

Edgar Filing: BIOMET INC - Form 10-Q

BIOMET INC
Form 10-Q
January 14, 2002

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 November 30, 2001.

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)

(219) 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 the past 90 days. Yes No

As of November 30, 2001, the registrant had 270,030,630 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 November 30, 2001 and May 31, 2001
(in thousands)

ASSETS

| | November 30, 2001 | May 31, 2001 |
|---|----------------------|-----------------|
| | ----- | ----- |
| | (Unaudited) | |
| Current assets: | | |
| Cash and cash equivalents | \$ 247,123 | \$ 235,091 |
| Investments | 35,455 | 52,627 |
| Accounts and notes receivable, net | 332,013 | 324,848 |
| Inventories | 309,008 | 277,601 |
| Deferred income taxes | 44,334 | 48,982 |
| Prepaid expenses and other | 25,186 | 29,230 |
| | ----- | ----- |
| Total current assets | 993,119 | 968,379 |
| | ----- | ----- |
| Property, plant and equipment, at cost | 360,789 | 325,890 |
| Less, Accumulated depreciation | 156,619 | 140,139 |
| | ----- | ----- |
| Property, plant and equipment, net | 204,170 | 185,751 |
| | ----- | ----- |
| Investments | 210,346 | 175,430 |
| Intangible assets, net | 7,915 | 8,848 |
| Excess acquisition costs over fair value of acquired net assets, net | 130,017 | 134,835 |
| Other assets | 17,052 | 16,068 |
| | ----- | ----- |
| Total assets | \$1,562,619 | \$1,489,311 |
| | ===== | ===== |

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

BIOMET, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

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at November 30, 2001 and May 31, 2001
(in thousands)

LIABILITIES AND SHAREHOLDERS' EQUITY

| | November 30, 2001 | May 31, 2001 |
|--|----------------------|-----------------|
| | ----- | ----- |
| | (Unaudited) | |
| Current liabilities: | | |
| Short-term borrowings | \$ 57,867 | \$ 62,734 |
| Accounts payable | 25,586 | 21,008 |
| Accrued income taxes | 27,987 | 31,085 |
| Accrued wages and commissions | 29,219 | 33,030 |
| Accrued litigation | 5,864 | 26,100 |
| Other accrued expenses | 60,754 | 67,865 |
| | ----- | ----- |
| Total current liabilities | 207,277 | 241,822 |
| Long-term liabilities: | | |
| Deferred federal income taxes | 6,433 | 5,783 |
| Other liabilities | 412 | 423 |
| | ----- | ----- |
| Total liabilities | 214,122 | 248,028 |
| | ----- | ----- |
| Minority interest | 98,024 | 95,097 |
| | ----- | ----- |
| Contingencies (Note 7) | | |
| Shareholders' equity: | | |
| Common shares | 118,340 | 108,918 |
| Additional paid-in capital | 48,732 | 48,732 |
| Retained earnings | 1,137,761 | 1,044,564 |
| Accumulated other comprehensive loss | (54,360) | (56,028) |
| | ----- | ----- |
| Total shareholders' equity | 1,250,473 | 1,146,186 |
| | ----- | ----- |
| Total liabilities and shareholders' equity | \$1,562,619 | \$1,489,311 |
| | ===== | ===== |

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

BIOMET, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF INCOME

for the six and three month periods ended November 30, 2001 and 2000
(Unaudited, in thousands, except per share amounts)

| | Six Months Ended | | Three Months Ended | |
|---|------------------|-----------|--------------------|-----------|
| | November 30, | | November 30, | |
| | 2001 | 2000 | 2001 | 2000 |
| | ----- | ----- | ----- | ----- |
| Net sales | \$561,409 | \$475,494 | \$289,387 | \$244,361 |
| Cost of sales | 156,426 | 139,194 | 79,034 | 71,027 |
| | ----- | ----- | ----- | ----- |
| Gross profit | 404,983 | 336,300 | 210,353 | 173,334 |
| Selling, general and administrative expenses | 207,995 | 170,114 | 106,679 | 87,180 |

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| | | | | |
|---|-----------|-----------|-----------|-----------|
| Research and development expense | 23,655 | 20,159 | 11,987 | 10,295 |
| | ----- | ----- | ----- | ----- |
| Operating income | 173,333 | 146,027 | 91,687 | 75,859 |
| Other income, net | 8,935 | 10,181 | 4,371 | 4,711 |
| | ----- | ----- | ----- | ----- |
| Income before income taxes and minority interest | 182,268 | 156,208 | 96,058 | 80,570 |
| Provision for income taxes | 61,876 | 53,512 | 32,607 | 27,562 |
| | ----- | ----- | ----- | ----- |
| Income before minority interest | 120,392 | 102,696 | 63,451 | 53,008 |
| Minority interest | 2,927 | 2,471 | 1,999 | 1,210 |
| | ----- | ----- | ----- | ----- |
| Net income | \$117,465 | \$100,225 | \$ 61,452 | \$ 51,798 |
| | ===== | ===== | ===== | ===== |
| Earnings per share: | | | | |
| Basic | \$.44 | \$.37 | \$.23 | \$.19 |
| | ===== | ===== | ===== | ===== |
| Diluted | \$.43 | \$.37 | \$.23 | \$.19 |
| | ===== | ===== | ===== | ===== |
| Shares used in the computation of earnings per share: | | | | |
| Basic | 269,635 | 267,384 | 269,809 | 267,729 |
| | ===== | ===== | ===== | ===== |
| Diluted | 272,747 | 270,129 | 272,822 | 270,708 |
| | ===== | ===== | ===== | ===== |
| Cash dividends per common share | \$.09 | \$.07 | \$ -- | \$ -- |
| | ===== | ===== | ===== | ===== |

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

BIOMET, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
for the six months ended November 30, 2001 and 2000
(Unaudited, in thousands)

| | 2001 | 2000 |
|--|-----------|-----------|
| | ---- | ---- |
| Cash flows from (used in) operating activities: | | |
| Net income | \$117,465 | \$100,225 |
| Adjustments to reconcile net income to net cash from operating activities: | | |
| Depreciation | 16,446 | 14,652 |
| Amortization | 6,089 | 5,745 |
| Gain on sale of investments, net | (89) | (1,284) |
| Minority interest | 2,927 | 2,471 |
| Deferred federal income taxes | 4,467 | (909) |
| Changes in current assets and liabilities, excluding effects of acquisitions: | | |
| Accounts and notes receivable, net | (8,249) | (8,407) |
| Inventories | (29,690) | (17,252) |
| Prepaid expenses and other | 3,625 | (9,803) |
| Accounts payable | 3,458 | (3,182) |
| Accrued income taxes | (2,812) | (3,209) |
| Accrued wages and commissions | (4,883) | 1,185 |
| Other accrued expenses | (24,401) | 3,902 |
| | ----- | ----- |
| Net cash from operating activities | 84,353 | 84,134 |
| | ----- | ----- |
| Cash flows from (used in) investing activities: | | |
| Proceeds from sales and maturities of investments | 66,316 | 33,742 |

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| | | |
|--|-----------|-----------|
| Purchases of investments | (81,562) | (35,817) |
| Capital expenditures | (34,025) | (16,434) |
| Acquisitions, net of cash acquired | -- | (90,602) |
| Other | (1,345) | (2,061) |
| | ----- | ----- |
| Net cash used in investing activities | (50,616) | (111,172) |
| | ----- | ----- |
| Cash flows from (used in) financing activities: | | |
| Decrease in short-term borrowings, net | (4,974) | (11,369) |
| Issuance of common shares | 9,422 | 13,571 |
| Cash dividends | (24,268) | (18,993) |
| | ----- | ----- |
| Net cash used in financing activities | (19,820) | (16,791) |
| | ----- | ----- |
| Effect of exchange rate changes on cash | (1,885) | (2,892) |
| | ----- | ----- |
| Increase (decrease) in cash and cash equivalents | 12,032 | (46,721) |
| Cash and cash equivalents, beginning of year | 235,091 | 213,606 |
| | ----- | ----- |
| Cash and cash equivalents, end of period | \$247,123 | \$166,885 |
| | ===== | ===== |

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 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 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 six-month period ended November 30, 2001 are not necessarily indicative of the results that may be expected for the fiscal year ending May 31, 2002. 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, 2001.

The accompanying consolidated balance sheet at May 31, 2001, has been derived from the audited Consolidated Financial Statements at that date, but does not include all disclosures required by 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 Arthrotek's arthroscopy products, EBI's softgoods and bracing 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 other. Other geographic markets include Canada, South America, Mexico, Japan and the Pacific Rim.

Net sales of musculoskeletal products by product category are as follows for the six and three months ended November 30:

Six Months Ended

Three Months Ended

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| | November 30, | | November 30, | |
|-----------------|----------------|-----------|--------------|-----------|
| | 2001 | 2000 | 2001 | 2000 |
| | (in thousands) | | | |
| Reconstructive | \$336,066 | \$287,893 | \$174,894 | \$145,801 |
| Fixation | 106,882 | 94,755 | 53,236 | 48,224 |
| Spinal products | 57,151 | 35,801 | 29,692 | 21,692 |
| Other | 61,310 | 57,045 | 31,565 | 28,644 |
| | ----- | ----- | ----- | ----- |
| | \$561,409 | \$475,494 | \$289,387 | \$244,361 |
| | ===== | ===== | ===== | ===== |

NOTE 2: COMPREHENSIVE INCOME.

Other comprehensive income 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 November 30, 2001 and 2000 was \$1,269,000 and \$(16,427,000), respectively. Other comprehensive income (loss) for the six months ended November 30, 2001 and 2000 was \$1,668,000 and \$(14,001,000), respectively. Total comprehensive income combines reported net income and other comprehensive income. Total comprehensive income for the three months ended November 30, 2001 and 2000 was \$62,721,000 and \$35,371,000, respectively. Total comprehensive income for the six months ended November 30, 2001 and 2000 was \$119,133,000 and \$86,224,000, respectively.

NOTE 3: INVENTORIES.

Inventories at November 30, 2001 and May 31, 2001 are as follows:

| | November 30, | May 31, |
|-----------------|----------------|-----------|
| | 2001 | 2001 |
| | (in thousands) | |
| Raw materials | \$ 35,834 | \$ 32,024 |
| Work-in-process | 37,081 | 31,082 |
| Finished goods | 120,042 | 108,704 |
| Consigned | 116,051 | 105,791 |
| | ----- | ----- |
| | \$309,008 | \$277,601 |
| | ===== | ===== |

NOTE 4: COMMON SHARES.

During the six months ended November 30, 2001, the Company issued 906,917 Common Shares upon the exercise of outstanding stock options for proceeds aggregating \$9,422,000. On July 9, 2001, the Company announced a three-for-two stock split payable August 6, 2001 to shareholders of record July 30, 2001. All information on the number of common shares and all per share data for the previous year have been restated for this stock split.

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.

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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 and tax credits.

NOTE 7: CONTINGENCIES.

On November 13, 2001, the United States Supreme Court ("Supreme Court") denied the Company's petition to review the \$20 million punitive damage award against the Company given to Raymond G. Tronzo by the United States District Court for the Southern District of Florida which affirmed a compensatory damage award of \$520. The Company had previously recorded a one-time special charge during the third quarter of fiscal 2001 of \$26.1 million, which represents the total damage award plus the maximum amount of interest that, as calculated by the Company, may be due under the award and related expenses. While the Company was disappointed in the Supreme Court's decision not to review the case, the Company has released \$20,236,000 from escrow. The amount of interest owed by the Company, if any, on this award continues to be in dispute; however, if a decision on the interest award is adverse to the Company, it should not exceed the amount of the remaining funds in escrow. The Supreme Court's decision does not affect the ongoing sales of any of Biomet's product lines.

There are various other claims, lawsuits, disputes with third parties, investigations and pending actions involving various allegations against the Company incident to the operation of its business, principally product liability and intellectual property cases. Each of these matters is subject to various uncertainties, and it is possible that some of these matters may be resolved unfavorably to the Company. The Company establishes accruals for losses that are deemed to be probable and subject to reasonable estimate. Based on the advice of counsel to the Company in these matters, management believes that the ultimate outcome of these matters and any liabilities in excess of amounts provided will not have a material adverse impact on the Company's consolidated financial position or on its future business operations.

NOTE 8: RECENT ACCOUNTING PRONOUNCEMENTS:

In June of 2001, the Financial Accounting Standards Board (FASB) approved the issuance of Statement 141, "Business Combinations", and Statement 142, "Goodwill and Other Intangible Assets". FASB Statement 141, among other things, requires that all business combinations be accounted for using the purchase method; use of the pooling-of-interest method is prohibited. The provisions of FASB Statement 141 will apply to all business combinations initiated after June 30, 2001. FASB Statement 142, among other things, requires that goodwill not be amortized but should be tested for impairment at least annually. The Company will adopt these two statements in the first quarter of fiscal 2003. The Company has not assessed the effect that the adoption of FASB Statement 142 will have on its financial position or results of operations.

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

FINANCIAL CONDITION AS OF NOVEMBER 30, 2001

The Company's cash and investments increased \$29,776,000 to \$492,924,000 at November 30, 2001, despite the \$24,268,000 cash dividend paid during the first quarter.

Cash flows provided by operating activities were \$84,353,000 for the first six months of fiscal 2002 compared to \$84,134,000 in 2001. The primary sources of

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fiscal year 2002 cash flows from operating activities were net income, depreciation and amortization offset by increases in accounts receivable and inventory and a decrease in other accrued expenses. Inventories increased from new product introductions and a buildup of inventory associated with the Company's establishment of its direct operations in Japan.

Cash flows used in investing activities were \$50,616,000 for the first six months of fiscal 2002 compared to a use of \$111,172,000 in 2001. The primary use of cash flows for investing activities were purchases of investments and purchases of capital equipment offset by sales and maturities of investments.

Cash flows used in financing activities were \$19,820,000 for the first six months of fiscal 2002 compared to a source of \$16,791,000 in 2001. The primary use of cash flows from financing activities was the cash dividend paid in the first quarter while the primary source of cash flows from financing activities was from cash receipts from stock option exercises.

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, common stock repurchases and potential business acquisitions.

RESULTS OF OPERATIONS FOR THE SIX MONTHS ENDED NOVEMBER 30, 2001 AS COMPARED TO THE SIX MONTHS ENDED NOVEMBER 30, 2000

Net sales increased 18% to \$561,409,000 for the six-month period ended November 30, 2001, from \$475,494,000 for the same period last year. Excluding the impact of foreign currency and discontinued products, which reduced the first six months sales by \$3.7 million and \$5.3 million, respectively, net sales increased 20% during the first six months of fiscal year 2002. The Company's U.S.-based revenue increased 22% to \$408,119,000 during the first six months, while foreign sales increased 8% to \$153,290,000. Excluding the negative foreign exchange adjustment and discontinued products, foreign sales in local currencies increased 15%. Biomet's worldwide sales of reconstructive products during the first six months of fiscal 2002 were \$336,066,000, representing a 17% increase compared to the first six months of last year. This increase was primarily a result of Biomet's continued penetration of the reconstructive device market led by the Repicci IITM Unicondylar Knee System, the Ascent™ Total Knee System, the M2a™ Taper Metal-on-Metal Hip System and 3i's dental reconstructive implants. Sales of fixation products were \$106,882,000 for the first six months of fiscal 2002, representing a 13% increase as compared to the same period in 2001. Sales of spinal products were \$57,151,000 for the first six months of fiscal 2002, representing a 60% increase as compared to the same period in 2001. Sales of spinal hardware contributed to this increase. Increases in both fixation and spinal products were positively influenced by the acquisition of Bioelectron in September of last fiscal year. The Company's sales of other products totaled \$61,310,000, representing a 7% increase over the first six months of fiscal year 2001, primarily as a result of increased sales of softgoods and bracing products and arthroscopy products, offset by the loss of internationally distributed products.

Cost of sales decreased as a percentage of net sales to 27.9% for the first six months of fiscal 2002 from 29.3% last year primarily as a result of increased sales of higher margin products and increased in-house manufacturing efficiencies. Selling, general and administrative expenses as a percentage of net sales increased from 35.8% for the first six months of last year to 37.0% for the current six month period. This increase in the percentage is a result of the Bioelectron acquisition and ongoing investments in the Company's global sales capabilities. Research and development expenditures increased during the first six months to \$23,655,000 reflecting the Company's continued emphasis on new product introductions. Operating income increased 18% to \$173,333,000 for the first six months of fiscal 2002. Other income decreased 12% resulting from

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the lower interest rates available on investable cash. The effective income tax rate decreased to 33.9% for the first six months of fiscal year 2002 from 34.3% last year primarily as a result of U.S. pretax income growing at a higher rate than international pretax income where tax rates are higher.

These factors resulted in a 17% increase in net income to \$117,465,000 from \$100,225,000 for the first six months of fiscal 2002 as compared to the same period in fiscal 2001. Basic earnings per share increased 19% from \$.37 to \$.44 for the periods presented, while diluted earnings per share increased 16% from \$.37 to \$.43 for the periods presented.

RESULTS OF OPERATIONS FOR THE THREE MONTHS ENDED NOVEMBER 30, 2001 AS COMPARED TO THE THREE MONTHS ENDED NOVEMBER 30, 2000

Net sales increased 18% to \$289,387,000 for the second quarter of fiscal 2002, as compared to \$244,361,000 for the same period last year. Excluding the impact of foreign currency which increased second quarter sales by \$1.1 million and discontinued products which reduced the second quarter sales by \$2.5 million, net sales increased 19% during the second quarter of fiscal year 2002. Operating income increased 21% from \$75,859,000 for the second quarter of fiscal 2001, to \$91,687,000 for the second quarter of fiscal 2002. During the second quarter, net income increased 19% to \$61,452,000 as compared to \$51,798,000 for the same period last year. Basic and diluted earnings per share increased 21% from \$.19 to \$.23 for the periods presented. The business factors resulting in these changes and relevant trends affecting the Company's business during the periods in question are comparable to those described in the preceding discussion for the six-month period.

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, 2001.

PART II. OTHER INFORMATION

Item 1: Legal Proceedings.

On November 13, 2001, the United States Supreme Court ("Supreme Court") denied the Company's petition to review the \$20 million punitive damage award against the Company given to Raymond G. Tronzo by the United States District Court for the Southern District of Florida which affirmed a compensatory damage award of \$520. The Company had previously recorded a one-time special charge during the third quarter of fiscal 2001 of \$26.1 million, which represents the total damage award plus the maximum amount of interest that, as calculated by the Company, may be due under the award and related expenses. While the Company was disappointed in the Supreme Court's decision not to review the case, the Company has released \$20,236,000 from escrow. The amount of interest owed by the Company, if any, on this award continues to be in dispute; however, if a decision on the interest award is adverse to the Company, it should not exceed the amount of the remaining funds in escrow. The Supreme Court's decision does not affect the ongoing sales of any of Biomet's product lines.

Item 6. Exhibits and Reports on Form 8-K

- (a) Exhibits. See Index to Exhibits.
- (b) Reports on Form 8-K.

A report on Form 8-K was filed October 31, 2001 with respect to item 4 of that form.

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SIGNATURES

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

BIOMET, INC.

(Registrant)

DATE: 1/11/2002

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

| Number Assigned in Regulation S-K Item 601 ----- | Description of Exhibit ----- | Sequential Numbering System Page Number of Exhibit ----- |
|---|--|--|
| (2) | No exhibit. | |
| (4) | 4.1 Specimen certificate for Common Shares. (Incorporated by reference to Exhibit 4.1 to the registrant's Report on Form 10-K for the fiscal year ended May 31, 1985). | |
| | 4.2 Rights Agreement between Biomet, Inc. and Lake City Bank, as Rights Agent, dated as of December 2, 1989. (Incorporated by reference to Exhibit 4 to Biomet, Inc. Form 8-K Current Report dated December 22, 1989, File No. 0-12515). | |
| (10) | No exhibit. | |
| (11) | No exhibit. | |
| (15) | No exhibit. | |
| (18) | No exhibit. | |
| (19) | No exhibit. | |
| (22) | No exhibit. | |
| (23) | No exhibit. | |
| (24) | No exhibit. | |

(99)

No exhibit.