 2016-13 will be effective for us as of January 1, 2020. While our review is ongoing, we believe ASU 2016-13 will only have applicability to our receivables from revenue transactions, or trade receivables. Under Topic 606, revenue is recognized when, among other criteria, it is probable that the entity will collect the consideration to which it is entitled for goods or services transferred to a customer. At the point that trade receivables are recorded, they become subject to the CECL model and estimates of expected credit losses on trade receivables over their contractual life will be required to be recorded at inception based on historical information, current conditions, and reasonable and supportable forecasts. While we believe that our current methodology for estimating the allowance for doubtful



accounts on our trade accounts receivables is reasonable, we have not concluded whether the application of the CECL model, when compared to our current methodology, will have a material impact to our allowance for doubtful accounts.

In January 2017, the FASB issued ASU No. 2017-04, Intangibles—Goodwill and Other (Topic 350): Simplifying the Test for Goodwill Impairment (“ASU 2017-04”), which removes Step 2 of the current goodwill impairment test, which was required if there was an indication that an impairment may exist, and the second step required calculating the potential impairment by comparing the implied fair value of the reporting unit’s goodwill with the carrying amount of the goodwill. Under the new guidance, an entity should perform its annual, or interim, goodwill impairment test by comparing the fair value of a reporting unit with its carrying amount, and then recognizing an impairment charge for the amount by which the reporting unit’s carrying value exceeds its fair value, not to exceed the carrying amount of the reporting unit’s goodwill. ASU 2017-04 is effective for annual reporting periods, and interim periods therein, beginning after December 15, 2019, with early adoption permitted and requires prospective adoption. Based upon our review of ASU 2017-04, we do not expect the guidance to have a material impact on our consolidated financial statements.

In August 2018, the FASB issued ASU No. 2018-15, Intangibles—Goodwill and Other – Internal-Use Software (Subtopic 350-40). This update aligns the requirements for capitalizing implementation costs incurred in a cloud computing arrangement that is a service contract with the requirements for capitalizing implementation costs incurred to develop or obtain internal-use software. This update will be effective for us in the first quarter of 2020. We do not expect the adoption of this guidance to have a material impact on our consolidated financial statements.

#### Recent Accounting Pronouncements Adopted in Fiscal 2018

In August 2016, the FASB issued ASU 2016-15, “Classification of Certain Cash Receipts and Cash Payments”, which aims to eliminate the diversity in the presentation of certain cash receipts and cash payments presented and classified in the statement of cash flows. The guidance addresses the following specific cash flow issues: (1) debt prepayment or debt extinguishment costs, (2) settlement of zero-coupon debt instruments or other debt instruments with coupon interest rates that are insignificant in relation to the effective interest rate of the borrowing, (3) contingent consideration payments made after a business combination, (4) proceeds from the settlement of insurance claims, (5) proceeds from settlement of corporate-owned life insurance policies, including bank-owned life insurance policies, (6) distributions received from equity method investees, (7) beneficial interests in securitization transitions and (8) separately identifiable cash flows and application of predominance principle. We adopted this guidance effective January 1, 2018 and it had no impact to our condensed consolidated statement of cash flows for the periods presented in this Quarterly Report on Form 10-Q.

In January 2017, the FASB issued ASU No. 2017-01, Business Combinations (Topic 805): Clarifying the Definition of a Business (“ASU 2017-01”). ASU 2017-01 clarifies the definition of a business when evaluating whether transactions should be accounted for as acquisitions (or disposals) of assets or businesses. The definition of a business affects several areas of accounting, including acquisitions, disposals, goodwill and consolidation. We adopted this guidance effective January 1, 2018 and it had no impact on our condensed consolidated financial statements for the periods presented in this Quarterly Report on Form 10-Q. The future impact of this guidance will depend on the nature of our future activities.

In May 2014, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) No. 2014-09, Revenue from Contracts with Customers (Topic 606). Under this ASU and subsequently issued amendments, revenue is recognized when control of the promised goods or services is transferred to our customers, in an amount that reflect the consideration we expect to be entitled to in exchange for those goods or services. Entities may use a full retrospective approach or report on the cumulative effect as of the date of adoption. We adopted this standard using the full retrospective transition method effective January 1, 2018.

While the adoption of the new standard did not have an impact on our reported net income for the periods presented in this quarterly report on Form 10-Q, approximately \$1.8 million and \$5.2 million of revenues that were previously classified in Other Revenues have been reclassified to Parts Revenues for the three and nine month periods ended September 30, 2018, respectively. These revenues relate to freight income associated with our parts transactions, and such income was not deemed to be a separate performance obligation under the new guidance. Accordingly, we also reclassified \$1.5 million and \$4.0 million of associated freight costs related to these parts transactions from Other Cost of Revenues to Parts Costs of Revenues for the three and nine months ended September 30, 2018, respectively. We have recast our results for the prior year three and nine month periods ended September 30, 2017 as shown in the tables below (amounts in thousands).

Three Months Ended September 30,  
2017

Statement of Income:	As		
	Previously	Adjustments	Current Presentation
Revenues:	Reported		
Equipment rentals	\$ 125,616	\$	\$ 125,616
New equipment sales	48,940		48,940
Used equipment sales	22,250		22,250
Parts sales	27,763	1,771	29,534
Services revenues	16,097		16,097
Other	18,496	(1,771)	16,725
Total revenues	259,162		259,162
Cost of revenues:			
Rental depreciation	43,255		43,255
Rental expense	19,988		19,988
New equipment sales	43,609		43,609
Used equipment sales	15,116		15,116
Parts sales	20,125	1,452	21,577
Services revenues	5,567		5,567
Other	17,476	(1,452)	16,024
Total cost of revenues	165,136		165,136
Gross profit	\$ 94,026	\$	\$ 94,026

## Nine Months Ended September 30, 2017

Statement of Income:	As		
	Previously	Adjustments	Current Presentation
Revenues:	Reported		
Equipment rentals	\$ 351,303	\$	\$ 351,303
New equipment sales	128,883		128,883
Used equipment sales	75,219		75,219
Parts sales	81,063	5,196	86,259
Services revenues	47,121		47,121
Other	51,764	(5,196)	46,568
Total revenues	735,353		735,353
Cost of revenues:			
Rental depreciation	125,996		125,996
Rental expense	58,524		58,524

Edgar Filing: H&E Equipment Services, Inc. - Form 10-Q

New equipment sales	114,440		114,440
Used equipment sales	51,979		51,979
Parts sales	58,696	4,039	62,735
Services revenues	15,898		15,898
Other	50,782	(4,039)	46,743
Total cost of revenues	476,315		476,315
	\$		
Gross profit	259,038	\$	\$ 259,038

Revenue Recognition

As further discussed below, upon the adoption of Topic 606 on January 1, 2018, we recognize revenue in accordance with two different accounting standards: 1) Topic 606 and 2) Topic 840 (which addresses lease accounting). As discussed above in “Pronouncements Not Yet Adopted”, Topic 842 will supersede Topic 840 upon our adoption of Topic 842 on January 1, 2019.

Under Topic 606, revenue from contracts with customers is measured based on the consideration specified in the contract with the customer, and excludes any sales incentives and amounts collected on behalf of third parties. A performance obligation is a promise in a contract to transfer a distinct good or service to a customer. We recognize revenue when we satisfy a performance obligation by transferring control over a product or service to a customer. The amount of revenue recognized reflects the consideration we expect to be entitled to in exchange for such products or services.

Nature of goods and services

The tables below summarize for the three and nine months ended September 30, 2018 our revenue by type and by the applicable accounting standard (amounts in thousands).

	Three Months Ended September 30, 2018			2017	
	Topic 840	Topic 606	Total \$	Topic 840 Topic 605	Total
Rental revenues	\$ 155,840	\$ 197	156,037	\$ 125,054	\$ 125,616
New equipment sales		68,233	68,233	48,940	48,940
Used equipment sales		30,294	30,294	22,250	22,250
Parts sales		31,484	31,484	27,763	27,763
Service revenues		16,426	16,426	16,097	16,097
Other	5,623	14,044	19,667	4,886	18,496
			\$		
Total revenues	\$ 161,463	\$160,678	322,141	\$ 198,791	\$ 259,162

Nine Months Ended September 30,

Edgar Filing: H&E Equipment Services, Inc. - Form 10-Q

	2018			2017		
	Topic 840	Topic 606	Total	Topic 840	Topic 605	Total
Rental revenues	\$ 428,115	\$ 1,112	\$ 429,227	\$ 349,704	\$ 1,599	\$ 351,303
New equipment sales		183,265	183,265		128,883	128,883
Used equipment sales		87,287	87,287		75,219	75,219
Parts sales		89,916	89,916		81,063	81,063
Service revenues		48,250	48,250		47,121	47,121
Other	15,565	39,477	55,042	12,951	38,813	51,764
Total revenues	\$ 443,680	\$ 449,307	\$ 892,987	\$ 362,655	\$ 372,698	\$ 735,353

---

12

Revenues by reporting segment are presented in note 10 of our condensed consolidated financial statements, using the revenue captions reflected in our condensed consolidated statements of income. We believe that the disaggregation of our revenues from contracts to customers as reflected above, coupled with further discussion below and the reporting segment in note 10, depicts how the nature, amount, timing and uncertainty of our revenues and cash flows are affected by economic factors.

#### Lease revenues (Topic 840)

As discussed above in “Pending Accounting Pronouncements Not Yet Adopted”, we expect to adopt Topic 842 on January 1, 2019. While our review of the revenue accounting under Topic 842 is ongoing, we have tentatively concluded that no significant changes are expected to our rental revenue accounting upon adoption of Topic 842.

**Rental Revenues:** Owned equipment rentals represent revenues from renting equipment. We account for these rentals as operating leases. We recognize revenue from equipment rentals in the period earned, regardless of the timing of billing to customers. A rental contract includes rates for daily, weekly or monthly use, and rental revenues are earned on a daily basis as rental contracts remain outstanding. Because the rental contracts can extend across multiple reporting periods, we record unbilled rental revenues and deferred rental revenues at the end of reporting periods so rental revenues earned is appropriately stated for the periods presented.

**Other:** Other rental revenues primarily represent services performed by us in connection with the rental of equipment to a customer, such as fuel consumption charges and damage waiver insurance. Fuel consumption charges are recognized upon return of the rental equipment when fuel consumption by the customer, if any, can be measured. Income from damage waiver insurance policies is recognized over the period the equipment is rented.

#### Revenues from contracts with customers (Topic 606)

The accounting for the types of revenues accounted for pursuant to Topic 606 are discussed below. Substantially all of our revenues under Topic 606 are recognized at a point-in-time rather than over time.

**Rental revenues:** These revenues represent revenues for services performed by us in connection with the rental of equipment and are comprised of customer training fees on rented equipment and erection and dismantling services on rental equipment. Revenues for these services are recognized upon completion of such services.

**New equipment sales:** Revenues from the sales of new equipment are recognized at the time of delivery to, or pick-up by, the customer, which is when the customer obtains control of the promised good.

**Used equipment sales:** Revenues from the sales of used equipment are recognized at the time of delivery to, or pick-up by, the customer, which is when the customer obtains control of the promised good.

**Parts sales:** Revenues from the sales of equipment parts are recognized at the time of pick-up by the customer for parts counter sales transactions. For parts that are shipped to a customer, we elected to use a practical expedient of Topic 606 and treat such shipping activities as fulfillment costs, thereby recognizing revenues at the time of shipment.

**Services revenues:** We derive our services primarily from maintenance and repair services to customers for their owned equipment. We recognize services revenues at the time such services are completed, which is when the customer obtains control of the promised service.

Other revenues: Other revenues relate primarily to hauling fees for transporting rental equipment to and from the customer and ancillary charges associated with maintenance and repair services. Such revenues are recognized at the time the services are completed.

#### Receivables and contract assets and liabilities

We manage credit risk associated with our accounts receivables at the customer level. Because the same customers typically generate the revenues that are accounted for under both Topic 606 and Topic 840, the discussions below on credit risk and our allowances for doubtful accounts address our total revenues from Topic 606 (Topic 605 for 2017) and Topic 840.

We believe concentration of credit risk with respect to our receivables is limited because our customer base is comprised of a large number of geographically diverse customers. Our largest customer accounted for less than one percent of total revenues for the three and nine months ended September 30, 2018, and for each of the last three full years. No single customer accounted for more than 10%

of our revenues on an overall or segment basis for any of the periods presented in this Quarterly Report on Form 10-Q. We manage credit risk through credit approvals, credit limits and other monitoring procedures.

We maintain an allowance for doubtful accounts that reflects our estimate of the amount of our receivables that we will be unable to collect. We develop our estimate of this allowance based on our historical experience with specific customers, our understanding of our current economic circumstances and our own judgment as to the likelihood of ultimate payment. Our largest exposure to doubtful accounts is in our rental operations. We perform credit evaluations of customers and establish credit limits based on reviews of our customers' current credit information and payment histories. We believe our credit risk is somewhat mitigated by our geographically diverse customer base and our credit evaluation procedures. During the year, we write-off customer account balances when we have exhausted reasonable collection efforts and determined that the likelihood of collection is remote. Such write-offs are charged against our allowance for doubtful accounts. Bad debt expense as a percentage of total revenues for the nine month periods ended September 30, 2018 and 2017 were approximately 0.3% and 0.4%, respectively. The actual rate of future credit losses, however, may not be similar to past experience. Our estimate of doubtful accounts could change based on changing circumstances, including changes in the economy or in the particular circumstances of individual customers. Accordingly, we may be required to increase or decrease our allowance for doubtful accounts.

We do not have material contract assets, impairment losses associated therewith, or material contract liabilities associated with contracts with customers. Our contracts with customers do not generally result in material amounts billed to customers in excess of recognizable revenue. We did not recognize material revenue during the three and nine months ended September 30, 2018 or 2017 that was included in the contract liability balance as of the beginning of such periods.

#### Performance obligations

Most of our Topic 606 revenue is recognized at a point-in-time, rather than over time. Accordingly, in any particular period, we do not generally recognize a significant amount of revenue from performance obligations satisfied (or partially satisfied) in previous periods, and the amount of such revenue recognized during the three and nine months ended September 30, 2018 and 2017 was not material. We also do not expect to recognize material revenue in the future related to performance obligations that are unsatisfied (or partially unsatisfied) as of September 30, 2018.

#### Payment terms

Our Topic 606 revenues do not include material amounts of variable consideration. Our payment terms vary by the type and location of our customer and the products or services offered. The time between invoicing and when payment is due is not significant. Our contracts do not generally include a significant financing component. Our contracts with customers do not generally result in significant obligations associated with returns, refunds or warranties. See above



for a discussion of how we manage credit risk.

Sales tax amounts collected from customers are recorded on a net basis.

#### Contract costs

We do not recognize any assets associated with the incremental costs of obtaining a contract with a customer (for example, a sales commission) that we expect to recover. Most of our revenue is recognized at a point-in-time or over a period of one year or less, and we use the practical expedient that allows us to recognize the incremental costs of obtaining a contract as an expense when incurred if the amortization period of the asset that we otherwise would have recognized is one year or less.

#### Contract estimates and judgments

Our revenues accounted for under Topic 606 generally do not require significant estimates or judgments as the transaction price is generally fixed and stated on our contracts. Our contracts generally do not include multiple performance obligations, and accordingly do not generally require estimates of the standalone selling price for each performance obligation. Also, our revenues do not include material amounts of variable consideration. Substantially all of our revenues are recognized at a point-in-time and the timing of the satisfaction of the applicable performance obligations is readily determinable. As noted above, our Topic 606 revenues are generally recognized at the time of delivery to, or pick-up by, the customer.

## (3) Acquisitions

## Contractors Equipment Center (“CEC”)

On January 1, 2018, we completed the acquisition of CEC, a non-residential construction focused equipment rental company with three branches located in the greater Denver, Colorado area. CEC had approximately 100 employees and approximately \$84 million of rental assets at original equipment cost as of December 31, 2017. CEC also had total revenues of approximately \$34 million in the year ended December 31, 2017. The acquisition significantly expands our presence in the Denver area and surrounding markets.

The aggregate consideration paid to the pre-acquisition owners of CEC was approximately \$132.4 million. The acquisition and related fees and expenses were funded through available cash. The following table summarizes the estimated fair values of the assets acquired and liabilities assumed as of the acquisition date. We do not expect any further changes to these assigned values.

	\$'s in thousands
Cash	\$ 1,244
Accounts receivable, net of allowance for doubtful accounts (1)	7,583
Inventory	504
Prepaid expenses and other assets	324
Rental equipment	55,342
Property and equipment	2,700
Intangible assets (2)	21,500
Total identifiable assets acquired	89,197
Accounts payable	(1,023)
Accrued expenses payable and other liabilities	(876)
Total liabilities assumed	(1,899)
Net identifiable assets acquired	87,298
Goodwill (3)	45,092
Net assets acquired	\$ 132,390

(1) The fair value of accounts receivable acquired was approximately \$7.6 million and the gross contractual amount was \$7.7 million.

(2) The following table reflects the estimated fair values and useful lives of the acquired intangible assets identified based on our purchase accounting assessments:

	Fair Value (amounts in thousands)	Life (years)
Customer relationships	\$ 21,000	10
Tradenames	300	1
Leasehold interests	200	10
	\$ 21,500	

(3) We have allocated the \$45.1 million goodwill among our six goodwill reporting units as follows (amounts in thousands):

Rental Component 1	\$25,233
Rental Component 2	18,391
New Equipment	217
Used Equipment	632
Parts	379
Service	240

The level of goodwill that resulted from the CEC acquisition is primarily reflective of CEC's going-concern value, the value of CEC's assembled workforce, new customer relationships expected to arise from the acquisition and expected synergies from combining operations. We currently expect the goodwill recognized to be 100% deductible for income tax purposes.

Total CEC acquisition costs were \$0.9 million, of which approximately \$0.2 million was incurred in the nine month period ended September 30, 2018.

Total revenues attributable to CEC since the acquisition were \$8.9 million and \$30.3 million for the three and nine month periods ended September 30 2018, respectively. Estimated net income attributable to CEC since the acquisition was \$1.2 million, or \$0.03 per share, for the three month period ended September 30, 2018 and \$3.9 million, or \$0.11 per share, for the nine month period ended September 30, 2018. It should be noted that since our acquisition of CEC, significant amounts of equipment rental fleet have been moved between H&E locations and the acquired CEC locations, the impact of which is included in these CEC operating results above, as it is impractical to report CEC operating results on a pure stand-alone basis post-acquisition.

Rental, LLC (dba "Rental Inc.")

On April 1, 2018, we completed the acquisition of Rental Inc., a non-residential equipment rental and distribution company with five branches located in Alabama, Florida and Western Georgia. Rental Inc. had approximately 65 employees and approximately \$35 million of rental assets at original equipment costs as of March 31, 2018, immediately prior to the acquisition. The acquisition expands our presence in the surrounding market.

The aggregate consideration paid to the owners of Rental Inc. was approximately \$68.6 million. The acquisition and related fees and expenses were funded through available cash and from borrowings under our Credit Facility (as defined below). The following table summarizes the estimated fair value of the assets acquired and liabilities assumed as of the acquisition date. The amounts presented here are preliminary and are subject to change. However, we do not expect material changes to these assigned values.

	\$'s in thousands
Cash	\$ 260
Accounts receivable, net of allowance for doubtful accounts (1)	2,873
Inventory	5,324
Prepaid expenses and other assets	47
Rental equipment	22,578
Property and equipment	1,935
Intangible assets (2)	10,200
Total identifiable assets acquired	43,217
Accounts payable	(439)

Edgar Filing: H&E Equipment Services, Inc. - Form 10-Q

Manufacturer flooring plans payable	(3,293)
Accrued expenses payable and other liabilities	(469)
Total liabilities assumed	(4,201)
Net identifiable assets acquired	39,016
Goodwill (3)	29,554
Net assets acquired	\$ 68,570

(1) The fair value of accounts receivables acquired was approximately \$2.9 million and the gross contractual amount was \$3.1 million.

(2) The following table reflects the estimated fair values and useful lives of the acquired intangible assets identified based on our purchase accounting assessments:

	Fair Value (amounts in thousands)	Life (years)
Customer relationships	\$ 10,000	10
Tradenames	200	1
	\$ 10,200	

(3) We have allocated the \$29.6 million goodwill among our six goodwill reporting units as follows (amounts in thousands):

16

---

Rental Component 1	\$9,064
Rental Component 2	5,445
New Equipment	10,217
Used Equipment	1,692
Parts	2,171
Service	964

The level of goodwill that resulted from the Rental Inc. acquisition is primarily reflective of Rental Inc.’s going-concern value, the value of Rental Inc.’s assembled workforce, new customer relationships expected to arise from the acquisition and expected synergies from combining operations. We currently expect the goodwill recognized to be 100% deductible for income tax purposes.

Total Rental Inc. acquisition costs were \$0.2 million, substantially all of which was incurred in the nine month period ended September 30, 2018.

Total revenues attributable to Rental Inc. since the April 1, 2018 acquisition were \$7.0 million and \$14.7 million for the three and nine month periods ended September 30 2018, respectively. Estimated net loss attributable to Rental Inc. since the acquisition was \$0.8 million, or \$0.02 per share, for the three month period ended September 30, 2018 and \$0.9 million, or \$0.02 per share, for the nine month period ended September 30, 2018. It should be noted that since our acquisition of Rental Inc., significant amounts of rental fleet have been moved between H&E locations and the acquired Rental Inc. locations, the impact of which is included in these Rental Inc. operating results above, as it is impractical to report Rental Inc. operating results on a pure stand-alone basis post-acquisition.

#### Pro forma financial information

We completed the CEC acquisition on January 1, 2018. Therefore, the operating results of CEC are included in our reported condensed consolidated statements of income for the full three and nine month periods ended September 30, 2018. We completed the Rental Inc. acquisition on April 1, 2018. Therefore, our reported condensed consolidated statements of income for the nine month period ended September 30, 2018 do not include Rental Inc. for the period January 1, 2018 through March 31, 2018.

The pro forma information below gives effect to the CEC and Rental Inc. acquisitions as if they had been completed on January 1, 2017 (the “pro forma acquisition date”). The pro forma information is not necessarily indicative of our results of operations had the acquisitions been completed on the above date, nor is it necessarily indicative of our

Edgar Filing: H&E Equipment Services, Inc. - Form 10-Q

future results. The pro forma information does not reflect any cost savings from operating efficiencies or synergies that could result from the acquisitions, nor does it reflect additional revenue opportunities following the acquisition. The pro forma adjustments reflected in the table below are subject to change as additional analysis is performed. The tables below present unaudited pro forma consolidated statements of income information for the three and nine month periods ended September 30, 2017 and the nine month period ended September 30, 2018 as if CEC and Rental Inc. were included in our consolidated results for the entire periods presented.

	(amounts in thousands, except per share data)			
	Three Month Period Ended September 30, 2017			
	H&E	CEC	Rental Inc.	Total
Total revenues	\$259,162	\$9,186	\$9,247	\$277,595
Pretax income	7,577	2,133	2,153	11,863
Pro forma adjustments to pretax income:				
Impact of fair value mark-ups/useful life changes on depreciation (1)	—	(823)	(713)	(1,536)
Intangible asset amortization (2)	—	(605)	(300)	(905)
Interest expense (3)	—	—	(451)	(451)
Elimination of historic interest expense (4)	—	425	90	515
Pro forma pretax income	7,577	1,130	779	9,486
Income tax benefit	(885)	(127)	(87)	(1,099)
Net income	\$ 8,462	\$1,257	\$ 866	\$10,585
Net income per share – basic	\$ 0.24	\$ 0.04	\$0.02	\$ 0.30
Net income per share - diluted	\$ 0.24	\$ 0.04	\$0.02	\$ 0.30

17

Edgar Filing: H&E Equipment Services, Inc. - Form 10-Q

	(amounts in thousands, except per share data)			
	Nine Month Period Ended September 30, 2017			
	H&E	CEC	Rental Inc.	Total
Total revenues	\$735,353	\$25,715	\$26,472	\$787,540
Pretax income	31,775	5,022	6,311	43,108
Pro forma adjustments to pretax income:				
Impact of fair value mark-ups/useful life changes on depreciation (1)	—	(2,535)	(2,094)	(4,629)
Intangible asset amortization (2)	—	(1,815)	(600)	(2,415)
Interest expense (3)	—	—	(1,226)	(1,226)
Elimination of historic interest expense (4)	—	1,225	292	1,517
Pro forma pretax income	31,775	1,897	2,683	36,355
Income tax expense	8,045	484	684	9,213
Net income	\$ 23,730	\$1,413	\$1,999	\$27,142
Net income per share – basic	\$ 0.67	\$0.04	\$0.06	\$ 0.76
Net income per share - diluted	\$ 0.67	\$0.04	\$0.06	\$ 0.76

	(amounts in thousands, except per share data)		
	Nine Month Period Ended September 30, 2018		
	H&E(5)	Rental Inc.(6)	Total
Total revenues	\$ 892,987	\$7,408	\$900,395
Pretax income	69,908	1,020	70,928
Pro forma adjustments to pretax income:			
Impact of fair value mark-ups/useful life changes on depreciation (1)		(749)	(749)
Intangible asset amortization (2)		(250)	(250)
Interest expense (3)		(480)	(480)
Elimination of historic interest expense (4)		82	82
Pro forma pretax income (loss)	69,908	(377)	69,531
Income tax expense (benefit)	18,345	(100)	18,245
Net income (loss)	\$ 51,563	\$ (277)	\$ 51,286
Net income (loss) per share – basic	\$ 1.45	\$(0.01)	\$ 1.44
Net income (loss) per share - diluted	\$ 1.44	\$(0.01)	\$ 1.43



- (1) Depreciation of rental equipment and non-rental equipment were adjusted for the fair value markups, and the changes in useful lives and salvage values of the equipment acquired in the acquisitions.
- (2) Represents the amortization of the intangible assets acquired in the acquisitions.
- (3) A portion of the consideration paid for Rental Inc. was funded with borrowings from our Credit Facility. Interest expense was adjusted to reflect the additional debt resulting from such acquisition.
- (4) Represents historic debt of CEC and Rental Inc. that is not part of the combined entity was eliminated.
- (5) H&E represents consolidated operating results as presented in this Quarterly Report on Form 10-Q for the nine month period ended September 30, 2018 and includes actual results for CEC for the nine months ended September 30, 2018 and actual results for Rental Inc. for the April 1, 2018 through September 30, 2018.
- (6) Represents Rental Inc. pro forma operating results for the three month period ended March 31, 2018. We completed the Rental Inc. acquisition on April 1, 2018.

## (4) Fair Value of Financial Instruments

Fair value is defined as the amount that would be received for selling an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The FASB fair value measurement guidance established a fair value hierarchy that prioritizes the inputs used to measure fair value. The three broad levels of the fair value hierarchy are as follows:

Level 1 – Quoted prices (unadjusted) in active markets for identical assets or liabilities

Level 2 – Quoted prices for similar assets and liabilities in active markets or inputs that are observable for the asset or liability, either directly or indirectly

Level 3 – Unobservable inputs for which little or no market data exists, therefore requiring a company to develop its own assumptions

The carrying value of financial instruments reported in the accompanying condensed consolidated balance sheets for cash, accounts receivable, accounts payable and accrued expenses payable and other liabilities approximate fair value due to the immediate or short-term nature or maturity of these financial instruments. The fair value of our letter of credit is based on fees currently charged for similar agreements. The carrying amounts and fair values of our other financial instruments subject to fair value disclosures as of September 30, 2018 and December 31, 2017 are presented in the table below (amounts in thousands) and have been calculated based upon market quotes and present value calculations based on market rates.

	September 30, 2018	
	Carrying Amount	Fair Value
Manufacturer flooring plans payable with interest computed		
at 4.50% (Level 3)	\$26,472	\$22,544
Senior unsecured notes with interest computed		
at 5.625% (Level 1)	950,000	947,625
Capital leases payable with interest computed		
at 5.929% (Level 3)	778	651
Letter of credit (Level 3)	—	116
	December 31, 2017	
	Carrying Amount	Fair Value

Edgar Filing: H&E Equipment Services, Inc. - Form 10-Q

Manufacturer flooring plans payable with interest computed		
at 4.50% (Level 3)	\$22,002	\$18,737
Senior unsecured notes with interest computed		
at 5.625% (Level 3)	944,088	619,019
Capital leases payable with interest computed		
at 5.929% to 9.55% (Level 3)	1,486	1,114
Letter of credit (Level 3)	—	116

At December 31, 2017, the fair value of our senior unsecured notes due 2025 was based on the present value of the notes based on our incremental borrowing rate as these notes were not available (registered) on a bond trading market as of December 31, 2017. At September 30, 2018, the fair value of our senior unsecured notes due 2025 were based on quoted bond trading market prices of those notes.

During the three and nine month periods ended September 30, 2018 and 2017, there were no transfers of financial assets or liabilities in or out of Level 1, Level 2 or Level 3 of the fair value hierarchy.

## (5) Stockholders' Equity

The following table summarizes the activity in Stockholders' Equity for the nine month period ended September 30, 2018 (amounts in thousands, except share data):

	Common Stock		Additional Paid-in Capital	Treasury Stock	Retained Earnings	Total Stockholders' Equity
	Shares Issued	Amount				
Balances at December 31, 2017	39,623,773	\$ 395	\$ 227,070	\$(61,749)	\$ 51,077	\$ 216,793
Stock-based compensation	—	—	2,998	—	—	2,998
Cash dividends declared on common stock (\$0.825 per share)	—	—	—	—	(29,514)	(29,514)
Issuance of common stock, net of forfeitures	125,776	1	(110)	—	—	(109)
Repurchase of 36,929 shares of restricted common stock	—	—	—	(1,323)	—	(1,323)
Net income	—	—	—	—	51,563	51,563
Balances at September 30, 2018	39,749,549	396	229,958	(63,072)	73,126	240,408

## (6) Stock-Based Compensation

We account for our stock-based compensation plans using the fair value recognition provisions of Accounting Standards Codification (“ASC”) 718, Stock Compensation (“ASC 718”). Under the provisions of ASC 718, stock-based compensation is measured at the grant date, based on the calculated fair value of the award, and is recognized as an expense over the requisite employee service period (generally the vesting period of the grant). Shares available for future stock-based payment awards under our 2016 Stock-Based Incentive Compensation Plan were 1,733,999 shares as of September 30, 2018.

## Non-vested Stock

The following table summarizes our non-vested stock activity for the nine months ended September 30, 2018:

	Number of Shares	Weighted Average Grant Date Fair Value
Non-vested stock at December 31, 2017	445,964	\$ 19.70
Granted	143,121	\$ 37.10
Vested	(178,212)	\$ 20.53

Edgar Filing: H&E Equipment Services, Inc. - Form 10-Q

Forfeited	(27,345 )	\$ 19.39
Non-vested stock at September 30, 2018	383,528	\$ 25.83

As of September 30, 2018, we had unrecognized compensation expense of approximately \$6.6 million related to non-vested stock that we expect to be recognized over a weighted-average period of approximately 2.2 years. The following table summarizes compensation expense related to non-vested stock, which is included in selling, general and administrative expenses in the accompanying condensed consolidated statements of income for the three and nine months ended September 30, 2018 and 2017 (amounts in thousands):

	For the Three Months Ended		For the Nine Months Ended	
	September 30, 2018	2017	September 30, 2018	2017
Compensation expense	\$ 917	\$ 720	\$2,998	\$2,614

(7) Income per Share

Income per common share for the three and nine months ended September 30, 2018 and 2017 are based on the weighted average number of common shares outstanding during the period. The effects of potentially dilutive securities that are anti-dilutive are not included in the computation of dilutive income per share. We include all common shares granted under our incentive compensation plan which remain unvested (“restricted common shares”) and contain non-forfeitable rights to dividends or dividend equivalents,

whether paid or unpaid (“participating securities”), in the number of shares outstanding in our basic and diluted EPS calculations using the two-class method. All of our restricted common shares are currently participating securities.

Under the two-class method, earnings per common share are computed by dividing the sum of distributed earnings allocated to common shareholders and undistributed earnings allocated to common shareholders by the weighted average number of common shares outstanding for the period. In applying the two-class method, distributed and undistributed earnings are allocated to both common shares and restricted common shares based on the total weighted average shares outstanding during the period. The number of restricted common shares outstanding was approximately 0.7% of total outstanding shares for each of the three months ended September 30, 2018 and 2017, and, consequently, was immaterial to the basic and diluted EPS calculations. Therefore, use of the two-class method had no impact on our basic and diluted EPS calculations for the periods presented. The following table sets forth the computation of basic and diluted net income per common share for the three and nine months ended September 30, 2018 and 2017 (amounts in thousands, except per share amounts):

	Three Months Ended September 30, 2018		Nine Months Ended September 30, 2017	
<b>Basic net income per share:</b>				
Net income	\$21,314	\$8,462	\$51,563	\$23,730
Weighted average number of common				
shares outstanding	35,719	35,543	35,649	35,494
Net income per share of common stock – basic	\$0.60	\$0.24	\$1.45	\$0.67
<b>Diluted net income per share:</b>				
Net income	\$21,314	\$8,462	\$51,563	\$23,730
Weighted average number of common shares outstanding	35,719	35,543	35,649	35,494
Effect of dilutive securities:				
Effect of dilutive non-vested restricted stock	207	172	255	162
Weighted average number of common shares				
outstanding – diluted	35,926	35,715	35,904	35,656
Net income per share of common stock – diluted	\$0.59	\$0.24	\$1.44	\$0.67
Common shares excluded from the denominator				
as anti-dilutive:				
Non-vested restricted stock	21	—	7	—

#### (8) Senior Secured Credit Facility

We and our subsidiaries are parties to a \$750.0 million Credit Facility with Wells Fargo Capital Finance, LLC as administrative agent, and the lenders named therein (the “Credit Facility”).

On December 22, 2017, we amended, extended and restated the Credit Facility by entering into the Fifth Amended and Restated Credit Agreement (the “Amended and Restated Credit Agreement”) by and among the Company, Great Northern Equipment, Inc., H&E Equipment Services (California), LLC, the other credit parties named therein, the lenders named therein, Wells Fargo Capital Finance, LLC, as administrative agent, the other credit parties named therein, the lenders named therein, and the joint lead arrangers, joint book runners, co-syndication agents and documentation agent named therein.

The Amended and Restated Credit Agreement, among other things, (i) extends the maturity date of the Credit Facility from May 21, 2019 to December 22, 2022, (ii) increases the commitments under the senior secured asset based revolver provided for therein from \$602.5 million to \$750 million, (iii) increases the uncommitted incremental revolving capacity from \$150 million to \$250 million, (iv) provides that the unused line fee margin will be either 0.375% or 0.25%, depending on the Average Revolver Usage (as defined in the Amended and Restated Credit Agreement) of the borrowers, (v) lowers the interest rate (a) in the case of base rate revolving loans, to the base rate plus an applicable margin of 0.50% to 1.00% depending on the Average Availability (as defined in the Amended and Restated Credit Agreement) and (b) in the case of LIBOR revolving loans, to LIBOR (as defined in the Amended and Restated Credit Agreement) plus an applicable margin of 1.50% to 2.00%, depending on the Average Availability, (vi) lowers the

margin applicable to the letter of credit fee to between 1.50% and 2.00%, depending on the Average Availability, and (vii) permits, subject to certain conditions, an unlimited amount of Permitted Acquisitions, Restricted Payments and prepayments of Indebtedness (in each case, as defined in the Amended and Restated Credit Agreement).

The Amended and Restated Credit Agreement continues to provide for, among other things, a \$30 million letter of credit sub-facility, and a guaranty by certain of the Company's subsidiaries of the obligations under the Credit Facility. In addition, the Credit Facility remains secured by substantially all of the assets of the Company and certain of its subsidiaries.

As of September 30, 2018, we were in compliance with our financial covenants under the Amended and Restated Credit Agreement. At September 30, 2018, we had \$219.0 million of borrowings outstanding under the Credit Facility and could borrow up to \$523.3 million and remain in compliance with the debt covenants under the Credit Facility. At October 18, 2018, we had \$532.4 million of available borrowings under our Credit Facility, net of a \$7.7 million outstanding letter of credit.

#### (9) Senior Unsecured Notes

On August 24, 2017, we completed an offering of \$750 million aggregate principal amount of 5.6250% senior notes due 2025 (the "New Notes") and the settlement of a cash tender offer (the "Tender Offer") with respect to our 7% senior notes due 2022 (the "Old Notes"). Net proceeds, after deducting \$10.3 million of estimated offering expenses, from the sale of the New Notes totaled approximately \$739.7 million. We used a portion of the net proceeds from the sale of the New Notes to repurchase \$329.7 million of aggregate principal amount of the Old Notes in early settlement of the Tender Offer, which the Company launched on August 17, 2017. Holders who tendered their Old Notes prior to the early tender deadline received \$1,038.90 per \$1,000 principal amount of Old Notes tendered, plus accrued and unpaid interest up to, but not including, the payment date of August 24, 2017. Effective as of August 24, 2017, we (i) provided notice of the redemption of all remaining Old Notes that were not validly tendered in the Tender Offer at the expiration time and (ii) satisfied and discharged the indenture governing the Old Notes in accordance with its terms. On September 25, 2017, we redeemed the remaining \$300.3 million principal amount outstanding of the Old Notes at a redemption price equal to 103.50% of the principal amount thereof, plus accrued and unpaid interest up to, but not including, the date of redemption.

The New Notes were issued at par and require semiannual interest payments on March 1st and September 1st of each year, commencing on March 1, 2018. No principal payments are due until maturity (September 1, 2025).

The New Notes are redeemable, in whole or in part, at any time on or after September 1, 2020 at specified redemption prices plus accrued and unpaid interest to the date of redemption. We may redeem up to 40% of the aggregate principal amount of the New Notes before September 1, 2020 with the net cash proceeds from certain equity offerings. We may also redeem the New Notes prior to September 1, 2020 at a specified "make-whole" redemption price plus accrued and unpaid interest to the date of redemption.

The New Notes rank equally in right of payment to all of our existing and future senior indebtedness and rank senior to any of our subordinated indebtedness. The New Notes are unconditionally guaranteed on a senior unsecured basis by all of our current and future significant domestic restricted subsidiaries. In addition, the New Notes are effectively subordinated to all of our and the guarantors' existing and future secured indebtedness, including the Credit Facility, to the extent of the assets securing such indebtedness, and are structurally subordinated to all of the liabilities and



preferred stock of any of our subsidiaries that do not guarantee the New Notes.

If we experience a change of control, we will be required to offer to purchase the New Notes at a repurchase price equal to 101% of the principal amount, plus accrued and unpaid interest to the date of repurchase.

The indenture governing the New Notes contains certain covenants that, among other things, limit our ability and the ability of our restricted subsidiaries to: (i) incur additional indebtedness, assume a guarantee or issue preferred stock; (ii) pay dividends or make other equity distributions or payments to or affecting our subsidiaries; (iii) purchase or redeem our capital stock; (iv) make certain investments; (v) create liens; (vi) sell or dispose of assets or engage in mergers or consolidations; (vii) engage in certain transactions with subsidiaries or affiliates; (viii) enter into sale-leaseback transactions; and (ix) engage in certain business activities. Each of the covenants is subject to exceptions and qualifications. As of September 30, 2018, we were in compliance with these covenants.

On November 22, 2017, we closed on an offering of \$200 million aggregate principal amount of 5.625% senior notes due 2025 (the "Add-on Notes") in an unregistered offering through a private placement. The Add-on Notes were priced at 104.25% of the principal amount. Net proceeds from the offering of the Add-on Notes, including accrued interest from August 24, 2017 totaled approximately \$209.2 million. The net proceeds of the offering, was used to repay indebtedness outstanding under the Credit Facility and for the payment of fees and expenses related to the offering. The remainder of the net proceeds will be used for general corporate purposes

and to fund potential acquisitions in connection with our ongoing strategy of acquiring rental companies to complement our existing business and footprint.

The Add-on Notes were issued as additional notes under an indenture dated as of August 24, 2017, pursuant to which we previously issued the New Notes as described above. The Add-on Notes have identical terms to, rank equally with and form a part of a single class of securities with the New Notes.

Pursuant to a registration rights agreement entered into between us, the guarantors of the New Notes and the initial purchasers of the New Notes, we agreed to make an offer to exchange (the "Exchange Offer") the New Notes and guarantees for registered, publicly tradable notes and guarantees that have terms identical in all material respects to the New Notes (except that the exchange notes will not contain any transfer restrictions) within a certain period of time following the completion of the offering. On January 17, 2018, the Company filed a registration statement on Form S-4 with respect to an offer to exchange the New and Add-on Notes and guarantees for registered, publicly tradable notes and guarantees that have terms identical in all material respects to the New and Add-on Notes (except that the exchange notes do not contain any transfer restrictions). This exchange offer closed on March 27, 2018.

The following table reconciles our Senior Unsecured Notes to our Condensed Consolidated Balance Sheets (amounts in thousands):

Balance at December 31, 2016	\$627,711
Accretion of discount on Old Notes through	
August 24, 2017	683
Amortization of note premium on Old Notes through	
August 24, 2017	(574 )
Amortization of deferred financing costs on Old Notes	
through August 24, 2017	153
Aggregate principal amount paid on Old Notes	(630,000)
Writeoff of unaccreted discount on Old Notes	5,294
Writeoff of unamortized premium on Old Notes	(4,452 )
Writeoff of deferred financing costs on Old Notes	1,185
Aggregate principal amount issued on New Notes	950,000
Note discount and deferred transaction costs on	
New Notes	(14,684 )
Note premium on New Notes	8,500
Accretion of discount on New Notes from	
August 24, 2017 through December 31, 2017	542
Amortization of note premium on New Notes from	
August 24, 2017 through December 31, 2017	(375 )
Amortization of deferred financing costs on New Notes	
August 24, 2017 through December 31, 2017	105

Edgar Filing: H&E Equipment Services, Inc. - Form 10-Q

Balance at December 31, 2017	\$944,088
Accretion of discount through September 30, 2018	1,154
Amortization of note premium through September 30, 2018	(797 )
Additional deferred financing costs on New Notes	(97 )
Amortization of deferred financing costs through	
September 30, 2018	236
Balance at September 30, 2018	\$944,584

(10) Segment Information

We have identified five reportable segments: equipment rentals, new equipment sales, used equipment sales, parts sales and services revenues. These segments are based upon how management of the Company allocates resources and assesses performance. Non-segmented revenues and non-segmented costs relate to equipment support activities including transportation, hauling, parts freight and damage-waiver charges and are not allocated to the other reportable segments. There were no sales between segments for any of the periods presented. Selling, general and administrative expenses as well as all other income and expense items below gross profit are not generally allocated to reportable segments.

Edgar Filing: H&E Equipment Services, Inc. - Form 10-Q

We do not compile discrete financial information by segments other than the information presented below. The following table presents information about our reportable segments (amounts in thousands):

	Three Months Ended		Nine Months Ended	
	September 30, 2018	September 30, 2017	September 30, 2018	September 30, 2017
<b>Segment Revenues:</b>				
Equipment rentals	\$156,037	\$125,616	\$429,227	\$351,303
New equipment sales	68,233	48,940	183,265	128,883
Used equipment sales	30,294	22,250	87,287	75,219
Parts sales	31,484	29,534	89,916	86,259
Services revenues	16,426	16,097	48,250	47,121
<b>Total segmented revenues</b>	<b>302,474</b>	<b>242,437</b>	<b>837,945</b>	<b>688,785</b>
Non-segmented revenues	19,667	16,725	55,042	46,568
<b>Total revenues</b>	<b>\$322,141</b>	<b>\$259,162</b>	<b>\$892,987</b>	<b>\$735,353</b>
<b>Segment Gross Profit:</b>				
Equipment rentals	\$78,041	\$62,373	\$210,246	\$166,783
New equipment sales	7,839	5,331	20,800	14,443
Used equipment sales	9,782	7,134	28,066	23,240
Parts sales	8,355	7,957	24,239	23,524
Services revenues	10,798	10,530	31,820	31,223
<b>Total segmented gross profit</b>	<b>114,815</b>	<b>93,325</b>	<b>315,171</b>	<b>259,213</b>
Non-segmented gross profit (loss)	(85 )	701	247	(175 )
<b>Total gross profit</b>	<b>\$114,730</b>	<b>\$94,026</b>	<b>\$315,418</b>	<b>\$259,038</b>

	Balances at	
	September 30, 2018	December 31, 2017
<b>Segment identified assets:</b>		
Equipment sales	\$93,860	\$58,125
Equipment rentals	1,153,244	904,824
Parts and services	19,392	16,879
<b>Total segment identified assets</b>	<b>1,266,496</b>	<b>979,828</b>
Non-segment identified assets	457,480	487,889
<b>Total assets</b>	<b>\$1,723,976</b>	<b>\$1,467,717</b>

The Company operates primarily in the United States and our sales to international customers for the three month periods ended September 30, 2018 and 2017 were 0.1% and 0.1%, respectively, of total revenues. Our sales to international customers for the nine month periods ended September 30, 2018 and 2017 were 0.2% and 0.3%, respectively. No one customer accounted for more than 10% of our revenues on an overall or segment basis for any of the periods presented.

(11) Condensed Consolidating Financial Information of Guarantor Subsidiaries

All of the indebtedness of H&E Equipment Services, Inc. is guaranteed by GNE Investments, Inc. and its wholly owned subsidiary Great Northern Equipment, Inc., H&E Equipment Services (California), LLC, H&E California Holding, Inc., H&E Equipment Services (Mid-Atlantic), Inc. and H&E Finance Corp. The guarantor subsidiaries are all wholly owned and the guarantees, made on a joint and several basis, are full and unconditional (subject to subordination provisions and subject to a standard limitation which provides that the maximum amount guaranteed by each guarantor will not exceed the maximum amount that can be guaranteed without making the guarantee void under fraudulent conveyance laws). There are no restrictions on H&E Equipment Services, Inc.'s ability to obtain funds from the guarantor subsidiaries by dividend or loan.

The consolidating financial statements of H&E Equipment Services, Inc. and its subsidiaries are included below. The financial statements for H&E Finance Corp. are not included within the consolidating financial statements because H&E Finance Corp. has no assets or operations.

## CONDENSED CONSOLIDATING BALANCE SHEET

	As of September 30, 2018			
	H&E Equipment Guarantor			
	Services	Subsidiaries	Elimination	Consolidated
	(Amounts in thousands)			
<b>Assets:</b>				
Cash	\$5,088	\$ —	\$ —	\$ 5,088
Receivables, net	152,395	38,910	—	191,305
Inventories, net	97,099	16,153	—	113,252
Prepaid expenses and other assets	9,228	140	—	9,368
Rental equipment, net	989,228	164,016	—	1,153,244
Property and equipment, net	96,063	17,340	—	113,403
Deferred financing costs, net	3,188	—	—	3,188
Investment in guarantor subsidiaries	259,298	—	(259,298 )	—
Intangible assets, net	29,285	—	—	29,285
Goodwill	76,317	29,526	—	105,843
<b>Total assets</b>	<b>\$1,717,189</b>	<b>\$ 266,085</b>	<b>\$ (259,298 )</b>	<b>\$ 1,723,976</b>
<b>Liabilities and Stockholders' Equity:</b>				
Amounts due on senior secured credit facility	\$219,018	\$ —	\$ —	\$ 219,018
Accounts payable	77,385	7,380	—	84,765
Manufacturer flooring plans payable	25,833	639	—	26,472
Accrued expenses payable and other liabilities	63,550	(1,959 )	—	61,591
Dividends payable	155	(51 )	—	104
Senior unsecured notes	944,584	—	—	944,584
Capital leases payable	—	778	—	778
Deferred income taxes	144,288	—	—	144,288
Deferred compensation payable	1,968	—	—	1,968
<b>Total liabilities</b>	<b>1,476,781</b>	<b>6,787</b>	<b>—</b>	<b>1,483,568</b>
Stockholders' equity	240,408	259,298	(259,298 )	240,408
<b>Total liabilities and stockholders' equity</b>	<b>\$1,717,189</b>	<b>\$ 266,085</b>	<b>\$ (259,298 )</b>	<b>\$ 1,723,976</b>

## CONDENSED CONSOLIDATING BALANCE SHEET

	As of December 31, 2017			
	H&E Equipment Services, Inc. Guarantor			
	Services	Subsidiaries	Elimination	Consolidated
	(Amounts in thousands)			
<b>Assets:</b>				
Cash	\$165,878	\$—	\$—	\$165,878
Receivables, net	138,657	37,424	—	176,081
Inventories, net	63,828	11,176	—	75,004
Prepaid expenses and other assets	9,030	142	—	9,172
Rental equipment, net	760,972	143,852	—	904,824
Property and equipment, net	89,952	11,837	—	101,789
Deferred financing costs, net	3,772	—	—	3,772
Investment in guarantor subsidiaries	222,217	—	(222,217 )	—
Goodwill	1,671	29,526	—	31,197
<b>Total assets</b>	<b>\$1,455,977</b>	<b>\$233,957</b>	<b>\$(222,217 )</b>	<b>\$1,467,717</b>
<b>Liabilities and Stockholders' Equity:</b>				
Accounts payable	78,811	10,970	—	89,781
Manufacturer flooring plans payable	20,300	1,702	—	22,002
Accrued expenses payable and other liabilities	67,466	(2,371 )	—	65,095
Dividends payable	197	(47 )	—	150
Senior unsecured notes	944,088	—	—	944,088
Capital leases payable	—	1,486	—	1,486
Deferred income taxes	126,419	—	—	126,419
Deferred compensation payable	1,903	—	—	1,903
<b>Total liabilities</b>	<b>1,239,184</b>	<b>11,740</b>	<b>—</b>	<b>1,250,924</b>
Stockholders' equity	216,793	222,217	(222,217 )	216,793
<b>Total liabilities and stockholders' equity</b>	<b>\$1,455,977</b>	<b>\$233,957</b>	<b>\$(222,217 )</b>	<b>\$1,467,717</b>

## CONDENSED CONSOLIDATING STATEMENT OF INCOME

Three Months Ended September 30, 2018

H&amp;E Equipment Guarantor

	Services	Subsidiaries	Elimination	Consolidated
	(Amounts in thousands)			
<b>Revenues:</b>				
Equipment rentals	\$ 133,023	\$ 23,014	\$ —	\$ 156,037
New equipment sales	48,861	19,372	—	68,233
Used equipment sales	23,868	6,426	—	30,294
Parts sales	27,054	4,430	—	31,484
Services revenues	14,048	2,378	—	16,426
Other	16,494	3,173	—	19,667
<b>Total revenues</b>	<b>263,348</b>	<b>58,793</b>	<b>—</b>	<b>322,141</b>
<b>Cost of revenues:</b>				
Rental depreciation	47,142	7,918	—	55,060
Rental expense	19,527	3,409	—	22,936
New equipment sales	43,187	17,207	—	60,394
Used equipment sales	15,692	4,820	—	20,512
Parts sales	20,029	3,100	—	23,129
Services revenues	4,883	745	—	5,628
Other	16,570	3,182	—	19,752
<b>Total cost of revenues</b>	<b>167,030</b>	<b>40,381</b>	<b>—</b>	<b>207,411</b>
<b>Gross profit (loss):</b>				
Equipment rentals	66,354	11,687	—	78,041
New equipment sales	5,674	2,165	—	7,839
Used equipment sales	8,176	1,606	—	9,782
Parts sales	7,025	1,330	—	8,355
Services revenues	9,165	1,633	—	10,798
Other	(76 )	(9 )	—	(85 )
<b>Gross profit</b>	<b>96,318</b>	<b>18,412</b>	<b>—</b>	<b>114,730</b>
Selling, general and administrative expenses	58,938	11,408	—	70,346
Merger costs (net of merger breakup fee proceeds)	219	—	—	219
Equity in earnings of guarantor subsidiaries	4,535	—	(4,535 )	—
Gain on sales of property and equipment, net	1,017	136	—	1,153
<b>Income from operations</b>	<b>42,713</b>	<b>7,140</b>	<b>(4,535 )</b>	<b>45,318</b>
<b>Other income (expense):</b>				
Interest expense	(14,073 )	(2,642 )	—	(16,715 )
Other, net	331	37	—	368
<b>Total other expense, net</b>	<b>(13,742 )</b>	<b>(2,605 )</b>	<b>—</b>	<b>(16,347 )</b>
<b>Income before income taxes</b>	<b>28,971</b>	<b>4,535</b>	<b>(4,535 )</b>	<b>28,971</b>
Income tax expense	7,657	—	—	7,657
<b>Net income</b>	<b>\$ 21,314</b>	<b>\$ 4,535</b>	<b>\$ (4,535 )</b>	<b>\$ 21,314</b>





## CONDENSED CONSOLIDATING STATEMENT OF INCOME

Three Months Ended September 30, 2017

H&amp;E Equipment Guarantor

	Services	Subsidiaries	Elimination	Consolidated
	(Amounts in thousands)			
<b>Revenues:</b>				
Equipment rentals	\$ 103,618	\$ 21,998	\$ —	\$ 125,616
New equipment sales	38,132	10,808	—	48,940
Used equipment sales	17,818	4,432	—	22,250
Parts sales	25,356	4,178	—	29,534
Services revenues	13,559	2,538	—	16,097
Other	13,625	3,100	—	16,725
Total revenues	212,108	47,054	—	259,162
<b>Cost of revenues:</b>				
Rental depreciation	35,886	7,369	—	43,255
Rental expense	16,630	3,358	—	19,988
New equipment sales	33,933	9,676	—	43,609
Used equipment sales	12,288	2,828	—	15,116
Parts sales	18,648	2,929	—	21,577
Services revenues	4,775	792	—	5,567
Other	13,229	2,795	—	16,024
Total cost of revenues	135,389	29,747	—	165,136
<b>Gross profit:</b>				
Equipment rentals	51,102	11,271	—	62,373
New equipment sales	4,199	1,132	—	5,331
Used equipment sales	5,530	1,604	—	7,134
Parts sales	6,708	1,249	—	7,957
Services revenues	8,784	1,746	—	10,530
Other	396	305	—	701
Gross profit	76,719	17,307	—	94,026
Selling, general and administrative expenses	44,408	10,795	—	55,203
Equity in earnings of guarantor subsidiaries	6,160	—	(6,160 )	—
Merger costs (net of merger breakup fee proceeds)	(6,506 )	—	—	(6,506 )
Gain on sales of property and equipment, net	342	1,983	—	2,325
Income from operations	45,319	8,495	(6,160 )	47,654
<b>Other income (expense):</b>				
Interest expense	(12,665 )	(2,395 )	—	(15,060 )
Loss on early extinguishment of debt	(25,363 )	—	—	(25,363 )
Other, net	286	60	—	346
Total other expense, net	(37,742 )	(2,335 )	—	(40,077 )
Income before income taxes	7,577	6,160	(6,160 )	7,577
Income tax benefit	(885 )	—	—	(885 )
Net income	\$ 8,462	\$ 6,160	\$ (6,160 )	\$ 8,462



## CONDENSED CONSOLIDATING STATEMENT OF INCOME

Nine Months Ended September 30, 2018

H&amp;E Equipment Guarantor

	Services	Subsidiaries	Elimination	Consolidated
	(Amounts in thousands)			
<b>Revenues:</b>				
Equipment rentals	\$367,314	\$ 61,913	\$ —	\$ 429,227
New equipment sales	144,462	38,803	—	183,265
Used equipment sales	70,256	17,031	—	87,287
Parts sales	77,488	12,428	—	89,916
Services revenues	40,808	7,442	—	48,250
Other	46,214	8,828	—	55,042
Total revenues	746,542	146,445	—	892,987
<b>Cost of revenues:</b>				
Rental depreciation	130,650	22,050	—	152,700
Rental expense	56,653	9,628	—	66,281
New equipment sales	127,982	34,483	—	162,465
Used equipment sales	47,084	12,137	—	59,221
Parts sales	56,972	8,705	—	65,677
Services revenues	14,000	2,430	—	16,430
Other	45,815	8,980	—	54,795
Total cost of revenues	479,156	98,413	—	577,569
<b>Gross profit (loss):</b>				
Equipment rentals	180,011	30,235	—	210,246
New equipment sales	16,480	4,320	—	20,800
Used equipment sales	23,172	4,894	—	28,066
Parts sales	20,516	3,723	—	24,239
Services revenues	26,808	5,012	—	31,820
Other	399	(152 )	—	247
Gross profit	267,386	48,032	—	315,418
Selling, general and administrative expenses	171,683	33,589	—	205,272
Merger costs (net of merger breakup fee proceeds)	439	—	—	439
Equity in earnings of guarantor subsidiaries	7,482	—	(7,482 )	—
Gain on sales of property and equipment, net	5,754	286	—	6,040
Income from operations	108,500	14,729	(7,482 )	115,747
<b>Other income (expense):</b>				
Interest expense	(39,669 )	(7,392 )	—	(47,061 )
Other, net	1,077	145	—	1,222
Total other expense, net	(38,592 )	(7,247 )	—	(45,839 )
Income before income taxes	69,908	7,482	(7,482 )	69,908
Income tax expense	18,345	—	—	18,345
Net income	\$51,563	\$ 7,482	\$ (7,482 )	\$ 51,563



## CONDENSED CONSOLIDATING STATEMENT OF INCOME

Nine Months Ended September 30, 2017

H&amp;E Equipment Guarantor

	Services	Subsidiaries	Elimination	Consolidated
	(Amounts in thousands)			
<b>Revenues:</b>				
Equipment rentals	\$288,610	\$ 62,693	\$ —	\$ 351,303
New equipment sales	106,626	22,257	—	128,883
Used equipment sales	60,292	14,927	—	75,219
Parts sales	73,955	12,304	—	86,259
Services revenues	39,650	7,471	—	47,121
Other	37,966	8,602	—	46,568
Total revenues	607,099	128,254	—	735,353
<b>Cost of revenues:</b>				
Rental depreciation	104,177	21,819	—	125,996
Rental expense	48,607	9,917	—	58,524
New equipment sales	94,617	19,823	—	114,440
Used equipment sales	42,442	9,537	—	51,979
Parts sales	54,085	8,650	—	62,735
Services revenues	13,464	2,434	—	15,898
Other	38,049	8,694	—	46,743
Total cost of revenues	395,441	80,874	—	476,315
<b>Gross profit (loss):</b>				
Equipment rentals	135,826	30,957	—	166,783
New equipment sales	12,009	2,434	—	14,443
Used equipment sales	17,850	5,390	—	23,240
Parts sales	20,099	3,425	—	23,524
Services revenues	26,186	5,037	—	31,223
Other	(312 )	137	—	(175 )
Gross profit	211,658	47,380	—	259,038
Selling, general and administrative expenses	140,522	31,806	—	172,328
Equity in earnings of guarantor subsidiaries	11,141	—	(11,141 )	—
Merger costs (net of merger breakup fee proceeds)	(6,506 )	—	—	(6,506 )
Gain on sales of property and equipment, net	1,971	2,460	—	4,431
Income from operations	90,754	18,034	(11,141 )	97,647
<b>Other income (expense):</b>				
Interest expense	(34,522 )	(7,143 )	—	(41,665 )
Loss on early extinguishment of debt	(25,363 )	—	—	(25,363 )
Other, net	906	250	—	1,156
Total other expense, net	(58,979 )	(6,893 )	—	(65,872 )
Income before income taxes	31,775	11,141	(11,141 )	31,775
Income tax expense	8,045	—	—	8,045
Net income	\$23,730	\$ 11,141	\$ (11,141 )	\$ 23,730



## CONDENSED CONSOLIDATING STATEMENT OF CASH FLOWS

Nine Months Ended September 30, 2018

H&amp;E Equipment Guarantor

	Services	Subsidiaries	Elimination	Consolidated
	(Amounts in thousands)			

Cash flows from operating activities:				
Net income	\$51,563	\$ 7,482	\$ (7,482 )	\$ 51,563
Adjustments to reconcile net income to net cash provided				
by operating activities:				
Depreciation and amortization on property and equipment	16,106	2,261	—	18,367
Depreciation of rental equipment	130,650	22,050	—	152,700
Amortization of intangible assets	2,415	—	—	2,415
Amortization of deferred financing costs	819	—	—	819
Accretion of note discount, net of premium amortization	357	—	—	357
Provision for losses on accounts receivable	1,474	582	—	2,056
Provision for inventory obsolescence	74	—	—	74
Change in deferred income taxes	17,869	—	—	17,869
Stock-based compensation expense	2,998	—	—	2,998
Gain from sales of property and equipment, net	(5,754 )	(286 )	—	(6,040 )
Gain from sales of rental equipment, net	(23,017 )	(4,624 )	—	(27,641 )
Equity in earnings of guarantor subsidiaries	(7,482 )	—	7,482	—
Changes in operating assets and liabilities:				
Receivables	(4,757 )	(2,068 )	—	(6,825 )
Inventories	(47,356 )	(8,999 )	—	(56,355 )
Prepaid expenses and other assets	173	2	—	175
Accounts payable	(6,491 )	(3,590 )	—	(10,081 )
Manufacturer flooring plans payable	5,533	(1,063 )	—	4,470
Accrued expenses payable and other liabilities	(8,665 )	(296 )	—	(8,961 )
Deferred compensation payable	65	—	—	65
Net cash provided by operating activities	126,574	11,451	—	138,025
Cash flows from investing activities:				
Acquisition of business, net of cash acquired	(196,027 )	—	—	(196,027 )
Purchases of property and equipment	(19,274 )	(7,764 )	—	(27,038 )
Purchases of rental equipment	(302,878 )	(47,768 )	—	(350,646 )
Proceeds from sales of property and equipment	7,672	286	—	7,958
Proceeds from sales of rental equipment	64,747	14,200	—	78,947
Investment in subsidiaries	(29,599 )	—	29,599	—
Net cash used in investing activities	(475,359 )	(41,046 )	29,599	(486,806 )
Cash flows from financing activities:				
Purchases of treasury stock	(1,323 )	—	—	(1,323 )
Borrowings on senior secured credit facility	1,142,811	—	—	1,142,811
Payments on senior secured credit facility	(923,793 )	—	—	(923,793 )
Dividends paid	(29,443 )	(4 )	—	(29,447 )
Payment of deferred financing costs	(97 )	—	—	(97 )



Edgar Filing: H&E Equipment Services, Inc. - Form 10-Q

Payments on capital lease obligations	(160 )	—	—	(160 )
Capital contributions	—	29,599	(29,599 )	—
Net cash provided by financing activities	187,995	29,595	(29,599 )	187,991
Net decrease in cash	(160,790 )	—	—	(160,790 )
Cash, beginning of period	165,878	—	—	165,878
Cash, end of period	\$5,088	\$ —	\$ —	\$ 5,088

31

## CONDENSED CONSOLIDATING STATEMENT OF CASH FLOWS

Nine Months Ended September 30, 2017

H&amp;E Equipment Guarantor

	Services	Subsidiaries	Elimination	Consolidated
	(Amounts in thousands)			

Cash flows from operating activities:				
Net income	\$23,730	\$ 11,141	\$ (11,141 )	\$ 23,730
Adjustments to reconcile net income to net cash provided				
by operating activities:				
Depreciation and amortization on property and equipment	15,778	2,314	—	18,092
Depreciation of rental equipment	104,177	21,819	—	125,996
Amortization of deferred financing costs	785	—	—	785
Accretion of note discount, net of premium amortization	239	—	—	239
Provision for losses on accounts receivable	2,336	712	—	3,048
Provision for inventory obsolescence	151	—	—	151
Change in deferred income taxes	7,752	—	—	7,752
Stock-based compensation expense	2,614	—	—	2,614
Loss on early extinguishment of debt	25,363	—	—	25,363
Gain from sales of property and equipment, net	(1,971 )	(2,460 )	—	(4,431 )
Gain from sales of rental equipment, net	(16,852 )	(5,344 )	—	(22,196 )
Equity in earnings of guarantor subsidiaries	(11,141 )	—	11,141	—
Changes in operating assets and liabilities:				
Receivables	(14,510 )	(1,301 )	—	(15,811 )
Inventories	(32,279 )	(6,651 )	—	(38,930 )
Prepaid expenses and other assets	(1,592 )	(14 )	—	(1,606 )
Accounts payable	41,670	452	—	42,122
Manufacturer flooring plans payable	(9,196 )	1,702	—	(7,494 )
Accrued expenses payable and other liabilities	(4,711 )	1,636	—	(3,075 )
Deferred compensation payable	44	—	—	44
Net cash provided by operating activities	132,387	24,006	—	156,393
Cash flows from investing activities:				
Purchases of property and equipment	(14,618 )	(1,384 )	—	(16,002 )
Purchases of rental equipment	(154,057)	(29,697 )	—	(183,754 )
Proceeds from sales of property and equipment	2,914	3,851	—	6,765
Proceeds from sales of rental equipment	51,699	14,617	—	66,316
Investment in subsidiaries	11,225	—	(11,225 )	—
Net cash used in investing activities	(102,837)	(12,613 )	(11,225 )	(126,675 )
Cash flows from financing activities:				
Purchases of treasury stock	(753 )	—	—	(753 )
Borrowings on senior secured credit facility	732,840	—	—	732,840
Payments on senior secured credit facility	(818,285)	—	—	(818,285 )
Dividends paid	(29,363 )	(6 )	—	(29,369 )
Principal payments on senior unsecured notes due 2022	(630,000)	—	—	(630,000 )
	(23,336 )	—	—	(23,336 )

Edgar Filing: H&E Equipment Services, Inc. - Form 10-Q

Costs paid to tender and redeem senior unsecured notes due  
2022

Proceeds from issuance of senior unsecured notes due 2025	750,000	—	—	750,000
Payments of deferred financing costs	(12,152 )	—	—	(12,152 )
Payments on capital lease obligations	—	(162 )	—	(162 )
Capital contributions	—	(11,225 )	11,225	—
Net cash used in financing activities	(31,049 )	(11,393 )	11,225	(31,217 )
Net decrease in cash	(1,499 )	—	—	(1,499 )
Cash, beginning of period	7,683	—	—	7,683
Cash, end of period	\$6,184	\$ —	\$ —	\$ 6,184

## ITEM 2. — MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion summarizes the financial position of H&E Equipment Services, Inc. and its subsidiaries as of September 30, 2018, and its results of operations for the three and nine month periods ended September 30, 2018, and should be read in conjunction with (i) the unaudited condensed consolidated financial statements and notes thereto included elsewhere in this Quarterly Report on Form 10-Q and (ii) the audited consolidated financial statements and accompanying notes to our Annual Report on Form 10-K for the year ended December 31, 2017. The following discussion contains, in addition to historical information, forward-looking statements that include risks and uncertainties (see discussion of “Forward-Looking Statements” included elsewhere in this Quarterly Report on Form 10-Q). Our actual results may differ materially from those anticipated in these forward-looking statements as a result of certain factors, including those factors set forth under Item 1A – “Risk Factors” of our Annual Report on Form 10-K for the year ended December 31, 2017.

### Overview

### Background

As one of the largest integrated equipment services companies in the United States focused on heavy construction and industrial equipment, we rent, sell and provide parts and services support for four core categories of specialized equipment: (1) hi-lift or aerial work platform equipment; (2) cranes; (3) earthmoving equipment; and (4) industrial lift trucks. By providing equipment rental, sales, on-site parts, repair and maintenance functions under one roof, we are a one-stop provider for our customers’ varied equipment needs. This full service approach provides us with multiple points of customer contact, enables us to maintain a high quality rental fleet, as well as an effective distribution channel for fleet disposal and provides cross-selling opportunities among our new and used equipment sales, rental, parts sales and services operations.

As of October 18, 2018, we operated 89 full-service facilities throughout the Intermountain, Southwest, Gulf Coast, West Coast, Southeast and Mid-Atlantic regions of the United States. Our work force includes distinct, focused sales forces for our new and used equipment sales and rental operations, highly skilled service technicians, product specialists and regional managers. We focus our sales and rental activities on, and organize our personnel principally by, our four core equipment categories. We believe this allows us to provide specialized equipment knowledge, improve the effectiveness of our rental and sales force and strengthen our customer relationships. In addition, we have branch managers for each location who are responsible for managing their assets and financial results. We believe this fosters accountability in our business and strengthens our local and regional relationships.

Through our predecessor companies, we have been in the equipment services business for approximately 57 years. H&E Equipment Services L.L.C. (“H&E LLC”) was formed in June 2002 through the business combination of Head & Engquist Equipment, LLC (“Head & Engquist”), a wholly-owned subsidiary of Gulf Wide Industries, L.L.C. (“Gulf Wide”), and ICM Equipment Company L.L.C. (“ICM”). Head & Engquist, founded in 1961, and ICM, founded in 1971, were two leading regional, integrated equipment service companies operating in contiguous geographic markets. In the June 2002 transaction, Head & Engquist and ICM were merged with and into Gulf Wide, which was renamed H&E LLC. Prior to the combination, Head & Engquist operated 25 facilities in the Gulf Coast region, and ICM operated 16 facilities in the Intermountain region of the United States.

Prior to our initial public offering in February 2006, our business was conducted through H&E LLC. In connection with our initial public offering, we converted H&E LLC into H&E Equipment Services, Inc. In order to have an operating Delaware corporation as the issuer for our initial public offering, H&E Equipment Services, Inc. was formed as a Delaware corporation and wholly-owned subsidiary of H&E Holdings L.L.C. (“H&E Holdings”), and immediately

prior to the closing of our initial public offering, on February 3, 2006, H&E LLC and H&E Holdings merged with and into H&E Equipment Services, Inc., which survived the reincorporation merger as the operating company. Effective February 3, 2006, H&E LLC and H&E Holdings no longer existed under operation of law pursuant to the reincorporation merger.

On January 1, 2018, we completed the acquisition of Contractors Equipment Center, an equipment rental company serving the greater Denver, Colorado area with three branches. On April 1, 2018, we completed the acquisition of Rental, LLC (dba "Rental Inc."), a non-residential equipment rental and distribution company with five branches located in Alabama, Florida and Western Georgia.

#### Critical Accounting Policies

Item 7, included in Part II of our Annual Report on Form 10-K for the year ended December 31, 2017, presents the accounting policies and related estimates that we believe are the most critical to understanding our consolidated financial statements, financial condition, and results of operations and cash flows, and which require complex management judgment and assumptions, or involve uncertainties. There have been no significant changes to these critical accounting policies and estimates during the three and nine

months ended September 30, 2018, except as disclosed in note 2 related to new revenue recognition guidance adopted on January 1, 2018. These policies include, among others, revenue recognition, the adequacy of the allowance for doubtful accounts, the propriety of our estimated useful life of rental equipment and property and equipment, the potential impairment of long-lived assets including goodwill and intangible assets, obsolescence reserves on inventory, the allocation of purchase price related to business combinations, reserves for claims, including self-insurance reserves, and deferred income taxes, including the valuation of any related deferred tax assets.

Information regarding our other significant accounting policies is included in note 2 to our consolidated financial statements in Item 8 of Part II of our Annual Report on Form 10-K for the year ended December 31, 2017 and in note 2 to the condensed consolidated financial statements in this Quarterly Report on Form 10-Q.

## Business Segments

We have five reportable segments because we derive our revenues from five principal business activities: (1) equipment rentals; (2) new equipment sales; (3) used equipment sales; (4) parts sales; and (5) repair and maintenance services. These segments are based upon how we allocate resources and assess performance. In addition, we also have non-segmented revenues and costs that relate to equipment support activities.

**Equipment Rentals.** Our rental operation primarily rents our four core types of construction and industrial equipment. We have a well-maintained rental fleet and our own dedicated sales force, focused by equipment type. We actively manage the size, quality, age and composition of our rental fleet based on our analysis of key measures such as time utilization (which we analyze as equipment usage based on: (1) a percentage of original equipment cost, and (2) the number of rental equipment units available for rent), rental rate trends and targets, rental equipment dollar utilization and maintenance and repair costs, which we closely monitor. We maintain fleet quality through regional quality control managers and our parts and services operations.

**New Equipment Sales.** Our new equipment sales operation sells new equipment in all of our four core product categories. We have a retail sales force focused by equipment type that is separate from our rental sales force. Manufacturer purchase terms and pricing are managed by our product specialists.

**Used Equipment Sales.** Our used equipment sales are generated primarily from sales of used equipment from our rental fleet, as well as from sales of inventoried equipment that we acquire through trade-ins from our equipment customers and through selective purchases of high quality used equipment. Used equipment is sold by our dedicated retail sales force. Our used equipment sales are an effective way for us to manage the size and composition of our rental fleet and provide a profitable distribution channel for disposal of rental equipment.

**Parts Sales.** Our parts business sells new and used parts for the equipment we sell and also provides parts to our own rental fleet. To a lesser degree, we also sell parts for equipment produced by manufacturers whose products we neither rent nor sell. In order to provide timely parts and services support to our customers as well as our own rental fleet, we maintain an extensive parts inventory.

**Services.** Our services operation provides maintenance and repair services for our customers' equipment and to our own rental fleet at our facilities as well as at our customers' locations. As the authorized distributor for numerous equipment manufacturers, we are able to provide service to that equipment that will be covered under the manufacturer's warranty.

Our non-segmented revenues and costs relate to equipment support activities that we provide, such as transportation, hauling, parts freight and damage waivers, and are not generally allocated to reportable segments.

For additional information about our business segments, see note 10 to the condensed consolidated financial statements in this Quarterly Report on Form 10-Q.

## Revenue Sources

We generate all of our total revenues from our five business segments and our non-segmented equipment support activities. Equipment rentals and new equipment sales account for more than half of our total revenues. For the nine month period ended September 30, 2018, approximately 48.1% of our total revenues were attributable to equipment rentals, 20.5% of our total revenues were attributable to new equipment sales, 9.8% were attributable to used equipment sales, 10.1% were attributable to parts sales, 5.4% were attributable to our services revenues and 6.1% were attributable to non-segmented other revenues.

The equipment that we sell, rent and service is principally used in the construction industry, as well as by companies for commercial and industrial uses such as plant maintenance and turnarounds, as well as in the petrochemical and energy sectors. As a result, our total revenues are affected by several factors including, but not limited to, the demand for and availability of rental equipment, rental rates and other competitive factors, the demand for new and used equipment, the level of construction and industrial activities, spending levels by our customers, adverse weather conditions and general economic conditions. For a discussion of the impact of seasonality on our revenues, see “Seasonality” below.

**Equipment Rentals.** Our rental operation primarily rents our four core types of construction and industrial equipment. We have a well-maintained rental fleet and our own dedicated sales force, focused by equipment type. We actively manage the size, quality, age and composition of our rental fleet based on our analysis of key measures such as time utilization (which we analyze as equipment usage based on: (1) a percentage of original equipment cost, and (2) the number of rental equipment units available for rent), rental rate trends and targets, rental equipment dollar utilization and maintenance and repair costs, which we closely monitor. We maintain fleet quality through regional quality control managers and our parts and services operations.

**New Equipment Sales.** We seek to optimize revenues from new equipment sales by selling equipment through a professional in-house retail sales force focused by product type. While sales of new equipment are impacted by the availability of equipment from the manufacturer, we believe our status as a leading distributor for some of our key suppliers improves our ability to obtain equipment. New equipment sales are an important component of our integrated model due to customer interaction and service contact and new equipment sales also lead to future parts and services revenues.

**Used Equipment Sales.** We generate the majority of our used equipment sales revenues by selling equipment from our rental fleet. The remainder of our used equipment sales revenues comes from the sale of inventoried equipment that we acquire through trade-ins from our equipment customers and selective purchases of high quality used equipment. Our policy is not to offer specified price trade in arrangements on equipment for sale. Sales of our rental fleet equipment allow us to manage the size, quality, composition and age of our rental fleet, and provide us with a profitable distribution channel for the disposal of rental equipment.

**Parts Sales.** We generate revenues from the sale of new and used parts for equipment that we rent or sell, as well as for other makes of equipment. Our product support sales representatives are instrumental in generating our parts revenues. They are product specialists and receive performance incentives for achieving certain sales levels. Most of our parts sales come from our extensive in-house parts inventory. Our parts sales provide us with a relatively stable revenue stream that is generally less sensitive to the economic cycles that tend to affect our rental and equipment sales operations.

**Services.** We derive our services revenues from maintenance and repair services to customers for their owned equipment. In addition to repair and maintenance on an as-needed or scheduled basis, we also provide ongoing preventative maintenance services to industrial customers. Our after market service provides a high-margin, relatively stable source of revenue through changing economic cycles.

Our non-segmented other revenues relate to equipment support activities that we provide, such as transportation, hauling, and damage waivers, and are not generally allocated to reportable segments.

#### Principal Costs and Expenses

Our largest expenses are the costs to purchase the new equipment we sell, the costs associated with the used equipment we sell, rental expenses, rental depreciation and costs associated with parts sales and services, all of which



are included in cost of revenues. For the nine month period ended September 30, 2018, our total cost of revenues was \$577.6 million. Our operating expenses consist principally of selling, general and administrative expenses. For the nine month period ended September 30, 2018, our selling, general and administrative expenses were \$205.3 million. In addition, we have interest expense related to our debt instruments. Operating expenses and all other income and expense items below the gross profit line of our consolidated statements of income are not generally allocated to our reportable segments.

We are also subject to federal and state income taxes. Future income tax examinations by state and federal agencies could result in additional income tax expense based on probable outcomes of such matters.

Cost of Revenues:

Rental Depreciation. Depreciation of rental equipment represents the depreciation costs attributable to rental equipment. Estimated useful lives vary based upon type of equipment. Generally, we depreciate cranes and aerial work platforms over a ten year estimated useful life, earthmoving over a five year estimated useful life with a 25% salvage value, and industrial lift trucks over a seven year estimated useful life. Attachments and other smaller type equipment are depreciated over a three year estimated useful life. We periodically evaluate the appropriateness of remaining depreciable lives assigned to rental equipment.

**Rental Expense.** Rental expense represents the costs associated with rental equipment, including, among other things, the cost of servicing and maintaining our rental equipment, property taxes on our fleet and other miscellaneous costs of rental equipment.

**New Equipment Sales.** Cost of new equipment sold primarily consists of the equipment cost of the new equipment that is sold, net of any amount of credit given to the customer towards the equipment for trade-ins.

**Used Equipment Sales.** Cost of used equipment sold consists of the net book value of rental equipment for used equipment sold from our rental fleet, the equipment costs for used equipment we purchase for sale or the trade-in value of used equipment that we obtain from customers in equipment sales transactions.

**Parts Sales.** Cost of parts sales represents costs attributable to the sale of parts directly to customers.

**Services Support.** Cost of services revenues represents costs attributable to service provided for the maintenance and repair of customer-owned equipment and equipment then on-rent by customers.

**Non-Segmented Other.** These expenses include costs associated with providing transportation, hauling and damage waiver including, among other items, drivers' wages, fuel costs, and our costs related to damage waiver policies.

**Selling, General and Administrative Expenses:**

Our selling, general and administrative ("SG&A") expenses include sales and marketing expenses, payroll and related benefit costs, insurance expenses, legal and professional fees, rent and other occupancy costs, property and other taxes, administrative overhead, depreciation associated with property and equipment (other than rental equipment) and amortization expense associated with capital leases and software. These expenses are not generally allocated to our reportable segments.

**Interest Expense:**

Interest expense for the periods presented represents the interest on our outstanding debt instruments, including aggregate amounts outstanding under our revolving senior secured credit facility (the "Credit Facility"), senior unsecured notes due 2025 and our capital lease obligations, as well as our extinguished senior unsecured notes due 2022 (the "Old Notes") for the periods during which such Old Notes were outstanding. Interest expense also includes interest on our outstanding manufacturer flooring plans payable which are used to finance inventory and rental equipment purchases. Non-cash interest expense related to the amortization cost of deferred financing costs and the accretion/amortization of note discount/premium are also included in interest expense.

**Principal Cash Flows**

We generate cash primarily from our operating activities and, historically, we have used cash flows from operating activities, manufacturer floor plan financings and available borrowings under the Credit Facility as the primary sources of funds to purchase inventory and to fund working capital and capital expenditures, growth and expansion opportunities (see also "Liquidity and Capital Resources" below). Our management of our working capital is closely tied to operating cash flows, as working capital can be significantly impacted by, among other things, our accounts receivable activities, the level of new and used equipment inventories, which may increase or decrease in response to current and expected demand, and the size and timing of our trade accounts payable payment cycles.

## Rental Fleet

A substantial portion of our overall value is in our rental fleet equipment. The net book value of our rental equipment at September 30, 2018 was \$1.2 billion, or approximately 66.9% of our total assets. Our rental fleet as of September 30, 2018 consisted of 40,766 units having an original acquisition cost (which we define as the cost originally paid to manufacturers or the original amount financed under operating leases) of approximately \$1.8 billion. As of September 30, 2018, our rental fleet composition was as follows (dollars in millions):

	Units	% of Total	Original Acquisition Cost	% of Original Acquisition Cost	Average Age in Months
Hi-Lift or Aerial Work Platforms	27,438	67.3 %	\$ 1,165.0	66.3	36.9
Cranes	250	0.6 %	88.5	5.0	58.3
Earthmoving	4,387	10.8 %	362.0	20.6	24.6
Industrial Lift Trucks	1,244	3.0 %	37.6	2.1	26.4
Other	7,447	18.3 %	105.4	6.0	28.5
Total	40,766	99.9 %	\$ 1,758.5	100.1	33.8

Determining the optimal age and mix for our rental fleet equipment is subjective and requires considerable estimates and judgments by management. We constantly evaluate the mix, age and quality of the equipment in our rental fleet in response to current economic and market conditions, competition and customer demand. The mix and age of our rental fleet, as well as our cash flows, are impacted by sales of equipment from the rental fleet, which are influenced by used equipment pricing at the retail and secondary auction market levels, and the capital expenditures to acquire new rental fleet equipment. In making equipment acquisition decisions, we evaluate current economic and market conditions, competition, manufacturers' availability, pricing and return on investment over the estimated useful life of the specific equipment, among other things. As a result of our in-house service capabilities and extensive maintenance program, we believe our rental fleet is well-maintained.

The original acquisition cost of our gross rental fleet increased by approximately \$356.1 million, or 25.4%, for the nine month period ended September 30, 2018, largely reflective of the CEC and Rental Inc. acquired fleets, combined with growth in rental capital expenditures to meet customer demand. The average age of our rental fleet equipment decreased by approximately 0.8 months for the nine months ended September 30, 2018.

Our average rental rates for the nine month period ended September 30, 2018 were 2.2% higher than in the nine month period ended September 30, 2017 and approximately 0.8% higher than the three month period ended June 30, 2018 (see further discussion on rental rates in "Results of Operations" below). Our average rental rates for the nine month period ended September 30, 2018 do not include rental rate data for (1) legacy Rental Inc. operations for the second quarter of 2018 and (2) legacy CEC operations for the first quarter of 2018.

The rental equipment mix among our four core product lines for the nine months ended September 30, 2018 was largely consistent with that of the prior year comparable period as a percentage of original acquisition cost.

Principal External Factors that Affect our Businesses

We are subject to a number of external factors that may adversely affect our businesses. These factors, and other factors, are discussed below and under the heading “Forward Looking Statements,” and in Item 1A—Risk Factors in this Annual Report on Form 10 K for the year ended December 31, 2017.

• **Economic downturns.** The demand for our products is dependent on the general economy, the stability of the global credit markets, the industries in which our customers operate or serve and other factors. Downturns in the general economy or in the construction and manufacturing industries, as well as adverse credit market conditions, can cause demand for our products to materially decrease.

• **Spending levels by customers.** Rentals and sales of equipment to the construction industry and to industrial companies constitute a significant portion of our total revenues. As a result, we depend upon customers in these businesses and their ability and willingness to make capital expenditures to rent or buy specialized equipment. Accordingly, our business is impacted by fluctuations in customers’ spending levels on capital expenditures and by the availability of credit to those customers.

• **Adverse weather.** Adverse weather in a geographic region in which we operate may depress demand for equipment in that region. Our equipment is primarily used outdoors and, as a result, prolonged adverse weather conditions may prohibit our

customers from continuing their work projects. Adverse weather also has a seasonal impact in parts of our Intermountain region, particularly in the winter months.

**Regional and Industry-Specific Activity and Trends.** Expenditures by our customers may be impacted by the overall level of construction activity in the markets and regions in which they operate, the price of oil and other commodities and other general economic trends impacting the industries in which our customers and end users operate. As our customers adjust their activity and spending levels in response to these external factors, our rentals and sales of equipment to those customers will be impacted. For example, high levels of industrial activity in our Gulf Coast and Intermountain regions have been a meaningful driver of recent growth in our revenues. However, the decline in oil and natural gas prices and the related downturn in oil industry activities during fiscal years 2014, 2015 and 2016 resulted in a significant decrease in our new equipment sales, primarily the sale of new cranes, due to lower demand. Although oil prices have subsequently stabilized and improved in 2017 and into 2018, we believe the uncertainty regarding future oil prices continues to impact customer capital expenditure decisions.

We believe that our integrated business tempers the effects of downturns in a particular segment. For a discussion of seasonality, see “Seasonality” on page 50 of this Quarterly Report on Form 10-Q.

## Results of Operations

The tables included in the period-to-period comparisons below provide summaries of our revenues and gross profits for our business segments and non-segmented revenues for the three and nine months ended September 30, 2018 and 2017. The period-to-period comparisons of our financial results are not necessarily indicative of future results.

### Three Months Ended September 30, 2018 Compared to the Three Months Ended September 30, 2017

#### Revenues.

	Three Months Ended		Total	Total	
	September 30,	September 30,	Dollar	Percentage	
	2018	2017	Increase	Increase	
	(in thousands, except percentages)				
<b>Segment Revenues:</b>					
Equipment rentals	\$ 156,037	\$ 125,616	\$ 30,421	24.2	%
New equipment sales	68,233	48,940	19,293	39.4	%
Used equipment sales	30,294	22,250	8,044	36.2	%
Parts sales	31,484	29,534	1,950	6.6	%
Services revenues	16,426	16,097	329	2.0	%
Non-Segmented revenues	19,667	16,725	2,942	17.6	%
Total revenues	\$ 322,141	\$ 259,162	\$ 62,979	24.3	%

**Total Revenues.** Our total revenues were approximately \$322.1 million for the three month period ended September 30, 2018 compared to \$259.2 million for the three month period ended September 30, 2017, an increase of \$63.0 million, or 24.3%. Revenues for all reportable segments and non-segmented other revenues are further discussed below.

**Equipment Rental Revenues.** Our revenues from equipment rentals for the three month period ended September 30, 2018 increased approximately \$30.4 million, or 24.2%, to \$156.0 million from \$125.6 million in the three month period ended September 30, 2017. The increase in equipment rental revenues was largely due to increased demand

and the equipment rental revenues from our CEC and Rental Inc. locations.

Rental revenues from aerial work platform equipment increased \$21.6 million while earthmoving equipment rental revenues and lift truck rental revenues increased \$7.2 million and \$1.2 million, respectively, for the three month period ended September 30, 2018. Other equipment rental revenues increased approximately \$0.7 million. Partially offsetting these rental revenue increases was a \$0.3 million decrease in crane rental revenues. Our average rental rates for the three month period ended September 30, 2018 increased 2.2% compared to the same three month period last year and increased approximately 0.8% from the three month period ended June 30, 2018.

Rental equipment dollar utilization (annual rental revenues divided by the average original rental fleet equipment costs) for the three month period ended September 30, 2018 was 35.9% compared to 36.0% in the three month period ended September 30, 2017, a decrease of 0.1%. The decrease in comparative rental equipment dollar utilization was the net result of the increase in equipment rental rates as noted above and a decrease in rental equipment time utilization. Rental equipment time utilization as a percentage of

original equipment cost was approximately 71.0% for the three month period ended September 30, 2018 compared to 73.3% in the three month period ended September 30, 2017, a decrease of 2.3%. The decrease in rental equipment time utilization as a percentage of original equipment cost was largely due to a \$354.8 million increase, or 25.3%, in our equipment rental fleet since September 30, 2017.

**New Equipment Sales Revenues.** Our new equipment sales for the three month period ended September 30, 2018 increased approximately \$19.3 million, or 39.4%, to \$68.2 million from \$48.9 million for the three month period ended September 30, 2017. This increase, as noted below, was driven primarily by increased sales of new cranes and earthmoving equipment, and the new equipment sales revenues from our Rental Inc. locations.

Sales of new cranes increased \$12.4 million, resulting from improved crane demand. Sales of new earthmoving equipment and new aerial work platform equipment increased \$5.3 million and \$2.7 million, respectively, while sales of new lift trucks increased \$0.4 million. Sales of new other equipment decreased \$1.5 million.

**Used Equipment Sales Revenues.** Our used equipment sales increased \$8.0 million, or 36.2%, to \$30.3 million for the three month period ended September 30, 2018, from approximately \$22.3 million for the same three month period in 2017.

Sales of used aerial work platform equipment increased \$8.2 million and sales of used other equipment increased \$1.4 million. Sales of used cranes and sales of used lift trucks each increased approximately \$0.2 million. Partially offsetting these increases was a \$2.0 million decrease in used earthmoving equipment.

**Parts Sales Revenues.** Our parts sales revenues for the three month period ended September 30, 2018 increased \$2.0 million, or 6.6%, to \$31.5 million from \$29.5 million for the same three month period last year. The increase in parts sales was due in part to the combined parts sales revenues from our CEC and Rental Inc. locations and an increase in earthmoving parts sales.

**Services Revenues.** Our services revenues for the three month period ended September 30, 2018 increased \$0.3 million, or 2.0%, to \$16.4 million from \$16.1 million for the same three month period last year. This increase in services revenues was substantially due to the services revenues from our CEC and Rental Inc. locations.

**Non-Segmented Other Revenues.** Our non-segmented other revenues consisted primarily of equipment support activities including fuel charges on rented equipment, transportation and hauling charges related to our equipment rental and maintenance and repair services, and damage waiver fees on rental equipment. For the three month period ended September 30, 2018, our other revenues were approximately \$19.7 million, an increase of \$2.9 million, or 17.6%, from approximately \$16.7 million in the same three month period in 2017. This increase was primarily driven by higher hauling revenues and damage waiver income associated with our equipment rental activities, combined with non-segmented other revenues from our CEC and Rental Inc. locations.

**Gross Profit.**

Three Months		Total	Total
Ended		Dollar	Percentage
September 30,		Increase	Increase
2018	2017	(Decrease)	(Decrease)
(in thousands, except percentages)			

Edgar Filing: H&E Equipment Services, Inc. - Form 10-Q

Segment Gross Profit:					
Equipment rentals	\$78,041	\$62,373	\$ 15,668	25.1	%
New equipment sales	7,839	5,331	2,508	47.0	%
Used equipment sales	9,782	7,134	2,648	37.1	%
Parts sales	8,355	7,957	398	5.0	%
Services revenues	10,798	10,530	268	2.5	%
Non-Segmented revenues gross profit (loss)	(85 )	701	(786 )	(112.1 )	%
Total gross profit	\$114,730	\$94,026	\$ 20,704	22.0	%

Total Gross Profit. Our total gross profit was \$114.7 million for the three month period ended September 30, 2018 compared to \$94.0 million for the same three month period in 2017, an increase of \$20.7 million, or 22.0%. Total gross profit margin for the three month period ended September 30, 2018 was 35.6%, a decrease of 0.7% from the 36.3% gross profit margin for the same three month period in 2017. The decrease in total gross profit margin was primarily due to revenue mix from a shift to lower margin new equipment sales revenues. Gross profit and gross margin for all reportable segments and non-segmented other revenues are further described below:



**Equipment Rentals Gross Profit.** Our gross profit from equipment rentals for the three month period ended September 30, 2018 increased \$15.7 million, or 25.1%, to approximately \$78.0 million from \$62.4 million in the same three month period in 2017.

The increase in equipment rentals gross profit was the result of a \$30.4 million increase in equipment rental revenues for the three month period ended September 30, 2018 compared to the same period last year, which was partially offset by an \$11.8 million increase in rental equipment depreciation expense and a \$2.9 million increase in rental expenses. The increases in both depreciation expense and rental expenses are primarily due to a larger fleet size in 2018 compared to 2017.

Gross profit margin on equipment rentals for the three month period ended September 30, 2018 was approximately 50.0% compared to 49.7% for the same period in 2017, an increase of 0.3%. As a percentage of equipment rental revenues, rental expenses were 14.7% for the three month period ended September 30, 2018 compared to 15.9% for the same period last year, a decrease of 1.2%, resulting primarily from the increase in equipment rental revenues. Depreciation expense was 35.3% of equipment rental revenues for the three month period ended September 30, 2018 compared to 34.4% for the same period in 2017, an increase of 0.9%, primarily as a result of the increase in depreciation expense resulting from the purchase accounting fair value step up adjustments on the CEC and Rental Inc. acquired rental fleets and the mix of rental equipment.

**New Equipment Sales Gross Profit.** Our new equipment sales gross profit for the three month period ended September 30, 2018 increased \$2.5 million, or 47.0%, to \$7.8 million compared to \$5.3 million for the same three month period in 2017 on a total new equipment sales increase of \$19.3 million. Gross profit margin on new equipment sales was 11.5% for the three month period ended September 30, 2018, compared to 10.9% for the same period last year, an increase of 0.6%. The increase in gross profit margin was primarily due to higher gross margins on sales of new aerial work platform equipment and new other equipment.

**Used Equipment Sales Gross Profit.** Our used equipment sales gross profit for the three month period ended September 30, 2018 increased approximately \$2.6 million, or 37.1%, to \$9.8 million from \$7.1 million in the same period in 2017 on a used equipment sales increase of \$8.0 million.

Gross profit margin on used equipment sales for the three month period ended September 30, 2018 was approximately 32.3%, up 0.2% from 32.1% for the same three month period in 2017, primarily as a result of the mix of used equipment sold and higher used cranes and used aerial work platform equipment sales gross margins. These improved gross margins were slightly offset by lower margins on sales of used equipment inventory acquired in the CEC and Rental Inc. acquisitions, reflecting the purchase accounting fair value step up basis adjustment applied to the acquired used equipment inventory and rental equipment.

Our used equipment sales from the rental fleet, which comprised approximately 88.4% and 91.2% of our used equipment sales for the three month periods ended September 30, 2018 and 2017, respectively, were approximately 156.2% and 150.9% of net book value for the three month periods ended September 30, 2018 and 2017, respectively.

**Parts Sales Gross Profit.** Our parts sales gross profit for the three month period ended September 30, 2018 was approximately \$8.4 million, an increase of \$0.4 million, or 5.0%, from gross profit of \$8.0 million for the same period last year on a parts sales increase of \$2.0 million. Gross profit margin for the three month period ended September 30, 2018 was 26.5%, a decrease of 0.4% from 26.9% in the same three month period in 2017, as a result of the mix of parts sold.

**Services Revenues Gross Profit.** For the three month period ended September 30, 2018, our services revenues gross profit increased \$0.3 million, or 2.5%, to \$10.8 million from \$10.5 million for the same three month period in 2017 on

a \$0.3 million increase in services revenues. Gross profit margin for the three month period ended September 30, 2018 was 65.7%, an increase of 0.3% from approximately 65.4% in the same three month period in 2017, as a result of services revenues mix.

Non-Segmented Other Revenues Gross Profit (Loss). Our non-segmented other revenues gross profit decreased approximately \$0.8 million, from a gross profit of \$0.7 million for the three month period ended September 30, 2017 to a gross loss of \$0.1 million in the three month period ended September 30, 2018. Gross margin for the three month period ended September 30, 2018 was (0.4)% compared to a gross margin of 4.2% in the same three month period last year, a decrease of 4.6%, primarily reflective of lower hauling and fuel margins in the current period.

Selling, General and Administrative Expenses (“SG&A”). SG&A expenses increased approximately \$15.1 million, or 27.4%, to \$70.3 million for the three month period ended September 30, 2018 compared to \$55.2 million for the three month period ended September 30, 2017.

Included in SG&A for the three month period ended September 30, 2017 is the reclassification of \$2.2 million of merger and acquisition transaction costs related to the termination of our previously proposed acquisition of Neff Corporation (“Neff merger costs”), which we did not ultimately consummate. These Neff merger costs, previously recognized and included in SG&A for the six

month period ended June 30, 2017, were reclassified to “Merger Costs (net of Breakup Fee Proceeds)” in the third quarter ended September 30, 2017 (see “Merger Costs (net of Merger Breakup Fee Proceeds)” discussion below for further information). Excluding this \$2.2 million favorable impact to SG&A expenses in the three month period ended September 30, 2017, total SG&A expenses for the three month period ended September 30, 2017 would have been \$57.4 million, or 22.2% of total revenues, compared to the current three month period ended September 30, 2018 SG&A expenses of \$70.3 million, or 21.8% of total revenues.

Employee salaries, wages, payroll taxes and related employee benefit and other employee expenses increased \$8.9 million, primarily as a result of our CEC and Rental Inc. acquisitions, a larger workforce and higher incentive compensation related to improved profitability. Legal and professional fees increased approximately \$1.5 million. Facility rent expenses and repairs and maintenance costs increased \$0.4 million. Our results for the three month period ended September 30, 2018 also include \$0.9 million of amortization expense associated with the recognition of intangible assets resulting from the CEC and Rental Inc. purchase price allocations.

Approximately \$0.6 million of the total increase in SG&A expenses was attributable to branches opened since June 1, 2017 (but excluding for this purpose branches acquired as a result of our CEC and Rental Inc. acquisitions) with less than three months of comparable operations in either or both of the three month periods ended September 30, 2018 and 2017.

Merger Costs (net of Merger Breakup Fee Proceeds). Pursuant to the terms of our terminated 2017 merger agreement with Neff, we received a \$13.2 million breakup fee concurrently with Neff’s termination of the merger agreement in the third quarter of 2017. Related estimated merger transaction fees totaled \$6.7 million, resulting in estimated net proceeds of \$6.5 million for the three month period ended September 30, 2017. As noted in the above SG&A Expenses discussion, approximately \$2.2 million of the merger costs reflected in this financial statement line items were originally recorded in SG&A Expenses in the six month period ended June 30, 2017 and were subsequently reclassified in the third quarter ended September 30, 2017 to this net merger costs financial statement line item.

Merger costs incurred in the three month period ended September 30, 2018 were approximately \$0.2 million.

Other Income (Expense). For the three month period ended September 30, 2018, our net other expenses decreased approximately \$23.7 million to \$16.3 million compared to \$40.1 million for the same three month period in 2017. Included in Other Income (Expense) for the three month period ended September 30, 2017 is a \$25.4 million loss on the early extinguishment of debt (see “Loss on Early Extinguishment of Debt” below).

Interest expense increased approximately \$1.7 million to \$16.7 million for the three month period ended September 30, 2018 compared to \$15.1 million for the same period last year. The increase in interest expense was due to additional interest costs of \$0.7 million associated with the upsize of our \$950 million 5.625% senior unsecured notes that were issued in the third and fourth quarters of 2017 compared to our \$630 million 7% senior unsecured notes, which were retired in the third quarter of 2017. Also, our interest costs related to the Credit Facility increased \$0.9 million due to higher average borrowings in the current year period combined with higher interest rate costs.

Loss on Early Extinguishment of Debt. We recorded a one-time loss on the early extinguishment of debt in the three month period ended September 30, 2017 of approximately \$25.4 million, reflecting payment of \$12.8 million of tender premiums associated with our repurchase of the Old Notes and \$10.5 million of premiums in accordance with the indenture governing the Old Notes to redeem the remaining untendered Old Notes, combined with the write off of approximately \$2.0 million of unamortized note premium, unaccreted note discount and unamortized deferred financing costs, related to the Old Notes.

Income Taxes. We recorded income tax expense of \$7.7 million for the three month period ended September 30, 2018 compared to an income tax benefit of \$0.9 million for the three month period ended September 30, 2017. The prior year income tax benefit was primarily due to a \$5.7 million discrete tax benefit resulting from the reversal of an unrecognized tax benefit due to expiration of statute of limitations in the three month period ended September 30, 2017. Our effective income tax rate was approximately 26.4% for the three month period ended September 30, 2018 compared to (11.7%) for the same period last year. This effective income tax rate decrease was primarily due to the reduction of favorable permanent differences in the prior year period and the decrease in the federal statutory tax rate from 35% to 21%, resulting from the Tax Cuts and Jobs Act of 2017 (“the Act”), enacted in the fourth quarter of 2017. Our accounting for the income tax effects of the Act has been completed.

Based on available evidence, both positive and negative, we believe it is more likely than not that our federal deferred tax assets at September 30, 2018 are fully realizable through future reversals of existing taxable temporary differences and future taxable income, and are not subject to any limitations.

Edgar Filing: H&E Equipment Services, Inc. - Form 10-Q

Nine Months Ended September 30, 2018 Compared to the Nine Months Ended September 30, 2017

Revenues.

	Nine Months Ended September 30, 2018      2017		Total Dollar Increase	Total Percentage Increase	
(in thousands, except percentages)					
Segment Revenues:					
Equipment rentals	\$429,227	\$351,303	\$77,924	22.2	%
New equipment sales	183,265	128,883	54,382	42.2	%
Used equipment sales	87,287	75,219	12,068	16.0	%
Parts sales	89,916	86,259	3,657	4.2	%
Services revenues	48,250	47,121	1,129	2.4	%
Non-Segmented revenues	55,042	46,568	8,474	18.2	%
<b>Total revenues</b>	<b>\$892,987</b>	<b>\$735,353</b>	<b>\$157,634</b>	<b>21.4</b>	<b>%</b>

**Total Revenues.** Our total revenues were \$893.0 million for the nine month period ended September 30, 2018 compared to \$735.4 million for the nine month period ended September 30, 2017, an increase of \$157.6 million, or 21.4%. Revenues for all reportable segments and non-segmented other revenues are further discussed below.

**Equipment Rental Revenues.** Our revenues from equipment rentals for the nine month period ended September 30, 2018 increased approximately \$77.9 million, or 22.2%, to \$429.2 million from \$351.3 million in the nine month period ended September 30, 2017. The increase in equipment rental revenues was largely due to increased demand and the equipment rental revenues from our CEC and Rental Inc. locations.

Rental revenues from aerial work platform equipment increased \$44.0 million while earthmoving equipment rental revenues increased \$16.4 million. Other equipment rental revenues increased \$4.9 million and lift truck rental revenues increased approximately \$1.9 million. Partially offsetting these rental revenue increases was a \$1.1 million decrease in crane rental revenues. The product line equipment rental revenue fluctuations above do not include the impact of legacy CEC and Rental Inc. equipment rental revenues by product line for the three month periods ended March 31, 2018 and June 30, 2018, respectively.

Our average rental rates for the nine month period ended September 30, 2018 increased 2.2% compared to the same nine month period last year. Our average rental rates for the nine month period ended September 30, 2018 do not include rental rate data for legacy CEC and Rental Inc. for the three month periods ended March 31, 2018 and June 30, 2018, respectively.

Rental equipment dollar utilization (annual rental revenues divided by the average original rental fleet equipment costs) for the nine month period ended September 30, 2018 was 35.4% compared to 34.5% in the nine month period ended September 30, 2017, an increase of 0.9%. The increase in comparative rental equipment dollar utilization was primarily the result of the increase in equipment rental rates, which was partially offset by a decrease in rental equipment time utilization. Rental equipment time utilization as a percentage of original equipment cost was approximately 71.1% for the nine month period ended September 30, 2018 compared to 71.4% in the nine month

period ended September 30, 2017, a decrease of 0.3%.

42

---

**New Equipment Sales Revenues.** Our new equipment sales for the nine month period ended September 30, 2018 increased \$54.4 million, or 42.2%, to \$183.3 million from \$128.9 million for the nine month period ended September 30, 2017. This increase, as noted below, was driven primarily by increased sales of new cranes and the new equipment sales revenues from our Rental Inc. locations.

Sales of new cranes increased \$42.1 million, resulting from improved crane demand. Sales of new aerial work platform equipment and sales of new earthmoving equipment increased \$5.8 million and \$5.2 million, respectively. Sales of new lift trucks increased \$1.2 million. Partially offsetting these increases was a \$2.1 million decrease in new other equipment sales. The product line new equipment sales revenue fluctuations above do not include the impact of legacy CEC and Rental Inc. new equipment sales revenues by product line for the three month periods ended March 31, 2018 and June 30, 2018, respectively.

**Used Equipment Sales Revenues.** Our used equipment sales increased \$12.1 million, or 16.0%, to \$87.3 million for the nine month period ended September 30, 2018, from \$75.2 million for the same nine month period in 2017.

Sales of used aerial work platform equipment increased \$16.9 million, while sales of used cranes and used other equipment increased \$0.9 million and \$2.0 million, respectively. Partially offsetting these increases were decreases in sales of used earthmoving equipment and used lift trucks of \$7.5 million and \$0.7 million, respectively. The product line used equipment sales revenue fluctuations above do not include the impact of legacy CEC and Rental Inc. used equipment sales revenues by product line for the three month period ended March 31, 2018 and June 30, 2018, respectively.

**Parts Sales Revenues.** Our parts sales for the nine month period ended September 30, 2018 increased approximately \$3.7 million, or 4.2%, to approximately \$89.9 million from \$86.3 million for the same nine month period last year. The increase in parts sales was largely attributable to increases in aerial work platform equipment and earthmoving equipment parts sales, combined with parts sales revenues from our CEC and Rental Inc. locations.

**Services Revenues.** Our services revenues for the nine month period ended September 30, 2018 increased \$1.1 million, or 2.4%, to approximately \$48.3 million from approximately \$47.1 million for the same nine month period last year. The increase in services revenues was primarily due to services revenues from our CEC and Rental Inc. locations and an increase in earthmoving services revenues.

**Non-Segmented Other Revenues.** Our non-segmented other revenues consisted primarily of equipment support activities including fuel charges on rented equipment, transportation and hauling charges related to our equipment rental and maintenance and repair services, and damage waiver fees on rental equipment. For the nine month period ended September 30, 2018, our other revenues were approximately \$55.0 million, an increase of \$8.5 million, or 18.2%, from approximately \$46.6 million in the same nine month period in 2017. This increase was primarily driven by higher hauling revenues and damage waiver income associated with our equipment rental activities, combined with non-segmented other revenues from our CEC and Rental Inc. locations.

**Gross Profit (Loss).**

Nine Months Ended September 30, 2018	2017	Total Dollar Increase	Total Percentage Increase
--------------------------------------------	------	-----------------------------	---------------------------------

Edgar Filing: H&E Equipment Services, Inc. - Form 10-Q

(in thousands, except percentages)

Segment Gross Profit:					
Equipment rentals	\$210,246	\$166,783	\$43,463	26.1	%
New equipment sales	20,800	14,443	6,357	44.0	%
Used equipment sales	28,066	23,240	4,826	20.8	%
Parts sales	24,239	23,524	715	3.0	%
Services revenues	31,820	31,223	597	1.9	%
Non-Segmented revenues gross profit (loss)	247	(175 )	422	241.1	%
Total gross profit	\$315,418	\$259,038	\$56,380	21.8	%

Total Gross Profit. Our total gross profit was \$315.4 million for the nine month period ended September 30, 2018 compared to \$259.0 million for the same nine month period in 2018, an increase of \$56.4 million, or 21.8%. Total gross profit margin for the nine month period ended September 30, 2018 was 35.3%, an increase of 0.1% from the 35.2% gross profit margin for the same nine month period in 2017. Gross profit and gross margin for all reportable segments and non-segmented other revenues are further described below:



**Equipment Rentals Gross Profit.** Our gross profit from equipment rentals for the nine month period ended September 30, 2018 increased approximately \$43.5 million, or 26.1%, to approximately \$210.2 million from \$166.8 million in the same nine month period in 2017.

The increase in equipment rentals gross profit was the result of a \$77.9 million increase in equipment rental revenues for the nine month period ended September 30, 2018 compared to the same period last year, which was partially offset by a \$26.7 million increase in rental equipment depreciation expense and a \$7.8 million increase in rental expenses. The increases in both depreciation expense and rental expenses are primarily due to a larger fleet size in 2018 compared to 2017.

Gross profit margin on equipment rentals for the nine month period ended September 30, 2018 was approximately 49.0% compared to 47.5% for the same period in 2017, an increase of 1.5%. As a percentage of equipment rental revenues, rental expenses were 15.4% for the nine month period ended September 30, 2018 compared to 16.7% for the same period last year, a decrease of 1.3%, resulting primarily from the increase in equipment rental revenues. Depreciation expense was 35.6% of equipment rental revenues for the nine month period ended September 30, 2018 compared to 35.9% for the same period in 2017, a decrease of 0.3%, primarily as a result of the increase in equipment rental revenues, which was partially offset by the increase in depreciation expense resulting from the purchase accounting fair value step up adjustments on the CEC and Rental Inc. acquired rental fleets and the mix of our equipment rental fleet.

**New Equipment Sales Gross Profit.** Our new equipment sales gross profit for the nine month period ended September 30, 2018 increased approximately \$6.4 million, or 44.0%, to \$20.8 million compared to \$14.4 million for the same nine month period in 2017 on a total new equipment sales increase of \$54.4 million. Gross profit margin on new equipment sales was 11.3% for the nine month period ended September 30, 2018, compared to 11.2% for the same period last year, an increase of 0.1%. The slight increase in gross profit margin was primarily due to the mix of new equipment sold.

**Used Equipment Sales Gross Profit.** Our used equipment sales gross profit for the nine month period ended September 30, 2018 increased \$4.8 million, or 20.8%, to \$28.1 million from \$23.2 million in the same period in 2017 on a used equipment sales increase of \$12.1 million. Gross profit margin on used equipment sales for the nine month period ended September 30, 2018 was approximately 32.2%, up 1.3% from 30.9% for the same nine month period in 2017, primarily as a result of the mix of used equipment sold and higher used equipment margins on used aerial work platform equipment. These improved gross margins were partially offset by lower margins on sales of CEC and Rental Inc. used equipment, reflecting the purchase accounting fair value step up basis adjustment applied to the acquired used equipment inventory and rental equipment.

Our used equipment sales from the rental fleet, which comprised approximately 90.4% and 88.2% of our used equipment sales for the nine month periods ended September 30, 2018 and 2017, respectively, were approximately 153.9% and 150.3% of net book value for the nine month periods ended September 30, 2018 and 2017, respectively.

**Parts Sales Gross Profit.** Our parts sales gross profit for the nine month period ended September 30, 2018 increased \$0.7 million, or 3.0%, to \$24.2 million, compared to \$23.5 million for the same nine month period last year on a \$3.7 million increase in parts sales revenues. Gross profit margin for the nine month period ended September 30, 2018 was 27.0%, a decrease of 0.3% from 27.3% in the same nine month period in 2017, primarily as a result of the mix of parts sold.

**Services Revenues Gross Profit.** For the nine month period ended September 30, 2018, our services revenues gross profit increased \$0.6 million, or 1.9%, to \$31.8 million from \$31.2 million for the same nine month period in 2017 on a \$1.1 million increase in services revenues. Gross profit margin for the nine month period ended September 30, 2018

was 65.9%, a decrease of 0.4% from 66.3% in the same nine month period in 2017, as a result of services revenues mix.

**Non-Segmented Other Revenues Gross Profit (Loss).** Our non-segmented other revenues gross profit increased \$0.4 million, from a gross loss of \$0.2 million for the nine month period ended September 30, 2017 to a gross profit of \$0.2 million in the nine month period ended September 30, 2018. Gross margin for the nine month period ended September 30, 2018 was 0.4% compared to a gross margin of (0.4)% in the same nine month period last year, an increase of 0.8%, primarily reflective of improved gross margins on hauling and transportation related charges in the current period and improved gross margin on damage waiver income.

**Selling, General and Administrative Expenses (“SG&A”).** SG&A expenses increased approximately \$32.9 million, or approximately 19.1%, to \$205.3 million for the nine month period ended September 30, 2018 compared to \$172.3 million for the nine month period ended September 30, 2017.

The net increase in SG&A expenses was attributable to several factors. Employee salaries, wages, payroll taxes and related employee benefit and other employee expenses increased \$22.7 million, primarily as a result of our CEC and Rental Inc. acquisitions, a larger workforce and higher incentive compensation related to improved profitability. Legal and professional fees increased \$2.2

million and liability insurance costs increased \$0.6 million. Utilities costs increased \$1.4 million and promotional expenses increased \$0.7 million. Additionally, our results for the nine month period ended September 30, 2018 also includes \$2.4 million of amortization expense associated with the recognition of intangible assets resulting from the CEC and Rental Inc. purchase price allocations.

Approximately \$3.0 million of the total increase in SG&A expenses was attributable to branches opened since January 1, 2017 (but excluding for this purpose branches acquired as a result of our CEC and Rental Inc. acquisitions) with less than nine months of comparable operations in either or both of the nine month periods ended September 30, 2018 and 2017.

As a percentage of total revenues, SG&A expenses were 23.0% for the nine month period ended September 30, 2018 compared to 23.4% for the same nine month period last year, a decrease of 0.4%, and is largely reflective of the increase in total revenues and the cost increases noted above.

Merger Costs (net of Merger Breakup Fee Proceeds). Pursuant to the terms of our terminated 2017 merger agreement with Neff, we received a \$13.2 million breakup fee concurrently with Neff's termination of the merger agreement in the third quarter of 2017. Related estimated merger transaction fees totaled \$6.7 million, resulting in estimated net proceeds of \$6.5 million for the nine month period ended September 30, 2017. As noted in the above SG&A Expenses discussion, approximately \$2.2 million of the merger costs reflected in this financial statement line items were originally recorded in SG&A Expenses in the six month period ended June 30, 2017 and were subsequently reclassified in the third quarter ended September 30, 2017 to this merger breakup fee line item.

Merger costs incurred in the nine month period ended September 30, 2018 were approximately \$0.4 million.

Gain on Sales of Property and Equipment, Net. During the nine month period ended September 30, 2018, we sold a parcel of company-owned land and realized a gain of approximately \$3.7 million, resulting in total net gains on sales of property and equipment of \$6.0 million for the period, compared to \$4.4 million for the nine month period ended September 30, 2017, an increase of \$1.6 million.

Other Income (Expense). For the nine month period ended September 30, 2018, our net other expenses decreased approximately \$20.1 million to \$45.8 million compared to \$65.9 million for the same nine month period in 2017. Included in Other Income (Expense) for the three month period ended September 30, 2017 is a \$25.4 million loss on the early extinguishment of debt (see "Loss on Early Extinguishment of Debt" below).

Interest expense increased approximately \$5.4 million to \$47.1 million for the nine month period ended September 30, 2018 compared to \$41.7 million for the nine month period ended September 30, 2017. The increase in interest expense was due to additional interest costs of \$5.6 million associated with the upsize of our \$950 million 5.625% senior unsecured notes that were issued in the third and fourth quarters of 2017 compared to our \$630 million 7% senior unsecured notes, which were retired in the third quarter of 2017. Interest costs related to the Credit Facility decreased \$0.2 million for the nine month period ended September 30, 2018 compared to the same period last year.

Loss on Early Extinguishment of Debt. We recorded a one-time loss on the early extinguishment of debt in the three month period ended September 30, 2017 of approximately \$25.4 million, reflecting payment of \$12.8 million of tender premiums associated with our repurchase of the Old Notes and \$10.5 million of premiums in accordance with the indenture governing the Old Notes to redeem the remaining untendered Old Notes, combined with the write off of approximately \$2.0 million of unamortized note premium, unaccreted note discount and unamortized deferred financing costs, related to the Old Notes.

Income Taxes. We recorded income tax expense of \$18.3 million for the nine month period ended September 30, 2018 compared to income tax expense of approximately \$8.0 million for the nine month period ended September 30, 2017. Our effective income tax rate was approximately 26.2% for the nine month period ended September 30, 2018 compared to approximately 25.3% for the same nine month period last year, an increase of 0.9%.

We recognized a \$5.7 million discrete tax benefit in the nine month period ended September 30, 2017, resulting from a reversal of an unrecognized tax benefit due to expiration of statute of limitations. Our effective income tax rate for the nine month period ended September 30, 2018 was 26.2% compared to 25.3% for the same period last year. This effective income tax decrease was primarily due to the decrease in the federal statutory tax rate from 35% to 21%, resulting from the the Act, enacted in the fourth quarter of 2017. Our accounting for the income tax effects of the Act has been completed.

Based on available evidence, both positive and negative, we believe it is more likely than not that our federal deferred tax assets at September 30, 2018 are fully realizable through future reversals of existing taxable temporary differences and future taxable income, and are not subject to any limitations.

## Liquidity and Capital Resources

Cash flow from operating activities. For the nine month period ended September 30, 2018, the cash provided by our operating activities was \$138.0 million. Our reported net income of \$51.6 million, when adjusted for non-cash income and expense items, such as depreciation and amortization, deferred income taxes, net amortization (accretion) of note discount (premium), provision for losses on accounts receivable, provision for inventory obsolescence, stock-based compensation expense and net gains on the sale of long-lived assets, provided positive cash flows of \$215.5 million. These cash flows from operating activities were also positively impacted by a \$4.5 million increase in manufacturing flooring plans payable and a \$0.2 million decrease in prepaid expenses and other assets. Partially offsetting these positive cash flows were a \$56.4 million increase in inventories, a \$10.1 million decrease in accounts payable, a \$9.0 million decrease in accrued expenses payable and other liabilities and a \$6.8 increase in receivables.

For the nine month period ended September 30, 2017, the net cash provided by our operating activities was \$156.4 million. Our reported net income of \$23.7 million, when adjusted for non-cash income and expense items, such as depreciation and amortization, deferred income taxes, net amortization (accretion) of note discount (premium), provision for losses on accounts receivable, provision for inventory obsolescence, stock-based compensation expense, loss on early extinguishment of debt, and net gains on the sale of long-lived assets, provided positive cash flows of approximately \$181.1 million. These cash flows from operating activities were also positively impacted by a \$42.1 million increase in accounts payable. Partially offsetting these positive cash flows were a \$38.9 million increase in inventories, a \$15.8 million increase in receivables, and a \$7.5 million decrease in manufacturing flooring plans payable, while accrued expenses payable and other liabilities decreased \$3.1 million and prepaid expenses and other assets increased \$1.6 million.

Cash flow from investing activities. For the nine month period ended September 30, 2018, our cash provided by our investing activities was exceeded by our cash used in our investing activities, resulting in net cash used in our investing activities of approximately \$486.8 million. The acquisitions of CEC and Rental Inc. totaled \$196.0 (net of cash acquired). Purchases of rental and non-rental equipment totaling \$377.7 million and proceeds from the sale of rental and non-rental equipment of approximately \$86.9 million.

For the nine month period ended September 30, 2017, the cash provided by our investing activities was exceeded by cash used in our investing activities, resulting in net cash used in our investing activities of \$126.7 million. This was a result of purchases of rental and non-rental equipment totaling \$199.8 million and proceeds from the sale of rental and non-rental equipment of approximately \$73.1 million.

Cash flow from financing activities. For the nine month period ended September 30, 2018, cash provided by our financing activities was \$188.0 million. Net borrowings under our Credit Facility for the nine month period ended September 30, 2018 were \$219.0 million, which was partially offset by dividends paid totaling \$29.4 million, or \$0.825 per common share. Treasury stock purchases totaled \$1.3 million. Payments on capital lease obligations were \$0.2 million and payments of deferred financing costs were \$0.1 million.

For the nine month period ended September 30, 2017, the cash provided by our financing activities was exceeded by our cash used in our financing activities, resulting in net cash used in our financing activities of approximately \$31.2 million. Dividends totaling approximately \$29.4 million, or \$0.825 per common share, were paid during the nine month period ended September 30, 2017. Net payments under the Credit Facility were \$85.4 million. Payments on capital lease obligations were \$0.2 million. In connection with the redemption of our Old Notes, we paid \$653.3 million, representing aggregate principal payments of \$630.0 million and tender and redemption premiums totaling approximately \$23.3 million. In connection with the issuance of our New Notes, net proceeds after deducting underwriting expenses of \$10.3 million, were \$739.7 million. Other transaction costs related to the New Notes were approximately \$1.6 million.

Senior Secured Credit Facility

We and our subsidiaries are parties to a \$750.0 million Credit Facility with Wells Fargo Capital Finance, LLC (as successor to General Electric Capital Corporation) as administrative agent, and the lenders named therein.

On December 22, 2017, we amended, extended and restated the Credit Facility by entering into the Fifth Amended and Restated Credit Agreement (the “Amended and Restated Credit Agreement”) by and among the Company, Great Northern Equipment, Inc., H&E Equipment Services (California), LLC, the other credit parties named therein, the lenders named therein, Wells Fargo Capital Finance, LLC, as administrative agent, the other credit parties named therein, the lenders named therein, and the joint lead arrangers, joint book runners, co-syndication agents and documentation agent named therein.

The Amended and Restated Credit Agreement, among other things, (i) extends the maturity date of the Credit Facility from May 21, 2019 to December 22, 2022, (ii) increases the commitments under the senior secured asset based revolver provided for

therein from \$602.5 million to \$750 million, (iii) increases the uncommitted incremental revolving capacity from \$150 million to \$250 million, (iv) provides that the unused line fee margin will be either 0.375% or 0.25%, depending on the Average Revolver Usage (as defined in the Amended and Restated Credit Agreement) of the borrowers, (v) lowers the interest rate (a) in the case of base rate revolving loans, to the base rate plus an applicable margin of 0.50% to 1.00% depending on the Average Availability (as defined in the Amended and Restated Credit Agreement) and (b) in the case of LIBOR revolving loans, to LIBOR (as defined in the Amended and Restated Credit Agreement) plus an applicable margin of 1.50% to 2.00%, depending on the Average Availability, (vi) lowers the margin applicable to the letter of credit fee to between 1.50% and 2.00%, depending on the Average Availability, and (vii) permits, subject to certain conditions, an unlimited amount of Permitted Acquisitions, Restricted Payments and prepayments of Indebtedness (in each case, as defined in the Amended and Restated Credit Agreement).

The Amended and Restated Credit Agreement continues to provide for, among other things, a \$30 million letter of credit sub-facility, and a guaranty by certain of the Company's subsidiaries of the obligations under the Credit Facility. In addition, the Credit Facility remains secured by substantially all of the assets of the Company and certain of its subsidiaries.

At September 30, 2018, we had total borrowings under the Credit Facility of \$219.0 million and we could borrow up to \$523.3 million and remain in compliance with the debt covenants under the Credit Facility. At October 18, 2018, we had \$532.4 million of available borrowings under our Credit Facility, net of a \$7.7 million outstanding letter of credit.

#### Cash Requirements Related to Operations

Our principal sources of liquidity have been from cash provided by operating activities and the sales of new, used and rental fleet equipment, proceeds from the issuance of debt, and borrowings available under the Credit Facility. Our principal uses of cash have been to fund operating activities and working capital (including new and used equipment inventories), purchases of rental fleet equipment and property and equipment, fund payments due under facility operating leases and manufacturer flooring plans payable, and to meet debt service requirements. In the future, we may pursue additional strategic acquisitions and seek to open new start-up locations. We anticipate that the above described uses will be the principal demands on our cash in the future.

The amount of our future capital expenditures will depend on a number of factors including general economic conditions and growth prospects. Our gross rental fleet capital expenditures for the nine month period ended September 30, 2018 were approximately \$374.5 million, including \$23.9 million of non-cash transfers from new and used equipment to rental fleet inventory. Our gross property and equipment capital expenditures for the nine month period ended September 30, 2018 were \$27.0 million. In response to changing economic conditions, we believe we have the flexibility to modify our capital expenditures by adjusting them (either up or down) to match our actual performance.

To service our debt, we will require a significant amount of cash. Our ability to pay interest and principal on our indebtedness (including the Credit Facility, the Senior Notes and our other indebtedness), will depend upon our future operating performance and the availability of borrowings under the Credit Facility and/or other debt and equity financing alternatives available to us, which will be affected by prevailing economic conditions and conditions in the global credit and capital markets, as well as financial, business and other factors, some of which are beyond our control. Based on our current level of operations and given the current state of the capital markets, we believe our cash flow from operations, available cash and available borrowings under the Credit Facility will be adequate to meet our future liquidity needs for the foreseeable future. As of October 18, 2018, we had \$532.4 million of available

borrowings under the Credit Facility, net of \$7.7 million of outstanding letters of credit.

We cannot provide absolute assurance that our future cash flow from operating activities will be sufficient to meet our long-term obligations and commitments. If we are unable to generate sufficient cash flow from operating activities in the future to service our indebtedness and to meet our other commitments, we will be required to adopt one or more alternatives, such as refinancing or restructuring our indebtedness, selling material assets or operations or seeking to raise additional debt or equity capital. Given current economic and market conditions, including the significant disruptions in the global capital markets, we cannot assure investors that any of these actions could be effected on a timely basis or on satisfactory terms or at all, or that these actions would enable us to continue to satisfy our capital requirements. In addition, our existing debt agreements, including the Credit Facility and the indenture governing the Senior Notes, as well as any future debt agreements, contain or may contain restrictive covenants, which may prohibit us from adopting any of these alternatives. Our failure to comply with these covenants could result in an event of default which, if not cured or waived, could result in the acceleration of all of our debt.

#### Quarterly Dividend

On August 8, 2018, the Company announced a quarterly dividend of \$0.275 per share to stockholders of record, which was paid on September 7, 2018, totaling approximately \$9.8 million. The Company intends to continue to pay regular quarterly cash dividends;



however, the declaration of any subsequent dividends is discretionary and will be subject to a final determination by the Board of Directors each quarter after its review of, among other things, business and market conditions.

#### Seasonality

Although we believe our business is not materially impacted by seasonality, the demand for our rental equipment tends to be lower in the winter months. The level of equipment rental activities is directly related to commercial and industrial construction and maintenance activities. Therefore, equipment rental performance will be correlated to the levels of current construction activities. The severity of weather conditions can have a temporary impact on the level of construction activities. Adverse weather has a seasonal impact in parts of the markets we serve, including our Intermountain region, particularly in the winter months.

Equipment sales cycles are also subject to some seasonality with the peak selling period during the spring season and extending through the summer. Parts and services activities are typically less affected by changes in demand caused by seasonality.

#### Contractual and Commercial Commitments

There have been no material changes from the information included in our Annual Report on Form 10-K for the year ended December 31, 2017.

#### Off-Balance Sheet Arrangements

There have been no material changes from the information included in our Annual Report on Form 10-K for the year ended December 31, 2017.

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

Our earnings may be affected by changes in interest rates since interest expense on the Credit Facility is currently calculated based upon the index rate plus an applicable margin of 0.50% to 1.00%, depending on the Average Availability (as defined in the Credit Facility), in the case of index rate revolving loans and LIBOR plus an applicable margin of 1.50% to 2.00%, depending on the Average Availability (as defined in the Credit Facility), in the case of LIBOR revolving loans. At September 30, 2018, we had outstanding borrowings under the Credit Facility totaling \$219.0 million. A 1.0% increase in the interest rate on the Credit Facility would result in an increase of approximately \$2.2 million in interest expense on an annualized basis. At October 18, 2018, we had borrowings outstanding totaling \$209.8 million, with \$532.4 million of available borrowings, net of \$7.7 million of outstanding letters of credit. We did not have significant exposure to changing interest rates as of September 30, 2018 on the fixed-rate senior unsecured notes. Historically, we have not engaged in derivatives or other financial instruments for trading, speculative or hedging purposes, though we may do so from time to time if such instruments are available to us on acceptable terms and prevailing market conditions are accommodating.

Item 4. Controls and Procedures

Management's Quarterly Evaluation of Disclosure Controls and Procedures

We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed in the reports that the Company files or furnishes under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to the Company's management, including its Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required financial disclosure.

Our Chief Executive Officer and Chief Financial Officer (our principal executive officer and principal financial officer, respectively) have evaluated the effectiveness of our disclosure controls and procedures (as defined in Rule 13a-15(e) and 15d-15(e) promulgated under the Securities Exchange Act of 1934, as amended) as of the end of the period covered by this Quarterly Report on Form 10-Q. Based on this evaluation, our principal executive officer and principal financial officer have concluded that, as of September 30, 2018, our current disclosure controls and procedures were effective.

The design of any system of control is based upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated objectives under all future events, no matter how remote, or that the degree of compliance with the policies or procedures may not deteriorate. Because of its inherent limitations, disclosure controls and procedures may not prevent or detect all misstatements. Accordingly, even effective disclosure controls and procedures can only provide reasonable assurance of achieving their control objectives.

Changes in Internal Control Over Financial Reporting

There were no changes in the Company's internal control over financial reporting (as defined in Exchange Act Rule 13a-15(f)) that occurred during the quarter ended September 30, 2018 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

## PART II. OTHER INFORMATION

### Item 1. Legal Proceedings.

From time to time, we are involved in various claims and legal actions arising in the ordinary course of our business. In the opinion of management, after consultation with legal counsel, the ultimate disposition of these various matters will not have a material adverse effect on the Company's consolidated financial position, results of operations or liquidity.

### Item 1A. Risk Factors.

In addition to the other information set forth in this Quarterly Report on Form 10-Q, you should carefully consider the factors discussed in Part I, Item 1A - "Risk Factors," in our Annual Report on Form 10-K for the year ended December 31, 2017, which could materially affect our business, financial condition or future results.

As of the date of this Quarterly Report on Form 10-Q, there have been no material changes with respect to the Company's risk factors previously disclosed on Form 10-K for the year ended December 31, 2017.

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

On August 1, 2018, 37,037 shares of non-vested stock that were issued in 2017 vested at \$35.85 per share. Certain holders of those vested shares returned an aggregate of 10,891 shares of common stock to the Company during the quarter ended September 30, 2018 as payment for their respective withholding taxes. This resulted in an addition of 10,891 shares to treasury stock.

On August 1, 2018, 38,583 shares of non-vested stock that were issued in 2016 vested at \$35.85 per share. Certain holders of those vested shares returned an aggregate of 11,274 shares of common stock to the Company during the quarter ended September 30, 2018 as payment for their respective withholding taxes. This resulted in an addition of 11,274 shares to treasury stock.

On August 3, 2018, 45,758 shares of non-vested stock that were issued in 2015 vested at \$35.78 per share. Certain holders of those vested shares returned an aggregate of 14,764 shares of common stock to the Company during the quarter ended September 30, 2018 as payment for their respective withholding taxes. This resulted in an addition of 14,764 shares to treasury stock.

Item 3. Defaults upon Senior Securities.

None.

Item 4. Mine Safety Disclosures.

Not applicable.

Item 5. Other Information.

None.

50

---

Item 6. Exhibits.

- 31.1 Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (filed herewith).
- 31.2 Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (filed herewith).
- 32.1 Certification pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (furnished herewith).
  
- 101.INS XBRL Instance Document (filed herewith).
- 101.SCH XBRL Taxonomy Extension Schema Document (filed herewith).
- 101.CAL XBRL Taxonomy Extension Calculation Linkbase Document (filed herewith).
- 101.DEF XBRL Taxonomy Extension Definition Linkbase Document (filed herewith).
- 101.LAB XBRL Taxonomy Extension Label Linkbase Document (filed herewith).
- 101.PRE XBRL Taxonomy Extension Presentation Linkbase Document (filed herewith).

SIGNATURES

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

H&E EQUIPMENT SERVICES, INC.

Dated: October 25, 2018 By: /s/ John M. Engquist

John M. Engquist

Chief Executive Officer

(Principal Executive Officer)

Dated: October 25, 2018 By: /s/ Leslie S. Magee

Leslie S. Magee

Chief Financial Officer and Secretary

(Principal Financial and Accounting Officer)