Scott P. Anderson
President & Chief Executive Officer

- Good morning and thanks for participating in our fourth quarter earnings conference call.
- Joining me today is Steve Armstrong, our executive vice president and chief financial officer.
- At the conclusion of our formal remarks, Steve and I will be pleased to take your questions.
- Since Regulation FD prohibits us from providing investors with any earnings guidance unless we release that information simultaneously, we provided financial guidance for fiscal 2012 in our press release earlier this morning.
- This guidance is subject to a number of risks and uncertainties that could cause Patterson's actual results to vary from our forecasts.
- These risks and uncertainties are discussed in detail in our Annual Report on Form 10-K and our other SEC filings, and we urge you to review this material.
- Turning to our fourth quarter results, we ended fiscal 2011 on a strong note due to the solid performances of each of our businesses.
- Consolidated sales of $883.8 million were up 9% from $812.8 million in last year's fourth quarter.
- Net income came to $62.7 million or $0.53 per diluted share, compared to $61.8 million or $.52 per diluted share in the year-earlier period.
- Now, for the next few minutes, I will provide some operational highlights of our three businesses.
- Sales of Patterson Dental Supply rose 5% in the fourth quarter to $573.1 million.
- We believe the fundamentals of the North American dental market are continuing to strengthen as evidenced by the 3% consumables sales growth that we posted for the quarter.
- Our consumables business has been strengthening in recent quarters, and we view this as a leading indicator of the overall dental market.
- As a result of improving market fundamentals, we believe dentists are gradually becoming more confident about investing in their practices.
- In addition, we instituted additional marketing programs at the beginning of the quarter.
- These factors helped generate the 11% sales growth of total equipment and software that we registered in the fourth quarter.
- Within this overall product category, sales of new-technology equipment, including CEREC dental restorative systems and digital radiography products, posted mid-teens growth, while sales of basic dental equipment recorded single-digit growth.
- All in all, we believe that we are rebuilding sales momentum in our dental equipment business and are forecasting equipment sales growth in the high single digits for fiscal 2012.
- However, it bears mentioning that our equipment sales may experience quarterly fluctuations as they have historically, given the sales cycles related to these capital expenditures and the potential impact of prevailing economic conditions.
- Turning now to Patterson Medical, sales of our rehabilitation supply and equipment unit increased 22% to $126.8 million in the fourth quarter.
- Although the rehabilitation businesses acquired in June 2010 from DCC Healthcare accounted for the majority of this unit's sales growth, we were encouraged by Patterson Medical's internal growth of 3%.
- Internally-generated sales attained planned levels and benefited from solid demand for the unit's industry-leading range of consumable supplies.
- Patterson Medical's overall results for this period continued to be affected somewhat by budgetary constraints imposed by the British government on healthcare expenditures, but the impact of this situation is lessening.
- Despite these austerity moves, Patterson Medical's U.K. based Homecraft Operation continued to grow during the fourth quarter as the unit's export business and the contribution from the DCC acquisitions resulted in Homecraft sales growth of 116%.
- Expenses related to the acquired DCC units also had an impact on Patterson Medical's results, but these expenses should continue to diminish significantly going forward as a percentage of revenue as the integration of these businesses proceeds on schedule.
- Patterson Medical's management team, especially the staff at the Homecraft unit, had a demanding year as they integrated an operation almost equal in size to their own, coped with an extremely difficult local market, and transitioned the top management of the unit.
- We are encouraged by Patterson Medical's fiscal 2011 performance and believe this unit is well positioned, domestically and internationally, as an ongoing growth driver.

- Turning to Webster Veterinary, sales of our veterinary unit increased 14% in the fourth quarter to $183.9 million.
- Webster's fourth quarter sales growth benefited from strong demand for new combination products in the flea/tick and heartworm category, which helped fuel a 12% increase in sales of consumable supplies.
- In addition, Webster posted continued strong sales of veterinary equipment and software, which rose 41% from last year's fourth quarter.
- Webster's equipment business has been growing at solid rates in recent quarters, and we intend to continue investing in this relatively new portion of Webster's operation that has expanded the unit's full-service platform.
- Regarding our financial outlook contained in this morning's release, we issued guidance of $1.90 to $2.00 per diluted share for fiscal 2012.
- This guidance includes the impact of increased non-cash expense related to the Employee Stock Ownership Plan, which will affect earnings by an estimated $0.12 beginning in fiscal 2012.
- Steve will provide more detail on this item in his remarks.
- In addition, fiscal 2012 will be a 52-week sales year, compared to the 53- week year in fiscal 2011 due to Patterson's 52/53-week fiscal year convention.
- We are optimistic about Patterson's near and longer-term prospects.
- Our markets are strengthening and have attractive long-term fundamentals.
- Our businesses are positioned to capitalize upon their market opportunities.
- And, we are generating strong operating cash flows, providing us with ample resources for supporting growth initiatives at our three units and programs aimed at further enhancing shareholder value.
- As previously reported, Patterson's board of directors increased our quarterly dividend from $0.10 to $0.12 per share in March.
- At the same time, our board also replaced an existing share repurchase program with a new 25 million share, five year buyback authorization.
- Using internally-generated cash, we repurchased approximately 1.9million shares in the fourth quarter under this new authorization.
- For the year, 3.3 million shares were repurchased, returning almost $100 million to our shareholders.
- When you add this amount to our dividend, we returned approximately $149 million to shareholders in fiscal 2011.
- Thank you. Now, Steve Armstrong will review some financial highlights from our fourth quarter results.

R. Steven Armstrong
Chief Financial Officer

- My comments will begin with an overview of the operating margin change that we experienced in the quarter.
- Our operating margin declined by 50 basis points in the quarter, with product margins declining 100 basis points, while increased revenues improved our expense leverage by 50 basis points.
- If you will recall, we said at this time a year ago that our gross margin for the fourth quarter of fiscal 2010 would not be sustainable in fiscal 2011.
- Our gross margin in last year's fourth quarter was positively impacted by period-specific items such as rebates and a higher level of contract sales.
- In addition, we expended more on promotional activities in the current quarter in the Dental segment.
- Although this initiative helped generate our strong equipment revenue growth, it negated our ability to expand margins.
- Specifically, the Dental margin was 12.9% for the quarter, flat with the prior year.
- The Veterinary and Medical segments reported operating margins of 6.4% and 14.5%, respectively.
- The decline in the operating margin of the Vet segment is the result of a substantial price increase by a pharmaceutical manufacturer on a line of products, as well as a lower level of vendor rebates in the current period.
- Medical's operating margin reflected the adverse impact of the integration of the businesses acquired from DCC Healthcare earlier in the fiscal year.

- As anticipated, the short-term impact of absorbing the DCC businesses is starting to dissipate as evidenced by a sequential 360 basis point improvement in the Medical operating margin in the quarter.
- Despite some of these factors, we were pleased with Patterson's fourth quarter performance.
- I now want to spend a few minutes addressing a unique situation that will impact our future operating metrics…one that is grounded in arcane accounting standards and not the fundamentals of our business.
- Our operating expense ratio in fiscal 2012 will create a new base-line for the expense structure of the Company.
- As many of you know, one of Patterson's long-term strategies has been to align our employees' interests with those of our shareholders by making the employees owners of the business through various retirement and equity plans.
- One of those plans, and our largest retirement plan, is the U.S.-based Employee Stock Ownership Plan, or ESOP.
- The ESOP was originally established in 1990 when the Plan acquired the equivalent of approximately 23 million shares.
- For the past 20 years, we have allocated those shares to the employees and have recognized retirement expense using the original cost of those shares.
- The final accounting for those original shares culminated in fiscal 2011.
- Because the ESOP had become such an ingrained part of Patterson's corporate culture, and an element that we wanted to perpetuate, an additional tranche of stock was purchased by the ESOP for $105 million in 2006.
- Although the accounting standards since 1990 were subsequently revised, our ESOP was grandfathered in under the old standards, which allowed us to continue accounting for the Plan based on the original, or in this case the 1990, cost of the shares to the ESOP.
- Our grandfathering under the old accounting standards has now ended, and starting in fiscal 2012, expense for the ESOP will be based on the current market value of the shares allocated to the employees each year.
- Our earnings guidance includes our best estimate of the expense for a competitive contribution to the ESOP in fiscal 2012.
- The estimated expense will increase our operating expenses by approximately $23 million, and will reduce our earnings by an estimated $0.12 per share in fiscal 2012.
- I want to emphasize that this is a non-cash expense.
- And again, the shares that will be allocated by the ESOP over the foreseeable future were acquired in 2006, and create the non-cash accounting expense for the Company.
- Obviously, this change creates a comparability discrepancy between our past and future accounting performance, but it does not alter Patterson's underlying cash generation ability.
- As I said at the outset, the fundamentals of our business remain fully intact despite this non-cash accounting issue.
- One other item of note with regard to comparability, as Scott noted, fiscal 2012 will be a 52-week year, versus our just-completed year that contained 53 selling weeks.
- This means there will be less opportunity to expand our operating expense leverage in fiscal 2012, particularly on fixed costs, on a comparative basis.
- The combination of the increased ESOP expense and the reduction in selling days will adversely impact our earnings per share by approximately $.14 to $.16 during the coming year.
- Moving on, our fiscal 2011 tax expense benefited from a full year of dividends paid on the shares held by our Employee Stock Ownership Plan.
- This portion of the dividend is deductible on our income tax return and accounts for the majority of the difference in the tax rates between fiscal 2010 and the current year.
- As we look to fiscal 2012, we expect a tax rate consistent with that for 2011, which would be in the mid to high 36% range.
- Looking now at our cash flow, we generated approximately $71 million from operations in the fourth quarter, compared to $112 million in the prior year.
- As you may recall, our cash flow in last year's fourth quarter benefited from a large sale of finance contracts that had accumulated from promotional activities in earlier periods.
- These contracts were not available for sale before then due to restrictions in our arrangements with our funding sources.
- A couple notes on the balance sheet, our DSO stood at 46 or slightly higher than the year-ago 44, which excludes the finance contracts just discussed.

- Our inventory turns declined to 6.9, from 7.1 one year ago.
- Looking ahead to fiscal 2012, we expect our CAPEX to approximate $30 million, while depreciation and amortization should be in the vicinity of $45 million.
- With that, I'll turn the call back to the conference operator, who will poll you for your questions.