BIOMET INC
Form 10-Q
April 12, 2002

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

FORM 10-Q

(Mark One)

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

For the quarterly period ended February 28, 2002.

OR

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

For the transition period from _______________ to _______________.

Commission file Number 0-12515.

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

Indiana	35-1418342
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

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

(219) 267-6639
(Registrant's telephone number, including area code)

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

As of February 28, 2002, the registrant had 267,986,633 common shares outstanding.

BIOMET, INC.

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PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

BIOMET, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS
at February 28, 2002 and May 31, 2001
(in thousands)

ASSETS

	February 28, 2002	May 31, 2001
	(Unaudited)	
Current assets:		
Cash and cash equivalents	$ 235,698	$ 235,091
Investments	42,675	52,627
Accounts and notes receivable, net	335,990	324,848
Inventories	318,975	277,601
Deferred income taxes	44,985	48,982
Prepaid expenses and other	23,069	29,230
Total current assets	1,001,392	968,379
Property, plant and equipment, at cost	373,472	325,890
Less, Accumulated depreciation	161,670	140,139
Property, plant and equipment, net	211,802	185,751
Investments	210,431	175,430
Intangible assets, net	7,775	8,848
Excess acquisition costs over fair value of acquired net assets, net	126,704	134,835
Other assets	18,078	16,068
Total assets	$1,576,182	$1,489,311

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

BIOMET, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

at February 28, 2002 and May 31, 2001
(in thousands)

LIABILITIES AND SHAREHOLDERS' EQUITY

	February 28, 2002 (Unaudited)	May 31, 2001
Current liabilities:		
Short-term borrowings	$ 76,815	$ 62,734
Accounts payable	32,708	21,008
Accrued income taxes	21,725	31,085
Accrued wages and commissions	31,047	33,030
Accrued litigation	5,864	26,100
Other accrued expenses	66,458	67,865
Total current liabilities	234,617	241,822
Long-term liabilities:		
Deferred federal income taxes	5,836	5,783
Other liabilities	403	423
Total liabilities	240,856	248,028
Minority interest	100,627	95,097
Contingencies (Note 7)		
Shareholders' equity:		
Common shares	121,562	108,918
Additional paid-in capital	48,235	48,732
Retained earnings	1,124,969	1,044,564
Accumulated other comprehensive loss	(60,067)	(56,028)
Total shareholders' equity	1,234,699	1,146,186
Total liabilities and shareholders' equity	$1,576,182	$1,489,311

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

BIOMET, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF INCOME
for the nine and three months ended February 28, 2002 and 2001
(Unaudited, in thousands, except per share amounts)

	Nine Months Ended February 28,		Three Months Ended February 28,	
	2002	2001	2002	2001
Net sales	$866,018	$742,657	$304,609	$267,163
Cost of sales	241,664	214,236	85,238	75,042
Gross profit	624,354	528,421	219,371	192,121
Selling, general and administrative expenses	320,846	293,189	112,851	123,075

Research and development expense	35,845	31,533	12,190	11,374
Operating income	267,663	203,699	94,330	57,672
Other income, net	11,807	14,107	2,872	3,926
Income before income taxes and minority interest	279,470	217,806	97,202	61,598
Provision for income taxes	94,800	74,624	32,924	21,112
Income before minority interest	184,670	143,182	64,278	40,486
Minority interest	5,531	4,752	2,604	2,281
Net income	$179,139	$138,430	$ 61,674	$ 38,205
Earnings per share:				
Basic	$ .66	$ .52	$ .23	$ .14
Diluted	$ .66	$ .51	$ .23	$ .14
Shares used in the computation of earnings per share:				
Basic	269,554	267,633	269,388	268,245
Diluted	272,543	270,561	272,265	271,530
Cash dividends per common share	$ .09	$ .07	$ --	$ --

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

BIOMET, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
for the nine months ended February 28, 2002 and 2001
(Unaudited, in thousands)

	2002	2001
Cash flows from (used in) operating activities:		
Net income	$179,139	$138,430
Adjustments to reconcile net income to net cash from operating activities:		
Depreciation	25,509	22,704
Amortization	9,087	9,094
Gain on sale of investments, net	(300)	(1,783)
Minority interest	5,531	4,752
Deferred federal income taxes	4,050	(583)
Changes in current assets and liabilities, excluding effects of acquisitions:		
Accounts and notes receivable, net	(13,421)	(29,348)
Inventories	(40,138)	(26,704)
Prepaid expenses and other	4,642	(11,323)
Accounts payable	10,441	(5,478)
Accrued income taxes	(9,712)	(5,943)
Accrued wages and commissions	(1,726)	4,179
Other accrued expenses	(27,334)	33,224
Net cash from operating activities	145,768	131,221
Cash flows from (used in) investing activities:		
Proceeds from sales and maturities of investments	87,728	41,481

Purchases of investments	(111,496)	(54,177)
Capital expenditures	(45,142)	(25,255)
Acquisitions, net of cash acquired	(6,735)	(90,602)
Other	(885)	(2,766)
Net cash used in investing activities	(76,530)	(131,319)
Cash flows from (used in) financing activities:		
Increase (decrease) in short-term borrowings, net	18,012	(12,788)
Issuance of common shares	13,896	16,471
Cash dividends	(24,268)	(18,993)
Purchase of common shares	(76,215)	--
Net cash used in financing activities	(68,575)	(15,310)
Effect of exchange rate changes on cash	(56)	4,975
Increase (decrease)in cash and cash equivalents	607	(10,433)
Cash and cash equivalents, beginning of year	235,091	213,606
Cash and cash equivalents, end of period	$235,698	$203,173

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

BIOMET, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1: BASIS OF PRESENTATION.

The accompanying consolidated financial statements include the accounts of Biomet, Inc. and its subsidiaries (individually and collectively referred to as the "Company"). The unaudited consolidated financial statements have been prepared in accordance with generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, they do not include all of the information and notes required by generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for the nine-month period ended February 28, 2002 are not necessarily indicative of the results that may be expected for the fiscal year ending May 31, 2002. For further information, refer to the consolidated financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the fiscal year ended May 31, 2001.

The accompanying consolidated balance sheet at May 31, 2001, has been derived from the audited Consolidated Financial Statements at that date, but does not include all disclosures required by generally accepted accounting principles.

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

Net sales of musculoskeletal products by product category are as follows for the nine and three months ended February 28:

	Nine Months Ended February 28, 2002	Nine Months Ended February 28, 2001	Three Months Ended February 28, 2002	Three Months Ended February 28, 2001
	(in thousands)			
Reconstructive	$520,831	$446,548	$184,765	$158,655
Fixation	160,430	147,304	53,548	52,549
Spinal products	89,609	62,230	32,458	26,429
Other	95,148	86,575	33,838	29,530
	$866,018	$742,657	$304,609	$267,163

NOTE 2: COMPREHENSIVE INCOME.

Other comprehensive income includes foreign currency translation adjustments and unrealized appreciation of available-for-sale securities, net of taxes. Other comprehensive income (loss) for the three months ended February 28, 2002 and 2001 was $(5,707,000) and $21,280,000, respectively. Other comprehensive income (loss) for the nine months ended February 28, 2002 and 2001 was $(4,039,000) and $7,279,000, respectively. Total comprehensive income combines reported net income and other comprehensive income. Total comprehensive income for the three months ended February 28, 2002 and 2001 was $55,967,000 and $59,485,000, respectively. Total comcomprehensive income for the nine months ended February 28, 2002 and 2001 was $175,100,000 and $145,709,000, respectively.

NOTE 3: INVENTORIES.

Inventories at February 28, 2002 and May 31, 2001 are as follows:

	February 28, 2002	May 31, 2001
	(in thousands)	
Raw materials	$ 33,374	$ 32,024
Work-in-process	45,171	31,082
Finished goods	125,492	108,704
Consigned	114,938	105,791
	$318,975	$277,601

NOTE 4: COMMON SHARES.

During the nine months ended February 28, 2002, the Company issued 1,341,520 Common Shares upon the exercise of outstanding stock options for proceeds aggregating $13,896,000. During the nine months ended February 28, 2002 the Company purchased 2,478,601 common shares at an aggregrate cost of $76,215,000, pursuant to the Common Stock repurchase programs authorized by the Board of Directors in December 2001. On July 9, 2001, the Company announced a three-for-two stock split payable August 6, 2001 to shareholders of record July 30, 2001. All information on the number of common shares and all per share data for the previous year have been restated for this stock split.

NOTE 5: EARNINGS PER SHARE.

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

NOTE 6: INCOME TAXES.

The difference between the reported provision for income taxes and a provision computed by applying the federal statutory rate to pre-tax accounting income is primarily attributable to state income taxes, tax benefits relating to operations in Puerto Rico, tax-exempt income and tax credits.

NOTE 7: CONTINGENCIES.

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

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

NOTE 8: RECENT ACCOUNTING PRONOUNCEMENTS:

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

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

FINANCIAL CONDITION AS OF FEBRUARY 28, 2002

The Company's cash and investments increased $25,656,000 to $488,804,000 at February 28, 2002, despite the $76,215,000 used to purchase shares during the quarter pursuant to the December 2001 share repurchase programs and the $24,268,000 cash dividend paid during the first quarter.

Cash flows provided by operating activities were $145,768,000 for the first nine months of fiscal 2002 compared to $131,221,000 in 2001. The primary sources of fiscal year 2002 cash flows from operating activities were net income, depreciation and amortization offset by an increase in inventory and a decrease in other accrued expenses. Inventories increased from new product introductions and a buildup of inventory associated with the Company's establishment of its direct operations in Japan. Other accrued expenses decreased from the payout in the Tronzo litigation as described in Note 7 of the Notes to Consolidated Financial Statements.

Cash flows used in investing activities were $76,530,000 for the first nine months of fiscal 2002 compared to a use of $131,319,000 in 2001. The primary use of cash flows for investing activities were purchases of investments and purchases of capital equipment offset by sales and maturities of investments. Included in capital expenditures are costs for the purchase and expansion of the Company's 3i facilities.

Cash flows used in financing activities were $68,575,000 for the first nine months of fiscal 2002 compared to a use of $15,310,000 in 2001. The primary use of cash flows from financing activities were the purchase of the Company's Common Shares as part of the Common Share repurchase programs and the cash dividend paid in the first quarter while the primary source of cash flows from financing activities was from cash receipts from stock option exercises and additional borrowings in Europe from the Biomer's line of credit. Biomer increased its line of credit from EUR 71 million to EUR 100 million during the current quarter.

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

RESULTS OF OPERATIONS FOR THE NINE MONTHS ENDED FEBRUARY 28, 2002
AS COMPARED TO THE NINE MONTHS ENDED FEBRUARY 28, 2001

Net sales increased 17% to $866,018,000 for the nine-month period ended February 28, 2002, from $742,657,000 for the same period last year. Excluding the impact of foreign currency and discontinued products, which reduced the first nine months sales by $4.6 million and $7.8 million, respectively, net sales increased 18.5% during the first nine months of fiscal year 2002. The Company's U.S.-based revenue increased 20% to $625,702,000 during the first nine months, while foreign sales increased 8% to $240,316,000. Excluding the negative foreign exchange adjustment and discontinued products, foreign sales in local currencies increased 14%.

Worldwide sales of Biomet's reconstructive devices increased 17% during the first nine months of fiscal 2002 to $520,831,000. Reconstructive devices were led by total knee sales, which increased 19% in the United States and 18% worldwide during the first nine months. Biomet's knee performance continues to be driven by the Repicci IITM Unicondylar Knee System and the AscentTM Total Knee System. Total hip sales increased 17% in the United States and 14% worldwide during the first nine months of fiscal 2002. The Company's M2aTM Taper Metal-on-Metal Hip System and Biomet's broad line of cementless total hip systems continue to drive this growth. 3i's dental reconstructive implants increased 16% in the United States and 17% worldwide during the nine-month period. Bone cements and accessories increased 31% worldwide for the nine-month period.

Fixation sales increased 9% to $160,430,000 for the first nine months of fiscal 2002. Fixation sales were led by electrical stimulation products which increased 16% worldwide during the nine-month period. External fixation sales increased 5% worldwide, internal fixation sales increased 8% worldwide, while craniomaxillofacial sales decreased 5% worldwide for the nine-month period.

Spinal sales increased 44% to $89,609,000 for the first nine months of fiscal 2002. Sales of spinal hardware and EBI's non-invasive SpinalPak Spinal Stimulation System contributed to this increase. Increases in both fixation and spinal products were positively influenced by the acquisition of Biolectron in September of last fiscal year.

The Company's sales of other products totaled $95,148,000, representing a 10% increase over the first nine months of fiscal year 2001, primarily as a result of increased sales of softgoods and bracing products and arthroscopy products, offset by the loss of internationally distributed products.

Cost of sales decreased as a percentage of net sales to 27.9% for the first nine months of fiscal 2002 from 28.8% last year primarily as a result of increased sales of higher margin products and increased in-house manufacturing efficiencies. Selling, general and administrative expenses as a percentage of net sales changed from 39.5% (36.0% excluding the Tronzo special charge) for the first nine months of last year to 37.0% for the current nine-month period. This increase in the percentage (excluding the special charge) is a result of ongoing investments in the Company's global sales capabilities, including implementing a direct selling organization in Japan. In addition, in the third quarter, the Company experienced approximately $1.5 million of additional expenses resulting from the reorganization of its Walter Lorenz subsidiary. Research and development expenditures increased during the first nine months to $35,845,000 reflecting the Company's continued emphasis on new product introductions. Operating income increased 31% (16% excluding the special charge) to $267,663,000 for the first nine months of fiscal 2002. Other income decreased 16% resulting from lower interest rates available on investable cash. The effective income tax rate decreased to 33.9% for the first nine months of fiscal year 2002 from 34.3% last year primarily as a result of U.S. pretax income growing at a higher rate than international pretax income where tax rates are higher.

These factors resulted in a 29% increase (15% excluding the special charge) in net income to $179,139,000 for the first nine months of fiscal 2002. Basic earnings per share increased 27% (14% excluding the special charge) from $.52 ($.58) to $.66 for the periods presented, while diluted earnings per share increased 29% (14% excluding the special charge) from $.51 ($.58) to $.66 for the periods presented.

RESULTS OF OPERATIONS FOR THE THREE MONTHS ENDED FEBRUARY 28, 2002
AS COMPARED TO THE THREE MONTHS ENDED FEBRUARY 28, 2001

Net sales increased 14% to $304,609,000 for the third quarter of fiscal 2002, as compared to $267,163,000 for the same period last year. Excluding the impact of foreign currency which decreased third quarter sales by $.9 million and discontinued products which reduced the third quarter sales by $2.5 million, net sales increased 15% during the third quarter of fiscal year 2002. Operating income increased 64% (13% excluding the special charge) to $94,330,000 for the third quarter of fiscal 2002. During the third quarter, net income increased 61% (11% excluding the special charge) to $61,674,000. Basic earnings per share increased 64% (10% excluding the special charge) from $.14 ($.21) to $.23 for the periods presented, while diluted earnings per share increased

64% (15% excluding the special charge) from $.14 ($.20) to $.23 for the periods presented. The business factors resulting in these changes and relevant trends affecting the Company's business during the periods in question are comparable to those described in the preceding discussion for the nine-month period.

Item 3. Quantitative and Qualitative Disclosures about Market Risks.

There have been no material changes from the information provided in the Company's Annual Report on Form 10-K for the year ended May 31, 2001.

PART II. OTHER INFORMATION

Item 1: Legal Proceedings.

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

Item 6. Exhibits and Reports on Form 8-K

(a) Exhibits. See Index to Exhibits.
(b) Reports on Form 8-K.
None.

SIGNATURES

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

BIOMET, INC.

(Registrant)

DATE: 4/12/2002

BY: /s/ GREGORY D. HARTMAN

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

(Signing on behalf of the Registrant and as Principal Financial Officer)

BIOMET, INC.

FORM 10-Q

INDEX TO EXHIBITS

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