THOMSON REUTERS STREETEVENTS

EDITED TRANSCRIPT

XRAY - Q1 2015 DENTSPLY International Inc Earnings Call

EVENT DATE/TIME: MAY 06, 2015 / 12:30PM GMT

OVERVIEW:

XRAY reported 1Q15 as-reported net income attributable to Co. of $64m or $0.45 per diluted share. Expects 2015 adjusted EPS to be $2.50-2.60.

CORPORATE PARTICIPANTS

Derek Leckow *DENTSPLY International Inc. - VP of IR*

Bret Wise *DENTSPLY International Inc. - Chairman and CEO*

Jim Mosch *DENTSPLY International Inc. - EVP and COO*

Chris Clark *DENTSPLY International Inc. - President and CFO*

CONFERENCE CALL PARTICIPANTS

Glen Santangelo *Credit Suisse - Analyst*

John Kreger *William Blair & Company - Analyst*

Nathan Rich *Goldman Sachs - Analyst*

Brandon Couillard *Jefferies LLC - Analyst*

Steven Valiquette *UBS - Analyst*

Steve Beuchaw *Morgan Stanley - Analyst*

Erin Wilson *BofA Merrill Lynch - Analyst*

Jeff Johnson *Robert W. Baird & Company, Inc. - Analyst*

Jon Block *Stifel Nicolaus - Analyst*

PRESENTATION

Operator

Good day and welcome to the DENTSPLY International first-quarter 2015 earnings call. Today's conference is being recorded.

At this time I would like to turn the conference over to Mr. Derek Leckow, Vice President of Investor Relations. Sir, you may begin.

Derek Leckow - *DENTSPLY International Inc. - VP of IR*

Thank you, Orlando. Good morning, everyone.

Thank you for joining us to discuss DENTSPLY International's first-quarter 2015 results. I'm joined by Bret Wise, DENTSPLY's Chairman and Chief Executive Officer, Chris Clark, our President and Chief Financial Officer, and Jim Mosch, our Executive Vice President and Chief Operating Officer.

I hope you had a chance to review our press release issued earlier this morning. A copy of the release and a set of supplemental slides and information relating to our non-GAAP financials are available for download in the investor relations section of our website www.dentsply.com under the heading quarterly results.

And please don't forget the Safe Harbor language and US GAAP reconciliation contained in today's release also pertain to this conference call. We may make forward-looking statements involving risks and uncertainties and these should be considered in conjunction with the risk factors and uncertainties that are described in the release and in our SEC filings.

It is possible that actual results may differ materially from the forward-looking statements that we may make today. The Company undertakes no obligation to update or revise any forward-looking statements to reflect events or circumstances that may arise after the date of this call.

With that, I would now like to turn the call over to Bret Wise. Bret?

Bret Wise - *DENTSPLY International Inc. - Chairman and CEO*

Thank you, Derek, good morning, everyone. Thank you again for joining us on the call this morning.

I have some opening comments and then I'll turn the call over to Jim for some operational review and Chris will cover the financial results in more detail, and of course we'll take your questions following our prepared remarks.

We're off to a reasonable start to the year with revenue growth picking up nicely in the US in the first quarter and adjusted EPS flat with the prior year. Results were slightly better than expected on earnings driven by growth in the US and 100 basis point improvement in operating margins, while growth in Europe was muted. FX rates deteriorated in the quarter after we last spoke to you in February.

On markets we saw good increase in activity and demand in the US as expected, consistent with the growth in employment over the past year. And at this point we would expect that to continue. Europe on the other hand was more mixed. Overall I'd say it's stable but differed substantially by country, some up and some down during the period. This is a bit weaker than we expected going into the quarter.

And rest of world markets as always were mixed but most were growing nicely with the exception of Japan, which as you know had a VAT tax increase April 1 last year, which created some pull forward into the first quarter of last year and a difficult baseline for the first quarter this year. And of course that will reverse in the second quarter.

At DENTSPLY our strategy remains the same which is to focus on innovation to fund future growth, while leaning out the organization, improving margins and asset utilizations and ROIC. And channeling funds to some key areas that can increase our impact on the market over the next several years. Jim and Chris will have more on that in a moment.

Looking at the first quarter, our revenue excluding precious metals declined by 8.4% for the quarter with constant currency and internal growth of positive 1.3%, while currency of course was negative 9.7%. Internal growth was comprised of 4.5% growth in the US, a negative 1.2% in Europe and CIS and a positive 1.9% growth for the rest of world category. The US growth rate was notably stronger than we've seen for some time, this was the best we've had in seven quarters and was driven by growth in essentially all principal product categories.

Results for some of the key dental shows in the US earlier in the year were very positive and reflected both a market that's growing in demand and also good interest in our portfolio. We're also pleased with our sales force execution in the US, both the direct businesses and those that go through our key distributor partners, and we view this as an area or an opportunity for reinvestment moving forward.

In Europe we saw a sequential slow down from the stronger growth we reported in the back half of last year. This market continues to be somewhat muted and it's inconsistent across country markets. This quarter we saw lower growth in several markets, including a continued decline in the CIS region.

We're not reading too much into that at this point as overall I'd say the region appears stable to us, and we expect to see some small up and down periods before this market starts to grow consistently again. Certainly the weaker currency and the stimulus now in place in Europe, we think gives us a reasonable chance that this market will pick up over the next year or so.

The biannual IDS trade show was held in March in Cologne, which was well attended as always. We saw strong interest in our products, although this tends to be more of an equipment driven show than a consumable show.

Our results in Europe also reflect our transitional activities impacting our lab business. As we've announced we are exiting certain equipment categories there. That's causing a temporary drag on results of sales of those product that are still in the baseline from prior year. Europe ex lab was essentially flat for us in the first quarter.

In rest of world we had 1.9% internal growth in total and roughly 5% internal growth without Japan, where the VAT tax increase of course is distorting things for a couple quarters here. We continue to enjoy strong growth in the Pacific Rim. Growth recovered substantially for us in Latin America, Canada was strong, while Australia and the Middle East were flattish and Japan was negative as expected due to the tax.

Adjusted EPS for the quarter was flat with last year at $0.59. This reflects of course a currency headwind we're facing, which is quite substantial, offset by improved margins and a slightly lower share count. Looking ahead at current rates, we continue to have -- we continue to expect that we'll have the currency headwind for the balance of the year at this point.

But of course we're focused on what we can do with our own operating model, where we can improve our efficiency as well as invest for faster growth. That being said, we're comfortable with our current guidance of $2.50 to $2.60 adjusted earnings per share for the full year.

That concludes my prepared remarks, I'd like to now turn the call over to Jim Mosch who has some comments on operations.

Jim Mosch - *DENTSPLY International Inc. - EVP and COO*

Thank you, Bret. I'd like to provide an operational update for Q1 and also provide some further perspectives on 2015 initiatives. I'll then turn it over to Chris for the financial review.

As outlined in February, we were looking forward to the International Dental Show in Cologne, Germany. While the IDS tends to focus on large equipment, it is also an important show for the introduction of new products in the consumables area, and I'd like to outline some of our key launches.

Our endodontic business launch WaveOne GOLD, which is an extension of our market-leading WaveOne reciprocating file system. WaveOne GOLD utilizes a patented heat treatment process, which improves file flexibility to negotiate difficult canal anatomy and also increase the safety due to higher resistance of cyclical fatigue.

A second launch, a new cordless motor platform under the brand names X-Smart iQ and VDW. CONNECT Drive has the ability to operate in both reciprocating and rotary modes. The new motor is connected to an iPad with an app-based interface that will provide an extensive and customizable filed library, as well as a patient education module. The platform is expandable, and in the future will incorporate apex locator capabilities, as well as treatment planning.

The restorative business continues their focus on procedural solutions to simplify restorative dentistry, while providing effective patient results. This included a series of our market-leading products in combination to effectively complete a class 2 restoration, which is the highest volume restorative dental procedure. The same philosophy is also applied to a crown and bridge solution as it relates to preparation and final placement of the prosthetic treatment.

The procedure focus has also been extended to post endodontic treatment restorations, which we refer to as RestoDonics. This employs the use of our market-leading endodontic portfolio Palodent Plus Matrix system and our bulk-fill composite SDR.

Our preventive business launch NUPRO White Varnish which has been successful the US market for over a year, but this was its initial launch into the European market. This IDS was the most comprehensive presentation of our preventive portfolio in the European market and we believe there are significant opportunities for geographic expansion and growth.

The prosthetic business presented their refocus to innovative all ceramic materials to be utilized in open platform digital systems. This was led by the launch of Cercon ht available in 16 vita shades as well as a special staining concept that supports small and medium-size labs. In addition there was a re-emphasis of our CELTRA Duo, which is our chair side high-strength glass ceramic material targeted at the fast-growing all ceramic category.

Most significant was that the prosthetics business presented a consolidated product platform that will be marketed and leveraged on a global basis versus more region specific brands. Overall IDS attendance was up and we are pleased with the interest in our new product portfolio.

Turning to operations, I'd like to outline the status of our initiatives to achieve a 20% operating margin by the end of 2017. As outlined previously, our European prosthetics group is engaging in restructuring discussions with our German Works Council.

This has resulted in the agreement to close one of the smaller facilities and the remaining restructuring is progressing. This effort is in alignment with the three manufacturing facilities and several field offices consolidated in 2014 and our focus to simplify our business model and leverage our asset base.

As we further address operating margin improvement, we have been refocusing and restructuring our global business model. This has resulted in the formation of three segments: Manufacturing businesses that primarily sell through our distribution partners, which reflect our dental consumables, endodontic and dental laboratory businesses. Second, manufacturing business that sell direct to clinicians our patients which reflect our healthcare orthodontic and implant business. And finally, regional commercial organizations composed of our country selling stations in select developed and emerging markets.

Within the manufacturing segments we will focus on global product platforms by clinical discipline and create consolidated functional organization. While this provides the opportunity to better leverage our asset base, more importantly it moves us from regionally focused businesses to global business strategies that we believe will drive long-term growth.

In the regional commercial segment we are moving from independent businesses in country to fully integrated country organizations. This structure allows us to leverage common commercial, clinical and customer strategies.

As we move forward through this strategic initiative, there's an amount of short-term distraction. However, this effort is necessary in order to achieve our operating improvement objectives and position our businesses more effectively to drive growth.

Closely aligned with our operating improvement objectives is a requirement for investments. As we look to growth, they fall in the categories of innovation, clinical education and sales excellence. Our investments in these areas focus us on expansion of R&D and investment in larger, and, no doubt, riskier innovation projects but with higher returns.

In the area of clinical education we believe that we educate more clinicians than any other company in the dental industry. And we have implemented a DENTSPLY 360 program which leverages our clinical education programs across our businesses and clinical disciplines and delivers comprehensive clinical support and product utilization to clinicians. This has been particularly effective with group practices and institutions.

Finally, sales excellence seeks to support the largest employee population in DENTSPLY, which is our field sales representatives. We have invested in sophisticated tools as it relates to sales force alignment, deployment and sales analytics, which have improved sales effectiveness and execution.

In addition to investing in sales representatives, we're also investing in global sales training development to ensure consistent sales capacity and competency on a global basis. We believe that the initiatives of strategic alignment, operating improvement and reinvestment will deliver long-term growth and results.

I'd now like to turn it over to Chris Clark to review the financial results.

Chris Clark - *DENTSPLY International Inc. - President and CFO*

Thank you, Jim, and good morning, everyone.

I'd like to provide some detail on our first-quarter results by reviewing key elements of our income statement, balance sheet and cash flow statement, as well as provide some additional color on capital deployment and highlight some of the few key related initiatives.

For the first quarter, sales excluding precious metals declined 8.4% compared to prior year, as internal growth of 130 basis points was more than fully offset by unfavorable currency translation of 970 basis points. The negative impact from currency on the top line was a bit larger than what we anticipated earlier in the quarter as the US dollar sequentially strengthened against most currencies as the quarter progressed, including a 2% strengthening against the euro on average from the rate we assumed at the time of our February earnings call.

Given the recent pullback of the dollar over the last week, based on current rates, the currency translation impact on our sales line for the full year is in line with the negative 800 basis points that we indicated on our call in February. Net acquisition growth in the quarter was negligible as we completed a small acquisition in Q4 but also had three divestitures over the last year that offset it from a sales perspective.

Gross profit rate on an adjusted basis in the first quarter was 59.8% of sales excluding precious metals, which was an improvement of 200 basis points over prior year. This reflects the favorable impact of mix, FX and price.

SG&A expenses on an adjusted basis were down 5.9% in the absolute, reflecting the currency translation impact. As a percentage of sales, excluding precious metals, SG&A expenses on an adjusted basis were 41.2% in the quarter, that's up 110 basis points compared to our rate in the first quarter of 2014.

And this reflects incremental trade show costs, largely those associated with the biannual International Dental Show, as well as increased professional services costs, including spending to support our global operating margin improvement initiatives. Collectively these two areas contributed approximately 100 basis points to the quarters increased SG&A rate.

Operating margin for the quarter improved by 100 basis points to 18.7% of sales, excluding precious metals on an adjusted basis, and this compares to 17.7% in the first quarter last year. This is on top of the 150 basis point improvement in adjusted operating margin in the first quarter of 2014 compared to the same period in 2013. Our performance this quarter reflects the gross margin and SG&A impacts that I just described, as well as the impact of our operating margin improvement initiatives.

One area where we are continuing to gain momentum is our global procurement initiatives, where we are focused on gaining the purchasing leverage from the collective spend across our global businesses, as opposed to approaching the market as individual companies or divisions.

This is an area where we've invested considerably over the past year, adding both internal and external resources. We're pleased with the progress of our global team, as targeted initiatives in the number of areas are delivering benefits including travel, office supplies, packaging, specific raw material components, temporary labor, OEM supply and others.

Our reported tax rate for the first quarter was 21.6%, while our adjusted operating tax rate was 22.9%, which was 30 basis points above our first-quarter rate last year. We anticipated continued headwind in the adjusted operating tax rate, as a result of our projected unfavorable geographic earnings mix in 2015 compared to prior year.

Net income attributable to DENTSPLY International on an as reported basis in the first quarter was $64 million or $0.45 per diluted share, and this compares to $72.9 million, or $0.50 per diluted share in the first quarter of 2014. These results include a number of items which we've listed in the schedules in the release. On an adjusted basis, net earnings were $3.6 million (Sic- see press release $83.6 m) in the quarter compared to $85.5 million in the prior-year quarter.

Adjusted diluted earnings per share were $0.59, equal to last year's first quarter, including the headwinds from currency and IDS that I outlined earlier. [Currency] represented a headwind to earnings in the quarter of approximately $0.035 per share, and this was a bit worse than what we anticipated coming into the quarter. This reflects the incremental strengthening of the dollar during the quarter that I mentioned earlier.

Moving on to cash flow, our operating cash flow for the quarter with $65.6 million and that's up 2% from last year's previous first-quarter record of $64.6 million, and is up 82% from $36.1 million in the first quarter of 2013. This was the fifth straight quarter with record cash flow for that calendar quarter.

Free cash flow for the quarter increased over prior year by $10 million, or 26%, and we continue to be pleased with our cash flow performance as our trailing 12-month operating cash flow was up 25% versus the previous 12 months ended March 2014. In addition, our free cash flow conversion ratio over that period is 150% of reported GAAP net income while our free cash flow yield is 6.6%.

Inventories finished at 118 days in March, that's up 5 days sequentially and down 2 days from prior year. We typically see a bit of an increase in inventory early in the year based on normal seasonal factors. We anticipate continued year-on-year improvements in the inventory levels moving forward and our Management teams have specific targets relative to inventories and working capital.

Accounts receivables were at 58 days in March; that's up 3 days from December and down 3 days from 61 days last March. Capital expenditures were $16 million in the quarter, while depreciation was $19 million and amortization was $11 million.

We've commented previously on the positive position our cash flow performance puts us in relative to capital deployment flexibility, and our first quarter demonstrates some of these benefits. During the quarter we repurchased 1.7 million shares of stock at an average cost of $52.08 per share.

In the quarter we returned $80 million to shareholders through share buybacks, net of option proceeds and dividends. Our leverage ratio, defined as net debt divided by trailing 12 months EBITDA, now stands at 2.1 at the end of March. Looking forward, our balance sheet and cash flow generation continue to provide us considerable flexibility to deploy capital through acquisition and share buybacks.

As we look to the remainder of 2015, we continue to build on the solid underlying operating margin and cash flow performance of the business in the first quarter and we're confident our initiatives to improve efficiencies are gaining traction. We commented on our call in February that the year-on-year comparisons would be significantly impacted by the much stronger US dollar compared to 2014. And as I mentioned, due to rate changes within the quarter, the headwinds we experience in the first quarter were a bit larger than anticipated both on the top and bottom lines.

Rates have come back to us a bit with the weakening of the US dollar over the past week and based on current rates we would project the full-year currency headwind to earnings to be about $0.14 per share net of our cash flow hedges, and that's consistent with what we indicated on our call in February.

As you may recall, these hedges helped to partially blend our FX impact over a rolling 18-month period. And while they don't eliminate or reduce the long-term impact of currency changes, they do reduce the volatility by essentially gradualizing those rate changes. Absent the cash flow hedges, the negative impact to earnings per share from currency would be approximately double the $0.14 that I just mentioned.

As I mentioned in February, one of the longer term benefits of our operating margin improvement initiative is to standardize production processes across similar facilities, which should allow us over time to flex a portion of our production between plants or geographies based on a range of factors, including currency movements. We also have worked to offset a portion of the currency headwind through targeted pricing and cost initiatives in the short term.

As Jim mentioned, as part of our operating improvement initiative, we are aligning our businesses based on business type, manufacturing businesses that sell predominately through distribution, manufacturing businesses that sell -- that primarily sell directly to end users, and finally geographic selling locations. And you will see that our segment reporting in our first quarter Form 10-Q and subsequent filings will reflect this alignment.

Finally as Bret indicated, we're maintaining our 2015 earnings per share guidance at $2.50 to $2.60 on an adjusted basis. That completes our prepared remarks, we certainly appreciate your support and we'd be glad now to take any questions that you might have.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions)

Glen Santangelo, Credit Suisse.

Glen Santangelo - *Credit Suisse - Analyst*

Bret, wanted to follow up on the revenue growth numbers. I think the problems in Europe seem to be pretty well documented but could you comment on the rest of the world category in terms of what you're seeing there? Because it seems like the growth has obviously decelerated a little bit and I think everyone's aware the issues in Japan and the tax issue, but maybe above and beyond that, could you maybe give us some commentary in terms of the outlook in some of the key markets there?

Bret Wise - *DENTSPLY International Inc. - Chairman and CEO*

Sure. I'd like to remind everybody that our rest of world category includes a mix of emerging markets and developed markets. So for instance, Japan, Canada and Australia are included in that category. Those markets are acting like developed markets at this point.

The Canadian market is growing pretty nicely for us. I think that's -- there's some tie to the United States there, not a direct tie but we see the outlook there being favorable at this point.

The Australian market is flat. I think that's consistent with some of the economic growth issues they have. There's some articles recently about perhaps a need to cut interest rates there. The currency is already quite weak and that raises of course the cost of doing business in Australia because it's an import economy for product like ours. So I don't see a substantial uptick there one way or another.

Japan, as you noted, acts like a developed market. It contracted in the first quarter, I think it will expand in the second quarter maybe even the third quarter because of the low baseline. But long term, Japan is a low growth stable market.

Now the rest of the rest of world category for us is of course emerging markets. We continue to see good growth and expect to see good growth in the Pacific Rim including China, which is -- it continues to be a robust market. But also some of the other countries in that category as well.

Latin America has been hot and cold. It had grown pretty consistently for us, coming up to the second quarter last year when the World Cup was in Brazil. It then had a couple of slow quarters of growth and this period recovered. Our hope is that's now on a more stable basis and will continue to grow, maybe not as fast as it was two or three years ago, but growth on a more stable basis going forward. The currency there is a big factor as well because of the depreciation of the real.

So it's hard to describe rest of world at one comment. It's a complex group of countries for us. But I think it's important to keep in mind it's a mix of both developed and developing markets.

Glen Santangelo - *Credit Suisse - Analyst*

All right, thanks for the comment. Maybe if I ask a follow-up question. It seems like on a more encouraging basis the margins and cash flows continue to improve, and as the leverage comes down, can you maybe give us some of your updated thoughts in terms of the capital deployment outlook? It seems like obviously the Company bought back some stock this quarter, but maybe as you look at your M&A pipeline, how does that stack up versus the attractiveness of buying back your own stock and how should we think about that? Thanks.

Bret Wise - *DENTSPLY International Inc. - Chairman and CEO*

Sure, Glen. First of all, we've -- I would reiterate what we've said earlier and that is that we're very focused on cash flow generation. You've seen that come up in the Company as well as with margins, asset turns are improving.

ROI has improved pretty substantially over the past three or four years. We think we're in a good position now to produce quite a bit of cash and that will be -- a first priority for that of course is reinvesting in the Company where we get a really good pay back on capital investment internally to grow both sales and earnings.

Second priority continues to be acquisitions. We're looking in acquisitions, we do have several candidates in the pipeline. We're in active discussions with several companies. There of course we're looking to get a reasonable return in ROIC over a period of time. As a top priority for external spend, I expect that to continue to be a reasonable part of the balance on capital deployment.

The third priority of course is returning cash to shareholders. What we said is that we're going to neutralize the equity program and then some. You've seen us do that over the last several quarters, we brought the share count down somewhat.

And I wouldn't be surprised by the way to see some further deleveraging at some point. We don't have -- deleveraging is event driven at this point when debt instruments mature, but I would think over the next couple of years, you'll see some further deleveraging as well. So that's the order of priorities at this point.

Glen Santangelo - *Credit Suisse - Analyst*

Okay, thank you.

Operator

John Kreger, William Blair.

John Kreger - *William Blair & Company - Analyst*

Bret, can you talk a little bit about what you're seeing in some of the key specialty markets? Are you seeing any lift for example in the orthodontic market? And I think in the past you've talked about some pricing pressure there, curious if you've seen any change?

Bret Wise - *DENTSPLY International Inc. - Chairman and CEO*

Sure. First of all specialty markets for us are comprised of endo, ortho and implant. The endo market continues to perform quite well for us. That's a product that's sold primarily through distribution but in a couple select countries sold direct. That's a market also where we've brought out quite a bit of innovation and we got a strong innovation pipeline going forward. So I expect that to continue to be a growth market for us.

Implant is a bit of a mixed bag. As we -- I commented earlier that it's growing nicely in the US. It's not growing in Europe at this point. We've got a new implant on the market that's gaining a lot of attention. We view that as an upside opportunity for us.

The orthodontic market is one that's been in a state of change for the last couple of years. There's been a lot of price pressure in that market. There continues to be a reasonable amount of price pressure. We've see some improvement in select country markets over the last year or so.

We might be reaching an inflection point I think in that market where it can improve for us. Right now it's a pretty good market for us in the US, more of a mixed market overseas. Jim, I don't know do you have anything to add on ortho?

Jim Mosch - *DENTSPLY International Inc. - EVP and COO*

Yes, I think from our standpoint what we've seen in the ortho market overall is that case starts globally appear to be flat. And that would indicate that they are slightly negative in the US and Europe and growing in rest of world. So the market overall is not significantly robust.

As Bret mentioned, the average sell price pressure than we have seen over the last couple years has continued. We were pleased we saw better performance in North America in the first quarter. So we're starting to see some movement. We are certainly being more aggressive in the marketplace and we are looking to gain share.

John Kreger - *William Blair & Company - Analyst*

That's helpful, thanks. And then Jim maybe if you could expand a little bit more on these new three reportable segments. What operational changes are you making beyond just a different way that you're reporting them to us? And I think you mentioned some short-term distractions, can you elaborate on that?

Jim Mosch - *DENTSPLY International Inc. - EVP and COO*

Certainly. I guess what I would say there's two key strategic elements here. One is to say that our ability to focus our businesses more globally. So we would have in the past, we would have specific businesses within the endodontic area for example. They certainly would have a global approach and they would work on certainly common programs, R&D, operational initiatives but they also had really very much a geographic focus.

And we would see that our groups were aligned in such a way that they would have focus on a given discipline in dentistry as well as geographic responsibilities. What we've done is we've really streamlined that and we sought to create segments of like businesses that focus on a given segment of customers.

Within these businesses, we sought to streamline their management structure and also to make -- create a strategy of global product portfolios. Where as opposed to looking at more regionally focused brands, we truly look globally category by category and line up brands in that fashion. We think that this approach is going to certainly create some efficiencies, but also give us a much more effective approach, a more strategic approach to the global market.

In our country organizations, I think the second thing that I mentioned was that we would look -- historically we had several different divisions operating within a country. We have sought to create really truly DENTSPLY country locations in which they all operate with a common strategy, they leverage resources and they focus on common customers. And we believe that there are a lot of efficiencies and certainly effectiveness in the market associated with doing that.

The distraction piece I would say it really comes from the standpoint that as you create -- as you realign the business strategically, as you create these efficiencies in the market place, there are changes that are occurring. There are changes in roles and responsibilities and people. You tend to see some efficiencies initially in the form of synergies. You've certainly seen some of that in our results in some of the restructuring that we've taken. But the longer term effectiveness in the marketplace does take some time as people learn new roles and new strategy.

John Kreger - *William Blair & Company - Analyst*

Great and then one last one. The US growth was really strong, curious if you think that type of growth is sustainable throughout the rest of the year?

Bret Wise - *DENTSPLY International Inc. - Chairman and CEO*

Well I think we've seen some pretty strong reports from our competitors and some of our distribution partners thus far about the US market. Of course we've said before that our -- the US market is driven primarily by job growth, in particular white-collar job growth. We've seen some pretty good improvements in that over the last several quarters, four or five quarters, and dentistry is a lagging indicator.

So typically we pick up a couple of quarters after the labor market picks up. So there's been some bumpy economic news in the last few weeks, but over the longer let's call it four or five quarters, it's been strong. And as long as that continues, I think that you'll continue to see the US dental market perform pretty well.

John Kreger - *William Blair & Company - Analyst*

Great, thanks.

Operator

Robert Jones, Goldman Sachs.

Nathan Rich - *Goldman Sachs - Analyst*

Hi this is Nathan Rich on for Bob this morning. Wanted to go back to the operating margin performance. Chris, you mentioned the number of moving pieces in your prepared remarks in terms of what drove the margin expansion. But wanted to ask if you're able to give us a sense of how much the efficiency initiatives may have contributed to operating margin in the quarter if you try to isolate that impact?

Chris Clark - *DENTSPLY International Inc. - President and CFO*

Yes it contributed in the neighborhood of 40 to 50 bps in terms of the improvements. So we're getting a sizable help from that. As I mentioned IDS and trade show costs obviously went the other way in the quarter. But again, overall we're seeing some nice lift and if you could look back historically at this type of internal sales growth level, we would struggle to get any real operating margin lift at that sales level.

So from that angle again, I think we're pleased with the traction and again on a number of fronts including the purchasing procurement initiative as I mentioned. But again I think that we're making real solid progress.

Nathan Rich - *Goldman Sachs - Analyst*

Great. And then I think on last quarter's call you guys had talked about initially expecting the first quarter to be the most challenging from an margin perspective, so wanted to get your updated thoughts on margin progression for the rest of the year.

Chris Clark - *DENTSPLY International Inc. - President and CFO*

Yes and as we looked at last year, last year's baseline we had a significant increase 13%, 14% in terms of earnings in the quarter. We knew we were coming up against that. We also -- as we looked at FX, FX we anticipated being $0.14 for the year. Maybe a little less than fair share in the quarter was what we anticipated came in pretty much in line with basically a straight line quarter.

But we also knew we had the IDS cost. So from that angle we thought that it was going to be a little bit more challenging in terms of the earnings side. We're pleased obviously with the underlying performance. As we move forward there's a number of factors still at play. We've got -- I think that we're pleased in terms of the traction as I mentioned on the efficiency program.

FX still remains a wild card. Certainly the US growth is a help here and as that -- assuming that continues, that's helpful. Europe is a bit of a wild card as well. So again I think we've got some puts and some takes but as Bret mentioned that's why were comfortable still with the range that we have.

THOMSON REUTERS

Nathan Rich - *Goldman Sachs - Analyst*

Great, thanks a lot.

Operator

Brandon Couillard, Jefferies.

Brandon Couillard - *Jefferies LLC - Analyst*

Bret back on Europe, could you break out the growth ex Russia and CIS and probably do you still think you're taking share in the broader European market?

Bret Wise - *DENTSPLY International Inc. - Chairman and CEO*

The growth ex CIS was still slightly negative for the quarter and that was driven by lab. Without the lab we would have been -- the rest of businesses in aggregate were growing. I don't have a specific number with that but it was one minus 1.2 with CIS so it'd be --

Do I think we're taking share there? I think we are, although the data we get out of Europe is not as good as the data we get out the US. I got to triangulate the reports from distributors as well as other direct businesses that report. And in total I'd say we're still a little bit better off than the competition in the European market.

Again, we don't -- even though it was slightly negative this quarter, we don't see that as a new trend. We think that market is going to come back for a number of reasons, and we're quite positive on our ability to grow in that market over the next year or so.

Brandon Couillard - *Jefferies LLC - Analyst*

Thanks. And then you'd elaborated a little bit more on some of the moves you've taken recently in terms of procedural selling efforts. Can you give us an update on exactly where you are terms of rolling out those types of programs and is that something you think can be noticeably accretive to the top line?

Jim Mosch - *DENTSPLY International Inc. - EVP and COO*

Brandon, this is Jim Mosch. Yes, we've -- our restorative group has probably led the way in this area probably followed by our endodontic businesses. And this procedural selling approach has been very, very well received.

We've rolled out the class 2 globally. We have started the crown and bridge procedure and RestoDontics are primarily in Europe and US at this point in time. Excuse me, crown and bridges in Europe and US and RestoDontics is in Europe. And we seek to create more of these programs.

And they probably do a couple of different things for us. One is they group our products in a logical sense in the way clinicians use them and how they understand they're to be used. They also make it very understandable for our field organization as they represent and position these products. And so we found it to be very, very effective in the marketplace.

It also helps us, which when we talked about some of our strategic initiatives, it also helps us to build bridges between our various businesses products, like endodontics and restoration, lab and restoratives. So we see that we will continue to work on these procedural programs and role them globally and they are definitely having an impact. We see substantial growth in the products that are in these procedural selling programs.

Brandon Couillard - *Jefferies LLC - Analyst*

Super, thank you.

Operator

Steven Valiquette, UBS.

Steven Valiquette - *UBS - Analyst*

So from my point of view obviously I still think the US growth was phenomenal acceleration. Somebody asked about it a little more color there I guess I got a few questions tied to that as well. Wanted to confirm I'm guessing that's still overwhelmingly driven by volume increases or I'm curious though if there was any sort of price or mix component that was affecting that? And then also it wasn't crystal clear but just to clarify maybe how much implant growth may have drove some of the acceleration US versus a basket of other products outside of implants? Thanks.

Bret Wise - *DENTSPLY International Inc. - Chairman and CEO*

Okay, Steve, I'll take a shot at some of this and Chris will probably fill in some of the blanks here as well. Implant growth didn't influence the number one way or another significantly in the quarter. So it was a broad basket of improvement across many product categories that we had. I think that the growth in the US is in part volume at this point. Price mix probably plays a role as well. I'm going to ask Chris is he can -- can you comment on --

Chris Clark - *DENTSPLY International Inc. - President and CFO*

Yes from a price standpoint, we think price is in line with what traditional price would be, typically in the 1.5 point range. We believe in the US improvements year on year and that's associated with the price increases we took last October.

Steven Valiquette - *UBS - Analyst*

Okay, that's helpful. Thanks.

Operator

Steve Beuchaw, Morgan Stanley.

Steve Beuchaw - *Morgan Stanley - Analyst*

A couple of fine points. First for Chris, it's clearly a strong story here in terms of the free cash flow growth, but given how many moving parts there are I wonder if you could speak to the sustainability of the free cash flow growth over the balance of the year or would you be willing to provide or update a figure on where you think cash flow -- free cash flow rather could come out for the full year?

Chris Clark - *DENTSPLY International Inc. - President and CFO*

Yes see we don't guide on that specifically, by what I would say is that again we've been helped over the last five, six quarters really with improvements in net working capital. We have a strong focus there.

But sometimes that's an actual improvement sequentially in terms of working capital coming down. In some cases like in the first quarter, it actually came up a little bit as we have some seasonality typically where we do bring inventories up a little bit in the first quarter and really the first half of the year and then it come down -- tend to come down in the second half of the year. But they did not increase as much as they did in the prior year.

So again, we have a very strong focus on net working capital. All of our business leaders have specific targets and objectives based on these. It's an element of the Senior Executive compensation plan as well. So again I think that that's certainly driving focus and I would anticipate that continuing to help.

I would say the reason why it may not be 100% sequential as we think about structural changes or anything in terms of changing any operational specifically regarding facilities, we would typically build some inventory, transitional inventory in between. So you may see some -- from time to time over the next several years some transitional inventory there. And as well obviously again the underlying demand coming through.

I would say from a CapEx perspective in the first quarter relating to free cash flow, first quarter was phasing-wise a little bit lower than what we would expect. I would still guide in the neighborhood of $100 million for the year. But again, obviously as we look we would anticipate continued improvements generally in terms of overall free cash flow over a longer period of time.

Steve Beuchaw - *Morgan Stanley - Analyst*

Much appreciated. And then a question on implants, I'm not sure if this is better for Bret or for Jim. But I would if you could talk about your experience over the last 12 months or so with EV on the market specifically with regard to market share. Now that you have the product line out there, the sales force ramped up, maybe not in all regions but in certain regions, how do you think about your competitive positioning relative to EV? Is this what you need to continue to hold or gain share in the market? And maybe this is more for Bret, how are you thinking given that experience about the potential for broadening the bag in implants? Thanks.

Jim Mosch - *DENTSPLY International Inc. - EVP and COO*

Yes, I'll handle the first question. The EV launch continues to go very well. I think as we've outlined in the past, I think this system was very much designed for clinicians. It offers a lot of simplicity and effectiveness in the implant procedure and really identifying, taking out steps, making it to be a very easy to use system.

As we reference last year, the -- we launched it later in a couple major markets really being the US and Germany. We really got going into Q3 of last year and as a result we expect to see continued growth in those regions.

Conversion rates are very good. And I think as a reference last time we are seeing that our EV conversion is up around 50% and growing rapidly. So we're pleased with how EV is positioned. And we believe that while we really officially launched this in March of last year, we think that the launch has a lot of legs left and that we continue to see penetration throughout the rest of the year.

I would also say that we continue to launch in the bio materials area which we did at IDS. We continue to expand our digital portfolio which we also did at IDS with the new SIMPLANT 17, a new -- a 3D editor for our ATLANTIS system, new ATLANTIS platforms. So EV is a big part of this story, but it is also a portfolio approach that will move us forward.

Bret Wise - *DENTSPLY International Inc. - Chairman and CEO*

Steve, I'll comment on the broadening the bag question. Jim described that we've -- in the bag we have today he have premium implants and basically all the support services that are needed to help the clinician be efficient in implant placement.

I assume by broadening the bag you're talking about either mid range or value priced implants versus the premium category. We continue to participate in that value range through our investment, minority investment in a South Korean implant company. We're monitoring that -- the market in total closely, it has become a reasonably large market.

As we evaluate companies in that category, we find a lot of that aren't making money, we find a few that are. So we're looking for the magic sauce there and we have not decided to make a move in that category at this date.

Steve Beuchaw - *Morgan Stanley - Analyst*

Much appreciated. Have a good morning.

Operator

Erin Wilson, Bank of America Merrill Lynch.

Erin Wilson - *BofA Merrill Lynch - Analyst*

Sorry if I missed this, but at the distributor level was there any meaningful distributor inventory restocking, destocking and in particular the US as well?

Chris Clark - *DENTSPLY International Inc. - President and CFO*

No, what we say Erin, Erin it's Chris, what we saw in the quarter was pretty consistent with what we saw in general in aggregate last year in the first quarter. So yes maybe some changes on an individual business plus or minus. But one exception to that obviously is Japan where again there was significant stocking in the prior year base.

Erin Wilson - *BofA Merrill Lynch - Analyst*

Okay, great. And then given the strong cash flow characteristics here and you mentioned M&A as one that top priorities, but what has been the hold up on the M&A activity, are valuations just egregiously high right now? Or is it patience around finding the right asset or can you elaborate what you're seeing out there?

Bret Wise - *DENTSPLY International Inc. - Chairman and CEO*

I think valuations are little bit frothy at this point, However, for the right asset we would probably pay up. I think it's more finding the transactions which are executable now, fit our strategy and also deliver the financial matrix that we want. I would say we're reasonably selective at this point. There have been some assets that have come to market that we've passed on just because they didn't fit those criteria for us.

Erin Wilson - *BofA Merrill Lynch - Analyst*

Okay, great. And then as we think about contributions from the launches at IDS over the course of the year, should we expect this to be similar to previous years or is anything expedited or delayed or anything like that would be helpful.

THOMSON REUTERS

Jim Mosch - *DENTSPLY International Inc. - EVP and COO*

Yes Erin, I think when we look at the IDS we tend to see maybe a little bit of a bump in the quarter after. But I would say generally the profile of launches -- IDS seems to have an impact on Germany and Europe. Rest of world launches come later. We have a good portfolio of launches throughout the balance of the year and I would expect that to be fairly consistent year on year.

Erin Wilson - *BofA Merrill Lynch - Analyst*

Okay, great. Thanks so much.

Operator

Jeff Johnson, Robert W. Baird.

Jeff Johnson - *Robert W. Baird & Company, Inc. - Analyst*

Wanted to check in one more question on the margin side. It looks like to me currency may be helped by about 50 basis points this quarter at the operating line, Chris can you confirm that? And then if that's true if margins are being rebased 50 basis points higher or so due to currency, is there a chance that 20% guidance for 2017 has some upward bias to it? It looks like to me this year you're already going to be north of 19% with the currency help there, so it would seem to me there might be some upward bias that 20% goal, but I'd like to hear your opinion on that.

Chris Clark - *DENTSPLY International Inc. - President and CFO*

Yes Jeff, there's no doubt that currency is having an impact on the operating margin. I think that obviously we gave you the impact on the top line, right now that impact on the top line is larger than the impact on the bottom line. And that obviously by definition driving operating margin improvement, if you will, from FX.

Some of that is -- a good chunk of that is becoming basically as a result of the cash flow hedges that as we indicated mitigate in the near term the full impact of FX coming through the P&L. So FX I would anticipate being a, and I think we commented on this in February, being a tailwind, if you will, right now to the operating margin improvement. But turnaround if these rates stay where they are, it'll turn around will be a headwind basically as the hedges basically expire and then it replace with hedges at the same rate, which would not have any impact.

So again, I think you're correct in terms of identifying FX is certainly helping us right now, we called it out. But again I think beyond that, the FX will swing around and be a hit to operating margin at some point if rates stay where they are.

Jeff Johnson - *Robert W. Baird & Company, Inc. - Analyst*

Okay, that's helpful. And then two little modeling questions here at the end. But equity and affiliates looks like it was a bigger loss than we've seen really in your history. Can you walk us through maybe that? And then net interest was a little higher as well and I'm assuming that has to do with hedging, but maybe any clarity there would be helpful for modeling purposes.

Chris Clark - *DENTSPLY International Inc. - President and CFO*

Yes, sure. So the equity piece comes from our investment in the South Korean implant manufacturer. And we have an ownership stake in that, a minority stake as well as some convertible bonds with that. And so as such as their stock price increases, the market value change and the convertible bond drops as the fair value of the liability of the bond increases on their books.

So we then have to take a -- basically our percent ownership of that drop and that's what you see coming through. So they had a pretty significant ramp up, if you will, in their stock price in the quarter and as such when that happens than that's a bigger loss coming through for us. And again that's moved from our non-GAAP results because it's a fair market value adjustment.

In terms of interest and other, several things going on there. In terms of the -- on a non-GAAP basis, basically which removes again the mark-to-market impacts. Basically net interest we had help in terms of lower debt levels but that's offset by lower interest income from derivatives.

And again what you see actually it's -- on a non-GAAP basis about $1 million year-on-year improvement combined between interest and other, and that's really mainly at this stage coming through the other income expense line which is favorable pick up on FX gain and loss in the quarter.

Jeff Johnson - *Robert W. Baird & Company, Inc. - Analyst*

All right, very helpful. Thanks, guys.

Operator

Jon Block, Stifel.

Jon Block - *Stifel Nicolaus - Analyst*

First question on Europe, if I look at European growth ex CIS it seemed like a stepped down from roughly 3.8% last quarter in 4Q to I think you mentioned negative 0.9% in 1Q 2015. And it doesn't look like it's a comp issue, so curious on any additional thoughts in Europe. It does appear like a pretty big step down and again one of your main competitors cited European weakness, but they seem to imply the weakness was maybe a little bit more temporary in nature. So can you touch on what you're seeing there and your confidence on restaging growth in Europe this year despite the comps getting more difficult (inaudible)?

Bret Wise - *DENTSPLY International Inc. - Chairman and CEO*

Yes, I'll take a stab at this and then Chris can comment if he has anything to add. We have seen the European market move around a quite a bit. There's -- it's not really one market, there's seven or eight key country markets in there. I'd say for the last two quarters of 2014 we saw a more consistent uptick across all those markets.

In the first quarter we saw more of a mix. So we saw some slowing in several country markets and we saw continued growth in several markets. As we talk to our people on the ground in those markets, they don't believe that it's a long-term negative trend. They think it is just the markets pausing for a bit, and they expect that those will recover and improve as we move through this year.

I don't have a lot more data than that other than the feedback we get from our people that are closest to the market. Chris, do you have anything to add to that?

Chris Clark - *DENTSPLY International Inc. - President and CFO*

Yes, I might add I think we said in last couple quarters as well when asked about Europe that it was tough to tell how much was us and how much is market. And again I think what we tried to indicate to you was that we weren't as confident that the underlying market was moving at that same rate as what we were. And again I think that obviously in the fourth quarter -- in the first quarter here we do believe the markets are a little bit more tempered per in line with Bret's comments.

The other piece I guess I would say is for us there's no doubt that the changes we're making on the lab business are probably incrementally more of a distraction as we move through this. It's a distraction, if you will, from an organizational perspective but as well we've announced the discontinuation, or the intended discontinuation of some product lines, and that's going to carry with it a headwind as well.

So we've got a few things I think a little bit more temporal in terms of unique to us particularly in the lab side that probably are taking in in a little bit bigger factor right now. Obviously we're doing the -- pursuing this action to improve that business moving forward and we're still confident in that trajectory.

Jon Block - *Stifel Nicolaus - Analyst*

Okay, great. And maybe one more for me, some other ones were previously answered. But you mentioned the implant strength in the US and that was aided by EV. Any changes in the mix you're seeing in the industry between specialist and GPs and obviously Straumann, they're out there with their efforts with one of the big distributors. And curious now that they might be six or so months into that initiative, your thoughts if you need to augment your selling efforts more specific to the GP channel? Thanks, guys.

Jim Mosch - *DENTSPLY International Inc. - EVP and COO*

Certainly, I will take that one. Jon, I guess what I would say is that when we look at that strategy, obviously there are GPs that are placing implants. We have GPs that are placing implants.

As you -- and that's a phenomenon that you very much see in the US market piece because you clearly have a specialist, a general practitioner delineation. When you go outside in other markets obviously you have all types of individuals are placing implants. So that strategy maybe is a little bit muted.

At this point in time we can't see that we've seen major movements as it relates to GPs placing implants. As we see the North American market today, still the majority of implants are placed by specialists, oral surgeons, peridontists, prosthodontists. And I think that is -- we believe that trend will continue.

Certainly that strategy can bear fruit, but it would take a very significant move to see it, is I guess is what I'd say just because of the predominance. We estimate that roughly 90% of implants are placed by specialists today. So that can give you an idea the magnitude of change that you would need in order to really see that impact.

At this point in time we work very actively with GPs on a restorative side. We have obviously a good digital portfolio which supports that as well. And from our standpoint, the general practitioners have a very positive financial situation in doing the restoration on implants. And we continue to work very, very hard to support that end of the business. If they have a desire to place, we support them on that as well.

Jon Block - *Stifel Nicolaus - Analyst*

Great, thanks for your help.

Operator

There are no additional questions, I'll turn the conference back over to Derek Leckow for any additional or closing remarks.

Derek Leckow - *DENTSPLY International Inc. - VP of IR*

Okay thank you all very much for your interest in DENTSPLY. That concludes our conference call. If you have other questions, I'm available for follow up. Thank you, bye.

Operator

And ladies and gentlemen, that does conclude our conference for today. We thank you for your participation.
