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BIOMET INC
Form 10-Q
October 11, 2005

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

FORM 10-Q

(Mark One)

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

For the quarterly period ended August 31, 2005.

OR

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

For the transition period from _____ to _____.

Commission file Number 0-12515.

BIOMET, INC.
(Exact name of registrant as specified in its charter)

Indiana
(State or other jurisdiction of
incorporation or organization)

35-1418342
(I.R.S. Employer
Identification No.)

56 East Bell Drive, Warsaw, Indiana 46582
(Address of principal executive offices)

(574) 267-6639
(Registrant's telephone number, including area code)

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

Indicate by check mark whether the registrant is an accelerated filer (as
described in Rule 12b-2 of the Exchange Act). Yes X No

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

As of August 31, 2005, the registrant had 249,077,173 common shares
outstanding.

BIOMET, INC.

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PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

BIOMET, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

at August 31, 2005 and May 31, 2005

(in thousands)

ASSETS

	August 31, 2005	May 31, 2005
	-----	-----
	(Unaudited)	
Current assets:		
Cash and cash equivalents	\$ 124,393	\$ 104,706
Investments	7,978	10,962
Accounts and notes receivable, net	455,821	479,745
Inventories	471,659	469,791
Deferred income taxes	73,607	72,732
Prepaid expenses and other	37,017	35,980
	-----	-----
Total current assets	1,170,475	1,173,916
	-----	-----
Property, plant and equipment, at cost	583,039	574,398
Less, Accumulated depreciation	256,219	251,511
	-----	-----
Property, plant and equipment, net	326,820	322,887
	-----	-----
Investments	61,252	61,406
Goodwill	432,255	435,621
Intangible assets, net	85,772	87,835
Other assets	15,830	14,912
	-----	-----
Total assets	\$2,092,404	\$2,096,577

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The accompanying notes are a part of the consolidated financial statements.

BIOMET, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS
at August 31, 2005 and May 31, 2005
(in thousands)

LIABILITIES AND SHAREHOLDERS' EQUITY

	August 31, 2005	May 31, 2005
	-----	-----
	(Unaudited)	
Current liabilities:		
Short-term borrowings	\$ 286,036	\$ 282,193
Accounts payable	55,067	57,021
Accrued income taxes	36,390	9,725
Accrued wages and commissions	53,450	62,171
Other accrued expenses	87,432	90,281
	-----	-----
Total current liabilities	518,375	501,391
Long-term liabilities:		
Deferred income taxes	29,819	31,255
	-----	-----
Total liabilities	548,194	532,646
	-----	-----
Contingencies		
Shareholders' equity:		
Common shares	190,235	188,162
Additional paid-in capital	67,760	67,613
Retained earnings	1,288,268	1,284,905
Accumulated other comprehensive income	(2,053)	23,251
	-----	-----
Total shareholders' equity	1,544,210	1,563,931
	-----	-----
Total liabilities and shareholders' equity	\$2,092,404	\$2,096,577
	=====	=====

The accompanying notes are a part of the consolidated financial statements.

BIOMET, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF INCOME
for the three months ended August 31, 2005 and 2004
(Unaudited, in thousands, except per share data)

	2005	2004
	----	----
Net sales	\$484,903	\$438,160
Cost of sales	134,495	125,972
	-----	-----
Gross profit	350,408	312,188
Selling, general and administrative expenses	178,182	160,460

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Research and development expense	20,816	18,476
In-process research and development	--	26,020
	-----	-----
Operating income	151,410	107,232
Other income (expense), net	558	(728)
	-----	-----
Income before income taxes	151,968	106,504
Provision for income taxes	51,669	46,071
	-----	-----
Net income	\$100,299	\$ 60,433
	=====	=====
Earnings per share:		
Basic	\$.40	\$.24
	=====	=====
Diluted	\$.40	\$.24
	=====	=====
Shares used in the computation of earnings per share:		
Basic	249,582	253,856
	=====	=====
Diluted	250,656	255,950
	=====	=====
Cash dividends per common share	\$.25	\$.20
	=====	=====

The accompanying notes are a part of the consolidated financial statements.

BIOMET, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
for the three months ended August 31, 2005 and 2004
(Unaudited, in thousands)

	2005	2004
	----	----
Cash flows from (used in) operating activities:		
Net income	\$100,299	\$ 60,433
Adjustments to reconcile net income to net cash from operating activities:		
Depreciation	15,277	14,044
Amortization	2,236	1,521
Write off of in-process research and development	--	26,020
Gain (loss) on sale of investments, net	(47)	282
Deferred income taxes	(1,425)	(2,671)
Changes in current assets and liabilities, excluding effects of acquisitions:		
Accounts and notes receivable, net	15,276	30,871
Inventories	(15,201)	(7,755)
Prepaid expenses	(4,547)	(5,341)
Accounts payable	3,034	(3,777)
Accrued income taxes	23,633	19,452
Other current liabilities	(6,705)	(14,179)
	-----	-----
Net cash from operating activities	131,830	118,900
	-----	-----
Cash flows from (used in) investing activities:		
Proceeds from sales and maturities of investments	11,854	8,602
Purchases of investments	(8,454)	(8,616)
Capital expenditures	(25,984)	(18,616)
Acquisitions, net of cash acquired	--	(266,229)
Other	247	(2,357)

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	-----	-----
Net cash used in investing activities	(22,337)	(287,216)
	-----	-----
Cash flows from (used in) financing activities:		
Increase in short-term borrowings, net	6,823	201,770
Issuance of common shares	2,798	6,312
Cash dividends	(62,473)	(50,872)
Purchase of common shares	(35,447)	(64,985)
	-----	-----
Net cash from (used in) financing activities	(88,299)	92,225
	-----	-----
Effect of exchange rate changes on cash	(1,507)	(1,437)
	-----	-----
Decrease in cash and cash equivalents	19,687	(77,528)
Cash and cash equivalents, beginning of year	104,706	159,243
	-----	-----
Cash and cash equivalents, end of period	\$124,393	\$ 81,715
	=====	=====

The accompanying notes are a part of the consolidated financial statements.

BIOMET, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1: BASIS OF PRESENTATION.

The accompanying consolidated financial statements include the accounts of Biomet, Inc. and its subsidiaries (individually and collectively referred to as the "Company"). The unaudited consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, they do not include all of the information and notes required by U.S. generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for the three-month period ended August 31, 2005 are not necessarily indicative of the results that may be expected for the fiscal year ending May 31, 2006. For further information, refer to the consolidated financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the fiscal year ended May 31, 2005.

The accompanying consolidated balance sheet at May 31, 2005, has been derived from the audited Consolidated Financial Statements at that date, but does not include all disclosures required by U.S. generally accepted accounting principles.

The Company operates in one business segment, musculoskeletal products, which includes the designing, manufacturing and marketing of reconstructive products, fixation devices, spinal products and other products. Other products consist primarily of EBI's softgoods and bracing products, Arthrotek's arthroscopy products, general instruments and operating room supplies. The Company manages its business segment primarily on a geographic basis. These geographic markets are comprised of the United States, Europe and the Rest of World. Major markets included in the Rest of World geographic market are Canada, South America, Mexico, Japan and the Pacific Rim.

Net sales of musculoskeletal products by product category are as follows for the three months ended August 31, 2005 and 2004:

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	2005	2004
	----	----
	(in thousands)	
Reconstructive Products	\$323,815	\$282,482
Fixation Devices	64,179	62,713
Spinal Products	55,326	52,909
Other Products	41,583	40,056
	-----	-----
Total	\$484,903	\$438,160
	=====	=====

As permitted by SFAS No. 123, the Company accounts for its employee stock options using the intrinsic value method. Accordingly, no compensation expense is recognized for the employee stock-based compensation plans. If compensation expense for the Company's employee stock options had been determined based on the fair value method of accounting, pro forma net income and diluted earnings per share for the three months ended August 31, 2005 and 2004 would have been as follows:

	2005	2004
	----	----
Net income as reported (in thousands)	\$100,299	\$ 60,433
Deduct: Total stock-based employee compensation expense determined under the fair value method for all awards net of related tax effects (in thousands)	2,149	1,533
	-----	-----
Pro forma net income (in thousands)	\$ 98,150	\$ 58,900
	=====	=====
Earning per share:		
Basic, as reported	\$0.40	\$0.24
	=====	=====
Basic, pro forma	\$0.39	\$0.23
	=====	=====
Diluted, as reported	\$0.40	\$0.24
	=====	=====
Diluted, pro forma	\$0.39	\$0.23
	=====	=====

In December 2004, the FASB issued SFAS No. 123(R), "Share-Based Payment", which is a revision to SFAS No. 123, "Accounting for Stock Based Compensation". SFAS 123(R) requires all share-based payments to employees, including stock options, to be expensed based on their fair values over the required award service period. Although it is difficult to predict the exact impact the adoption of SFAS 123(R) will have on the Company's consolidated earnings due to the number of variables involved, we believe the above pro forma disclosures provide an appropriate indicator of the level of expense that may be recognized upon adoption of the statement. The SEC has amended the compliance dates of SFAS 123(R) requiring adoption in the first fiscal year beginning after June 15, 2005. The Company intends to adopt SFAS 123(R) on June 1, 2006.

NOTE 2: COMPREHENSIVE INCOME.

Other comprehensive income (loss) includes foreign currency translation adjustments and unrealized appreciation of available-for-sale securities, net of taxes. Other comprehensive income (loss) for the three months ended August 31, 2005 and 2004 was \$(25,304,000) and \$1,462,000, respectively. Total comprehensive income combines reported net income and other comprehensive income (loss). Total comprehensive income for the three months ended August 31, 2005 and 2004 was \$74,995,000 and \$61,895,000, respectively.

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NOTE 3: INVENTORIES.

Inventories at August 31, 2005 and May 31, 2005 are as follows:

	August 31, 2005	May 31, 2005
	-----	-----
	(in thousands)	
Raw materials	\$ 50,329	\$ 50,676
Work-in-process	55,842	56,610
Finished goods	206,512	200,041
Consigned distributor	158,976	162,464
	-----	-----
	\$471,659	\$469,791
	=====	=====

NOTE 4: COMMON SHARES.

During the three months ended August 31, 2005, the Company issued 155,864 Common Shares upon the exercise of outstanding stock options for proceeds aggregating \$2,798,000. Purchases of Common Shares pursuant to the Common Share Repurchase Programs aggregated 957,400 shares for \$35,447,000 during the three months ended August 31, 2005.

NOTE 5: EARNINGS PER SHARE.

Earnings per common share amounts ("basic EPS") are computed by dividing net income by the weighted average number of common shares outstanding and excludes any potential dilution. Earnings per common share amounts assuming dilution ("diluted EPS") are computed by reflecting potential dilution from the exercise of stock options.

NOTE 6: INCOME TAXES.

The difference between the reported provision for income taxes and a provision computed by applying the federal statutory rate to pre-tax accounting income is primarily attributable to state income taxes, tax benefits relating to operations in Puerto Rico, tax-exempt income, tax credits and the in-process research and development which is not tax affected.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL
CONDITION AND RESULTS OF OPERATIONS

FINANCIAL CONDITION AS OF August 31, 2005

The Company's cash and investments increased \$16,549,000 to \$193,623,000 at August 31, 2005. This increase resulted from positive cash flow from operations offset by the \$62,473,000 dividend paid during this quarter and the \$35,447,000 used to purchase shares during this quarter pursuant to the Company's share repurchase programs.

Cash flows provided by operating activities were \$131,830,000 for the first three months of fiscal 2006 compared to \$118,900,000 in 2005. The primary sources of fiscal year 2006 cash flows from operating activities were net income, depreciation, a decrease in accounts receivable and an increase in accrued income taxes. The primary use was an increase in inventories. Accounts receivable normally decreases in Europe during the summer months as sales decrease slightly due to the vacation period, but cash receipts

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continue. Accrued income taxes increased during the quarter due to the first quarter tax estimates being due after the quarter end. Inventories increased primarily as a result of new product introductions (specifically in Europe for the Oxford and Vanguard Knee Systems and the Company's new bone cement products). Accounts and notes receivable and inventory balances decreased during the three month period by \$8.6 million and \$13.3 million, respectively, due to currency exchange rates.

Cash flows used in investing activities were \$22,337,000 for the first three months of fiscal 2006 compared to \$287,216,000 in 2005. The primary use of cash flows from investing activities in fiscal 2006 was capital expenditures. The Company continues to upgrade its instruments used in various international markets and to support the new implant systems being launched. In addition, 3i is currently expanding its manufacturing facilities in Florida.

Cash flows used in financing activities were \$88,299,000 for the first three months of fiscal 2006 compared to source of \$92,225,000 in 2005. The primary uses were the cash dividend paid and the share repurchase programs. In July 2005, the Company's Board of Directors declared a cash dividend of twenty five cents (\$0.25) per share payable to shareholders of record at the close of business on July 15, 2005. Over the last eleven quarters, the Company has used \$877,000,000 to purchase its common stock.

Currently available funds, together with anticipated cash flows generated from future operations are believed to be adequate to cover the Company's anticipated cash requirements, including capital expenditures, research and development costs and share repurchases.

RESULTS OF OPERATIONS FOR THE THREE MONTHS ENDED AUGUST 31, 2005 AS COMPARED TO THE THREE MONTHS ENDED AUGUST 31, 2004

Net sales increased 11% to \$484,903,000 for the first quarter ended August 31, 2005, from \$438,160,000 for the same period last year. Excluding the positive impact of foreign currency, net sales growth for the first quarter was 10%. The Company's U.S.-based revenue increased 7% to \$317,326,000 during the first quarter of fiscal 2006, while foreign sales increased 18% to \$167,577,000. Excluding the positive foreign exchange adjustment, foreign revenue increased 16%. The Company's worldwide sales of reconstructive products during the first quarter of fiscal 2006 were \$323,815,000, representing a 15% increase compared to the first quarter of last year. This increase came through balanced growth in all of the reconstructive product categories. Sales of fixation products were \$64,179,000 for the first quarter of fiscal 2006, representing a 2% increase as compared to the same period in fiscal 2005. Sales of spinal products were \$55,326,000 for the first quarter of fiscal 2006, representing a 5% increase as compared to the same period in fiscal 2005. Fixation and spinal product sales have been negatively impacted by the combination of the Interpore and EBI sales forces, and at the same time the integration of Biomet's internal fixation sales force into EBI's fixation sales force. During the fourth quarter of last year and the first quarter of this year, EBI has introduced several new products in both the internal fixation and spinal implant markets that we believe will have a positive impact on sales in the future. In addition, during the first quarter, the Company announced the appointment of Bart Doedens, M.D. as the new president of EBI's operations following the resignation of James R. Pastena. EBI's fixation, spinal stimulation and softgoods and bracing products have continued to underperform management's expectations and it is hoped that Dr. Doedens will provide the leadership necessary to improve EBI's performance in these markets. The Company's sales of other products totaled \$41,583,000, representing a 4% increase over the first quarter of fiscal year 2005.

Cost of sales decreased as a percentage of net sales to 27.7%, for the first quarter of fiscal 2006 from 28.7% during the same period last year. After

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adjusting for last year's impact of inventory step-up relating to acquisitions, cost of sales as a percentage of net sales increased from 27.2%. This increase was primarily a result of higher growth rates in foreign sales, where gross margins are lower, versus domestic sales. Selling, general and administrative expenses, as a percentage of net sales, increased to 36.7% compared to 36.6% for the first quarter last year. Research and development expenditures increased 13% during the first quarter to \$20,816,000 reflecting the Company's continued emphasis on new product introductions. Operating income increased 41% from \$107,232,000 for the first quarter of fiscal 2005, to \$151,410,000 for the first quarter of fiscal 2006. After adjusting operating income for prior year's acquisition related expenses of \$33,022,000, operating income increased 8%. Other income increased from \$(728,000) last year to \$558,000 this year. Other income has been positively impacted by an increase in cash available for investments and an increase in interest rates. The effective income tax rate decreased to 34.0% for the first quarter of fiscal year 2006 from 43.3% last year primarily as a result of the write-off of in-process research and development last year not being tax affected.

These factors resulted in a 66% increase in net income to \$100,299,000 for the first quarter of fiscal 2006 as compared to \$60,433,000 for the same period in fiscal 2005, while basic and diluted earnings per share increased 67%, from \$0.24 to \$0.40 for the periods presented. Before acquisition related expenses last year, net income increased by 10%, while basic and diluted earnings per share increased 11% for the periods presented.

Item 3. Quantitative and Qualitative Disclosures about Market Risks.

There have been no material changes from the information provided in the Company's Annual Report on Form 10-K for the year ended May 31, 2005.

Item 4. Controls and Procedures.

(a) Evaluation of Disclosure Controls and Procedures. As of the end of the period covered by this report, the Company carried out an evaluation, under the supervision and with the participation of its management, including the Company's Chief Executive Officer and Chief Financial Officer, of the effectiveness of the Company's disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934). Based on this evaluation, the Company's Chief Executive Officer and Chief Financial Officer have concluded that the Company's disclosure controls and procedures are effective in timely notification to them of information the Company is required to disclose in its periodic SEC filings and in ensuring that this information is recorded, processed summarized and reported within the time periods specified in the SEC's rules and regulations.

(b) Changes in Internal Control. During the first quarter of fiscal 2006, there were no changes in internal control over financial reporting that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II. OTHER INFORMATION

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

(c) Stock Repurchases

As of August 31, 2005, the Company had two publicly-announced share repurchase programs outstanding. The first, announced March 22, 2005, approved the purchase of shares up to \$100 million in open market or privately negotiated transactions expiring March 21, 2006. The second, announced June 30, 2005, approved the purchase of 2,500,000 shares to be automatically purchased in equal installments over a twelve-month period expiring June 29, 2006. Information on

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shares repurchased in the most recently completed quarter is as follows:

Period	Total Number of shares Purchased	Average Price Paid Per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans	Maximum Number of Shares (or Approximate Dollar Value) that May Yet be Purchased Under the Plans
June 1-30	None	\$ --	None	\$78,031,085
July 1-31	727,400	36.92	727,400	2,310,000 shares and \$58,049,629
August 1-31	230,000	37.36	230,000	2,080,000 shares and \$58,049,629
Total	957,400	37.02	957,400	2,080,000 shares and \$58,049,629

Item 4. Submission of Matters to a Vote of Security Holders.

The Annual Meeting of Shareholders of the Company was held on September 23, 2005. At the Annual Meeting:

1. The following persons were elected as Directors of the Company for a three-year term expiring in 2008.

Name	Votes For	Votes Withheld
C. Scott Harrison, M.D.	211,225,212	9,334,357
Sandra A. Lamb	216,518,600	4,040,969
Niles L. Noblitt	212,811,357	7,748,212
Kenneth V. Miller	214,054,484	6,505,085
Marilyn Tucker Quayle	213,972,260	6,587,309

The following directors will continue in office until their term expires at the 2006 Annual Meeting of shareholders: Dane A. Miller, Ph. D.; Jerry L. Ferguson; Thomas F. Kearns, Jr.; and Daniel P. Hann.

The following directors will continue in office until their term expires at the 2007 Annual meeting of shareholders: M. Ray Harroff; Jerry L. Miller; Charles E. Niemier; and L. Gene Tanner.

2. The amendment to the Biomet, Inc. 1998 Qualified and Non-Qualified Stock Option Plan to increase by 5,000,000 Common Shares the number of Common Shares available for grant under the Plan was ratified by the shareholders as follows: Votes For - 163,221,320; Votes Against - 778,825; and Abstentions and Broker Non-Votes - 1,337,968.

3. The appointment of Ernst & Young LLP as independent accountants for the Company for the fiscal year ending May 31, 2006 was ratified by the shareholders, as follows: Votes For - 218,442,776; Votes Against - 778,825; and Abstentions and Broker Non-Votes - 1,337,968.

Item 6. Exhibits and Reports on Form 8-K

(a) Exhibits. See Index to Exhibits.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the

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registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

BIOMET, INC.

DATE: 10/10/2005

BY: /s/ Gregory D. Hartman

Gregory D. Hartman
Senior Vice President - Finance
(Principal Financial Officer)

(Signing on behalf of the registrant
and as principal financial officer)

BIOMET, INC.

FORM 10-Q

INDEX TO EXHIBITS

Exhibits.	Descriptions.
31.1	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Written Statement of Chief Executive Officer and Chief Financial Officer Pursuant to Sections 906 of the Sarbanes-Oxley Act of 2002.