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XRAY - Q3 2012 Dentsply International Inc Earnings Conference Call

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OVERVIEW:

XRAY reported net income attributable to Co., on as reported basis of $53.4m or $0.37 per diluted share and on adjusted non-GAAP basis of $74.1m or $0.51 per diluted share. Expects full-year 2012 adjusted diluted EPS to be $2.19-2.24.

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PRESENTATION

Operator

Good day, and welcome to the DENTSPLY International third quarter 2012 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. Please go ahead, sir.

Derek Leckow - *DENTSPLY International Inc - VP IR*

Thank you very much Alicia, and thank you all for joining us this morning to discuss DENTSPLY International third quarter 2012 results. Joining us on the call today are Bret Wise, Chairman and CEO; Chris Clark, President and COO; and Bill Jellison, Senior Vice President and CFO. We'll have some prepared remarks and then we'll be glad to answer any questions that you may have.

I hope you all had a chance to review our press release which we issued earlier this morning. A copy of the press release is also available for download on our website, www.dentsply.com. We've also provided a set of supplemental slides to accompany this call, also available for download under the Investor Relations section.

Before we get started it is important to note that this call may include forward-looking statements involving risks and uncertainties. These should be considered in conjunction with the risk factors and uncertainties that are described in our SEC filings. 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, and a recording of this call in its entirety will be available on our website.

As you can see in this release, our results this quarter include a number of a nonrecurring items and other non-GAAP adjustments. Our comments on this call will focus on results, including certain adjustments that provide operational insight beyond some of the distortion from these items. These items are noted on the non-GAAP reconciliation tables contained in the release. You will note that our earnings guidance is also presented on an adjusted basis.

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

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

Thank you, Derek. Good morning everyone. Thanks for joining us on our call this morning.

Today we are very pleased to report another record third quarter with strong sales growth and by acquisitions, but also internal growth across all of our major regions. Adjusted earnings growth was also double digit, which we viewed as a strong performance in light of a relatively weak globally economic environment here. Overall, looking at the market first, in our view the global dental market in the third quarter was generally comparable to what we saw in the second quarter.

The US is stable but not really robust at this point. Europe continues to be a mix of slow growth in the north and continued contraction in the south. Combined the European market is probably flat, plus or minus, at this point.

The rest of the world markets, which as you know comprises many different countries for us, continues to be a mix of slow growth in the developed regions that we have in that category, and mid- to in some cases double digit growth in most of developing markets that we include in rest of world. Overall, I'd say the market, the dental market, is doing okay at this point, but it is not great.

Getting into details a bit on our sales performance, on an organic basis it was notably better than what we view as the market growth at this point across most geographic regions, and also in most product categories. Total growth with precious metals was a positive 12.3%, and without metal was positive 14.8%. This 14.8% growth was driven by acquisition growth, which was a positive 15.4%, but also by internal growth which was positive 4.7%, giving us constant currency growth for the quarter at a little bit over 20%.

Currency was negative by 5.3%, and that of course creates headwind for earnings as we discussed in our we discussed in our second quarter call, particularly with the weakening of the euro over the second and third quarter. The 4.7% internal growth was spread pretty equally across the regions with the US up 3.9%, Europe up 5.2%, and rest of world was up 5.1%. Also important, this the first quarter in six that the orthodontics business has turned around and been accretive to our growth, consistent with our relaunch plans, that of course we've discussed on numerous of these calls dating all the way back to the natural disaster in Japan in March 2011.

Internal growth ex-ortho in Japan was a positive 2.8% so ortho added about 190 basis points this quarter. Just as a reminder, from the second quarter call we did relaunch the orthodontics line in Europe late in the second quarter. So we were live in the market for the entire third quarter. In US we went live in August in the third quarter, so the impact in this quarter was much less in the US.

For competitive reasons, we are going to get away from giving you precise information by region on orthodontics; however, for your purposes you should assume that the impact of orthodontics was much greater in Europe this quarter than in the US, due to the timing of the relaunch execution as discussed here. And Chris is going to have some further comments on orthodontics in his prepared remarks as well this morning.

Lastly on internal growth, there's some important calendar implications for us this quarter in packing our measurement, meaning changes in shipping days, particularly for Astra Tech in September. Bill's going to cover this in more detail, but I think it is fair to say that the way the calendar happened to fall this quarter reduced our internal growth by more than a full percentage point.

From a product category perspective, our internal growth was the highest in the dental specialties, followed by consumables, both of which were positive, and lab was slightly negative in this quarter. There's always a lot of interest about implants where our growth was slightly negative in this quarter, and that's impacted by the calendar days' timing that Bill is going to cover.

From an earnings standpoint, we are very pleased to see some expansion in our adjusted operating margins year-over-year this quarter, and that's despite having Astra Tech in the base only for one month last year, and of course for all three months this year. We view this is an important step forward in restoring our operating margins to the pre-acquisition levels that we saw over time, and we're pleased to see the margin expansion begin to merge here, although it's small, it's only 10 basis points on an adjusted basis points on an adjusted basis. We are also targeting some good operating margin improvement as we move forward, despite being a slow growth market at this point.

The Astra Tech acquisition continues to perform well, although we would like to have seen a stronger implant market at this point. The slower growth in the implant market is providing us with some opportunities, perhaps flexibility actually, to pursue synergies more quickly than we would have otherwise if we had been in a different market circumstance at this point.

We're also pleased with the continued growth of our Healthcare business. We now refer to that business as Wellspect. It was renamed in August of this year, and it is performing well, even in the midst of a slow growth economy. Today we're very focused, of course, on completing the integration, achieving the synergies, maximizing our digital portfolio, and for the dental business realizing the benefit the part of a much larger and focused dental products Company.

So at this point we feel pretty good about how we've successfully made our way through a slow growth market at this point. We've been through many currency fluctuations. We've absorbed an orthodontic supply outage that essentially consumed 5% of our revenue, and we feel pretty good about how we've integrated the largest acquisition in our history.

But we do see number of great opportunities going forward. Our product portfolio today is very strong, as is our pipeline of products coming forward. We have good opportunities to improve margins as we continue to drive synergy opportunities from the integration, but also in our base business as well. And we also believe that the broader dental market will gradually improve once job growth begins to take hold.

Lastly, looking at the outlook, and as noted in our release, we're modifying our guidance slightly for the full year by increasing the low end of the range, such that the new guidance for full year 2012 is now $2.19 to $2.24. That concludes my prepared remarks. I'd like to now turn the call over to Chris Clark.

Chris Clark - *DENTSPLY International Inc - President and COO*

Thank you Bret, and good morning everyone. I'm going to take a few moments and provide some deeper insights into the recovery of our orthodontics business, as well as a brief update on our Astra Tech integration efforts.

As Bret mentioned, we've now relaunched our orthodontics products line on a global basis, with the US relaunch following that of Europe and the rest of the world. In aggregate, the orthodontics business contributed 190 basis points of internal growth on a global basis, and also solid earnings improvement, both of which were in-line with our internal expectations. We are pleased with a number of very loyal customers that have come back to the business as result of product availability, and by our sequential progression over the past couple quarters. We have been saying that we expected to recapture about a third of our lost share quickly, and that has proven to be true and very much inline with our expectations.

One highlight that I'd like to mention from the past quarter was a European GAC Symposium in Lisbon last month, which was a significant gathering of our largest European customers, and also had record International representation. We were very pleased with the positive tone of the customer base and excitement regarding our plans and approach, including our expanded investments in R&D which I commented on last quarter's call. Our focus now expands to the next segment of lost customers, who will be much more difficult to recapture as a result of the competitive nature of the orthodontics market, and also the aggressive actions that we anticipate from our competitors as they try to hold onto these former GAC users.

We anticipate an aggressive fight at the street level to gather back our customer base, really a battle on kind of an account by account basis over the next few years. We're helped in our efforts here by the strength of our brands, and also by the goodwill that was created by our transparent approach to our customer base throughout the supply crisis. While we continue to believe that this will be a multiyear competitive effort to recapture our lost market share, our performance to date and trajectory are in line with what we expected, and we believe that orthodontics will continue to be accretive to our growth rate during the recovery process.

I'd now like to provide some brief comments on the Astra Tech integration efforts. In short, we continue to be pleased with the overall progress of the integration. We've now expanded our launch of the DENTSPLY implants organization to include Italy, Nordics, Dentalux in United Kingdom. That's in addition to the launches in North America and Iberia earlier this year. We're moving forward with other countries between now and early 2013.

Sales training continues to be a significant focus, and we are pleased with the competency and also the confidence levels that the sales organizations are showing with the combined product portfolio. Customer feedback to the combined organization and the integrated DENTSPLY implants portfolio has been very positive, as was the reaction to the integrated DENTSPLY implants presence at the recent European Academy of Osseointegration meeting that was held in Copenhagen earlier this month.

Beyond the field integration activities, we're also proceeding on track with our headquarter integration efforts, and overall we are very much aligned with our cost synergy assumptions. Moreover, the business is increasingly addressing strategic areas, such as clinical research, key opinion leader management, research and development and strategic marketing, really on an integrated basis rather than as two separate businesses. We're very pleased with the level of collaboration and with the morale within the team, as they clearly see the strength of the combined DENTSPLY implants organization and the significant market potential that we have moving forward.

While the implant market may not be a strong right now as we might've hoped, the strategic and synergistic benefits of the acquisition integration are every bit of what we expected, and we remain very pleased with the progress. I'd now like to turn the call over to Bill Jellison, who will cover the financial results for the quarter in greater detail. Bill?

Bill Jellison - *DENTSPLY International Inc - SVP and CFO*

Thanks Chris. Good morning, everyone.

Bret already discussed our sales growth within the quarter, but I would like to add a couple of additional comments. We believe the calendar had a negative impact on our sales growth by approximately 1 to 1.5 percentage points in the quarter, due to two issues. First, the third quarter of this year had one less selling day than the third quarter last year. But second, the month of September this year had two fewer selling days than it did last year, and September is the only month in the quarter that Astra Tech is included for the calculation of our internal growth, since that is when it began being included in our consolidated financial statements last year.

So we believe on an -- or that our internal growth rate of closer to 6% -- or closer to 4% excluding ortho Japan, is more representative of the performance that we had in the third quarter of this year adjusted for days. This is only an estimate to allow you to better understand our results, though, for the third quarter. In looking at our geographic mix of sales ex-precious metals in the third quarter of 2012, the US was 36% of our total sales, Europe represented 42%, and the rest of the world was 22% of sales. Despite the recent weakening of the dollar within the quarter, we still were negatively impacted by a strong dollar year-over-year in the third quarter by 5.3 percentage points.

Our earnings per share were also negatively impacted by FX rates in the quarter, and the impact was probably in the range of about negative $0.01 to a negative $0.02 per share, and on a year-to-date basis it was approximately a negative $0.04 to $0.05 per share. At current exchange rates, we expect the fourth quarter impact of exchange to be a little bit better but still negative, probably in the 2% to 3% range, both on sales and on earnings. As Derek mentioned and as you can see in our earnings release in this quarter, this quarter included a number of items which impacted our results. By excluding these items from our results we believe the adjusted figures provide a more comparable picture of the Company's performance, and most of the following comments exclude the impact of these items.

Gross profit margins on an adjusted basis as a percentage of sales ex-precious metal content in the third quarter of 2012 were 56.9% compared to 56% for the third quarter of 2011. When compared to the same period last year, the gross profit margin rate was positively impacted by improved pricing, foreign exchange rates, and products mix.

SG&A on an adjusted basis was $256.7 million, or 39.7% of sales ex-precious metals in the third quarter of 2012, versus 38.8% in the prior year's third quarter. Astra Tech, which runs higher SG&A expenses then our base business, has a negative mix impact on SG&A expenses as a percent to sales, however next quarter this will be in both the current year and the base period, and when more comparable on year-over-year basis.

Operating margin rates based on sales excluding precious metals on an adjusted basis were 17.3% compared to 17.2% last year in the same period. Despite not having Astra Tech in two months of the base period, we were still able to begin to show some year-over-year improvements in the rate. As Bret noted, our orthodontic business began to show year-over-year improvement once again in the quarter after the negative impacts we experienced with our supplier that was impacted by the natural disaster in Japan which occurred in 2011. While the year-to-date impact is still negative by approximately $0.01 to $0.02 per share over last year, we expect this to be flat to slightly positive for the full year of 2012.

Net interest and other expense in the third quarter on a reported basis was $12.9 million, compared to $20.8 million last year in the third quarter. This reduction in expense resulted primarily from about $12 million of acquisition expenses associated with the closing of the Astra Tech transaction in last year's third quarter, which we highlighted as an adjustment for our non-GAAP EPS. On an adjusted basis, this category is higher by approximate $4 million compared to last year in the quarter, which is primarily associated with higher interest expense as the financing for the acquisition was not in place for the whole third quarter of last year.

Our reported tax rate for the third quarter was 25%, however there are tax adjustments reflected in the rate of both periods. On an adjusted basis, our operating tax rate for this quarter was slightly over 23%, compared to a slightly higher adjusted tax rate in the third quarter of last year. We believe that an adjusted operating tax rate of approximate 23% to 23.5% is reasonable, both for the balance of this year as well as for 2013.

We continue to work on our international structuring as we finalize some of the activities and impacts from our recent acquisitions, and we continue to expect some favorable impacts from these efforts, especially in areas of improved cash flow and repatriation efficiencies. Net income attributable to DENTSPLY International in the third quarter of 2012 on an as-reported basis was $53.4 million or $0.37 per diluted share, compared to $60.6 million or $0.42 per diluted share in the third quarter of 2011.

Net income attributable to DENTSPLY on adjusted non-GAAP basis was $74.1 million or $0.51 per diluted share in 2012, compared to $66.2 million or $0.46 per diluted share in the third quarter of 2011. Cash flow from operating activities in the first nine months of 2012 was approximately $202 million compared to $2 million -- or $255 million in the same period last year. Cash flow from operating activities, though, in the third quarter increased approximately 10% compared to the third quarter of last year.

Inventories increased in the first nine months of the year in support of the rebuilding of inventory for our orthodontics relaunch to support inventory levels during our integration activities, and to support a couple of our other product lines. Cash flow was also negatively impacted by the timing of some tax payments that fell into the first half of this year.

Our capital expenditures were $65 million in the first nine months of the year, with depreciation and amortization at $103 million. Inventory days were 111 at the end of the third quarter of 2012, compared to 109 days at the end of the third quarter of 2011 and 100 days at the end of last year. Our accounts receivable days were 60 days, including slightly higher days for Astra Tech, at the end of the third quarter of 2012, compared to 61 days at the end of the third quarter of 2011. At the end of the third quarter of 2012 we had $56 million in cash and short term investments, and our total debt was $1.65 billion at the end of that third quarter.

Finally, as Bret stated, we are updating our earnings guidance for 2012. As you recall, our previous earnings guidance was $2.18 to $2.24 per share on an adjusted basis. As we look toward a year end we are comfortable now with guidance for earnings on an adjusted basis of $2.19 to $2.24 per diluted share.

That concludes our prepared remarks, and we'd thank you for your support, and we'd be glad to answer any questions that you may have at this time.

QUESTIONS AND ANSWERS

Operator

Thank you.

(Operator Instructions)

We will go first to Brandon Couillard from Jefferies.

Brandon Couillard - *Jefferies & Company - Analyst*

Hi, good morning. Things for taking the question. Bret or Bill, what was the core implant revenue growth experience, excluding the effects of the shipping day variances, and if you could comment just on the trends you saw by geography, I guess on a core basis, that would be helpful, and then I know one of your competitors called out a pretty abrupt market issue in Japan. How was your -- how did your business fare in that region, and could you quantify the size of your implant revenue in that market?

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

Sure, Brandon, good morning. Core implant growth for us was negative, slightly negative as we said. If you'd looked at it days adjusted, it would've been flat, maybe slightly positive. I think the trends are that the US market continues to grow, the European market probably is not growing at this point, and then in the rest of the world category it kind of varies by country, and also a lot of those markets you sell products by tender. So there can be kind of on large time sales that can be disruptive. Looking at the trends for us, the US was our best market, Europe was next, rest of world was the slowest market for us, but as you point out here that includes Japan where the market was disrupted by several events. Japan is not particular large for us. It probably -- Japan for the whole Company is 4% of our revenue, and in our implant business it's probably around that, plus or minus a percentage point or so. So it did have an impact on us in the rest of world category, but it is not really that significant as a percent of the total implant business.

Brandon Couillard - *Jefferies & Company - Analyst*

Thanks, and then Bill, can you give us an update on operating cash flow and CapEx expectations for the year, and should we anticipate CapEx to step down materially next year, and then just what are your thoughts about capital redeployment near-term?

Bill Jellison - *DENTSPLY International Inc - SVP and CFO*

Sure. So on the CapEx side of the equation, I think that originally at the beginning of the year we said that CapEx spending was probably going to be in the $100 million to maybe $120 million range. I think we've obviously looked at number of those projects, and some of that has been just taking time to actually get into the system and getting actually spent. I'd say that instead of that range, it is probably going to be in maybe the $90 million to $100 million range yet this year, but some of those projects are obviously still in the scope. They will probably get spent next year. I believe that if you look at kind of a spend level, it is probably going to be incrementally again higher than it is this year. So probably closer to maybe the $120 million, $110 million to $120 million level next year, although we've not really giving any specific guidance on the year and/or our CapEx.

As it relates to cash flow, I think that we've got some good projects that are continuing to progress forward. We've built the inventories this year, which have obviously had a negative impact on cash flow early on, for a couple of specific reasons. I think that's probably going to be reduced as we move forward over the next few quarters, as we ultimately get a couple of those areas back down to a level that we think is more appropriate, and I think that as we move toward the end of this year we will probably have, again, a strong fourth quarter cash flow.

Brandon Couillard - *Jefferies & Company - Analyst*

Great, thank you.

Operator

We will go next to Glen Santangelo from Credit Suisse.

Glen Santangelo - *Credit Suisse - Analyst*

Yes. Bret, I just want to kind of follow up with some of your opening remarks. You seemed to talk about the US dental business as sort of continuing to grow at a relatively anemic pace, and you talk about Europe being flat, and yet I kind of look at the same-store results, or internal growth numbers, constant currency that you guys are putting up, and days adjusted. It seems like it is closer to mid-single-digits, and so I was wondering if you could just help us reconcile maybe what's enabling DENTSPLY to kind of grow, let's call it 300 to 500 basis points faster than the market? Is it a market share issue, or it something within your customer base? Any sort of color would be helpful.

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

Okay. Glen, I will try to do that. When you look at our internal growth this quarter at 4.7%, 190 basis points, that is orthodontics. So something in the 2.5% to 3% range is kind of the organic growth rate. It would be higher on this days adjusted basis, but let's call it a 2% to 3%. I do believe that the global dental market is growing a little bit slower than that. Certainly Europe is a little bit slower than that, but our business has been taking share in Europe for numerous quarters in a row here. I'm not even sure how far back I should go, but I think ex-orthodontics we've been positive 10 or 11 quarters.

Chris Clark - *DENTSPLY International Inc - President and COO*

11 quarters.

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

11 quarters in a row, which is in many ways remarkable, given the economic circumstances there. We did, going back to 2008, 2009, we did increase and make some important investments in R&D, and we had been pretty transparent with the investment community that was going to result in more new products coming out. Those products hit in 2011, early 2012. They've been performing very well. I think they've been driving market share gains for us. So we have been performing above the market across numerous regions. I didn't really get into the US here, but US, Europe, and also rest of world categories because of those new product launches as they've rolled out. So even as we anniversary those, we're still growing above market, and I think it's still attributable to the new innovation we brought out, not only 2011 but 2012 and what we're going to bring out in 2013.

Glen Santangelo - *Credit Suisse - Analyst*

Okay, thanks. That's helpful Bill, if I could maybe just follow up with you regarding the FX commentary you made. I think you suggested in 4Q that you thought that FX would have about a negative two to three percentage point impact on the top line and earnings. Could you just give us a sense for what some of your currency expectations are that you're using within your existing model to come to those assumptions?

Bill Jellison - *DENTSPLY International Inc - SVP and CFO*

Well, generally when we make comments on the currencies moving forward, at least from a street perspective, we are talking about rates that are consistent with kind of where they are running right now. So that would include something in the euro range that's in the $1.29 to $1.32 kind of range, and I think that's probably consistent. That will allow us to be about 0.5 of the impact roughly. We add 5%, little over 5%, of a negative impact in the third quarter. That should reduce that to close to 0.5 of that level by the fourth quarter if those rates hold up.

Glen Santangelo - *Credit Suisse - Analyst*

Okay, thank you very much.

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

Thank you.

Operator

We will go next to Steve Beuchaw from Morgan Stanley.

Steve Beuchaw - *Morgan Stanley - Analyst*

Hi, good morning guys.

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

Good morning.

Steve Beuchaw - *Morgan Stanley - Analyst*

Given that we've heard the commentary on Europe, it sounds a little bit more conservative in the last quarter. I wonder if you could give us an update on what you're seeing there with the regional breakout? Is it still a fairly isolated southern European issue? Have we've seen anything incrementally in the northern countries, some of the more centralized countries?

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

Thanks Steve, and good morning. I would say I wouldn't characterize our comments here different than they were before. If they came across that way, it wasn't intended. We're kind of seeing the same market development in Europe that we've been seeing for the last several quarters. The third quarter's always a little tough for Europe because there's some extended vacation periods and so forth, so the entire market seasonally slows down in the third quarter. So you kind of focus your view on what happens in September in that market, but I haven't seen, or we haven't seen really any dramatic change there. We see the countries in the north continue to perform reasonably well in that environment, not robust growth but growing, and we see the countries in the south still contracting. So kind of like -- that market appears to be stable but not at a great level right now, and as I said before, or in our prepared remarks, the US seems to be comparable to what we saw in the second quarter as well. So the global developed market, part of the global dental market, seems to be pretty stable.

Steve Beuchaw - *Morgan Stanley - Analyst*

Okay, thanks. That's very helpful. Than one on your comments around the med tech tax. Is still the view that we think we can pass that through here in the US with some sort of adjusted approach to the market going into 2013?

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

Yes, on the med tech tax, this is -- the timing of this is getting close here. The law goes into effect January 1, 2013. There's been no guidance on implementation yet issued by the Administration, and some guidance is needed here. But we are kind of operating under the belief that it will go live, despite there some pretty widespread opposition in Congress due to the impact on job creation, innovation, and of course there is always some chance that something will happen in this in this lame duck session. But we are doing our planning as if that's going to go live.

We're going to be implementing price increases January 1. We think we will -- those price increases will largely offset the medical device tax. I mean, there may be some small leakage in one line or another, but I don't think so at this point. We fully believe that our competitors will do the same thing and that cost, although it is small compared to the dentist total cost, will get passed through to the dentist. So yes, we are still of the belief that it will go effective and that probably going effective without implementation guidance, by the way. It will go effective and we're going to implement price increases. January 1.

Steve Beuchaw - *Morgan Stanley - Analyst*

Okay. Thanks so much, everyone.

Operator

We will go next to John Kreger from William Blair.

John Kreger - *William Blair & Company - Analyst*

Hi, thanks very much. I realize you don't normally give formal guidance for '13 until the fourth quarter call, but any kind of early thoughts if you think about the puts and takes. Seems like it maybe a tougher macro environment, but also a better contribution from orthodontics, and perhaps Astra integration? Do you think you'll be able to deliver better earnings growth perhaps in '13 versus what it looks like you'll get in '12?

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

Well, John, as you noted in the beginning of your comment, we are just entering our planning's phase, our planning stage for next year. We do our budget planning throughout November, and we kind of arrive at an outcome and targets for next year kind of mid-December. So I don't want to bypass that process in any way. You did raise a couple of issues in your comments here, the orthodontics will be a factor next year because it was a pretty large drag in the first half of 2012, although we are getting earnings growth from orthodontics now in the back half, and the integration, of course, will be proceeding, perhaps even at an accelerated pace as we enter 2013. So those are both important point for us to consider. Also important is our new product launches coming up, as well as whatever currency impact will have on the business in 2013. I don't know. Bill, do you have anything to add at this point on planning for next year?

Bill Jellison - *DENTSPLY International Inc - SVP and CFO*

No. I mean I think at this stage, we obviously don't give any kind of directional guidance for next year until we release earnings. So I think Bret's comments are solid. There's obviously a number of things that we believe that we have at least driving our business that should allow us to continue to get growth above and beyond broader market level growths, and we think that those positive factors should hopefully have some benefits for us as we move forward, but we won't give any kind of official guidance until we get into next year.

John Kreger - *William Blair & Company - Analyst*

Great, thanks. Maybe as a follow-up, can you just expand a bit more on what you're seeing in the orthodontics market as you fully relaunch your product line? Have you seen slowing in that broader market environment, given the tough macro-environment, or has that held up better than the implant market? What sort of pricing changes are you seeing from your competitors as they try to hold onto that share that they took from you guys in the past year?

Chris Clark - *DENTSPLY International Inc - President and COO*

John, it is Chris. I will take a shot at that. In terms of us having a read on the case start trend, if you will, I'm not sure we're going to be the best barometer of that, because again obviously any change in that is going to be pretty well muted based on what we see in the context of our numbers with the recovery of bringing the most loyal customers back that we've got over the last couple of quarters. I mean, my sense is that it probably is a bit slower directionally, but in terms of a real read on that, I think there's so much noise probably in our orthodontics numbers that's going to be tough for us to tell, or get more specific on. In terms of pricing, I think, as maybe as I characterized in my comments, we've gotten really the first third, if you will, back pretty much as expect, maybe a little bit faster than expected. We do think that the next third's going to be more challenging, in part because of pricing and promotional activities from competition, and there's no doubt that we're going to have to be aggressive to go after that. So I think that we are viewing this really as a prolonged street battle, and again, I think our team is up to but I think it's going to take us a while here for this next stage.

John Kreger - *William Blair & Company - Analyst*

Okay, great. Thank you.

Operator

We will go next to Jeff Johnson from Robert Baird.

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

Thanks, good morning. Can you guys hear me okay?

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

Yes, you're fine.

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

All right, great. Bret, I know you don't want to go to 2013 guidance. Let me just ask a couple questions here on maybe fourth quarter guidance. You come up against your first of a couple very tough US organic growth comps. What I think is, I've talked to you guys over the last few months. It sounds like those new products that launched a year ago have kind of built a new base of business. So should we be looking at that US organic growth comp as a big headwind or as kind of you should still be able to grow in line or above market off of the higher base of those new product sales?

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

Good morning, Jeff. That's a good question. We're coming up against two quarters where we are above 7% growth in the US, and so we do have a very strong base there, but as you point out, the portfolio is expanded with these new products, and that's why we had that accelerated growth last year. So these products are now still growing, albeit not quite at the pace they were then, obviously. So it is a high baseline, but we believe we can grow over that baseline and continue to deliver above market growth, despite having very tough comp to come up against for the next several quarters.

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

All right, great. Bill, I know you don't typically, or you don't like to guide on the margin at all, but fourth quarter last year was kind of the big margin hit down to 16% on an adjusted operating basis. It was down, I think, 400 basis points, if I remember. Good margin this quarter, even with Astra Tech in there. You were able to go up year-over-year by 10 bips. Should we be thinking about a strong, like 100, 150 basis points expansion next quarter, or am I too aggressive in those thoughts?

Bill Jellison - *DENTSPLY International Inc - SVP and CFO*

Well, you're right, Jeff. We really don't get into kind of the specific operating margin improvement on a quarterly basis, but I think that we are obviously with our year-end guidance, you know exactly what our guidance must be now for the quarter itself. So I think that you can probably kind of build into that, based on kind of the expected growth levels that we're going to have for the overall business. But I think it is at least fair to say that we've had a couple different comparisons that are in those numbers, both with the orthodontic business as well as with not having Astra Tech in our base. So at least now on a comparable basis year-over-year period, you should at least get a better picture of kind of what that's looking like and how we are positioned moving forward.

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

Jeff, I'd add, this is Bret, I would add to that operating margin -- we're very focused on operating margin expansion, and you probably saw that in our prepared remarks here. This is the first quarter, despite not having Astra Tech fully in the base, this is the first quarter we got some operating margin expansion post-acquisition, and in our prepared remarks we intended to indicate that we are very focused on operating margin expansion going forward. So it is high on our list of priorities at this point.

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

All right, that's helpful. Thanks Bret. Then last two, just quick follow-ups here for me. One, on the Japan dental implant issue. Is that just an extension, as we've heard it, of some of the issues in Korea about a year ago or so, just some media reports and things like that, or is there something structurally that could really suppress that Japanese dental implant market for an extended period of time? Then last question, just on the med tech tax. I've heard from a few of my guys out there in the field that there could be a chance here that dental gets excluded completely from the med tech tax. There's some legislative efforts at least underway on that, and I've heard it as high as maybe a 50% chance that's happening, or that could happen. Any thoughts from your end?

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

Okay. Jeff, first on the Japanese issue. There was a little bit of a media flurry that was kind of anti-dental implants, and that did impact the growth here in the short-term. I suspect that to play its way through, like that has happened in other markets with other products. There's nothing inherently dangerous about dental implants. It is a market where you need good research, you need some good clinical evidence. It takes a lot of clinical education, which is expensive, and many times it takes a direct sales force that can support the doctor. We have heard theories that dental implants don't -- no longer require that support, and thus people should just cut out the customer support and drop the price. I don't think that's a formula for success in this market.

This is a complicated surgery, and it requires that clinical support for the customer, the doctor here to get the patient outcomes. So as far as Japan, we think it'll play its way through, but it might reinforce the need for good, strong clinical education behind these brands, behind these products. With respect to the med tech tax. I don't want to go too deeply into that, but there's always a possibility that there could be a carve-out for dental. I mean, dental wasn't covered in the coverage of the new healthcare law, yet ended up paying the tax, which is kind of disconnect. Other areas of healthcare which weren't covered -- that didn't have coverage in the Act, like hearing or vision were exempted from the tax. So there's a lot of talk in Washington about getting something done on that. Getting things done in Washington is not easy, even in a normal environment, but I think is particularly difficult right now. We will have to see what happens in the lame duck session. Jeff, are you still with us, or operator, are you with us and ready to go to the next question?

Operator

Yes, sir. We will go next to Scott Green from Bank of America.

Scott Green - *BofA Merrill Lynch - Analyst*

Hi, thanks for the question.

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

Scott, we cannot hear you on this end.

Operator

Looks like his line dropped. Scott, if you're still on the line if you can press star-1. We will go next to Robert Jones from Goldman Sachs.

Unidentified Participant - - *Analyst*

For Bob Jones. I just wanted to ask, with regards to the implant market what you've seen, how it is done globally and what are your just general expectations for the implant market going forward?

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

Well, I think the implant market has probably slowed a bit. We've only got two competitors that have reported. One did a pre-release report, and so we are still waiting on a couple of companies to report to really have a full view of what the market is, but our guess is that the market has slowed kind of sequentially here. Third quarter is not a great quarter to evaluate it because the dental implant market is more mature in Europe, and Europe takes extended vacations in the third quarter. But if we had to guess, we'd say it slowed a little bit. It is an expensive procedure. It is a discretionary procedure, and it is entirely possible that as the economy kind of recovers that dental implants will start to grow more rapidly. We saw that in the early signs of recovery maybe a year ago, dental implants accelerated, and I think that would be true again if we saw some economic improvement over the coming months or quarters, that we would see the same thing happened with dental implants.

Unidentified Participant - - *Analyst*

That's very hopeful. Just to ask also, I see the US sales were very strong internally this quarter. I just want to know, are those sustainable? Do you think that those can be that robust going forward?

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

Our US sales growth I think was 3.9%. I think that's actually in some ways a little bit slower than we had, like for instance fourth quarter last year and first quarter this year. US market to us looks like it is performing pretty stable with what we saw in the second quarter. We will know more, of course, when the distributors report in the coming weeks. But I think from our perspective, we see the portfolio we have and we see how the

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products are performing versus the market, and we're continue to take share in that market, in the US market, and thus, we believe basically whatever happens with the market we can continue to grow at a premium to that.

Unidentified Participant - - *Analyst*

Okay, great. Thank you very much.

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

Thank you.

Operator

Once again we will go to Scott Green from Bank of America Merrill Lynch.

Scott Green - *BofA Merrill Lynch - Analyst*

Hi, can you hear me now?

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

Yes, you are fine, Scott.

Scott Green - *BofA Merrill Lynch - Analyst*

All right, great. Thanks for the questions. First I had one on the med tech tax. Are you assuming any pre buying ahead of that? Normally you get some pre buying ahead of normal rate increases, and maybe this one is even more in the news. Just curious about your thoughts there.

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

It is entirely possible that as we communicate our price increases to the distributor channel, it's entirely possible that some distributors will want to buy ahead of that price increase, and thus have that margin enhancement opportunity for them. It is too early for us to tell. We've kind of Incorporated in our range, we are sitting here with a $0.05 range for the fourth quarter, which is a little broader than we normally have. So with the high end of that range we are -- that would probably encompass some buy-ahead on the med tech tax issue and the price increase issue that we are going to implement. But at this stage I think it is too early to tell. We probably won't know for sure what that's going to look like until we get well into December.

Scott Green - *BofA Merrill Lynch - Analyst*

Okay. All right, then could you elaborate on implant growth. Just curious, you talk about you've relaunched the new DENTSPLY Implants brand earlier in the US and Spain, and now Italy, UK. What impact does that have when you relaunch on growth in those markets? Are you seeing a positive benefit from that, just on that new brand campaign?

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

No, I wouldn't characterize it that way. I'm going to make a comment. Chris has been closer to this than I. So he may have some further comments, but when we launched DENTSPLY Implants, what it means is we are launching the integration, meaning bringing the two organizations together. Frankly, that's more disruptive than helpful versus market growth. We end up changing rep territories, we pull reps out of the field to train them. We end up changing the product packaging, et cetera, et cetera, and the CE set up changes as well, the clinical education set up kind of changes as well. So I think what you see with us launching DENTSPLY Implants meaning from market to market, it is not really a boost to growth, it is almost more of an interruption, but that's where we getting to the synergies, that's where we are bringing the organizations together to try to harvest the synergies from the acquisitions. So I think it's an important step. Chris, I don't know if you have anything to add to that?

Chris Clark - *DENTSPLY International Inc - President and COO*

Yes. I'd characterize it, Scott, as a kind of a short-term distraction, a necessary short-term distraction for the reasons Bret mentioned. I mean, you've got new reps with new things in their bag, new products in their bag that they have to learn, new territories in many cases, new managers in many cases. But the fact is, you kind of go through that because of the significant potential, obviously of the combined organization. I think that what we are really excited about is just the positive reaction of our people, but also of our customer base to that combined portfolio and that combined business, and so again, I think that it is a necessary distraction in the short term to get the long-term gain, or medium-term gains, and it is pretty much playing out very much as we expected.

Scott Green - *BofA Merrill Lynch - Analyst*

Okay. That's helpful. And then I think the last quarter you suggested that inventories would decline in the back half of the year, and I think they were up again modestly in the third quarter. Just curious if you could update us on that and how you see inventories in the field as well that the dentists are holding?

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

Sure. I think two things there. First off, in the quarter, quarter-to-quarter, at the end of this a quarter we had about 111 days, and we actually still had about 111 days at the end of the third quarter. We are still obviously kind in the midst of the ortho relaunch, and obviously some of the integration activities and some of the new ones that Chris just talk about. I'd say that it is probably still going to take us a few quarters to get the inventory back down to kind of where we'd really like to have it in place. From a dealer perspective, or the amount of inventory at the dealer levels, actually that inventory level is down year-over-year somewhat. So there's no increase in dealer inventory levels over the last year.

Scott Green - *BofA Merrill Lynch - Analyst*

Okay, and lastly, is there a way you could characterize 2013 in terms of product launches as stronger than normal, or an average year, or lighter than normal?

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

Well, 2013 is a IDS year. So in March we will have the International Dental Show in Germany. That is usually a show where we kind of accelerate product launches, because we only have access to that group every two years. So 2013 could be kind of slightly better than normal year, I would say.

Scott Green - *BofA Merrill Lynch - Analyst*

Good, thank you.

Operator

At this time we have no further questions. Mr. Leckow, I would like to turn the call back over to you for any additional or closing comments.

Derek Leckow - *DENTSPLY International Inc - VP IR*

Well, thank you, everyone. That concludes our conference call today. We thank you for your interest in DENTSPLY, and if you have any follow-up questions please contact Investor Relations. Goodbye.

Operator

That does conclude today's conference. We thank you for your participation.