

THOMSON REUTERS

PLACEHOLDER TRANSCRIPT

Q1 2005 Mettler-Toledo International Earnings Conference Call

EVENT DATE/TIME: MAY 03, 2005 / 9:00PM GMT



CORPORATE PARTICIPANTS

Mary Finnegan *Mettler-Toledo International - Treasurer, Investor Relations*
Robert Spoerry *Mettler-Toledo International - President and CEO*
Bill Donnelly *Mettler-Toledo International - CFO*

CONFERENCE CALL PARTICIPANTS

Tycho Peterson *J.P. Morgan - Analyst*
Peter Olson *Thomas Weisel Partners - Analyst*
Derik De Bruin *UBS - Analyst*
Darryl Pardi *Merrill Lynch - Analyst*
Scott Wilkin *UBS - Analyst*
Vivek Khanna *Argus Partners - Analyst*
Bill Donnelly
Paul Knight

PRESENTATION

Operator

Ladies and gentlemen, thank you for standing by and welcome to the first quarter 2005 Mettler-Toledo International earnings conference call. My name is Carlo, and I will be your coordinator for today's presentation. [OPERATOR INSTRUCTIONS] I would now like to turn the presentation over to your host for today's conference, Ms. Mary T. Finnegan, treasurer and investor relations. Please proceed, ma'am.

Mary Finnegan *Mettler-Toledo International - Treasurer, Investor Relations*

Thanks, Carlo. Good afternoon, everyone. I am Mary Finnegan, treasurer, and I am also responsible for investor relations for Mettler-Toledo, and I want to welcome you to the call this afternoon.

I am joined by Robert Spoerry, our chairman and CEO, and Bill Donnelly, our chief financial officer.

I will start by covering some administrative matters, and I will then turn the call to Robert, who will provide you highlights on the quarter. Bill will then cover the financials in detail, and then Robert will update you on current market conditions and our strategic initiatives. Of course, we will have time for Q&A at the end. Now for the administrative matters.

First, this call is being webcast and is available for replay on our website. A copy of the press release we issued today is also available on our website. You should be aware that statements on this call, which are not historical facts, may be considered forward-looking statements for the purposes of the Safe Harbor provision under the Private Securities Litigation Reform Act.

Forward-looking statements involve risks and uncertainties that could cause actual events or results to differ materially from those expressed or implied. For further information concerning issues that could materially affect performance related to forward-looking statements, please refer to our filings with the SEC. We undertake no responsibility to release publicly any revisions to forward-looking statements.

One other item -- on today's call we may use non-GAAP natural measures. More detailed information with respect to use of and differences between the non-GAAP financial measures and the most directly comparable GAAP measure is provided in the press release. I will now turn the call over to Robert.

Robert Spoerry *Mettler-Toledo International - President and CEO*

Thanks, Mary. I want to thank you for joining us today on this call. We are pleased with our first quarter results, and I will start by providing some summary comments on the quarter.

We achieved EPS of \$0.47 in the quarter, an increase of 15% over prior year. We are pleased with this strong result. Our sales growth in the quarter was an increase of 6%, of which currency was a benefit of 3%, and our local currency growth was 3%. This was in line with our



expectation. We are especially pleased to see strong performance in the Americas. Our gross margins in the quarter were excellent with 110 basis-point increase over the prior year. Finally, our cash flow generation fell below the prior year was in line with our expectation and reflected comparison issue with last year. We remain on track for our full-year cash flow targets.

Bill will now provide more details on the financials.

Bill Donnelly *Mettler-Toledo International - CFO*

Okay, thanks, Robert, and hello, everybody. We had a solid first quarter with earnings per share of \$0.47, which was a 15%, or \$0.06-per-share increase versus the prior year. We are pleased to start off the year that way with these solid results. Now let me go into some more detail starting with sales.

Sales in the quarter were \$337.2 million, an increase of 6% consisting of a 3% local currency growth and the 3% currency benefit. Adjusted for product lines being exited, our growth was 4% in the quarter.

As most of you know, we focused on local currency sales growth, which drives our operating performance rather than U.S. dollar sales growth. So for the remainder of the sales discussion, the numbers I'll be discussing, or the percentages I'll be discussing are on a constant currency basis. And then, of course, all comparisons are to Q1 of last year.

Let me start by breaking down sales by geographic destination. Growth in the Americas increased 7%. That was higher than we expected when we spoke last time. Laboratory and industrial products had strong sales growth, while retail was only slightly ahead of last year in the Americas. The stronger sales in the Americas helped to offset a slower-than-expected start in Europe where we had a 1% decline in local currency. Our expectations were for modest sales growth in the quarter. Contributing to the shortfall was a sales decline in retail, which had a strong first quarter in Q1 of last year. Laboratory was a little softer than we expected, and we had a slight growth in industrial in Europe.

Sales growth in Asia, rest of the world, increased 4%, pretty much on target with what we expected. On our conference call last quarter, we anticipated lower sales growth in the first part of the year because of tough comparisons. As a reminder, we had 18% sales growth in the region in Q1 of last year.

Turning from geography to business area, let me start with lab. Laboratory products were up 2% over the prior year, similar to what we saw in the fourth quarter. Adjusted for product lines we were exiting, sales growth was 3% in the quarter. Process analytics and analytical instruments had strong sales growth. Sales growth in drug discovery products was solid, while the balance business was down slightly.

Turning to the industrial products area, we had a strong quarter with sales growth of 6%, both our core industrial products as well as our product inspection business performed quite well in the quarter.

Finally, for retail, sales were down 2% in the quarter, which was below what we had expected, and this was driven by tougher conditions in Europe.

Now let me move to the rest of the P&L. Gross margins increased by 110 basis points in the first quarter. A few factors contributed to this improvement including increased sales volume, which leveraged our fixed-cost structure, favorable -- sorry -- unfavorable product mix and benefits of our cost rationalization efforts.

We are also seeing the benefit from more effective pricing via Project Spinnaker, which Robert will speak about in a few minutes. These positive factors were offset by somewhat higher steel prices.

R&D amounted to \$20.8 million, or 6.2% of sales, on target with what we expected and modestly below last year in local currency terms. SG&A was \$106 million and was up 10% in dollar terms. This was 3% accounted for the exchange rates, and the remaining 7% growth was in local currency. The factors that contributed to the growth in local currency were higher corporate governance costs including



SOX-related costs and investments around Project Spinnaker, our growth initiative, as well as higher variable compensation. Together, these three items accounted for 4% of the increase, the remaining 3% are more general-type increases and spread across the board. The net sum of these items resulted in adjusted operating income of \$35.7 million, which is a 9% increase over the prior year.

Now continuing down the rest of the P&L, amortization amounted to \$2.8 million in the quarter, interest expense was \$3.5 million, and our tax rate continued at 30%. This results in a net income of \$20.8 million and an earnings per share of \$0.47, again compared to \$0.41 in the year-ago period.

Now on to cash flow -- net cash flow provided by operations was \$6.7 million, slightly below our expectations. As I mentioned on our last conference call, we expected Q1 cash flow to be well below prior year. We have a couple of items impacting comparability in Q1. First, we paid out \$15 million more in variable compensation this quarter than in Q1 of last year. Our variable comp for 2004 is paid out in the first quarter of 2005. In 2004, we exceeded our targets while in 2003 we, frankly, were below them.

The other item impacting comparability is the timing of supplier payments, which accounted for about \$12 million of the difference. Our DSOs remained constant at 52 days, while our inventory turns improved from 4.4 to 4.6. I am happy with this improvement, but we are working to drive this number up above 5 in the coming years.

We remain confident in our full-year cash flow target of around \$140 million. This represents operating cash flow less capital expenditures. Although we are starting down this year, we expect to recover in the upcoming quarters.

We purchased 528,000 shares of stock this quarter for a total value of \$28.4 million. As I mentioned last time, our intention is to use our free cash flow in share repurchases. This, of course, could change with a sizable acquisition or other developments, but we are now working towards this target.

Our capital structure remains very strong. At the end of the quarter, we had net debt of \$160 million versus the 12-month EBITDA of \$209 million, which results in a net debt-to-EBITDA ratio of 0.8 times. This gives us plenty of financial flexibility to continue our share repurchase program and have room for acquisitions.

In terms of guidance for 2005, on our last call we outlined guidance for sales growth in the 3% to 5% range -- that's local currency organic growth -- and earnings per share in the 2.65 to 2.75 range. We see no need to change those assumptions. In terms of Q2, current consensus is \$0.71 per share, and I think that's a reasonable number.

Okay, that's it from my side, and now I'm going to turn it back to Robert.

Robert Sperry *Mettler-Toledo International - President and CEO*

Thanks, Bill. I want to start by adding to Bill's comment on sales performance and on our outlook for the remainder of the year. I will then cover some developments with respect to our strategic initiatives.

Looking at our geographic markets, as mentioned at the beginning of the call, I was really pleased to see the strong result in the Americas, plus a very solid performance with strong growth in almost all product lines. The growth in the Americas was above expectations for the quarter, and we do not expect it to continue at this level for the full year.

The strong performance in the Americas helped to offset the slower-than-expected start in Europe. We expect to have positive growth in Europe this year, so you should see improving performance in the coming quarters. In fact, order entry in our European industrial business was quite good this quarter, which supports our outlook for improved performance.

Asia, in total, came in where we expected. China had solid sales growth, but it was below the very high level recognized last year. As we mentioned on our last call, we expect growth in China this year to be in the low double-digit range rather than in the 20%-plus level that we saw last year.



Last year, we were positively impacted in Q1 by the estimate of SARS, particularly in the first quarter of the year that carried on.

We do see evidence of China's economy quoting, especially on certain bigger government type projects. Our other businesses continue to do very well in China. Of course, our strategy for China remains firm; that is, to capitalize on the growth areas in this region and to leverage our low-cost manufacturing capabilities.

Now, turning to market conditions in our businesses where we had a slightly different mix to our sales growth than we expected at the beginning of the quarter. I will start with the industrial business, which, as you have heard from Bill, was up strongly with 6% local currency sales growth. The good performance was seen across most product lines, and geographically was particularly strong in the Americas. I expect that we'll see some slowdown in the Americas in the coming quarters, and offsetting that, improving results in Europe and Asia.

Our laboratory business started slower than expected. Analytical instruments had a very strong quarter, and our drug discovery business had solid sales growth. Pipettes continued to generate solid revenue growth driven by the international expansion. Balances has a tough comparison, but we expect to see this to improve in the coming quarter with the launch of our new line of high-end analytical balances, and the upgrade of our basic cost-effective line.

As you heard, retail came in slightly below last year, which I point out was a strong quarter and as we were rolling out a major project in Germany at that time. We continue to have solid interest in our global food-retailing platform, UC, which I discussed on our last call. It would expect to have some growth in the low to mid-single-digit range for the remainder of the year.

Taken altogether, we remain comfortable with the guidance previously given to you for local currency sales growth of 3% to 5% for the remainder of the year.

I will now update on strategic development. Innovation, especially around products remains the core of our strategies. This quarter, we have many examples of important new product launches. We are now launching our high-end analytical balance XP. This is the last major piece to complete and upgrade of our balance line, which was started two years ago. XP is aimed at the regulated market, like the pharmaceutical industry, and provides significant values to our customers with the design features such as unique suspended weigh-in grid design, which provides greater speed and accuracy. It also has built-in warning system to prevent inaccurate use of the balance and easier man/machine interface. Because of its better accuracy, it reduces the required minimum weight, thereby creating substantial cost savings for our customers on expensive chemicals and substances. The XP is combined with our lab software, it gives us a clear solution advantage in this very important segment.

Two weeks ago, we participated at the Interpack Show in Germany. This is the largest show of its kind in the packaging industry, and it's held every three years. Our product-inspection business launched many new products at this show, which I want to highlight to you briefly. First, we introduced the X series of check weighers. Check weighers are about half of the product inspection business, and are a very profitable part of our offering, and we have a very strong leadership in that line. Most of our check weighers are sold into food and pharma manufacturing facilities, and they made some very important innovation in the X series that we think are very well received from customers.

First, the customer wants to have simplification of their inspection processes. We have done a few things to facilitate this need, including incorporating a very intuitive operating terminal with our color touch screen, which is easy to operate and requires minimal training. The terminal is designed to control multiple inspection devices, therefore reducing the number of operator interfaces of the plant flow. You can easily integrate the metal detector or other inspection devices and control them from the control of the check weighing. Even the mechanical design of the check weigh has been improved to allow for easier physical integration of multiple inspection devices.

The X series also has the most modern software platform in the industry with an open-system architecture, easy connectivity, and standard interfaces to typical plant communication protocols like Fieldbus, PROFIBUS, and Ethernet.

Finally, the X series has the most sanitary design in the industry with a stainless steel open frame design. It is the only check weigher to



have IP69 weighting between that it holds the highest possible rating for water and [unintelligible]. This allows for easy cleaning with a high-pressure water hose down. The X series is the most hygienic check weigher on the market, which is extremely important to our food customers where sanitation issues are critical.

We also introduced at Interpack our new x-ray system, which we call "T-10." X-ray is a small but fast-growing segment within the product inspection division. T-10 represents our effort to offer the market a stand-up and easy-to-operate solution as compared to customized, highly complex systems, which dominated the market so far. T-10 will be priced approximately one-third below the previous x-ray product and will focus on contamination detection and mass control. We have made a significant effort to make this product better-suited for the large food market by systematically adding a color touch screen, increasing the durability of its design, simplifying its use, and serviceability, and have even made it better-suited for the wash-down environment to a better, easy-clean design.

The last item we will be introducing is a new family of metal detectors under the Profile name. As a reminder, metal detector is nearly half of our product inspection sales, and we have a very strong and profitable position under the Safeline brand. Profile pulls many of the same themes as the X series and the T-10. It's easier to operate, has color touch screen, allows for better connectivity with the plant information system, and is more easily integrated with other equipment from the plant floor. Profile is the first metal detector in the market because the single pass setup and automatically clustering the product. These two features alone can reduce the setup time by as much as 80%. The Profile also includes self-monitoring for full conditions. This is a great feature because of the customers. It is also about up-time. Self-monitoring will eliminate most up and down time. If you further reinforce Safeline's reputation for having the highest up times of any metal detectors in this market.

In addition to technology innovation, we have been talking to you for several quarters regarding Project Spinnaker, which is aimed at accelerating our organic sales growth rate. As you know, sales growth is the most important driver for earnings growth. Through Spinnaker, we believe we have a significant opportunity to expand our market share to accelerate the replacement of our installed base, and to increase the productivity of our sales force for more effective sales and marketing. We also believe that through Spinnaker, we can improve the productivity of our sales force, our service force, and through better use of automation tools.

Let me take a minute to update you on current focus areas for Project Spinnaker. First of all, on pricing. As Bill already mentioned, pricing has played an important role in our margin expansion in this quarter. We have increased service pricing across the board, and product pricing in most lines in most countries. We are not doing this process blindly. In fact, in selected few segments, we have been more drastic in pricing in order to be price competitive. But, generally speaking, we have chosen to raise our prices.

Secondary of Spinnaker's lead generation, where we have the ambitious target for increasing the number of leads significantly, we continue to invest in various forms of lead generation and remain convinced that this method will succeed. Successful lead generation program will be the most important part in improving sales productivity and this metric that we will monitor closely. At the heart of lead generation is our segment marketing initiatives and all our business units have now an action plan for segment marketing in course of the year.

In parallel, we have expanded our telemarketing resources to follow-up on lead qualification and direct marketing. Initial results are very promising. We believe that as the program continues to gain momentum and the techniques become more refined, we will be able to raise the productivity of our sales efforts.

Another area we will be addressing with Spinnaker is sales through indirect channels. We refer to this initiative as our "volume strategy." We have always been very successful in direct sales of high-value solution as evidenced by our strong market shares. The volume market is also a significant size but we need a separate business model for this market, and have developed a task force for the implementation of that. They are currently evaluating supply chain, channel strategy, product mix, marketing programs. We are confident that this will open up new market opportunities for us in the future.

Finally, with respect to field automation, we have formed a competency center to support the automation of the field organization. New automation tools, like CRM, have already been rolled out to the field organization in past years. We have now selected a tool for the automation of our service business, and that with a certain software modification, we will roll it out globally.

As you can see, our strategic initiatives remain right on target. Before I open for questions, I want to summarize what we discussed today.

We are pleased to have achieved our financial targets for the quarter. Sales growth was on track, and we see strong improvements in gross margin, which led to a 15% earnings growth. We remain optimistic for the remainder of this year.

That's it from our side, and now I'd like to ask the Operator to open the line for questions.

QUESTIONS AND ANSWERS

Operator

[OPERATOR INSTRUCTIONS] Tycho Peterson, J.P. Morgan.

Tycho Peterson *J.P. Morgan - Analyst*

Hi, thank you for taking my call and congratulations on the quarter. Wondering if you could provide a little bit more color on some of the softness you saw in Europe? I think, in particular, you talked about softness in the lab market. Is this pharma or academic or both?

Robert Sperry *Mettler-Toledo International - President and CEO*

The softness in Europe, indeed, was partly in lab, but that's also partly in retail. Maybe first commenting on the retail piece -- in retail, we actually had a very strong first quarter last year, and that strong quarter was based on the major rollout we had with a big customer in Germany. Now, the last part, you know, is currently more the traditional pharmaceutical biopharma industry, and not really the academic sector, where we were hurt. As you know, the academic sector is, anyway, a small part in our global mix.

We have had European customers reach -- did actually, really, not invest much in the first quarter and they say that they wait 'til they see the year develop before they're going to release and, in that sense, it was a little difficult. But also last year we had a very successful start with the new laboratory products in Europe. We rolled them out first in Europe before we rolled them out later in the other parts of the world. So it was partly also comparison issue.

I would expect that in the lab in Europe things will improve because we're going to have very fascinating new product launches, as I just explained before. The XP analytical line is just one of many new products we're launching. We have actually new PH meters, we have new titration equipment, and that all is just happening, you know, this week or partly already concluded. So we should see those benefits coming in the coming quarters.

Tycho Peterson *J.P. Morgan - Analyst*

Okay, and then with regards to China, you talked about that potentially recovering to double digits for this year. Do you have early signs that the market is turning around there? How do you gauge that?

Robert Sperry *Mettler-Toledo International - President and CEO*

First of all, the first quarter we saw high single, low double-digit growth in China, and that's a fine achievement if I compare that to the first quarter last year where we had the soft carryover, as I mentioned before. Our expectation is that this government call-down programs, while they are effective right now, will hopefully be a little more relaxed in the second half of the year, and through that we should see good growth coming back in the second half of the year in China.

We also continue to make aggressive investment in China -- maybe not so much just in our infrastructure, but really kind of strengthening our sales networks throughout the country. China is a big country, and we don't have a strong presence in each and every region of that country. So we make that investment and, of course, that also should help us continue the growth back there.

Operator

Paul Knight with Thomas Weisel Partners.



Peter Olson Thomas Weisel Partners - Analyst

Hi, this is Peter Olson in for Paul Knight. I wonder if you could comment about the slow start you saw in the lab instrument business, and where was that coming from -- pharma or biotech?

Robert Spoerry Mettler-Toledo International - President and CEO

The slow start we had came really mainly from Europe. The U.S. business actually was good, solid in the lab. If I look at it more by product line, the analytical instrument did well, so did Altacam [ph]. It was more on the balance side. The balances were slightly down globally versus last year. I would say that, really, the typical effect we see when we announce new product lines. When we announce new product lines, very often customers would know that and wait 'til they see the new product before they buy. But I also explained just before, you know, the impact of maybe some investment stops in the European biopharma companies.

Peter Olson Thomas Weisel Partners - Analyst

Could you repeat the projected growth rates you have for the three divisions?

Robert Spoerry Mettler-Toledo International - President and CEO

Bill, do you want to take that question?

Bill Donnolly

Sure. In terms of the laboratory and the industrial businesses -- actually, all three businesses this year -- we entered the year expecting that we'd be in the mid-single-digit growth rate for all three. I think we're off to a slower start in retail and a slightly better start in industrial, but they should all be kind of in that range for the full year.

Peter Olson Thomas Weisel Partners - Analyst

Okay, and what's the fastest-growing business area you have? Like, say, is it food preparation or something in China?

Bill Donnolly

I think process analytics has been going really well for us. That's where we're doing chemical analysis on water purity and things like that. Our Ingold brand, and our Thornton brand have been growing quite nicely. I would say that's probably the single best area.

Peter Olson Thomas Weisel Partners - Analyst

What geography?

Bill Donnolly

That we sell around the globe but, of course, we have bigger positions in the United States and Europe.

Peter Olson Thomas Weisel Partners - Analyst

Thank you. One last question -- how much of your manufacturing do you have in China and India?

Bill Donnolly Mettler-Toledo International - CFO

Not to much in India. India mostly just serves the Indian market, which isn't that material for us, but if you were to look at products of our product sales, we are now, let's say, mid-teens kind of level in terms of product sales on products manufactured in China.

I was just going to add that now China is about \$100 million kind of a market for us, too, and I guess you can see that in our disclosure numbers.

Operator

Derik De Bruin with UBS.



Derik De Bruin UBS - Analyst

Hi, thank you, and nice quarter. So a couple of questions -- given that there have been some signs of pharma cooling, I guess, and one of the issues with metal products is the fact that you make them so well they last so long, it often takes a long time for people to replace products. Are you concerned at all that there might be some delay and uptake of some new products if things are a little bit slow?

Robert Sperry Mettler-Toledo International - President and CEO

Derik, of course, this is a question, which we fight with almost every day. You are absolutely right. Our product lasts forever, and the trick to trigger to replacing these is innovation. And, of course, this innovation, which we are providing to our customers, we need to provide a return on the investment. Maybe I should use now the XP balance product, which we just launched and try to articulate to you what kind of value propositions there are in that product.

Whenever somebody does a measurement on the balance, they need actually to appear to U.S. pharmacopoeia in the regulated application. This will tell you how you determine the minimum weight you can use the balance for. We have, today, with the XP, significantly more accurate balances, which is a big deal, because we said you can reduce the minimum weight to what we had for people had used so far -- significantly below what competition can do.

Chemical substances, which they weigh, can be sometimes very costly -- can be 10, even 40,000 per gram. You can imagine that can be translated to big cost savings. Then another big feature the product has, it has kind of an automatic control on the setup and in case something is not set up properly, actually, you cannot work with the product. So it adds tremendously to the safety. People often do a job on a balance, and actually the balance is not set up properly, and so they actually had the wrong results. We have seen the new product incorporated as in the technology, which can detect whether it is properly set up. So that's another big, big feature we have in there.

The third one, the balance, is actually much faster than previous technology. We're awfully excited there. The new tool prepares compounds for screening properties also, highly repetitive work, very often labor-intensive. Of course, if you can do the job significantly better, you can save a lot of labor cost.

So these are the challenges. We need to bring this value proposition constantly to our customers, and that way I think we have a very fair chance to rake [ph] up the replacements.

Derik De Bruin UBS - Analyst

Talking about your indirect in Project Spinnaker, your indirect distribution, looking at that now -- I know some of your Ohouse [ph] products are distributed through other companies, and I think some of your RAININ products, as well. Are you looking at putting some of the other higher-end Mettler-Toledo products into, say, the Fisher, VWRs [ph] of the world?

Robert Sperry Mettler-Toledo International - President and CEO

Actually, Fisher and VWR are very important customers for the low-end Mettler-Toledo balances already, and they are long-lasting partners, and we have been both very successful working together.

However, this may be something, which we don't exploit in every part of the world to its full extent. And when I look at our offering, you know, we certainly have typically designed a product but also increasingly, due to the Chinese low-cost capabilities, we have strong low-end offering. For this low-end offering, we need other forms of marketing, distribution, and service. Of course, to some extent, Ohouse is playing in that -- our second brand for balances, and we can certainly to another business level gain many more market share in these low-end markets. This is, by the way, not only true for laboratory products, I will say this goes across also some of the industrial and the retail products.

Derik De Bruin UBS - Analyst

And then just one final question -- what's left on -- just refresh me on your share buyback authorization -- what's left on it and where do you see the share count by year-end? I realize, of course, that's dependent upon what you see in terms of potential acquisitions but just some general ideas.



Bill Donnelly Mettler-Toledo International - CFO

Okay, so in terms of how much availability, it was a \$200 million program that was approved at the end of last year. We've spent about \$28 million so far, and our current free cash flow estimates are in the range of \$140 million or so, and we've disclosed, hey, we'd like to repurchase about that number of shares. And so we've done about \$28 million so far. So you could imagine the share count would go down proportionately.

In terms of an estimated share count at the end of the year, it should be in the range of around 43 million shares or so.

Operator

Darryl Pardi, Merrill Lynch.

Darryl Pardi Merrill Lynch - Analyst

Good evening. What was the net price increase in the quarter? What's your outlook for the year, Bill?

Bill Donnelly Mettler-Toledo International - CFO

I maybe would describe it -- just to say it a little differently is net realized price increases. We raised prices this year across most of our products in the range of 50 basis points up to 2%, and maybe even a few more than that. But, of course, we don't expect to realize all that. If I look at the current quarter in terms of the 110 basis-point improvement, I would say that there are two positive factors that are driving that number. One would be pricing, and the other would be the volume impact. And those two together are probably about 200 basis points. And then you've got a couple of things going the other way, and that is the mix was a little bit negative with us selling more industrial products, you know, the industrial products have a lower gross profit margin than the lab products. And then, secondly, we did take it on the chin a little bit with foreign exchange. You know, we're not exporter from Europe into the United States, and so that hurt on the cost-of-sales line, and those two together kind of net off against the positive benefits of volume and price.

Darryl Pardi Merrill Lynch - Analyst

Speaking of FX -- devaluation of the REM-NB [ph], would that be a wash for Mettler, because you manufacture approximately the same portion of revenues that you have and generate in China or would that affect profitability?

Bill Donnelly Mettler-Toledo International - CFO

I looked at that at the beginning of the year, and so I can't imagine that it's change materially, and the answer would be on an operating profit point of view, it's net neutral, okay? And it's for the reasons you just described. I do have a bit of an intercompany exposure that I have not hedged, and, as you know, Darryl, the cost of trying to hedge the REM-NB for the last 12 months is out of this world. So I think I have an exposure there of -- Mary's giving me hand signals -- 5 million to 7 million, and you can kind of do the math on that. So that would be more of a foreign exchange kind of other income charge if it happened today.

We actually started in the fourth quarter managing -- the exposure was up in the \$20 million range, and we managed it down in the last couple of quarters.

Darryl Pardi Merrill Lynch - Analyst

I don't know if I'd doing my math wrong, I come out to -- when I take the cash that you used to purchase shares, divide by the 528,000 shares, I come up with an average purchase price of about 53.70, which is above the range where the stocks traded.

Bill Donnelly Mettler-Toledo International - CFO

Okay, why don't you give us a second. We actually get a report on that. Merrill Lynch is our purchaser, Darryl, so I can't believe that would have happened. So let me check that one, and we'll let you know in a second.

Darryl Pardi Merrill Lynch - Analyst

Robert, could you discuss what the adoption has been for LabX for the balances. Have you rolled out some of the new instruments, what the adoption has been in the software in coordination with those sales?



Robert Sperry Mettler-Toledo International - President and CEO

LabX reception in the market is excellent. I guess you recall from previous statements on the titration equipment, actually, probably 35% of the products are, to date, sold with LabX. What concerns the balance piece, we are not yet in significant volume, however, we have very significant interest from the customers. The decision-making process here is just a little longer because it is now also in IT. But the prospects are very promising, and I am very convinced this is going to become a success. Again, particularly when I combine that with the new balances -- these new balances, as you recall, they have much improve man-machining to face, the color touch screen and through that, of course, we can much better integrate that product into centralized LabX workstation. So, Darryl, if it's only for the optionality that people know that we have it, and they can buy it at the late point, it's already a great sales tool today.

Bill Donnelly Mettler-Toledo International - CFO

Hey, Darryl, the answer to your other question is that there is a -- at the end of last year there was \$1.3 million open position, so we paid -- we had purchased the stock on December -- whatever the last trading day was -- but we didn't pay the cash out until the first bank day of January, and so there's 1.3 million of cash out the door this year that relates to purchases that we owned at the end of last year -- in effect, the flow. And if you adjust for that, it's \$51.

Operator

Scott Wilkin with UBS.

Scott Wilkin UBS - Analyst

Bill or Robert, just wanted to get your comments, if I could, just on maybe the pipeline. Robert, I think you mentioned risk intake activity in April. You historically have been very conservative guys, and you look around at some of the comps, you know, pretty much across the board, folks have experienced a slowdown in the first quarter, and you guys seem relatively confident about your guidance and about the rest of the year. I'm guessing it has something to do with the order flow that you're seeing. Could you just elaborate a little bit, qualitatively there, on what's giving you the confidence here by maintaining guidance for the year?

Robert Sperry Mettler-Toledo International - President and CEO

Maybe the way we look at a year is, of course, based on order intake, but that's not the only guiding principle, I think. It starts earlier and we, of course, know the inquiry levels -- the inquiries concerning the quote level, and, of course, as long as the probability of turning quotes into orders remains the same. That's a good forecasting way.

I, of course, on order intake, can tell you that we have the [unintelligible] of a couple of weeks. You know we have typically order from six, seven, eight weeks, so it's not really deep into the year, but from all I see in terms of order intake we carried from last year into this year, order intake, we also filled up in Q1, we remain really confident for the rest of the year.

Yes, you are right, we are typically a little conservative as we start the year, knowing that usually you'll not see every problem around the corner, and certainly now the case, you know, we did hope a little better improvement to see in Europe, and that didn't really come through and, for that reason, our conservative guideline, as you call it, probably was the right thing to do.

Nevertheless, I would expect that Europe gets better. We have very strong orders, particularly in the industrial business in Europe, and that certainly will help in the near future.

Scott Wilkin UBS - Analyst

That's helpful. Just turning to operating expense item SG&A, I think, Bill, you mentioned that you were 7% local growth and then net of SOX and Spinnaker startup costs, it was more like 4%. So can I take those costs as being one-time or front-half loaded, and that you would not be burdened with some of that expense in the second half?

Bill Donnelly Mettler-Toledo International - CFO

In terms of the SOX piece, it's for sure, Scott, that we will not -- we are incurring more SOX cost pro rata at the beginning of the year, will incur, probably, actually, a little bit less at the end of the year.



In terms of Spinnaker, I think we are making a conscious effort and are redeploying some resources from other areas to focus on these growth things. So I think that's a little bit dependent on how we see the returns on those investments, but I think Robert and I and the rest of the organization are committed to investing in these marketing and sales efforts to try to accelerate the growth level.

With regard to variable comp, which was the third element, and if you kind of net those out, it actually brings you down to about 3% growth in the other areas. We have a variable comp scheme, as you know. We felt a good quarter and if we kind of pro-rated that out for the year, it was higher than we had projected in the comparable quarter of Q1 of last year. Actually, if I look at the later quarters in Q1, we finished the year quite strong, so we were absorbing relatively higher variable comp in the later quarters of last year. So there should be some recovery there if we stayed on the current track but, again, if we start exceeding target, that might go up slightly.

Scott Wilkin UBS - Analyst

Oh, yeah, that will be a good problem.

Bill Donnelly Mettler-Toledo International - CFO

That would be a good problem.

Scott Wilkin UBS - Analyst

And just on the balance sheet, I didn't catch the -- my calculation of DSOs shows that it was up versus year-end and also first quarter last year. I didn't get the comparison number that you provided, Bill, because I know you adjust it, do it a little differently.

Bill Donnelly Mettler-Toledo International - CFO

We literally do it down to the day, so we know what our sales numbers are, and it's the exact same -- 52 days for both periods. Actually, one of the guys just slipped me a report, it's even down to the decimal point -- 52.4 for both periods.

Scott Wilkin UBS - Analyst

The movement in absolute dollars is more of a currency?

Bill Donnelly Mettler-Toledo International - CFO

It's more currency-driven, correct, and it might be to the weighting within the quarter. It could be that March was relatively -- actually, if I think about the three months in the quarter, March was relatively the stronger month.

Operator

Vivek Khanna with Argus Partners.

Vivek Khanna Argus Partners - Analyst

Hi, good evening. I just had a question on the -- can you talk about the organic growth in the pharma/biopharma end market?

Bill Donnelly Mettler-Toledo International - CFO

Okay, as you know, almost half of our laboratory sales are oriented towards pharma, and so if we look at our lab numbers overall, we had 2% growth, and if you pull out the exited product line, that number goes up to 3. If you were to measure that by, in more details, by geography, in the U.S. we did relatively better, and in Europe we did relatively worse, and within our Chinese business, that wasn't the strongest part of our -- or I should say, Asia business, as you know, China is a large part of it, that wasn't the relatively stronger number. I think that answers it for you.

Vivek Khanna Argus Partners - Analyst

In terms of your guidance, Bill, of 3% to 5% revenue growth, what has to go right to get to the upper end of that and just any thoughts on what may allow you to get to the upper end of that guidance?

Bill Donnelly Mettler-Toledo International - CFO

I guess if I go back to how we guided you at the beginning of the year, we're hoping that Europe improves, I think. Just, if you think about it in this current quarter, if we have almost half of our businesses in Europe, if that grows 2% versus -- that grows minus 1, that alone is



150 basis points. So Europe is clearly one of the more important pieces to that puzzle. And then, of course, actually, Asia/Rest of World, we think that you'll see a better number coming out the third and fourth quarter than you saw in the first quarter or you're probably going to see in the second quarter.

Vivek Khanna *Argus Partners - Analyst*

And so looking today, as Robert was saying, you're seeing European orders actually improve from what you experienced in the first quarter?

Bill Donnelly *Mettler-Toledo International - CFO*

We had --

Robert Sperry *Mettler-Toledo International - President and CEO*

In the industrial business.

Vivek Khanna *Argus Partners - Analyst*

Sorry.

Bill Donnelly *Mettler-Toledo International - CFO*

Right.

Vivek Khanna *Argus Partners - Analyst*

But not all of Europe, is that making that subtle difference -- differentiation?

Bill Donnelly *Mettler-Toledo International - CFO*

Actually, I think, in general, the order growth across product lines was better in Europe than the sales growth but, in particular, the industrial order growth was quite good.

Robert Sperry *Mettler-Toledo International - President and CEO*

In terms of countries, you know, probably France is still a tough market. The other markets seem to be in okay shape.

Operator

[OPERATOR INSTRUCTIONS] Paul Knight.

Paul Knight

What was the guidance for the quarter -- the EPS?

Bill Donnelly *Mettler-Toledo International - CFO*

For Q2?

Paul Knight

Yes.

Bill Donnelly *Mettler-Toledo International - CFO*

\$0.71. Are there any other questions, Operator?

Operator

No, sir, not at this time.

Bill Donnelly *Mettler-Toledo International - CFO*

Okay, thank you very much, everybody. Have a good evening.

Mary Finnegan *Mettler-Toledo International - Treasurer, Investor Relations*

Thanks, guys.

Operator

Ladies and gentlemen, we thank you for your participation in today's conference. This concludes your presentation, and you may now disconnect.

DISCLAIMER

Thomson Reuters reserves the right to make changes to documents, content, or other information on this web site without obligation to notify any person of such changes.

In the conference calls upon which Event Briefs are based, companies may make projections or other forward-looking statements regarding a variety of items. Such forward-looking statements are based upon current expectations and involve risks and uncertainties. Actual results may differ materially from those stated in any forward-looking statement based on a number of important factors and risks, which are more specifically identified in the companies' most recent SEC filings. Although the companies may indicate and believe that the assumptions underlying the forward-looking statements are reasonable, any of the assumptions could prove inaccurate or incorrect and, therefore, there can be no assurance that the results contemplated in the forward-looking statements will be realized.

THE INFORMATION CONTAINED IN EVENT BRIEFS REFLECTS THOMSON REUTERS'S SUBJECTIVE CONDENSED PARAPHRASE OF THE APPLICABLE COMPANY'S CONFERENCE CALL AND THERE MAY BE MATERIAL ERRORS, OMISSIONS, OR INACCURACIES IN THE REPORTING OF THE SUBSTANCE OF THE CONFERENCE CALLS. IN NO WAY DOES THOMSON REUTERS OR THE APPLICABLE COMPANY ASSUME ANY RESPONSIBILITY FOR ANY INVESTMENT OR OTHER DECISIONS MADE BASED UPON THE INFORMATION PROVIDED ON THIS WEB SITE OR IN ANY EVENT BRIEF. USERS ARE ADVISED TO REVIEW THE APPLICABLE COMPANY'S CONFERENCE CALL ITSELF AND THE APPLICABLE COMPANY'S SEC FILINGS BEFORE MAKING ANY INVESTMENT OR OTHER DECISIONS.

©2019 Thomson Reuters. All Rights Reserved.



THOMSON REUTERS

PLACEHOLDER TRANSCRIPT

Q2 2005 Mettler-Toledo International Earnings Conference Call

EVENT DATE/TIME: JULY 28, 2005 / 9:00PM GMT



CORPORATE PARTICIPANTS

Mary Finnegan *Mettler-Toledo International - Treasurer, IR*
Robert Spoerry *Mettler-Toledo International - Chairman, CEO*
Bill Donnelly *Mettler-Toledo International - CFO*

CONFERENCE CALL PARTICIPANTS

Darryl Pardi *Merrill Lynch - Analyst*
Paul Knight *Thomas Weisel Partners - Analyst*
Peter McDonald (ph) *UBS - Analyst*
Sara Michelmore *SG Cowen - Analyst*
Richard Eastman *Robert W. Baird & Company - Analyst*
Vivek Khanna (ph) *Argus Partners - Analyst*
David Gidion *J.P. Morgan - Analyst*
Scott Wilkins *UBS - Analyst*

PRESENTATION

Operator

Good day,ladies and gentlemen. And welcome to the Mettler-Toledo International Q2 2005 earnings conference call. My name is Carlo and I'll be the coordinator for today's presentation. At this time, all participants are in a listen-only mode. We will be facilitating a question-and-answer session during today's presentation. [OPERATOR INSTRUCTIONS]

I would now like to turn the presentation over to Mary Finnegan, Treasurer and Investor Relations. Please proceed, ma'am.

Mary Finnegan *Mettler-Toledo International - Treasurer, IR*

Thank you. Good afternoon. I'm Mary Finnegan, Treasurer and responsible for Investor Relations at Mettler-Toledo. And I want to welcome you to the call this afternoon. I'm joined by Robert Spoerry, our Chairman and CEO; and Bill Donnelly, our Chief Financial Officer. I'll start by covering some administrative matters. I will then turn the call to Robert, who will provide you highlights on the quarter. Bill will, then, cover the financials in details, and then Robert will update you on current market conditions and our strategic initiatives. Of course, we'll have time for Q&A at the end.

Now, for the administrative matters. First, this call is being webcast and is available for replay on our website at www.MT.com. A copy of the press release we issued today is also available.

You should be aware that statements on this call, which are not historical facts, may be considered forward-looking statements for the purposes of Safe Harbor Provision under the Private Securities and Litigation Reform Act of 1995. Forward-looking statements involve risks and uncertainties that could cause actual events or results to differ materially from those expressed or implied. For further information concerning issues that could materially affect our performance, please refer to our filings with the SEC. We undertake no responsibility to release, publicly, any revisions to forward-looking statements as a result of subsequent events or developments.

One other item on today's call -- we may use non-GAAP financial measures. More detailed information with respect to use of and differences between the non-GAAP financial measures and the most directly comparable GAAP measures is provided in the press release. I'll now turn the call over to Robert.

Robert Spoerry *Mettler-Toledo International - Chairman, CEO*

Thanks, Mary. I wanted to thank you you all for joining us, today, on this call. We are very pleased with our second quarter results, particularly the improved local currency sales growth and it's a very strong increase in our EPS, after, of course, adjusting for one-time items which Bill will explain later on.

Our sales gross in the quarter was an increase of 7%, of which currency was benefiting us 2% and we grew in local currency by 5%. We are especially pleased to see better performance in Europe, which was [indiscernible] with most of our laboratory and industrial product lines in Europe showing good growth.



EPS, after excluding the one-time pipette litigation charge and investigation costs from last year, was up strong 13%. Finally, our cash flow generation was solid in the quarter.

Our outlook for the remainder of the year is very positive and we are about efficient to achieve our financial targets for the year. Bill will now provide more details on the financials.

Bill Donnelly *Mettler-Toledo International - CFO*

Thanks, Robert. Hello, everybody. We had a good second quarter and, as Robert just highlighted, we achieved a 13% or \$0.08 per share increase, if you adjust for the one-time items. Let me go into some additional details, starting with sales.

Sales in the quarter \$368.6 million, an increase of 7%, consisting of a 5% local currency growth and a 2% currency benefit. In addition, exited product lines reduced sales by, approximately, 1% in the quarter.

Before I get into details on sales, I want to remind you that we focus on local currency sales growth, which drives our operating performance and is a much better measure for us than U.S. dollar sales growth. So we'll focus on numbers and constant currency for the remainder of the sales discussion. All comparisons are versus the second quarter of last year.

I'll start with sales by geographic destination. Europe recognized a 3% local currency sales growth. Sales growth was solid in most laboratory and industrial product lines, while retail was down.

In the Americas, sales grew at 3%, although this was below the level we saw in the first quarter, it was in line with our expectations. Sales growth in the Americas was relatively consistent among lab, industrial and retail-oriented products.

Sales growth in Asia/ Rest of World, was up 13% in local currency, a little better than we expected at the beginning of the quarter. China was inline with our expectations, while Japan and southeast Asia came in a little stronger. Sales in the region were strong in most product lines.

Turning from geography to business area, let me start with lab which had a strong second quarter, with sales up 6% over the prior year. Exited product lines hurt lab growth by approximately 1% in the quarter. The sales growth was driven by Balances, Analytical Instruments, and as well, Process Analytics. Sales growth in Drugs Discovery was down slightly against the strong comp from the prior year but orders, at the same time, were actually up.

Industrial Products were also strong in the quarter, up 6% over the prior year. Our core Industrial and Product Inspection Businesses performed well, while our Transport and Logistics Business had a very strong quarter. Robert is going to provide you an update on our T&L Business a little later in the call.

Finally, in retail, sales were down 3% in the quarter, due to decline in Europe.

Let's move down the rest of the P&L. Gross margins were 48.9% as compared to 48.7% last year. We continued to benefit from cost rationalization programs to reduce overhead costs, as well as procurement and redesign efforts to produce product cost. Pricing was strong in most product areas, except retail, and steel prices tended to hurt our industrial product lines.

R&D amounted to \$20.9 million or 5.7% of sales, on target with what we expected and slightly higher than last year. SG&A was \$108 million, up 7% in U.S. dollars. Of this increase, 3% was due to currency and the remaining 4% was local currency growth. Factors contributing to the local currency growth were investments in our global sales and marketing efforts and higher corporate governance costs, including [SACH]-related costs. These were partially offset by investigation costs included in last year's amount. The net sum of these items resulted in an adjusted operating profit of \$51.4 million as compared to \$46.7 million in the prior year.

Continuing down the P&L, amortization amounted to \$3 million in the quarter, interest expense was \$3.8 million. Our tax rate, excluding



one-time charges, was 30% in the quarter. We recorded a one-time charge related to our previously disclosed pipette litigation of \$21.8 million or \$13.1 million after tax or \$0.30 per share.

Let me walk you through the details of this charge. Of the total, \$19.9 million is non-cash write-off of the intangible asset associated with the license agreement that under dispute. The judgment terminated the contract and, although we're still considering our legal options with respect to the case, we determined that the asset has been impaired and should be written off. Also included in the charge are litigation-related costs of \$1.9 million.

As previously stated, we do not believe that the judgment will have a material impact on ongoing financial results. We will replace the product whose license we lost with a product we already sold in the European market, but had not sold in the U.S. market. Even if we lose some sales, our margin will eventually be higher because we'll manufacture these products.

The net result is net income of \$18.3 million and earnings per share of \$0.42 per share, which includes \$0.30 charge previously discussed -- or just discussed above. On a comparable basis, that is, if we exclude one-time charge of pipette litigation, as well as the investigation costs from last year, earnings per share was up a strong \$0.13 (ph) -- 13% in the quarter.

Let me turn to cash flow, net cash provided by operations was \$50.6 million, an increase of 11% over the prior year amount of \$45.5 million. DSO improved in the quarter from 51 days down to 48 days, and we continue to see improvements in our ITO, which improved to 4.7 from 4.5 last year. We're pleased with these continued improvements in working capital.

During the quarter, we repurchased 977,900 shares of stock for a total of \$46.3 million. And as I mentioned last time, our intention is to use our free cash flow in 2005 for share repurchases. This, of course, could change with a sizeable acquisition or other developments but we're now moving towards this target.

Our capital structure remains strong. At the end of the quarter we had \$160.8 million of net debt and -- versus a last 12 months EBITDA of \$213.8 million, which gives us net debt-to-EBITDA of .8 times. This gives us adequate financial flexibility to continue our share repurchase program and have room for possible acquisitions.

One topic I wanted to comment on, is our plans with respect to the American Job Creations Act of 2004 that allows the repatriation of foreign earnings at substantially reduced tax rate. We're currently finalizing our analysis, but estimate that we'll repatriate approximately \$400 million in cash from our foreign operations. These earnings are primarily from our low-tax countries of Switzerland and China. This will result in one-time tax charge of up to \$15 million with cash costs lower of about \$8 million, because of the utilization of tax credits. We expect to have a significant pay-back on the \$8 million over the next five years, with anticipated tax savings of, approximately, \$40 million.

The implementation of this tax act will result in our balance sheet being, quote, unquote, grossed up. That is, we'll have debt overseas and excess cash in the United States. We estimate that in two years our balance sheet will be back to its quote, unquote, previous state. In terms of what we'll do with the cash, we'll expend it per the guidelines outlined in the tax act; however we're making no changes to our uses of our cash flow that we've discussed with you in the past. That is, we'll continue to use our free cash flow for share repurchases and acquisitions. We expect to finalize the American Job Creations Act in the third quarter.

In terms of guidance for the remainder of 2005, we now believe that we'll end up at the high -- mid to high end of previously given guidance of local currency sales growth and earnings per share. These ranges are for local currency sales growth 3 to 5% and earnings per share in the \$2.65 to \$2.75 range. In terms of Q3 guidance, current consensus is \$0.65 per share, which we think is reasonable. Our earnings per share guidance does not include one-time charges related to the pipette litigation nor any impact of the Job Creation Act. That's it for my side. And now I'll turn it back to Robert.

Robert Sperry Mettler-Toledo International - Chairman, CEO

Thanks, Bill. I want to start by adding to Bill's comment on sales performance and on our outlook for the remainder of the year. I will then provide an update on selected strategic initiatives.



Looking at our geographic markets, as mentioned at the beginning of the call, I was really pleased to see the sales growth and the improvement of sales growth in Europe in the quarter. In Europe, sales were solid, both in the laboratory and industrial product line with transportation and logistic being very strong, in particular. Retail was below last year as they faced very challenging comparisons. Expect to see improvements in our European retail business during the remainder of the year. Overall, across all businesses, expect sales in Europe for the full year to be in the range of low single digit.

Sales growth in the Americas came in pretty much as we expected. Industrial growth was solid, but that's expected. We saw it below the very strong level we had in the first quarter. Retail has a solid growth, which was better than in Q1. As we look at Q3, order intake on the industrial in the Americas looks very solid.

In terms of Asia, China came in as expected. They face tough comparisons with the prior year. China has strong backlog entering into Q3. Japan and southeast Asia had very strong sales growth in the quarter. And we don't think we will continue that -- that that will continue for the rest of the year.

Now turning to market conditions in our different businesses. Laboratory had a strong quarter and this, despite a very solid quarter last year. Balances as well as Analytical Instruments were the principle growth drivers. Drug Discovery was down, slightly, in the quarter, but has a much better backlog than at the same time last year. It continued to see strong demands in our Process Development Area with continued weakness in our Discovery Business.

Industrial had another quarter of solid growth. Industrial growth in Asia was strong and our Transportation Logistic Business globally had outstanding quarter. As we've not spoken about this business recently, I thought I would provide brief update on the business.

We've been a pioneer in the development of the [Indiscernible] and basic capture technologies for the transportation and logistic industry for many years. And we have the most accurate and highest throughput solutions in the industry. Our solution help freight carriers recover revenues through [indiscernible] pricing, based on dimension, as well as weight. Our solutions also have operational cost savings and help, of course, the information of the [Indiscernible].

Sales growth in the second quarter was strong, both in the U.S. and Europe. In the United States, dimensioning is a more mature technology and carries focus is more on the improvement of the read rate, the ability of the system to read accurately the bar coding. They are adding more readers, demanding faster and more accurate solutions and increasingly looking at camera-based systems, which gives two dimensional capabilities. We have [indiscernible] the radio solutions to address these needs.

In Europe, the market dynamics are somewhat different. The technology adoption of the dimension is not mature. Furthermore, we see a lot of consolidation in this market as many big U.S. carriers look to expand the geographic presence. Our opportunities in the business includes Asia, which is owned a small portion of the total business now, but has tremendous opportunities for growth.

You also see opportunities selling to warehouse or logistic companies who want to install dimensioning instruments so they know they are being charged correctly. They have need for systems which are smaller and more flexible than those used. We are holding out such a solution in several markets in Europe. Although our Transportation and Logistic Business is small portion of the overall industrial business, it has a strong growth dynamics.

Finally, a word to retail. As I said before, retail was down in the quarter. We select challenging comparison in the second half of the year and based on our strong project pipeline, we would expect to see modest growth in the retail for the remainder of the year and low single digit growth for the full year. That's all I wanted to cover in terms of the businesses.

In terms of our strategic initiatives, I want to provide you an update on Project Spinnaker which, as you know, we initiated about year ago with the goal of improving our organic sales growth. Most of you know that the more than 75% of our product lines, we have the number one global market leadership position. Even so, our world market share costs all our products is around 20%. So we believe we can increase the market share by increasing that -- the effectiveness of our sales, service and marketing organization. In the course of the



Project Spinnaker we identified many opportunities and for the time being, we narrowed the list to four focus areas; namely, segment marketing, regeneration, field automation, and pricing.

Today, let me talk -- take you through what we're specifically doing in one of these areas, namely, in the area of regeneration; and also have your measuring the progress on this initiative. Since the first quarter of the year, we are measuring leads in our sales organization throughout the world. Our goal is not to just obtain great number of leads but rather, a great number of high-quality leads. We're also tracking the source of leads, which includes leads from our service organization, from e-mail campaigns, seminars, direct mail campaigns, exhibition, trade shows or our telemarketing departments. We also continue to closely track the lead generation from our web track form.

In addition to tracking leads, we're implementing marketing initiatives to generate more leads. As you know, one key initiative to generate more leads is segment marketing. Since the beginning of this year, we've added 10 new segment marketing campaigns in such areas as cosmetics, snack food, flavors, [Indiscernible] and the chemical industry. Our segment marketing campaigns have proven to be very successful in generating new leads in sales.

Our initiatives to increase our leads include significant increases in telemarketing, or providing incentives to our service organization. Finally, we are also expanding our electronic lead generation to enhancing our web consent through e-mail campaigns, online ads and expanding the use of key word in search engines.

Now, of course, you wonder about the results. The results of all of this effort is significant increase in the number of leads. In those units, that we have [Indiscernible] along with our Spinnaker implementation we are seeing very significant double-digit growth in the numbers of leads. We are convinced that the increase in the number of leads will increase our sales momentum.

Project Spinnaker is more directed to the top line growth, but also, as you know, we have defensive strategic initiatives which will help us to improve our cost effectiveness and also efficiency of our working capital, including our efforts around supply-chain management. Our goals in supply-chain management are two-fold: To reduce the cost of managing our inventory, as well to reduce the inventory levels.

Last year, we expanded our procurement initiatives to include the full supply chain to gain greater efficiencies of costs and assets. This made many good progresses and are now very short with starting the operation of our North American logistic cup in Ohio. In addition to cost savings from a more centralized approach, this move will help us to reduce inventory levels. We are already seeing improvement in our inventory terms but see further opportunities to increase the inventory term to five times.

On the procurement side, we continue to be able to offset price increases with savings in other areas. Overall, our material purchasing, our material costs are flat, despite inflation and pressure from the field and other commodity price.

In summary, we are very pleased with the result of the quarter and the progress on our initiatives. Our sales growth has improved, and order entry or backlog as we enter Q3 is very solid. We remain cautiously optimistic for the remainder of the year. That's all I wanted to report and now I want to ask the Operator to open the lines for questions.

Operator

Thank you, sir.

QUESTIONS AND ANSWERS

Operator

[OPERATOR INSTRUCTIONS] Our first question from the line of Darryl Pardi with Merrill Lynch.

Darryl Pardi Merrill Lynch - Analyst

Good evening, Robert, Bill, Mary.



Robert Spoerry Mettler-Toledo International - Chairman, CEO

Hi, Darryl.

Darryl Pardi Merrill Lynch - Analyst

Hey, Bill, the gross margin expansion was a bit lower than I anticipated and a bit lower than we've seen in the past few quarters. Yet the sales mix, I think about lab being up 6% and retail down a bit, would have expected that to widen a bit more. Is there anything in the quarter that led to that sort of narrower or -- less gross margin expansion?

Bill Donnelly Mettler-Toledo International - CFO

I think one thing is, you start -- we start seeing it in quarter of the prior year -- around this time last year is when we were starting to pick up, quite nicely as, maybe, let's say one comment. I think the comparisons are getting a little bit tougher.

But probably if I dig into the details, we were -- we had a higher mix, as Robert mentioned, of T&L projects within the group. Gross profit margin on those, cause it's kind of a systems project and we're integrating in other people's product, would have eaten into it a little bit. And, as well, we saw pressure in terms of retail pricing.

We looked at the details in terms of pricing on Laboratory and most of our Industrial products and Process Analytics and even Product Inspection; and we generally are quite happy with realized pricing levels. But retail due to, let's say, some pressure on some larger orders was weaker than we expected in the current quarter. We also took, I think, if I looked at the year-on-year numbers, we had a little bit more inventory charges in the period, but I think pricing and retail and the mix towards T&L were probably bigger effects.

Darryl Pardi Merrill Lynch - Analyst

Okay. The Chinese government floating you on, looks like we could see as much as a 10% move over the next 6 to 12 months. Are you still thinking that will be neutral to results with higher dollar sales in China offsetting the higher expenses?

Bill Donnelly Mettler-Toledo International - CFO

Yes. Of course, we need to monitor it every quarter and there could be periods where we move a little bit one way, depending on how much production we're shifting at one point in time versus how fast we're growing the local business. But using the first half of the year numbers it's pretty close to neutral and we're going to take, I think Mary told me today, relatively small kind of one-time, had a balance sheet exposure I think of 100, or 150 grand as a result of the balance sheet -- you know, we had dollar receivables in the Rainin Company. So there was a little bit of a hit, there, for Q3 but not a material number.

Darryl Pardi Merrill Lynch - Analyst

Okay. And, Robert, could you talk about progress with -- or where customers are implementing Lab X for the Balances?

Robert Spoerry Mettler-Toledo International - Chairman, CEO

Yes. Happy to do that. Progress on that equation is excellent. We're probably there at the percentage of 30 to 40% of the instruments being sold in conjunction with Lab X. On Balances we have many pilot installation in all key markets -- long and good profit rate. It's a very clear differentiator and also, as you know, very key for the push our new products. The value proposition of Lab X is really strong, in combination with the new Balances. And of course in that sense, we not only interested to see it on the progress of Lab X for Balances but also impact it has on the new balances itself.

In terms of the Balance business, frankly, I was very happy with the growth we've seen in the quarter. In spite of a difficult comparison to the previous year. I think that it shows that the new product are very well-received. Hopefully, we can continue to build on that in the rest of the year.

Darryl Pardi Merrill Lynch - Analyst

Okay. Great. And, at this point, are you now offering, on the pipette side -- are you now offering the basic pipettes, the [Thin-on] LTS pipettes in the U.S. in place of Gilson?



Robert Spoerry Mettler-Toledo International - Chairman, CEO

Yes, of course. Maybe just for everybody, as part of this termination of the contract with Gilson, we have, now, of course to find alternative solutions. We have comparable products which are more economic, which we have sold outside of the U.S. and, of course, just now launching these product in the U.S. We have on those products, many factory costs which are, frankly, much, much below the purchase price we had to pay to Gilson beforehand and, of course, selling those products.

We are very pleased with the acceptance of these products in the U.S. market and we are optimistic that we are going to kind of protect our operating profits. Though might lose -- or we will lose some sales volume, but we'll sell our own products and because we manufacturer them, we have, also, the manufacturing margins. And in spite of some sales decline, they'll, of course, enjoy the better margin and hopefully help to us remain on the high profitability level.

Darryl Pardi Merrill Lynch - Analyst

Okay. Do you know who they -- what the route to market is now? In absence of Gilson in the U.S.?

Robert Spoerry Mettler-Toledo International - Chairman, CEO

No. It's unclear to us.

Bill Donnelly Mettler-Toledo International - CFO

They have a small distributor that's announced they have distribution rights. Whether they'll be others, as well, we're not sure yet.

Darryl Pardi Merrill Lynch - Analyst

Okay.

Robert Spoerry Mettler-Toledo International - Chairman, CEO

I mean, as Bill mentioned before, of course we keep our options open. And of course we're considering to further appeal. But, of course, for the moment, the situation is clear and we are selling what we have.

Darryl Pardi Merrill Lynch - Analyst

Great. Thank you very much.

Bill Donnelly Mettler-Toledo International - CFO

Thank you.

Operator

And our next question from the line of Paul Knight with Thomas Weisel partners.

Paul Knight Thomas Weisel Partners - Analyst

Bill, how much cash did you say you're bringing back?

Bill Donnelly Mettler-Toledo International - CFO

\$388 million, approximately, \$400 million.

Paul Knight Thomas Weisel Partners - Analyst

So that's -- where's that on the balance sheet?

Bill Donnelly Mettler-Toledo International - CFO

We're -- we haven't done it yet, but we will be doing it, so we're going to take down -- use existing cash balances, which, as you can see, the amount of cash we have on the balance sheet today is mostly located overseas. And then we're going to make some borrowings, as



well at -- on the overseas lines and then take that money back to the United States, pay down some debt here. But, then, sit with the higher cash balance for a couple of years, assuming that we don't do anything. But, of course, we're going to be targeting acquisitions, as well.

Paul Knight Thomas Weisel Partners - Analyst

What do you assume for foreign currency impact just the current exchange rate?

Bill Donnelly Mettler-Toledo International - CFO

When you say foreign currency -- ?

Paul Knight Thomas Weisel Partners - Analyst

When you give the second half projections, you're assuming what type of translation rate environment?

Bill Donnelly Mettler-Toledo International - CFO

The current rates.

Paul Knight Thomas Weisel Partners - Analyst

And then, Robert, on the organic growth, you're now guiding 3 to 5%, what do you think the normalized organic growth is going to be after all of the internal initiatives are accomplished?

Robert Sperry Mettler-Toledo International - Chairman, CEO

First, the full-out guidance is on the higher end of the range.

Paul Knight Thomas Weisel Partners - Analyst

Yes.

Robert Sperry Mettler-Toledo International - Chairman, CEO

And, I always did say, in a normal economic environment we can go in the range of 5 to 6%. And I think, what we have shown here in the quarter is good proof of that. And with all of the other things we do with respect to Project Spinnaker, among others initiatives, but also new products, I'm really optimistic this is very doable.

Paul Knight Thomas Weisel Partners - Analyst

Okay. And then lastly, what did you say in the north -- in the Americas growth rate was, Bill?

Bill Donnelly Mettler-Toledo International - CFO

3% in the quarter.

Paul Knight Thomas Weisel Partners - Analyst

Okay. Thanks.

Operator

And, sir, our next question from the line of [Peter McDonald] (ph) with UBS.

Peter McDonald UBS - Analyst

Thanks for taking my question and good quarter. First, how much left on the share repurchase plan?

Bill Donnelly Mettler-Toledo International - CFO

We have, approximately, \$123 million remaining on the programs, and we have, of course, the opportunity to expand that with court approval as well.



Peter McDonald UBS - Analyst

You plan on drawing that down mostly this year, or -- ?

Bill Donnelly Mettler-Toledo International - CFO

I think we've stated previously, we would target around our level of free cash flow.

Peter McDonald UBS - Analyst

Okay.

Bill Donnelly Mettler-Toledo International - CFO

I think people are assuming some number in the \$140 million kind of a range.

Peter McDonald UBS - Analyst

Also, pharma spending seems to be rebounding a bit could you maybe talk about the outlook in that segment a little bit?

Bill Donnelly Mettler-Toledo International - CFO

Pharma spending?

Robert Sperry Mettler-Toledo International - Chairman, CEO

Hey, Peter, I think, first of all, the Pharma results have been encouraging in channelling Q2. And, yet, our [Indiscernible] in Q2, better than in Q1, and in that sense we're certainly optimistic, yes.

Peter McDonald UBS - Analyst

Okay. And finally, maybe talk a little bit about where the areas of focus is for your acquisition plan?

Robert Sperry Mettler-Toledo International - Chairman, CEO

Same as we told you in the past. In terms of businesses, we focus on opportunities in the field. And to find Packaging Inspection, but that would be metal detectors, check weighers or x-ray or related technology. The reason why we say that, these products have great value proposition to the custom, in terms of productivity improvement and product safety, food safety. We see there are some opportunities to further expand.

Then, number two, of course, in channel what we'll call or Laboratory business, just adding on other product lines. And, then, number three, Process Analytics. Process Analytics is a business which does very well within total portfolio file businesses. And we would see there, also, further opportunity to extend measuring parameters, which we cover currently.

Peter McDonald UBS - Analyst

Okay. Thanks a lot.

Robert Sperry Mettler-Toledo International - Chairman, CEO

Thank you.

Bill Donnelly Mettler-Toledo International - CFO

Thank you.

Operator

Sir, our next question from the line of Sara Michelmores with SG Cowen.

Sara Michelmores SG Cowen - Analyst

Good evening, everyone.



Bill Donnelly Mettler-Toledo International - CFO

Hi, Sara.

Sara Michelmore SG Cowen - Analyst

Bill, just quick housekeeping. What was the share count at the end of the quarter, please?

Bill Donnelly Mettler-Toledo International - CFO

43.035 million Thanks for the precision. Robert, I just a question on this European retail business. It's been down pretty significantly the last couple of quarters, you touched on it briefly. I'm just wondering if you could talk a little bit about the market dynamics, there. A - the market growth; B -- if there's any new competitive dynamic going on? Lastly, how do you get that business back into positive territory?

Robert Sperry Mettler-Toledo International - Chairman, CEO

Okay. Of course, as you all know, European retail was difficult after the conversion of the Euro, where a lot of the trading was replaced. And, therefore, the market declined just after that, significantly. We had some quarters, with growth, others where we had also some decline. But the European retail business, for example, last year, single digit growth, so that wasn't that bad. In Q1 and Q2 this year we had difficult comparison versus last year, because last year we had one big order. the timing of this project is just a little different. The outlook for Europe, actually, for the second half is showing decent growth, meeting our range and we'll be okay with the number.

Sara Michelmore SG Cowen - Analyst

Okay. So we are looking for a mid-single -- at least a positive growth number for that European retail business in the second half of the year?

Robert Sperry Mettler-Toledo International - Chairman, CEO

Yes. Again, just to repeat myself, we had a mid-single digit growth last year. in total.

Sara Michelmore SG Cowen - Analyst

That's very helpful.

Robert Sperry Mettler-Toledo International - Chairman, CEO

What we're doing to get this -- we have a lot of new products with a lot of new capabilities [indiscernible], which I mentioned many times before. Bill did also mention that we had some pricing pressure from customer in that business, we actually make big concerted moves for product cost reduction and we have very specific targets, but not only targets. we actually have very specific, concrete measures which give us a lot of belief that we're going to meet the targets. And we're going to have good product cost reduction to come in the course of next year on those product lines.

Sara Michelmore SG Cowen - Analyst

Okay. Then on the Industrial Business, clearly had a much stronger first half on organic bases, I think, than you all were expecting heading into the year. Just wondering if you think that's sustainable near-term?

Robert Sperry Mettler-Toledo International - Chairman, CEO

Yes. A good part of the growth comes from the P&L business and you know, frankly, the backlog is very strong in that business -- the backlog this year. With all of the new products we have I'm optimistic, as well. And, then, last not least, I mentioned that very briefly, so far, we have been very much focused on the big transportation companies in that segment. But when we start to look at the other opportunities in that business, like, the smaller warehouse shipper segment, but also the OEM system integrator we see additional opportunities. We, actually, having ready with new products for those markets. And furthermore, Asia, frankly, a market which is [indiscernible]the technology, but we know from many of our bigger companies, the bigger companies, again, those global express carrier and they are ready with big investment coming from eastern Asia.

Sara Michelmore SG Cowen - Analyst

Great. Thanks, everyone.



Operator

Sir, our next question is from the line of Richard Eastman Robert Baird.

Richard Eastman Robert W. Baird & Company - Analyst

Yes. Hi, Bill, Robert, Mary.

Robert Sperry Mettler-Toledo International - Chairman, CEO

Hi, Rich.

Richard Eastman Robert W. Baird & Company - Analyst

Just a quick question on the Service business in the quarter, how did that fare year-over-year? Is that running yet?

Bill Donnelly Mettler-Toledo International - CFO

Yes. In terms of the overall Service Business -- give me just two seconds. It was -- Service in the quarter was up in local currency -- 5%. And so inline with the product business.

Richard Eastman Robert W. Baird & Company - Analyst

Okay. And what personal of sales roughly?

Bill Donnelly Mettler-Toledo International - CFO

It was \$84 million.

Richard Eastman Robert W. Baird & Company - Analyst

Okay. I can do that. Okay. And, then, just a second question. Bill, you had mentioned in your commentary, again, the Americas was up 3% versus the 7% first quarter. You mentioned that the 3% on plan?

Bill Donnelly Mettler-Toledo International - CFO

Yes.

Richard Eastman Robert W. Baird & Company - Analyst

I'm curious, just explain that a little bit. It doesn't look like the comparison was really difficult. And I'm curious, is that just some lumpy shipments that, perhaps, fell into the first quarter? Or how should we view that business, going forward? If, in fact, it is not slowing down relative to your plan, how should we view that business for the second half of '05?

Bill Donnelly Mettler-Toledo International - CFO

Okay. First of all, maybe it was a little bit us having insight in terms of when the T&L business would actually be shipped, timing wise, in terms of the order backlog. But just to give you a feel, we were in the Americas -- in Q1, the 7% was against a zero growth quarter in the prior year. And the 3% this quarter was against a 4% growth in the prior period. Now, I think we're certainly expecting something above the 3% for the next two quarters.

Richard Eastman Robert W. Baird & Company - Analyst

Okay. All right. And, is it -- you use that -- is that driven by -- which of the three business groups?

Bill Donnelly Mettler-Toledo International - CFO

Actually, if I go down the list, pretty much everybody should have some level of growth there. I -- especially -- with just picking a couple examples. Auto Chem has a couple of million more backlog. The Retail business we're expecting a pick-up.

Richard Eastman Robert W. Baird & Company - Analyst

Okay.



Bill Donnelly Mettler-Toledo International - CFO

Second half. So.

Richard Eastman Robert W. Baird & Company - Analyst

Okay. And, then, just one specific question on the Lab business. Given the Lab was up 6% in local currency, was Balances -- were Balances up more than 6%?

Robert Spoerry Mettler-Toledo International - Chairman, CEO

We were around that number, at the high-end, yes.

Richard Eastman Robert W. Baird & Company - Analyst

Okay. Very good, thank you.

Robert Spoerry Mettler-Toledo International - Chairman, CEO

Welcome.

Operator

And, sir, your next question from the line of [Vivek Khanna] (ph) with Argus Partners.

Vivek Khanna Argus Partners - Analyst

Hello, good evening. I had a couple of questions. Can you just tell us when you will anniversary these exited product lines?

Bill Donnelly Mettler-Toledo International - CFO

Pretty -- it will go through -- okay, the largest one of them, which relates to this Electronics Business we did in Life Science area, will still have a comparison through to the fourth quarter. Beyond that, not really.

Vivek Khanna Argus Partners - Analyst

So, mainly in the fourth quarter you will exit it?

Bill Donnelly Mettler-Toledo International - CFO

Yes.

Vivek Khanna Argus Partners - Analyst

Then, what was the China growth in the quarter, did you give -- I don't think you gave that.

Bill Donnelly Mettler-Toledo International - CFO

China was up 7% in terms of the sales number, I think. And, probably, close to double that on the order side.

Robert Spoerry Mettler-Toledo International - Chairman, CEO

Order entry was very strong.

Vivek Khanna Argus Partners - Analyst

Great. And then what's your view on margin expansion, here? It seems like the margins fairly flat, year-over-year. Just wondering what, if you get, maybe -- when do we start to see some real margin expansion? If we get to 7% revenue growth? What's the magical number here?

Bill Donnelly Mettler-Toledo International - CFO

I -- we're optimistic that we'll continue to deliver nice margin expansion. I think we're at this 5% level, we'll continue to get improvements and if we get something above 5%, even more. We're optimistic.

Vivek Khanna Argus Partners - Analyst

And, then, the rational for bring the dollar -- for borrowing in European countries and bringing them to the U.S. is it more economical? Is that why you're doing that?

Bill Donnelly Mettler-Toledo International - CFO

Sure. Kinda the way U.S. works is, that if you have earnings taxed overseas at lower rate, then the U.S. rate, which is 35% for federal income taxes, the minute you bring that dividend of that earnings home, you have to pay up to the 35% rate.

So let's say in Switzerland today, we pay around 20% or so they'd want to tax 15% on that -- lay a 15% tax on top of the dividend. And there's a tendency to try to keep the money overseas and find other ways to get yourself liquidity in the United States, if you can, via making European acquisitions or other types of investments. And this is an opportunity for us to do this and will save us taxes over the coming years -- pretty -- a good pay back.

Vivek Khanna Argus Partners - Analyst

Have you been able to identify any acquisitions or it's still very preliminary?

Bill Donnelly Mettler-Toledo International - CFO

I think preliminary, but I think it's also fair to say I would feel -- I think it's fair to say we all feel better about the pipeline today, than one year ago.

Vivek Khanna Argus Partners - Analyst

Great. Thank you very much. Nice quarter.

Bill Donnelly Mettler-Toledo International - CFO

Thank you.

Operator

[OPERATOR INSTRUCTIONS] Sir, our next question is from the line of [David Gidion] (ph.) with J.P. Morgan.

David Gidion J.P. Morgan - Analyst

Hi, guys, how are you doing? Calling on behalf of Tycho Peterson, tonight. Answered most of my questions. One question we did have, in regards to China, again, could you maybe share some color on where you are in the manufacturing shift in China?

Robert Spoerry Mettler-Toledo International - Chairman, CEO

Yes. I can give you some ideas there. Probably 15% of our sales are -- group sales from products manufactured in China. We're constantly transferring more production to China, probably in three years from now, the number is going to be 25% or so.

Of course, aside from just the manufacturing, the procurement, which I mentioned before, works also in global sourcings and investment plans to source more and in China, in terms of parts, components or sub-assembly and had, of course, a positive impact.

David Gidion J.P. Morgan - Analyst

Okay.

Robert Spoerry Mettler-Toledo International - Chairman, CEO

And manufacturing capacity and we have three plans. We have the plans, not only the manufacturing capabilities, but also R&D capabilities. We have in the range of tons and tons of plenty R&D guys in China. These guys design products for the local market but these products, which are designed for the global markets, are very often both complementary low-end products for the low -- global [Indiscernible] distribution.



David Gidion J.P. Morgan - Analyst

Okay. Thank you very much.

Robert Sperry Mettler-Toledo International - Chairman, CEO

Very welcome.

Operator

And, sir, we have a question from the line of Scott Wilkins with UBS.

Scott Wilkins UBS - Analyst

Yes. Good afternoon. Just have, first, just a question on the cash flow, Bill. Is your guidance for free cash flow still 140? Did I hear that right?

Bill Donnelly Mettler-Toledo International - CFO

Yes. That's the number we're targeting.

Scott Wilkins UBS - Analyst

Just looking at the first half of this year, I think it's around \$45 million or so, you're about \$20 million below the pace last year. So, where do you see the big catch collection opportunity in the second half that will get you to that target?

Bill Donnelly Mettler-Toledo International - CFO

Okay. So, maybe I should start by explaining why it's down and then, what we -- if I look at it, it's mostly due to two items where we had additional cash flow, let's see benefit last year. The first one being the impact of our bonus programs at -- throughout the whole organization. We accrue bonuses for one year and pay them out in the next year. And that impact in -- on cash flow in 2004 versus 2005 was a negative \$15 million in this years. Then we had, I think, about \$11 million on the payable side outflow year-to-date. The -- so, we will have profit growth. We'll recover the payables number by the end of the year, is my expectation.

And we're seeing improved working capital on DSO inventory turns through our supply management initiative, among other things, I think that -- and, of course, we have a base growth in our EBITDA. So I think taking all of those things together, that's what -- that's how we see the year coming out.

Scott Wilkins UBS - Analyst

That's helpful. Just with the cash balance, it looks like -- looks like you used some debt, it looks like to finance some of the stock repurchase. Just curious why you're looking to build up cash on the balance sheet, right now? And not just using the cash flow to repurchase stock?

Bill Donnelly Mettler-Toledo International - CFO

I think that's a great question, Scott, and it fits into the 965 or the Tax Act I described in my conference call script. The way that worked is we are building up cash balances to make our dividends under that plan. Normally, throughout the year bring money back from switzer land and China into the U.S., but because of the benefits under the Tax Act, we're waiting to do it until we quote, unquote, finalize our plan. And that has a technical meaning when I say that. And we expect do that in Q3 and you'll see us bring -- gross-up our -- borrow overseas, as well as take the catch overseas and bring it back to the United States.

Scott Wilkins UBS - Analyst

Got it. Just a question kind-of following on along to Vivek's question on operating expenses, just on operating expenses. I think I heard you right, that SG&A expense is up 4% on a local currency basis. Just curious, why the increase there? And why not more leverage? And, then, second, I didn't catch the local currency growth in R&D. And maybe, I know you guys have been spending heavily in R&D, and have--



Bill Donnelly Mettler-Toledo International - CFO

Actually --

Scott Wilkins UBS - Analyst

-- a nice new product pipeline, just wondering if you are going to need to spend at that level, going forward?

Bill Donnelly Mettler-Toledo International - CFO

Actually, maybe I just answer the R&D one first. Really wasn't much growth and I think it was 1% in local currency on the R&D side.

Let's talk about SG&A for a second. So first comment would be that in -- we're making some investments on the Spinnaker side, some upfront investments. Robert talked a lot about the telemarketing, but as well other things. There's some lead time between -- first step is making the investment; second step is increasing the leads, which we're now seeing now. Then we believe there's a ratio we can expect for the increase of leads, in terms of increase sales on a time line.

Scott Wilkins UBS - Analyst

When do you start to get some of that leverage, do you think?

Robert Sperry Mettler-Toledo International - Chairman, CEO

Actually, I think part of it we already saw that quarter. Our sales growth, clearly, has been better in Q2 than it was previous quarters.

Bill Donnelly Mettler-Toledo International - CFO

Yes, if you adjust for the exited product line, the 6% number was one of the best numbers we reported in a while. Then we expect to hope -- we expect that we'll continue to see above our recent growth rates in the coming quarters.

Then, second thing is, that, and I think I described this a little bit on the phone call, in last quarter, and that is we're somewhat more front-loaded in terms of our corporate governance, Sarbanes-Oxley type cost, this year versus last year. The last year Q3 and Q4 had a lot of those types of costs and this year I'm accounting for them ratably, throughout the year.

Scott Wilkins UBS - Analyst

One last one, since I think I'm one of the last people here. Exited products, anymore opportunity for that, going forward? Any other thing you could divest that would be able to improve the return profile company?

Bill Donnelly Mettler-Toledo International - CFO

We're continuously looking at those opportunities, but there's nothing imminent.

Scott Wilkins UBS - Analyst

Got it, thanks a lot, guys.

Bill Donnelly Mettler-Toledo International - CFO

Thanks, Scott.

Operator

Sir, we have no further questions at this time. Back over to the group for any closing remarks?

Mary Finnegan Mettler-Toledo International - Treasurer, IR

Thank you for joining us on the call today. If you have any questions, don't hesitate to give us a call.

Bill Donnelly Mettler-Toledo International - CFO

Thank you.



Robert Spoerry *Mettler-Toledo International - Chairman, CEO*

Thank you, bye-bye.

Operator

Ladies and Gentlemen, we thank you for your participation in today's conference. This does conclude your presentation.

DISCLAIMER

Thomson Reuters reserves the right to make changes to documents, content, or other information on this web site without obligation to notify any person of such changes.

In the conference calls upon which Event Briefs are based, companies may make projections or other forward-looking statements regarding a variety of items. Such forward-looking statements are based upon current expectations and involve risks and uncertainties. Actual results may differ materially from those stated in any forward-looking statement based on a number of important factors and risks, which are more specifically identified in the companies' most recent SEC filings. Although the companies may indicate and believe that the assumptions underlying the forward-looking statements are reasonable, any of the assumptions could prove inaccurate or incorrect and, therefore, there can be no assurance that the results contemplated in the forward-looking statements will be realized.

THE INFORMATION CONTAINED IN EVENT BRIEFS REFLECTS THOMSON REUTERS'S SUBJECTIVE CONDENSED PARAPHRASE OF THE APPLICABLE COMPANY'S CONFERENCE CALL AND THERE MAY BE MATERIAL ERRORS, OMISSIONS, OR INACCURACIES IN THE REPORTING OF THE SUBSTANCE OF THE CONFERENCE CALLS. IN NO WAY DOES THOMSON REUTERS OR THE APPLICABLE COMPANY ASSUME ANY RESPONSIBILITY FOR ANY INVESTMENT OR OTHER DECISIONS MADE BASED UPON THE INFORMATION PROVIDED ON THIS WEB SITE OR IN ANY EVENT BRIEF. USERS ARE ADVISED TO REVIEW THE APPLICABLE COMPANY'S CONFERENCE CALL ITSELF AND THE APPLICABLE COMPANY'S SEC FILINGS BEFORE MAKING ANY INVESTMENT OR OTHER DECISIONS.

©2019 Thomson Reuters. All Rights Reserved.



THOMSON REUTERS

PLACEHOLDER TRANSCRIPT

Q3 2005 Mettler-Toledo International Earnings Conference Call

EVENT DATE/TIME: NOVEMBER 03, 2005 / 10:00PM GMT



CORPORATE PARTICIPANTS

Mary Finnegan *Mettler-Toledo - Treasurer, IR*
Robert Spoerry *Mettler-Toledo - Chairman, President, CEO*
Bill Donnelly *Mettler-Toledo - CFO*

CONFERENCE CALL PARTICIPANTS

Derik De Bruin *UBS - Analyst*
Richard Eastman *Robert W. Baird - Analyst*
Darryl Pardi *Merrill Lynch - Analyst*
Sara Michelmores *S.G. Cowen - Analyst*
David Katekian *JPMorgan - Analyst*
Mike Hamilton *RBC Dain Rauscher - Analyst*
Scott Wilken *UBS - Analyst*
J.P. Jaketin *Thomas Weisel Partners - Analyst*
Vivek Khanna *Argus Partners - Analyst*

PRESENTATION

Operator

Good day, ladies and gentlemen, and welcome to the third-quarter 2005 Mettler-Toledo International conference. My name is Kellera, and I will be your coordinator for today. At this time, all participants are in listen-only mode. We will be facilitating a question-and-answer session toward the end of today's conference. (OPERATOR INSTRUCTIONS). As a reminder, this conference is being recorded.

I would now like to turn the presentation over to your host for today's conference, Ms. Mary Finnegan. Please proceed, ma'am.

Mary Finnegan *Mettler-Toledo - Treasurer, IR*

Thank you. Good afternoon. I am Mary Finnegan, Treasurer, and responsible for investor relations at Mettler-Toledo. And I want to welcome you to the call. I am joined by Robert Spoerry, our Chairman and CEO, and Bill Donnelly, our Chief Financial Officer.

I will start by covering some administrative matters. I will then turn the call to Robert, who will provide you highlights of the quarter. Bill will then cover the financials in detail, and then Robert will provide commentary on our outlook and business. Of course, we will have time for Q&A at the end.

Now for the administrative matters -- first, this call is being webcast, and is available for replay on our website. A copy of the press release we issued today is also available on our website.

You should be aware that statements on this call which are not historical fact may be considered forward-looking statements for purposes of the Safe Harbor provisions under the Private Securities Litigation Reform Act of 1995. Forward-looking statements involve risks and uncertainties that could cause actual events or results to differ materially from those expressed or implied. For further information concerning issues that could materially affect performance related to forward-looking statements, please refer to our filings with the SEC. We undertake no responsibility to release any revisions to forward-looking statements as a result of subsequent events or developments.

One other item -- on today's call, we may use non-GAAP financial measures. More detailed information with respect to use of and differences between the non-GAAP financial measures and the most directly comparable GAAP measure is provided in the press release. I will now turn the call to Robert.

Robert Spoerry *Mettler-Toledo - Chairman, President, CEO*

Thank you, Mary. I want to thank you all for joining us today on this call. We're very pleased with all aspects of our financial results for the third quarter of this year. Our sales growth was strong at 7%, which was both the recorded growth rate, as well as the local currency growth rate. All key businesses demonstrated growth. Our food retailing and transportation and logistics were particularly strong. In



addition, sales growth was robust in all geographic parts of the world.

Our operating profit and cash flow generation was very strong, and our EPS growth excluding onetime items, was excellent at 24% growth.

As we look to the future, we are cautiously optimistic for the remainder of this year and for 2006. We will explain our outlook in more detail later in the call.

Let me now turn it over to Bill, who will take you through the financial results for the quarter. Bill?

Bill Donnelly *Mettler-Toledo - CFO*

Thanks, Robert. And hello, everybody. We had a great quarter. EPS was \$0.72 per share. This compares to \$0.58 last year, excluding in both periods the onetime items. As Robert mentioned, this represents a 24% growth, which we're very pleased with.

Now, let me take you through some additional details, starting with sales. Sales in the quarter were \$365.4 million, an increase of 7% in both reported dollars and in local currency. To say it another way, we had no material impact from currency on our sales this quarter.

Let me give you more details on sales by geography and business area. All comparisons are versus the third quarter of last year, and all growth is in local currency.

I will start with sales by geographic destination. Sales growth in Europe was up 7% in local currency, one of the strongest growth rates we've had in several years. Product inspection, transport and logistics and food retailing all were strong drivers of this European sales growth. Our lab business in Europe was up slightly against a very strong Q3 of last year.

Sales growth in the Americas was up 5%. Retail had double-digit growth; industrial and lab had mid single-digit growth in the quarter.

Sales growth in Asia/Rest of World increased 11% in local currency. As expected, China's growth accelerated over the level we saw in Q2 and was up 17% versus the prior year. All product areas showed strong growth in Asia/Rest of World in the quarter.

Turning from the geographical perspective to business areas, let me start with industrial, which had one of their best quarters, with local currency sales growth up 9%. Excluding our T&L business, our core industrial business was up 4% in the quarter with particularly strong growth in Asia. T&L had very strong growth due to significant projects in both United States and Europe. Product inspection also had a good quarter with strong sales growth.

Our laboratory business was up 3% over the prior year. Exited product lines reduced labs growth by 1% in the quarter. Drug discovery had a strong quarter, with double-digit growth, and this is versus a strong quarter from one year ago. We had low single-digit growth in balances and mid single-digit growth in analytical instruments and process analytics. Pipette sales were basically flat for the quarter. Finally, food retailing was up 14% versus last year with very strong growth in both the Americas and Europe.

Now let me move further down the P&L. Gross margins were 49% as compared to 48.5 last year. We continue to benefit from cost rationalization programs to reduce overhead costs as well as procurement and redesign efforts to reduce product costs. Some of you may have expected to see an even larger increase in our margins given the 7% sales growth, but as a reminder, the excess growth came from primarily retail and T&L, and these businesses have -- transport and logistics, just to be clear. These businesses have gross margins below the group average.

R&D in the quarter amounted to \$19.3 million or 5.3% of sales. This percentage is slightly below the level you have seen over the last several quarters. This represents a couple of things -- first of all, a conscious effort on our part to redirect R&D dollars to our marketing initiatives, specifically Spinnaker, which are aimed at improving our topline growth, and also impacting was the timing of certain R&D projects between quarters. We expect R&D to remain in this 5 to 6% range.



SG&A was \$108.8 million, an increase of 4% in both U.S. dollars and local currency terms. We continue to make investments in our global sales and marketing initiatives and reallocate investments from R&D to marketing. This quarter also included increases in variable compensation due to strong sales growth, continued investments in China. And we also had some restructuring charge in litigation costs which were offset by investigation-related costs in the prior year.

The net sum of these items resulted in adjusted operating income of \$50.9 million or 13.9% of sales as compared to 43.5 million or 4.7% of sales in the prior year. The prior year amount excludes investigation-related items. We are very pleased with our 17% growth and the margin improvement achieved in the quarter.

Continuing down the P&L, amortization amounted to \$2.8 million. Interest expense was \$4 million. This results in a net income of \$31 million, \$0.72 per share EPS-wise, which excludes the \$0.12 tax charge. On a comparable basis -- that is, if we exclude the onetime items that occurred in both periods -- earnings per share was up 24% in the quarter.

Now, let me walk you through the nonrecurring tax items that we had this quarter. First, as we told you last quarter, we intend to bring back approximately \$400 million in cash from our foreign operations in conjunction with the American Jobs Creation Act. As I think most of you are aware, this tax legislation gives companies like us the ability in 2005 to bring back earnings to the United States at substantially reduced tax rates. The incremental tax expense associated with the \$400 million dividend is \$13.1 million, and was recognized this quarter. The other nonrecurring item we recognized this quarter was a \$7.7 million benefit due to the favorable resolution of certain tax matters, of which the settlement of a tax audit was the principal item.

One additional matter -- we will close this quarter on an amended and restated bank facility. We will increase our bank capacity from 300 million to 450 million, and extend its maturity for two years until 2010. As I mentioned on the last call, with the 965 Act, our balance sheet will be temporarily grossed up -- that is, we will have borrowings in Europe and cash in United States. Given the favorable bank market and higher utilization due to 965, we felt it was an opportune time to amend and extend our facility.

Now, let me turn to cash flow. We were pleased with cash flow generation in the quarter. Net cash provided by operations was \$60.3 million, an increase of 28% over the prior year amount of 47 million. We saw improvements in DSO, which were 49 days in the quarter, a two-day improvement over the prior year. ITO on an LTM basis is now at 4.89. We are pleased with this improvement, and see further opportunity to continue to improve this going forward.

Now, let me cover our share repurchase program. During the quarter -- the third quarter, we repurchased 675,900 shares of stock for a total of \$33.5 million. To date in 2005, we have purchased 2.2 million shares, or approximately 5% of our outstanding shares. We had a \$200 million program in place which was approved by our Board last year. We expect to use approximately 150 of this by the end of this year. In order to provide continued availability for share repurchases in 2006, today, the Board authorized an additional \$200 million to be utilized through the end of 2007. We will continue to use our free cash flow for share repurchases, as we believe it is an excellent way to return value to shareholders.

Our capital structure is very strong. At the end of the first quarter, we had net debt of 134 million versus the last 12 months EBITDA of a 223.4 million, which results in a net debt to EBITDA ratio of just 0.6 times. With this strong balance sheet, excellent cash flow generation, and an expanded bank facility, we have ample financial flexibility to repurchase shares and to pursue our acquisition strategy.

Let me now discuss our guidance. With respect to the remainder of 2005, we now believe that we will finish the year in the \$2.80 range. The \$2.80 range does not include onetime items that we covered earlier. For Q4, this implies earnings per share in the \$0.90 range. Looking closer at Q4, I do not expect to see the same sales growth level that we had in Q3, which benefited from the project business in T&L and the retail. In fact, some of the strength we saw in Q3 may have some impact, a little, on Q4. I would expect sales growth in the quarter -- the fourth quarter, that is -- to be in the 4 to 5% range that we have previously provided.

As we look to 2006, we are optimistic that we can have another good year, but are realistic that there are reasons to be cautious on the economy, including the impact of rising oil prices and the sustainability of the European recovery. We will closely monitor the economy



and adjust our plans as necessary. But today, we felt quite positive about our market position and our ability to execute our strategic initiatives. Assuming an economic environment similar to today, we believe we can achieve local currency sales growth in the 4 to 6% range next year.

There may be some variability between quarters, but we believe a target of 5% is realistic. A 5% local currency sales growth would result in earnings per share in the range of 3.20 to 3.25. At the midpoint of this range, this translates to about 15% earnings per share growth for next year. And we're pleased with that. It's in line with our targets.

In times of quarterly breakdown, we'll provide more guidance as the year progresses. But I would note that we expect to be in the range in Q1 of about \$0.53 per share.

The final topic I want to cover is our equity-based compensation. We've always had options under our equity compensation program. And last year, we sought shareholder approval to add restricted stock as well. Our most senior executives will continue to receive options, as we feel strongly that their compensation should be tied directly to the creation of shareholder value.

We have reduced the number of nonexecutive managers that are eligible for equity compensation. Beginning this year, these managers will receive restricted stock. We believe the Company will gain more from these employees at the same cost through the use of a restricted stock program as compared to stock options. The actual cost of the program under FAS 123R will not change significantly as a result of the restricted stock component.

As you saw in our footnotes last year, the impact of FAS 123 was \$0.15 per share in 2004, and is expected to be at a similar level this year. We estimate that the impact of our stock-based compensation programs in 2006 will be about \$0.13 per share. This amount is not reflected in the guidance I mentioned earlier. We have benchmarked these amounts, and are confident that they are reasonable and represent a good long-term value to our shareholders.

Okay. That is it for my side, and I would now like to turn it back to Robert.

Robert Sperry Mettler-Toledo - Chairman, President, CEO

Thank you, Bill. I will begin by providing some additional comments on Q3, and then I will recap some of the key initiatives from last year.

Let me start with our lab results for Q3. We saw solid demand for our analytical instruments, particularly our thermal analysis and pH meters. Process analytics as well had another solid quarter. In balances, we continue to do quite well on the high-end as our products sold for tangible value to customers, particularly those in regulated markets. On the low-end or entry-level products, you do see some weakness. As part of Project Spinnaker, we have a task force developing a strategy to address this end of the market -- not only for balances, but for all of the low end products as well. They are evaluating supply chain, channel strategy, product mix, and marketing programs for this customer base. As we begin to implement this strategy, I would expect to see better growth from this end of the market.

You heard from Bill that pipette sales were basically flat in the quarter. This reflects reduced pricing levels from our standard jazz (ph) pipette products sold in the U.S. As a result of the litigation earlier in the summer, our distribution agreements with (ph) certain third-party manufacturers plan to chase (ph) pipettes was canceled. We are now selling direct in the U.S. our own manufactured products. Although the price are lower, our margins are higher because we managed back (ph) rather than just distribute those products.

The last piece of our laboratory business is drug recovery, which had a strong quarter and did defy (ph) a strong quarter from a year ago. Most of our ultra cam (ph) business is focused on the process development and scale-up needs of large pharmaceutical customers.

In process development, chemists and engineers determine how to manufacture a drug that has been discovered earlier. We have a leading market position in this area, and are generally considered the standard in the market. Our solutions consist of automated lab reactors, which simulates the manufacturing process in the laboratory vessel, as well as real-time analytics, which consist of probes that monitor in reaction that monitors the reaction in the vessel. We see the strong dynamics of this business continuing as pharma



companies have tremendous incentives to accelerate this process and move the drug through the manufacturing quickly. We recently received a sizable order of automated lab reactors and analytics from a large pharmaceutical customer. A portion was shipped in Q3 with the majority of it to be shipped in Q4.

Turning now to the industrial business, which you have seen had a great quarter. Growth was driven by our transportation and logistics business. We spoke about this business on our last call, so I won't cover it all again. But hopefully, you remind (ph) that we are pioneers in the development of automatic dimensioning and basic capture technology for the transportation and logistics industry, and that we have the most accurate and the highest throughput solutions in this industry.

This is a project business. And we have several projects in both the U.S. and Europe that contributed to the growth in the quarter. Our outlook for this business is solid. But we do recognize that unlike most of our other businesses, there is variability in sales growth by quarter.

Our product inspection business had also a strong quarter. We have a record number of new products in this business, as we have significantly revamped our product portfolio over the last year. The upgrading of the product portfolio allows us to continue to globalize our offering and to move ahead of competition in many important design areas.

Recently, at the packaging show in Las Vegas, we unveiled to the North American market a new metal detector and a new checkweigher. We also launched a more standardized X-ray product to complete our range in this market. We view the dynamics of this market as strong, driven by the food manufacturers' desire to protect their brands from exposure to consumer health and safety concerns as well as government regulation.

Our high-end industrial business, which combined industrial scales and terminals with software packages, is also well. These solutions help customers manage data, such as transaction processing, formulation, batching, and support statistical process control. Finally, our standard industrial business performs well, driven by the infrastructure spending in China.

Now turning to retail, we had the growth of 14% in local currency. We have been talking for the last few quarters about the opportunities in this business. Somewhat like our transportation and logistics business, part of this business is also project related. And therefore, it has variability to its sales. We had several projects in Europe that we have been expecting for some time. In the U.S., we benefited from legislation surrounding nutrition labeling, as well as the growth in our data management software business. We expect solid results in the retail in Q4 as well.

That covers my comments on the quarter, and now I want to add some comments on our strategic initiatives for 2006 and beyond. As Bill already mentioned, we're cautious on the economy, and will continue to monitor it and adjust (ph) our plans accordingly. However, we have many positive strategic initiatives that we believe will yield benefits in 2006.

Let me cover the highlights, beginning with Project Spinnaker. As most of you are aware, we have the number one position in the vast majority of our products. And yes, our worldwide (ph) market share is around 20%. We believe we can increase this market share by increasing the effectiveness of our self-service and marketing organization. Project Spinnaker identified many opportunities, and we are now focused on four of them -- namely segment marketing, lead generation, field automation and pricing.

We are continuing to drive the segment base approach to marketing across all our product lines. So with this effort, we're identifying new segments that can be added to our marketing initiative.

We're also generating more and more leads via the Internet, through significantly increased telemarketing resources and also others (ph) we've met (ph). We are closely tracking and measuring these leads to understand the ultimate effectiveness of turning these leads into sales. We are in sales more disciplined in our discounting practice, and thereby are achieving better pricing.

Finally, we have put a task force together to identify ways to improve the productivity of our sales and service force through more automation in the field. We believe we are in the early stages of this initiative, and we continue strong execution. Spinnaker shall



contribute to the growth for many more years.

The next strategic initiative I want to cover is the development of emerging markets. Our primary focus continues to be on China. We have increased the percentage of goods manufactured in China from 3% in 1998 to nearly 20% by the end of this year. Our strategy in China is twofold -- first, to capitalize on growth opportunities in the domestic market, and second, to provide low-cost production for our global distribution channel.

We see (ph) continued opportunities, and have committed to build a manufacturing facility in China in the course of 2006 and early 2007. This facility will replace an existing one and nearly double the capacity of the existing site. The cost of the facility will be in the range of \$10 million, and we are confident it will yield excellent results.

Looking forward, our investor business will continued to benefit from infrastructure growth in China. As GDP per capita increases, we foresee significant growth opportunities across our higher end business, as demand for laboratories instruments, product inspection equipment, and similar products should grow significantly. In short, we feel strong, and we feel strongly that we will continue the sizable opportunities for growth in China.

Another emerging market area that we see opportunities is India. We have had our Company in India in place since 1990, which focused on our industrial business. And we have worked through a distributor for our laboratory offering. Given the growth in this market and our desire to more aggressively develop market, we will soon begin selling direct also for those laboratory products. We already have doubled the size of our direct salesforce in anticipation, and see solid opportunity for growth in this region.

New products continue to be a central part of our strategic initiative. As we look out over the next twelve months, you'll see many new launches of products and upgrades through the software offerings. We're also focused on cost, and have several initiatives to reduce product costs and improve the management and logistics of our supply chain. I've already covered our low-cost manufacturing in China, and we think we can save more than 30% in manufacturing costs.

In supply chain management, we're working on fully integrating our supply chain from development through logistics. We believe that significant opportunities exist through further supply consolidation, low-cost country sourcing, and the drive (ph) internally to share components and modules across the product lines. We also believe we can further streamline our logistics processes, which are quite global through the growing importance of our Chinese operations. Both (ph) together, we see opportunities to continue to reduce product, product costs, and process costs and reduce inventory investments in the coming years.

In summary, you can see we have many initiatives in place. And with solid execution, we believe we can achieve solid growth. With the benefit of these strategic initiatives and the economic environment similar to today, I believe the 5% sales growth and the dollar (ph) -- 3.20 to 3.25 in EPS, which translates into 15% EPS growth, are ambitious but reasonable targets for next year.

Before I open the line for questions, I want to comment on the press release we issued this afternoon, concerning the 10b5-1 plan for the sale of my 1996 options. The plan calls for the sale of 867,000 expiring options in the coming months (ph). These options were granted at the time of the buyout from Ciba-Geigy, and we were not a public company. And they will expire in 2006. At the time of our buyout and later times, I also purchased 346,826 shares of Mettler-Toledo stock, which I will own and have no intention of selling.

Of course, I remain fully committed to Mettler-Toledo, and the sale is being driven by the pending expiration of the option. My direct holdings in Mettler-Toledo in the form of stock and remaining options represent more than 20 times my annual base salary. I wanted to communicate directly to you my intentions. And of course, you will see the required filing over the course of the coming months as the sale transactions are completed.

That is all what we have from our side. And I now would like to ask the operator to open the line for questions.

QUESTIONS AND ANSWERS



Operator

(OPERATOR INSTRUCTIONS). Derik De Bruin, UBS.

Derik De Bruin UBS - Analyst

Congratulations on a great quarter. Just looking at the guidance for '06, are you assuming that you're going to continue a moderate level of share buyback through that time?

Bill Donnelly Mettler-Toledo - CFO

Yes, similar to the amount that we repurchased this year (multiple speakers) set to repurchase this year.

Derik De Bruin UBS - Analyst

All right. And when you look at the -- you said some of your lower-end instruments -- there was a little softness in some of those -- weaknesses. Any indication of where that's coming from?

Robert Sperry Mettler-Toledo - Chairman, President, CEO

I think the low-end of the market is just more price sensitive. There are of course more competitors who have low-end products. It's not our nature to compete too much on price. And I think maybe it's also a reaction to the very strong offering we have on the high-end, as we are so strong on the high-end, many of our competitors just shifted much more of their focus to the low-end, which takes a little bit of the strength we have.

As I mentioned, this softness in a smaller part, actually, of our total market is recognized. And we see actually quite a bit of opportunity to address that part of the market in a highly effective way. The contacts (ph) have been worked out. The strategies are in place. And we will soon start with the execution. And I'm pretty sure we will put some things quite differently in place, and through that establish competitiveness and leadership for the part of the market.

Again, I want to remind everybody the core of our business is always the high-end. And the low-end is something which never has been our stronghold, but more kind of an adjacency -- but I think an adjacency that will get increasingly competitive.

Derik De Bruin UBS - Analyst

Along those lines, what type of gross margin expansion do you think you could possibly see next year?

Bill Donnelly Mettler-Toledo - CFO

We're looking at about 50 basis points -- and a couple of assumptions in that number. One is that we're kind of assuming a currency environment similar to what we saw today. As you know, we can kind of have gross up effects and things on the topline. And we're also assuming some higher growth rates in Asia than we will experience in the United States or Europe. And while at an OP level, we're doing as well in Asia as we do in other parts of the world, at a gross margin level, we don't do as well. And the reason for that is we have lower distribution costs -- and particularly, I have China in mind there. Lower prices, but lower distribution costs as well.

Derik De Bruin UBS - Analyst

Okay. And just in terms of the currency impact on the topline for next year, are you thinking you're probably getting a headwind of around -- what? 2, 3% maybe?

Bill Donnelly Mettler-Toledo - CFO

For the full year, if we take the rates, I think, at the beginning of this week or so today or -- not that (ph) -- 2%.

Derik De Bruin UBS - Analyst

Okay. Thank you very much.



Bill Donnelly Mettler-Toledo - CFO

Hey, Derek, maybe one comment, just in case -- for everybody else on the call, a 2% headwind on the topline and no headwind at the earnings line. And again, that goes to our balance in nondollar revenues and nondollar expense.

Operator

Richard Eastman, Robert W. Baird.

Richard Eastman Robert W. Baird - Analyst

Robert, could you just give a little bit of color -- within the lab segment, could you just give some thoughts as to maybe what the different customer bases bid within lab -- pharma, industrial lab, academic?

Robert Sperry Mettler-Toledo - Chairman, President, CEO

I guess I can comment that maybe by segment, by industry, probably both important to maybe even talk about customers -- individual customers. Pharma spending in general, I think, it's slightly reduced. However, it depends heavily by individual customers. I think some pharma companies are actually doing quite well. And there, we see good investment levels. And maybe there are others who are more on the cost savings, and therefore, the demand isn't so strong. Other industries pay -- I think cosmetics, chemical, food companies -- pretty good. I think certainly slightly better than what we have seen before.

Geographically, not much difference. I think the lab business -- certainly, as mentioned, it's very well in the U.S., Europe -- maybe a little softer; but from the order intake we had in Europe, that's actually -- that's pretty encouraging. And Asia, as usual, did well.

Richard Eastman Robert W. Baird - Analyst

Okay. So is it safe to say that -- just, I guess, characterizing -- the other industries grew at a better pace than pharma in the quarter?

Robert Sperry Mettler-Toledo - Chairman, President, CEO

I think pharma was all actually altogether okay -- maybe not as strong as all the time.

Bill Donnelly Mettler-Toledo - CFO

The product area that we have that has the highest percentage of pharma is the (multiple speakers) autocam (ph) business, and that had the highest growth rate within lab. I generally think we did probably even a little bit better on some of those lab customers. (multiple speakers) on some of the pharma people we cover (ph).

Richard Eastman Robert W. Baird - Analyst

How did the service piece of the business do in the quarter?

Bill Donnelly Mettler-Toledo - CFO

We had a good growth in service in the quarter. Topline growth was 5% on the topline.

Richard Eastman Robert W. Baird - Analyst

Okay. All right, and then maybe just a last question, in terms of India, just what would be a relative size of that business?

Robert Sperry Mettler-Toledo - Chairman, President, CEO

We'll find out. And the reason why I say it that way -- the reason for really changing the situation in India was that our distributor always helps (ph). He does a hell of a job, and we have a very high marketshare. And my experience is when we step into a market and try and supply our own methods, realize that the market is usually significantly bigger. (multiple speakers)

Richard Eastman Robert W. Baird - Analyst

And is the strategy there to be -- with low-end products, you went through distribution, and now going direct will be the high-end, much like it is elsewhere?



Robert Spoerry Mettler-Toledo - Chairman, President, CEO

Well, actually, that distributor handles all of our laboratory business. On the industrial side, he has already in place our own organization. That organization was put in place in the late '90s. Of course, the beauty of that is that we just can bolt on the lab business on the existing infrastructure. And as I mentioned during the call, we have been quite aggressive in adding people and setting up the organization. I expect substantial growth from India next year. And for substantial growth, I think there can be a couple of million dollars over the year.

Richard Eastman Robert W. Baird - Analyst

Okay. And then forgive me, just one last question. Could you just remind me -- in terms of the pipette business, the distribution agreement -- what's the impact on the revenue line there? Our ASP is down, but our margins are up. But what's the revenue impact on an annual basis -- about?

Bill Donnelly Mettler-Toledo - CFO

About? Okay, so just -- I'm not sure if I have your question precisely. But we -- of the product line we're talking about, last year, I think we sold about \$13.9 million of that product line. That product line will be down slightly in dollar terms -- on, let's say, the first we would get six to nine months afterwards -- it will be up on unit terms, actually, with our equivalent replacement product. And we would think over a 12-month period, we'll be OP neutral.

Richard Eastman Robert W. Baird - Analyst

Okay. But we're just -- in terms of sales, the negative sales impact -- we're just talking millions of dollars -- 3 to 5 million or something?

Bill Donnelly Mettler-Toledo - CFO

Yes, that's probably about right.

Operator

Darryl Pardi, Merrill Lynch.

Darryl Pardi Merrill Lynch - Analyst

What were the orders in transport and logistics for? I know what the products are, but to ground shippers, air shippers? Was it one customer in the U.S. and Europe?

Robert Spoerry Mettler-Toledo - Chairman, President, CEO

No, it was several customers in the U.S. and in Europe. It was mainly ground transportation. And the applications for these typical help applications that we will do the tracking of parcels, combining weighing technology, dimensioning technology, barcode reading, visual technology -- all integrated in one system across all in motion with high throughput.

Darryl Pardi Merrill Lynch - Analyst

Okay. And it sounds like the majority of the orders were delivered in Q3. Is that correct?

Bill Donnelly Mettler-Toledo - CFO

We actually have some backlog going into Q4 as well. And as well on the retail side.

Darryl Pardi Merrill Lynch - Analyst

I'm sorry; as well as on the what side?

Bill Donnelly Mettler-Toledo - CFO

As well as the retail side being another piece of the business that's somewhat project oriented that we expect to see some benefit in Q4 as well.



Darryl Pardi Merrill Lynch - Analyst

How penetrated is the ground shipping market at this point? I know it's a new customer base or a newer customer base for you.

Robert Sperry Mettler-Toledo - Chairman, President, CEO

It really depends on how you segment the market. If you look at these big transportation companies and their big hubs, no -- that market is quite well penetrated in the U.S. So in case they buy -- if you have projects like we had, then it's productivity-improvement driven, and also the technology integration.

In Europe, however, it's not nearly as penetrated. Actually, the UK was the first market to move towards that technology. France followed afterwards. We have heard from one customer who has moved in Germany. And hey, usually, if that starts, others will follow, and still apply the same pricing methods -- namely, a pricing method which is based on the so-called dimensional weight. So you take weight information and volume information.

Now this is -- you know, the big carriers and their hubs -- now of course you can take this then a step further into a market segment which we call the warehouse and shipping market. And that part of the market, frankly, is not developed at all yet. And we are just launching for that part of the market new product which then -- typical manufacturing companies produce the warehouse and shipping applications. The desire of everybody is to capture those data as early as possible, and in that sense, of course, there could be a significant opportunity also in the part of the market.

Darryl Pardi Merrill Lynch - Analyst

What do you think the size of that opportunity is relative to ground shipping?

Robert Sperry Mettler-Toledo - Chairman, President, CEO

I think that opportunity is probably three or four times larger than the existing opportunity. It takes still, of course, time to develop it. And you should not think that it's just going to happen at once. I think that will be a gradual process.

Darryl Pardi Merrill Lynch - Analyst

Okay. Bill, now that you have got or will have significant cash balance in the U.S., could we expect to see an acceleration of the share repurchase program?

Bill Donnelly Mettler-Toledo - CFO

That's not currently our intention. We would expect that just because of the way our cash flow pattern is during the year, as well -- Q1 is usually one of the lighter quarters cash flow wise. And we do have -- it's a grossed-up position, right? So we have debt balances in Europe and cash balances in the United States. So at this point, anyway, we're not planning any dramatic acceleration.

Darryl Pardi Merrill Lynch - Analyst

Does it make sense to deploy that cash, though?

Bill Donnelly Mettler-Toledo - CFO

I understand the logic. At the same time, in terms of our debt balances over in Europe, it will cause us to borrow more money -- incrementally more money in Europe as well then. The first quarter is not a strong cash flow quarter for us, so the idea of reaching in and borrowing a little bit more and redeploying it on -- you're redeploying the cash balance out in the United States. I'm not sure if that's maybe consistent with how we run the program. And also, I'd guess, there's a certain assumption that we have about cash flow throughout the year, and this idea of kind of the gradual repurchases over time. I think we're not trying to, let's say, make accelerated buyback under the plan. It's more kind of a gradual return of cash flow to shareholders, leaving room in the balance sheet for acquisitions.

Darryl Pardi Merrill Lynch - Analyst

Okay. Last question on -- the inventory turns just continue to improve. And you've added about a half turn since the beginning of '04. And I'm just curious for -- if you can give us some sense on how far you think you can continue to improve that?



Bill Donnelly *Mettler-Toledo - CFO*

I think if you go out, let's say, three to five years, we'd like to think we could get it to six.

Operator

Sara Michelmore, S.G. Cowen.

Sara Michelmore *S.G. Cowen - Analyst*

I am sorry if I missed this, but Bill, I was hoping you could talk about your organic revenue growth assumption of 5% in 2006 and the underlying assumptions there in terms of the product lines, as well as the geographies since things have bounced around so much this year?

Bill Donnelly *Mettler-Toledo - CFO*

Sure. In terms of -- let's start maybe with the businesses. In terms of our lab business, we are thinking of a growth rate in, let's say, 5 to 6% kind of a range. On the industrial business, because we're going to have the -- maybe some difficult comparisons with the T&L business. And we're not so sure that one -- maybe we have a little bit more caution about, let's say, infrastructure projects around the world, we are assuming more in the 4 to 5% kind of range. And in the retail one, there's always more variability in that. But we are currently assuming for budgeting purposes between 4 and 8%.

Then maybe thinking about it geographically -- we're assuming we can get around 10% growth or so coming out of Asia/Rest of World. And let's say 3 to 5% growth coming out of both Europe and the Americas.

Sara Michelmore *S.G. Cowen - Analyst*

Okay. That's very helpful. And could you just -- do you happen to have the share count at the end of the quarter as opposed the average over the quarter?

Bill Donnelly *Mettler-Toledo - CFO*

Sure. At the end of the quarter, it was 42.7 million.

Operator

David Katekian (ph), JPMorgan.

David Katekian *JPMorgan - Analyst*

I have a question on the FAS charges. You guys are anticipating \$0.16 over the 2006 year. And do you guys have any idea on timing for that -- sort of when they may fall into --

Bill Donnelly *Mettler-Toledo - CFO*

I apologize -- you broke up a little bit. You were asking about 123R?

David Katekian *JPMorgan - Analyst*

Yes, you guys --

Bill Donnelly *Mettler-Toledo - CFO*

It should come ratably over the year.

David Katekian *JPMorgan - Analyst*

Okay, so there's no sort of upfront more in 1Q or anything like that?

Bill Donnelly *Mettler-Toledo - CFO*

No, I did hear -- again, you were breaking up -- the current estimate is about \$0.13 per share. I thought you might have 16. So I just want to correct that if it was -- unless I misheard.



David Katekian JPMorgan - Analyst

Okay. Can you hear me better now or --?

Bill Donnelly Mettler-Toledo - CFO

Yes, I can hear you better now. So we're estimating about \$0.13 per share for the full year, and that should happen ratably over the quarter.

David Katekian JPMorgan - Analyst

Got you. Okay. And then, I know you talked a little bit about Europe sort of looking in the 3 to 5% growth range. Can you may be provide a little more color on which segments you think you're going to see more growth out of Europe and sort of your outlook for Europe in general?

Bill Donnelly Mettler-Toledo - CFO

Sure. First, as you heard from our numbers coming out this quarter, we did see improved growth in Europe. We see continued opportunity to penetrate in the lab area and the industrial area. And I would say this very much links to some assumptions about market share gain as a result of our Project Spinnaker. And then, we did assume a positive number for retail in Europe as well. But there's some implied more volatility in that number I think (ph) given the bigger range as well for the full year there. But of course, Europe is a big piece of our retail business.

Operator

(OPERATOR INSTRUCTIONS). Mike Hamilton, RBC Dain Rauscher.

Mike Hamilton RBC Dain Rauscher - Analyst

Good evening. Could you just take a couple of minutes commenting on how you look at project business -- what piece of the total it is, how you price it, whether there's any incremental cost risk to that business?

Bill Donnelly Mettler-Toledo - CFO

Okay, so first of all, maybe when we say project business, it might have a different -- we're not talking -- in the industrial world, it's not like a Fisher Rosemount during a big distributed control system or something where we're doing percentage of completion accounting or something. When we say project, of course, there is some integration elements to it -- and putting it into a customer's site and usually linking with some IP systems. But it's not, let's say, a big risk in terms of -- from an engineering point of view.

Robert Sperry Mettler-Toledo - Chairman, President, CEO

Bill, if I may interrupt here, I just give an example -- let's go to retail. We may have a customer who feels this UC platform we have is great, and it fulfills most of his application needs, those which we have planned to -- built into the product. But he may say, hey, I need another feature which is relevant for my business.

And to give you an example, actually, we have one customer who feels he wants to use the display of the retail sales for cost promotion, but then during the front (ph) of the counter (ph) you buy some meat -- actually, on the display, it would say, when you buy meat, you can have actually a coupon for the buying. So that is what they call cost promotion. They do these programs to sell more at the same time.

Now, what that would mean -- we then need to somehow enhance the system software capabilities. We would do that traditionally with specialized partners. Such a project check can be very well-managed. It starts with the requirements definition. Then of course once we know that, we know the cost. We have a premonitoring system. And of course, timelines -- if he then has to do rollout (ph), we also do first testing in our labs. And we make pilot installations with the customers, and the customer is happy when we go into further rollout.

Hey, with that I just want to tell you this project adaptation are mostly software integration, as Bill mentioned before. And they're kind of -- they build on what we have. And in terms of the risk involved, it's really not significant. Now with that, maybe I want to give it back to you, Bill.



Bill Donnelly Mettler-Toledo - CFO

So I kind of heard maybe in your question -- when you asked that question about pricing, it's still our standard software packages and hardware which still accounts for the largest percentage of the overall price to the customer. So that maybe gives you a feel about risk. And when we use the word project, we are often referring to the fact that the customer is larger in size -- it's an order for, let's say, multiple hubs or multiple stores in retail. And probably, we have in our mind at least \$0.5 million orders is a typical big project. And so hey, I'm kind of now -- did I get most of what you are asking there, Mike?

Mike Hamilton RBC Dain Rauscher - Analyst

Yes, that was very clear. Thanks.

Operator

Scott Wilken (ph), UBS.

Scott Wilken UBS - Analyst

Just following up on the last question, Bill, is there any way you can quantify the dollar impact from the project work, or maybe the onetime sort of order flow so when we're looking at next year, we can think about what that represents in terms of a comparison issue?

Bill Donnelly Mettler-Toledo - CFO

I think if you pulled out the P&L and the retail piece of the business, probably the growth rate in the quarter was, let's say 4.5% or so.

Scott Wilken UBS - Analyst

Okay. So the difference there between the 7 and the 4.5 would be the onetime aspect?

Robert Spoerry Mettler-Toledo - Chairman, President, CEO

Yes, but we always still have projects.

Bill Donnelly Mettler-Toledo - CFO

We'll have some projects, just maybe the onetime might not be -- just at this quarter, if I just wasn't in that business -- we know that in earlier quarters, for example, retail has been down, as you know. And we have certain assumptions about it over the medium-term. And this was a quarter that it was particularly beneficial. And in other quarters, it's been down.

Robert Spoerry Mettler-Toledo - Chairman, President, CEO

Probably, if you look at year to date, you get a couple (ph) capacity (ph).

Scott Wilken UBS - Analyst

Okay. That's helpful. And then just looking at free cash flow -- if I'm doing my math right, I think trailing 12 months is something like 155 million. I know you had some timing issues in the fourth quarter last year. So could you maybe talk about -- is 155 million, sort of the right range for the year in terms of free cash flow? Or is there going to be some more onetime issues?

Bill Donnelly Mettler-Toledo - CFO

Just to make sure -- you're saying on a trailing 12 months, you got to 155?

Scott Wilken UBS - Analyst

154. Yes

Bill Donnelly Mettler-Toledo - CFO

154 -- so, hey, I think we're looking at a Q4 that's comparable to the prior year. Actually, it could be up. So at least the way you're calculating, I probably have a somewhat different number in mind on a trailing 12 months, and that's why maybe I'm off, but --



Scott Wilken UBS - Analyst

So you're saying, Bill, that the fourth quarter will be similar this year to last year?

Bill Donnelly Mettler-Toledo - CFO

Fourth quarter will be similar to the prior year.

Scott Wilken UBS - Analyst

So that would be more like 170 something. Does that sound right?

Bill Donnelly Mettler-Toledo - CFO

Actually, no, I -- but maybe we're calculating it slightly different.

Scott Wilken UBS - Analyst

Okay. The way you would calculate it, what would you come up with?

Bill Donnelly Mettler-Toledo - CFO

I think it has got to be in the 140-ish range. It's about -- we're going to have free cash flow about flat year-on-year.

Scott Wilken UBS - Analyst

Okay. And then the new facility -- the \$10 million for that; will that be spent in '06?

Bill Donnelly Mettler-Toledo - CFO

(multiple speakers)

Robert Sperry Mettler-Toledo - Chairman, President, CEO

A good part will be 2006; some, 2007.

Scott Wilken UBS - Analyst

Okay, so we can think about the CapEx requirements being at least 10 million higher next year?

Robert Sperry Mettler-Toledo - Chairman, President, CEO

Not that much.

Bill Donnelly Mettler-Toledo - CFO

We'll try to cut back in other pieces of the business. But it should go up between five and 10 million.

Scott Wilken UBS - Analyst

And then just last question on the share count -- I didn't quite hear what you said in terms of finishing out the year in terms of share repurchase. Could you just reiterate that?

Bill Donnelly Mettler-Toledo - CFO

In the fourth quarter, we would expect to purchase between 40 and 45 million shares -- a dollar's (ph) worth of shares.

Operator

Paul Knight, Thomas Weisel Partners.

J.P. Jaketin Thomas Weisel Partners - Analyst

This is J.P. Jaketin (ph) in for Paul Knight. I wanted to apologize, because I jumped in on the call a little late if you had already gotten to some of these questions. But I wanted to talk about the tax rate for the third quarter. What exactly -- what was that figure?



Bill Donnelly Mettler-Toledo - CFO

So we had these two somewhat offsetting nonrecurring items. If you exclude those two items, it was 30%. And then the other two items were 13 million -- about.

J.P. Jaketin Thomas Weisel Partners - Analyst

And then like (multiple speakers) the 7.7 (ph) million, right? Okay. Great, thanks. And then how is the acquisition pipeline looking for you guys?

Robert Spoerry Mettler-Toledo - Chairman, President, CEO

As usual, we work on of course acquisition opportunities. We are, as I mentioned many, many times, very careful in stepping through an acquisition. The screening will be a strategic fit. Can we operationally absorb it and manage it? And last, but not least, will it make financial -- is it financially sound?

Of course, we announce these acquisitions when they're ready to announce. So I cannot really be specific on anything. I also want to reiterate, and you have seen that with the guidance for next year, we're not dependent on acquisitions. We will have very solid earning growth based on our organic growth. The 5% we have given you translates into 15% EPS growth for next year. At that speaks (ph) on the operating leverage we have. And there is also a quite significant focus in the organization on this organic growth. This organic growth -- we know what we buy, and translates into very handsome profit growth.

J.P. Jaketin Thomas Weisel Partners - Analyst

Great.

Robert Spoerry Mettler-Toledo - Chairman, President, CEO

But that being said, of course, acquisitions will be part of our future, and we will announce them when they're ready to announce.

J.P. Jaketin Thomas Weisel Partners - Analyst

One other question. Could you guys break out the different things like labs, industrials, retail -- in terms of like what proportion of the total net sales they made up?

Bill Donnelly Mettler-Toledo - CFO

Sure. In the quarter, lab was 44%, industrial was 43, and retail was 13.

Operator

Vivek Khanna, Argus Partners.

Vivek Khanna Argus Partners - Analyst

I just wanted to go back to the organic -- the growth rate that -- Bill, that you touched on that some of it was onetime in nature. And just looking at the project orders, are these anticipated, or they just come out of nowhere, and so you're kind of surprised by these large orders for retail, I guess, and in the T&L business?

Bill Donnelly Mettler-Toledo - CFO

We get them every year. But for us to have 14% growth in retail, is better than the corporate average, as they say. But we have medium-term targets that that should be a mid single-digit growth business. But it's got to be more lumpy and more volatile than some of the other businesses. And that's principally due to the mix of large projects at any one point in time. So next year, we're going to have this, let's say, 4 to 8% kind of growth rate in retail. And that will be against the backdrop of the 14% growth rate in this current quarter.

Vivek Khanna Argus Partners - Analyst

And then -- so you said 4 to 6% retail, and what did you say for industrial and lab? Sorry, I missed that.

Bill Donnelly Mettler-Toledo - CFO

Just to be clear, I said to 4 to 8 for retail, with 6 kind of being the median. And then 5 to 6 in lab, and 4 to 5 in industrial.

Vivek Khanna Argus Partners - Analyst

Okay. And then do you mind just telling us how -- in the lab business how you're -- I think you may have said -- how the balances business and then how the analytical instrument business fit in that segment?

Bill Donnelly Mettler-Toledo - CFO

Sure. In the current quarter, we didn't have -- we had low single digit growth in the lab balance business. We had actually double-digit growth in drug discovery. And in the analytical instruments and process analytics, we had kind of mid single-digit growth rates. Pipettes were flat in the quarter, and that's because they were down slightly on the standard shaft products, but actually up in units. That's mostly just the pricing strategy we have currently in the market.

Vivek Khanna Argus Partners - Analyst

Okay, great. Thanks. Nice quarter.

Operator

Gentlemen, ma'am, we have no further questions at this time. Please proceed with your closing remarks.

Robert Spoerry Mettler-Toledo - Chairman, President, CEO

I would like to thank everybody for joining us tonight. You certainly have heard that we're very pleased with the quarter. We hope you're pleased as well. And with that, I want to wish you a very nice evening. Thanks for joining us today. Bye-bye.

Operator

Ladies and gentlemen, thank you for your participation in today's conference. This concludes the presentation. You may now disconnect.

DISCLAIMER

Thomson Reuters reserves the right to make changes to documents, content, or other information on this web site without obligation to notify any person of such changes.

In the conference calls upon which Event Briefs are based, companies may make projections or other forward-looking statements regarding a variety of items. Such forward-looking statements are based upon current expectations and involve risks and uncertainties. Actual results may differ materially from those stated in any forward-looking statement based on a number of important factors and risks, which are more specifically identified in the companies' most recent SEC filings. Although the companies may indicate and believe that the assumptions underlying the forward-looking statements are reasonable, any of the assumptions could prove inaccurate or incorrect and, therefore, there can be no assurance that the results contemplated in the forward-looking statements will be realized.

THE INFORMATION CONTAINED IN EVENT BRIEFS REFLECTS THOMSON REUTERS'S SUBJECTIVE CONDENSED PARAPHRASE OF THE APPLICABLE COMPANY'S CONFERENCE CALL AND THERE MAY BE MATERIAL ERRORS, OMISSIONS, OR INACCURACIES IN THE REPORTING OF THE SUBSTANCE OF THE CONFERENCE CALLS. IN NO WAY DOES THOMSON REUTERS OR THE APPLICABLE COMPANY ASSUME ANY RESPONSIBILITY FOR ANY INVESTMENT OR OTHER DECISIONS MADE BASED UPON THE INFORMATION PROVIDED ON THIS WEB SITE OR IN ANY EVENT BRIEF. USERS ARE ADVISED TO REVIEW THE APPLICABLE COMPANY'S CONFERENCE CALL ITSELF AND THE APPLICABLE COMPANY'S SEC FILINGS BEFORE MAKING ANY INVESTMENT OR OTHER DECISIONS.

©2019 Thomson Reuters. All Rights Reserved.



THOMSON REUTERS

PLACEHOLDER TRANSCRIPT

Q4 2005 Mettler-Toledo International Earnings Conference
Call

EVENT DATE/TIME: FEBRUARY 10, 2006 / 1:00PM GMT



CORPORATE PARTICIPANTS

Mary Finnegan *Mettler-Toledo Intl. - Treasurer, IR*
Robert Spoerry *Mettler-Toledo Intl. - Chairman, President, CEO*
Bill Donnelly *Mettler-Toledo Intl. - CFO*

CONFERENCE CALL PARTICIPANTS

Paul Knight *Thomas Weisel Partners - Analyst*
Jennifer Follis *JPMorgan - Analyst*
Derik De Bruin *UBS - Analyst*
Mike Hamilton *RBC Dain Rauscher - Analyst*
Richard Eastman *Robert W. Baird - Analyst*
Darryl Pardi *Merrill Lynch - Analyst*
Vadit Khanna *Argus Partners - Analyst*
Herb Tanner *Tanner Capital - Analyst*

PRESENTATION

Operator

Good day and welcome, ladies and gentlemen, to the fourth-quarter 2006 Mettler-Toledo International conference call. My name is Audrey and I will be your conference coordinator for today. At this time all participants are in a listen-only mode. We will be facilitating a question-and-answer session towards the end of this conference. (OPERATOR INSTRUCTIONS). As a reminder, ladies and gentlemen, this conference is being recorded for replay purposes. I would now like to turn the presentation over to Ms. Mary Finnegan. Please proceed, Ma'am.

Mary Finnegan *Mettler-Toledo Intl. - Treasurer, IR*

Thanks, Audrey. Good morning, everyone. I am Mary Finnegan, Treasurer and responsible for Investor Relations at Metter-Toledo, and I want to welcome you to the call this morning. I'm joined by Robert Spoerry, our Chairman and CEO, and Bill Donnelly, our Chief Financial Officer. I will start by covering some administrative matters and then turn the call to Robert who will provide you highlights of the quarter. Bill will then cover the financials in detail and Robert will provide commentary on our outlook and business. Of course we'll have time for Q&A at the end.

Now for the administrative matters. First, this call is being webcast and is available for replay on our website. A copy of the press release we issued today is also available on our website. You should be aware that statements on this call which are not historical facts may be considered forward-looking statements for purposes of the Safe Harbor provision under the Private Securities Litigation Reform Act of 1995.

Forward-looking statements involve risks and uncertainties that could cause actual events or results to differ materially from those expressed or implied. For further information concerning issues that could materially affect performance related to forward-looking statements, please refer to our filings with the SEC. We undertake no responsibility to release any revisions to forward-looking statements as a result of subsequent events or developments.

One other item, on today's call we may use non-GAAP financial measures. More detailed information with respect to the use of and differences between the non-GAAP financial measures and the most directly comparable GAAP measures is provided in the press release. I'll now turn the call to Robert.

Robert Spoerry *Mettler-Toledo Intl. - Chairman, President, CEO*

Thanks, Mary. Good morning, everybody. I want to thank you for joining us today on this call. We are very pleased with the strong finish we had in 2005 as evidenced by our Q4 results. Sales growth in local currency was 7% and was driven by robust demand for our laboratory products, continued growth in China and another strong quarter in food retailing. We are very pleased with our gross margin expansion and the solid increase in operating profit recognized in the quarter.

Our EPS growth was again excellent and we are pleased to have achieved a 20% growth in EPS for the full year 2005. Although we



remain cautious on the global economy, with the strong results we had in Q4 we are revising and increasing our targets for this year 2006. We will explain this in more detail later on the call. Let me now turn it over to Bill who will take you through the financial results.

Bill Donnelly *Mettler-Toledo Intl. - CFO*

Thanks, Robert, and good morning, everyone. As Robert mentioned, we had another great quarter of operating performance and ended the year on a strong note. In fact, this is our strongest quarter ever. Earnings per share was \$1.04 versus \$0.81 last year which includes \$0.02 of investigation cost. Excluding this item earnings per share grew 25% in the quarter. EPS for the full year, excluding onetime items in both periods, increased 20%. Our press release contains details on the onetime items.

Now let me go into some additional details starting with sales. Sales in the quarter were 411.2 million, an increase of 7% in local currency. For the first time in quite a while we had a negative currency impact to our sales number reducing growth by 4% which then resulted in sales growth in reported dollars of 3%.

I think it's worth covering in a little detail the impact of currencies to our financials. As you know, it is local currency sales growth which is the most important driver to our operating profit performance. Although we're impacted on the sales line due to the strengthening or weakening of the dollar, because we are relatively naturally hedged, the impact at the operating profit line tends to be negligible.

Another way to explain this is that our non-dollar costs equate to our non-dollar revenues and therefore the currency effects on sales do not fall through to operating profit. Our natural hedge is not perfect by each currency; we do have an exposure between the Swiss franc and the euro. Should the Swiss franc strengthen against the euro that would hurt us, while if it weakens against the euro it helps us. Historically these currencies have traded in a relatively narrow band.

I would expect that the currency will drag on the sales line in 2006, but I'm not expecting anything material at the operating profit level given current levels of the Swiss franc/euro. I realize that I've covered the currency impact in the past, but I thought it was worth going over again now that there is a negative impact to the top line and we may have some new people on the phone today.

Now let me go into more details on sales first by geography and then by business area. All comparisons are versus the fourth quarter of 2004 and all growth is in local currency. I'll start with sales by geographic destination. Sales growth in the Americas was up 12%, one of the strongest rates we've seen in a number of years. Our laboratory and food retailing businesses were the principal drivers of growth this quarter. Growth in laboratory products was broad based with most productlines showing nice growth. While Q4 last year was somewhat lackluster for lab in the Americas, this year's performance was excellent.

Retail was up strong double-digits in the quarter; for the full year we had a growth of 7% in the Americas. Sales growth in Europe was up 2%; our laboratory products had strong growth despite a strong quarter a year ago. Retail had another quarter of double-digit sales growth while our industrial business was down. For the full year sales growth in local currency was 3% in Europe. Sales growth in Asia/Rest of the World increased 9% in local currency; China had another good quarter with 19% sales growth. The other regions also had growth with the exception of Japan which was down. Industrial growth was particularly strong in this region. For the full year local currency growth in Asia was 9%.

Turning from geography to products, let me start with our laboratory products which had their strongest quarter of the year with local currency sales growth of 9% in the quarter which brought us to a 5% growth for the full year. Balances had solid growth in Q4 while analytical instruments were up double-digits. Pipettes increased nicely with our continued expansion overseas; AutoChem had mid single-digit growth; process analytics had a great quarter with double-digit sales growth.

Moving to industrial. Sales in our industrial businesses were up 1% in the quarter and 5% for the full year. For the quarter our standard industrial business was up mid single-digits driven by strong growth in China. Our transport and logistics business was up in the quarter but, unlike Q3, was not a key contributor to the overall industrial growth. Product inspection was down; weak spending by food companies in Europe and the Americas combined with our intro of a new portfolio, product portfolio and transition to new technologies dampened sales in the quarter. We expect to see improved performance in product inspection as 2006 progresses.



Finally, food retailing was up 22% in the quarter. We had strong sales growth in the second half of the year as compared to a weaker first half of the year in food retailing. For the year in total food retailing grew by 8% and, as I mentioned on the last call, we generally expect medium term sales growth for food retailing to be in the 4 to 8% range.

Now let me move down the rest of the P&L. We're pleased with our gross margin level of 50.6% as compared to 49.7% last year. Principal contributors to this gross margin expansion are -- volume, further benefits from cross rationalization programs to reduce overhead as well as procurement and redesign efforts to reduce product costs. We also continued to benefit from realized price increases.

R&D amounted to \$20.8 million or 5.1% of sales. This represents a 1% local currency decline. As mentioned last quarter, we are making a conscious effort to redirect R&D to our Spinnaker initiatives which are aimed at improving our sales growth. Although this was true in the second half of 2005, we have recently identified some additional R&D projects that we're initiating and I expect increased R&D investment in 2006.

SG&A was 118.5 million and was 1% higher than the prior year in dollar terms. In local currency terms it increased by 6% which excludes the impact of the investigation that we had last year. Included in the fourth quarter is increased expense associated with variable comp and costs associated with option exercises. The net sum of these results in adjusting operating income gives us \$68.8 million or 16.7% of sales as compared to \$60.1 million or 15.1% of sales in the prior year. The prior year amounts I noted exclude the investigation related costs. We're very pleased with this 14% operating profit growth and the related margin improvement achieved in the quarter.

Now continuing down the rest of the P&L, amortization was \$2.8 million and interest expense was \$3.6 million. This gave us a net income of \$44.2 million and an earnings per share of \$1.04. This represents a 25% increase over the prior year and excludes the investigation-related costs of the prior year. For the full year earnings per share was \$2.94 which does not include \$0.42 of charges. These charges consist of the onetime \$0.30 charge on the intangible write-offs and legal costs associated with pipette litigation and a \$0.12 charge for nonrecurring tax items associated with earnings repatriation under the American Jobs Creation Act. Excluding the onetime items in both periods earnings per share grew by 20% this year.

Now turning to cash flow, we're pleased with the solid finish to the year and that we exceeded our full-year targets for cash flow. In the quarter net cash from operations was \$59.5 million as compared to \$44.1 million in the previous year. This represents a 10% increase if we exclude from last year's numbers a \$10 million voluntary pension payment. We saw further improvements in DSO which was at 48 days at the end of the year versus 51 at the end of 2004. We also saw steady improvement in IPO which finished the year at 4.9. For the full year net cash from operations was \$177.1 million and free cash flow was \$148 million. We're happy with both of these levels.

Let me cover now our share repurchase program. During the quarter we purchased 1 million shares of stock for a total of \$57.8 million. For the full year we purchased 3.2 million shares or \$164.5 million. Our repurchases in 2005 represent 7% of our outstanding shares. We intend to continue to use our free cash flow for share repurchases as we believe it's an excellent way to return value to shareholders. Our capital structure remains strong. At the end of the quarter we had net debt of \$125.6 million versus a last 12 month EBITDA of 232.7 million which gave us a net debt to EBITDA ratio of 0.5 times.

As I mentioned on the last call, we closed a new bank facility in the quarter which provides for \$450 million of capacity over the next five years. With our strong balance sheet and excellent cash flow generation we have ample financial flexibility to repurchase shares as well as to pursue acquisitions.

Let me now update you on our guidance for 2006. We continue to feel positive but are realistic that there are reasons to be cautious on the economy including the impact of rising oil prices and the sustainability of the European recovery. We will closely monitor the economy and adjust our plans as necessary. Assuming an economic environment similar to today, we continue to believe that local currency sales growth in the 4 to 6% range is achievable. There may be some variability between the quarters, but we believe a target of 5% is realistic for the year.

We now believe that a 5% local currency sales growth would result in adjusted earnings per share of \$3.30 to \$3.35 for the year. This



compares to earnings per share in the range of \$3.20 to \$3.25 that we communicated after last quarter. In addition to the stronger than expected finish to 2005, we plan to invest a little more in R&D this year than we had expected previously. This spending relates to a number of exciting product opportunities we recently identified which hopefully will provide strong growth for the future. Of course all guidance being provided does not include the impact on our stock-based compensation programs which we will expense this year per the guidelines of FAS 123R. We estimate that the full-year impact of this expense to be \$0.13 for 2006.

Now in terms of the first quarter we expect sales growth to be in the 5 to 5.5% range which would result in an EPS in the range of \$0.54 to \$0.57 per share. At the midpoint of the range that's an 18% growth rate. Again, this range does not include FAS 123R expense which we would estimate at \$0.03 for the first quarter. We will provide additional quarterly guidance on the next call, but I will point out that due to the strong second half of 2005 I would expect EPS growth to be stronger in the first half of 2006 versus the second half. Okay, that's it for my side and I'd now like to turn it back to Robert.

Robert Spoerry Mettler-Toledo Intl. - Chairman, President, CEO

Thanks, Bill. I will start by providing commentary on 2005 and the increased outlook for this year before I discuss our initiatives to drive growth and profitability in 2006. Last year we generated in local currency a sales growth of 5%. As Bill mentioned, we continue to feel comfortable with a similar growth level for what you saw in last year and that is local currency growth in the 4 to 6% range.

In terms of geographic breakdown we would expect growth in Europe and the Americas to be in the 3 to 5% range. In Europe we saw trends to improve during the course of the year and expect these trends to continue. In the Americas we do not expect our transport and logistics and food retailing business to be as strong as in 2005, but expect solid growth in our laboratory products, also our other industrial productlines. In Asia we would expect growth in the 10% range with solid performance across the board.

Let me add some insights by business area. I will start with lab. In 2005 we had solid growth across most of our productlines as a result of the many new products we have launched. We have a number of new product launches again this year and would expect similar customer level investment as we had last year. Overall we expect growth in the 5 to 6% range for the laboratory business, a little better than what we saw last year.

In our industrial instruments we would expect sales growth in the 4 to 5% range. We had unusually high growth in transportation and logistics business in 2005 which we do not expect to repeat, although we do expect solid growth in the other industrial productlines this year. Product inspection growth was more modest in 2005 and with the benefits of the full-year run rate on the numerous new product launches we would expect improved growth in the packaging inspection business in this year. Taken together we would expect similar growth rates for industrial in 2006 as we saw last year.

Finally, in food retailing, this business has a little more volatility than our other businesses. In 2005 we ended the year with 8% sales growth which is at the high-end of the 4 to 8% range we expect from this business. Our strong performance in 2005 was driven by the solid execution of our strategic initiatives. Let me highlight these initiatives which I believe position us for continued growth in 2006 and beyond.

I will begin with Project Spinnaker which is now firmly rooted in our organization. In fact we have seen benefits in our 2005 results. The aim of this initiative is to increase our sales growth rate, enhance sales productivity and gain market share through excellence in sales, service and marketing. Spinnaker's growth rate initiatives with many components. We started to implement in late 2004 and will have new ideas for execution over the coming years.

On the last call I spoke on our progress in segment marketing and regeneration. Today I would like to comment on the area of pricing. It began by analyzing our pricing down to the customer and sales (indiscernible) level. With this additional transparency we identified opportunities to adjust our pricing to find the right balance between volume and price as well as additional opportunities to improve our realized prices by changing certain processes.

The first processes to be changed were to provide our sales force with additional training on value selling. For example, we developed Internet-based tutorials and toolkits to help them better communicate and sell value for our products to the customer. The second



process change is to implement a structured and rigorous process control around discounting. We have rolled out both of these changes to some parts of the organization and we will continue to roll out over the course of the year.

We believe pricing continues to help our gross and margin expansion. We expect more progress also this year. Furthermore, we have raised list prices substantially across all products effective beginning of January. We estimate we will realize a net increase of approximately 1% across the Group. In our laboratory and industrial offering we expect a somewhat higher realization. Our retail business, however, continues to face a challenging pricing environment and our expectation in that business is that we will not realize price increases for this year.

Next I would like to give you an update on service. In 2005 service grew a little less than our product sales. In recent years service has been able to grow faster than product sales and we expect to see continued growth in the years to come. As you know, service is also quite profitable with margins above the product business. With this background of high growth rates and high margins we are implementing a series of initiatives which should help us to capture the opportunities in service.

Now I want to explain how we intend to capture these opportunities. It starts with clearly defining the service products we want to sell. Over the last year we have made a conscious effort to integrate the development of our service products into the product development process. When we launch a new product we want to ensure we are launching also a related service offering. Hand in hand with this approach is the development of marketing brochures and communication documents that articulate the scope and value of our service offering.

These service marketing tools help our salespeople to affectively sell our service offering upfront with the product sales. We clearly recognize that the best time to sell a service contract is at the time of the product sale and we are now better equipped than ever to do this. Also in the service area we are unbundling our calibration offering in order to be more price competitive in the standard maintenance segment.

Calibration has always been a core service offering and customers are now looking for additional calibration services to meet various regulatory and quality standards. As calibration becomes more value added we are separating it from our standard offering in order to more effectively market and price this offering. This also ensures that our standard maintenance offering remains price competitive. In summary, with our global network in which our customers can obtain uniform services throughout the world, we believe we are strongly positioned to capture opportunities in this market.

The third strategic area is the one focused on the emerging markets and our strategies (indiscernible) on China in which we have been operating for 18 years. We had another year of solid growth in 2005 and in 2006 we estimate that China will become our second largest end-user market. We see continued strong growth opportunities as Western customers shift manufacturing to this region and domestic companies grow with the local needs as well as positive opportunities from the exports.

To better accommodate for this growth we are making important organizational changes. Mainly [breaking] up our current Chinese organization into a new marketing organization and a separate producing organization. This is the same organizational concept we have a place in the Americas and in Europe. The marketing organization can focus their initiatives on capturing more opportunities by expanding our regional coverage in China and implementing many of the Spinnaker's proven practices namely in the area of segment marketing and regeneration.

Our producing organization on the other side can further enhance our cost competitiveness, quality orientation also improve our product development efforts. As we mentioned last quarter, we will begin to replace the oldest of our three facilities with an expanded one, nearly doubling the capacity of the existing site. We believe these changes will enhance our already strong market share and further -- and provide us further manufacturing efficiency thus allowing us to continue our excellent track record in this region.

The fourth strategic focus area is the one of technology leadership and in 2005 we continued to reinforce this leadership with a broad range of new offerings, particularly in the balance and product inspection business. We have a solid pipeline as we enter this year as evidenced by the upcoming launch of a high-capacity microbalance that has the ability to weigh with unprecedented accuracy various



types of fine substances or chemicals. There is no comparable product on the market with this type of accuracy and it allows customer to (indiscernible) more samples directly in the container thereby reducing losses and improving productivity without sacrificing accuracy.

Another lab innovation soon to be launched is a high-speed system to calibrate single and multi-channel pipettes, the only compact industry of its kind in the market. 20 times faster than conventional balances for calibration, this instrument and its use of (indiscernible) software speeds up a time-consuming process by allowing the calibration of all channels of a pipette being calibrated at once and guaranteed precision and accuracy of the pipette being assured. Pipette manufacturers, service providers and pharmaceutical and biotech companies can increase productivity, optimize service and minimize support costs and gain more secure results to meet their ISO requirements. These are only two examples of new launches, we have many other introductions in the course of this year and our pipeline is quite strong.

Our fifth strategic initiative is that we're working diligently to improve our cost structure in a sustainable way. On the procurement front we have been able to offset commodity related increases with savings in other areas. We continue to consolidate our supplier base and are increasing sourcing components from low-cost countries. Although our supply chain has great complexity, we have been able to increase our inventory productivity. As you heard from Bill, we had further improvements in our IPO in the fourth quarter and also for the entire year. So this initiative as well as several others we believe we can gain cost efficiency and improve our working capital productivity.

In addition to our strategic initiatives our financial strength gives us excellent position for the future. We believe our sales growth, operating leverage and earnings growth are a big advantage for us. Given that we don't have significant capital requirements our cash flow when combined with our strong balance sheet provides us with excellent ability to repurchase the shares. As Bill stated, during 2005 we repurchased 3.2 million shares or 7% of our outstanding shares. We will continue to use our free cash flow for share repurchases as we believe it's an excellent way to return value to shareholders. Our balance sheet is strong and provides us also with ample capacity for acquisitions.

That is all that I did want to cover with you. And I would like to have the operator to open the line for questions.

QUESTIONS AND ANSWERS

Operator

(OPERATOR INSTRUCTIONS). Paul Knight, Thomas Weisel Partners.

Paul Knight *Thomas Weisel Partners - Analyst*

Hi, Robert. Could you talk about the 12% North America and the 9% Asian growth? Was Japan slow in the quarter or was the U.S. just really good? What's kind of going on with the dynamics of those two markets?

Robert Sperry *Mettler-Toledo Intl. - Chairman, President, CEO*

In the U.S. we had a very good performance in Q4 and in Asia, China had very solid growth. I think, Bill, you need to back me up here, Japan -- Japan was slightly down. But really the main growth in China or the growth in Asia came from China.

Paul Knight *Thomas Weisel Partners - Analyst*

China in total grew 19% in the quarter. What's going on in Japan? You're not the only firm that said Japan was lighter. It is their budget year or what?

Robert Sperry *Mettler-Toledo Intl. - Chairman, President, CEO*

I think some changes were made by how they are spending the money. Typically the fiscal year for many companies ends in March. So you typically have end of March a big spike. Last year, however, the law was changed and so many companies have also changed their spending patterns which leads to a better start into the new year after March, but somehow reduced spending a little later in the year. I think in general Japan is okay in terms of the economy and the overall investments cycle I think is more just a change in the pattern in last year.



Paul Knight *Thomas Weisel Partners - Analyst*

And then lastly, why do think your transportation scale business is going to be slower growth this year than '05?

Robert Spoerry *Mettler-Toledo Intl. - Chairman, President, CEO*

'05 was extraordinarily strong. We had really very, very strong growth driven by some big projects and these projects are just more volatile. You may have one or two more this year and then one or two less next year and that's just the way it is. But the fundamentals are still very solid off of that market.

Paul Knight *Thomas Weisel Partners - Analyst*

Okay, thank you.

Operator

Jennifer [Follis], JPMorgan.

Jennifer Follis *JPMorgan - Analyst*

Good morning. I have two questions actually. The first is in Asia outside of China and Japan if you could give a little more color on how other areas are impacting the business? And secondly, what areas for M&A do you see as good opportunities in 2006?

Bill Donnelly *Mettler-Toledo Intl. - CFO*

Maybe I'll handle the growth in other parts of the world. We would generally look at two main categories -- there would be Southeast Asia, we had nice growth in Southeast Asia both for the quarter and for the year. And then India is another important and growing market for us. We invested a lot in distribution in the fourth quarter and we saw good growth coming out of India.

In terms of -- so those would be the Asian pieces. We also have in the Asia/Rest of World number lumped some of the Eastern European countries and we had good growth in Russia as well as some of the other countries in that area this year.

Robert Spoerry *Mettler-Toledo Intl. - Chairman, President, CEO*

In terms of M&A, adjusting our growth trends, our main area of focus will be for laboratory products, just expanding our product offerings. Then also in process analytics where we will be interested to expand the parameters we offer to the market today (indiscernible) packaging expansion -- packaging inspection. You could also imagine further capabilities for controlling certain quality attributes in packaged goods.

In terms of the acquisition pipeline, maybe also a few comments here. In the last two years we have been really launching this Project Spinnaker with a key objective of maximizing the organic growth. I think we see very good evidence that that program works. In that sense we believe also organic growth is something which provides a fast return for the investment of shareholders and therefore takes a lot of focus for just on the organic growth. That does not mean that we are [excluding] acquisitions for our future -- not at all. But of course it tells us that we are not dependent on acquisitions. We have a very good organic growth already without having to pursue acquisitions.

In terms of current activities, of course, as usual we announce matters when they are ready to be announced.

Jennifer Follis *JPMorgan - Analyst*

Okay. Thank you.

Operator

Derik de Bruin, UBS.



Derik De Bruin UBS - Analyst

Good morning. Good quarter. Mettler's fourth-quarter gross margin tends to be seasonally higher. And certainly the 50.6% margin -- I believe that's a record gross margin for the Company. I guess how can we look at the margin expansion going forward and how much more room is there to go and how do we start looking at the run rate of the Company?

Bill Donnelly Mettler-Toledo Intl. - CFO

First, your analysis is correct because the fourth quarter has just more sales dollars in it. And with the variable contribution on our product business in particular you see always the highest gross margin percentage in the fourth quarter. If you look, we nicely expanded gross margins for the full year and we were pleased with that, just a reminder, about 70 basis points or so over the course of the full year. And we're always targeting trying to reduce on the cost side, so the elements of that are in particular China manufacturing.

If I look out to 2006 and beyond, we are introducing a number of new Chinese manufactured products for (indiscernible) the industrial side for next year and see more opportunity down the road so that will be a plus on the material cost side. As well we continue, as Robert spent some time on the call today, focusing on doing a better and better job on the pricing side and generally we think pricing will be a positive factor for us.

So at this point in time we talk often about this 50 to 100 basis points operating profit margin improvement that we kind of give ourselves as a target for every year. And we continue to think that gross margins will play an important role in that and at this point are kind of looking at our margins and getting scared of them, let me say it this way.

Derik De Bruin UBS - Analyst

Okay. And I guess is there any -- I mean, when you're increasing the R&D in '06, is there any one specific area that is of key interest to you in increasing the focus or is it (inaudible) based?

Robert Sperry Mettler-Toledo Intl. - Chairman, President, CEO

Not being too specific, but this increased R&D spending will be mainly for laboratory products.

Derik De Bruin UBS - Analyst

Okay. Now are you looking at expanding your analytical instrument offering going into other areas -- spectrometry or something like that? Would you consider developing that -- those products or sticking with the Thermo analysis and along those lines?

Robert Sperry Mettler-Toledo Intl. - Chairman, President, CEO

What you have seen in the past, that of course our laboratory product portfolio has grown over the years either through in-house R&D or adding technologies and products through acquisitions. If we enter a new field we always enter it with the objective of coming out a leader in that market and we have seen proof of marketshare correlating to return on sales. So in that sense we are not entering into segments where others are very strong and the market positions are well taken. And maybe some of those productlines you just mentioned before probably are well taken position and it would make much sense for us to try to compete with some of the big guys there.

Derik De Bruin UBS - Analyst

Great, thank you very much.

Operator

Mike Hamilton, RBC Dain Rauscher.

Mike Hamilton RBC Dain Rauscher - Analyst

I would like to follow-up on your thoughts on margin here near term. We go back in the last few years and transition from fourth quarter to first quarter we've obviously got volume but we've obviously had some things in line of cost rationalization, plant moves, etc. How are you feeling on the normalized progression -- make it easy, take that operating margin from fourth quarter to first quarter given what you're looking at?



Bill Donnelly Mettler-Toledo Intl. - CFO

Okay, so we have maybe on the gross profit margin line, if you were to look at the first quarter of last year we had 48.3% and that compares to what we just finished at 51.2%. Or sorry, 50.6%, and so we would expect in the course of 2006 to expand our operating -- or our gross profit margins contributing to the overall operating profit margin in the expansion at least 25 basis points, hopefully a little bit more.

And in the first quarter it would let's say be in that range, although there's -- a little bit depends on the mix of products, I would highlight that. We did finish with some more backlog on the retail side, but if retail comes in about let's say our normal level, somewhere between 4 and 8% I would expect we'd be able to get 25 basis points, hopefully maybe a little more on the gross profit margin line in the first quarter.

Mike Hamilton RBC Dain Rauscher - Analyst

Anything in the last couple quarters that has been unusual in terms of costs? In other words, are you incurring anything on the cleanup of getting facilities moved and related?

Bill Donnelly Mettler-Toledo Intl. - CFO

No, probably the -- in the third quarter we had a higher mix of project industrial business and retail business which probably dampened the margin a little bit. And in the fourth quarter, because we had such a strong margin from laboratory products, that grew up quite well on the gross profit line. If you were to look on the operating profit line, there was certainly -- the way we timed our variable, the way variable comp works or how we record variable comp -- because we had a strong finish to the year the fourth quarter had a disproportionate amount of variable comp expense. And there were some option exercises associated with expiring options and, of course, there are some social costs on those going through the P&L, but those would be the main items, Mike.

Mike Hamilton RBC Dain Rauscher - Analyst

Thanks. Tax rate outlook on '06?

Bill Donnelly Mettler-Toledo Intl. - CFO

At this point in time we see no reason to change what's been our 30% rate recently. But like always, we're trying to do good on the rate or improve the rate but as well focus on cash taxes as well.

Mike Hamilton RBC Dain Rauscher - Analyst

And if anything the Asian growth putting a bias downward on that? On the overall tax rate?

Bill Donnelly Mettler-Toledo Intl. - CFO

Just to maybe be clear with your comment, I think that as China has lower tax rates, you're correct, Mike, today and with China growing in theory that works. We also tend to think that the tax rate in China will grow in the coming year. So there will probably be some offsetting affects there. It will stay lower than the U.S. rate, but we do expect rates to increase in China in the coming years.

Mike Hamilton RBC Dain Rauscher - Analyst

Fair enough. How about CapEx outlook at this stage?

Bill Donnelly Mettler-Toledo Intl. - CFO

We're building a new plant in China, we talked about that a little bit last quarter, so I think we're going to have it grow into the high 30s for this year.

Mike Hamilton RBC Dain Rauscher - Analyst

Thank you very much and congratulations.

Operator

(OPERATOR INSTRUCTIONS). Richard Eastman, Robert W. Baird.



Richard Eastman Robert W. Baird - Analyst

Could you just give a little bit of commentary around the industrial business in Europe in the fourth quarter? Was that a tough comp or one might have expected it to be up a little bit?

Bill Donnelly Mettler-Toledo Intl. - CFO

There are a couple things going on there. So first, maybe I'll cover three pieces. One would be that in a relatively small product sector some standard industrial scales that we sell into like paint companies, that business was down in the fourth quarter. We had some project business on the P&L side that was a difficult comparison in the fourth quarter. And then spending with the food companies, you guys I mean have seen it a lot with Kraft in the United States, but Unilever is going through some similar experiences in Europe in terms of branded products. And on the product inspection piece of the business we saw reduced spending with food companies.

Then while we're really pleased with the new product portfolio on the product inspection side, we introduced a new metal detector, a new check weigher and a couple of new x-ray machines. Sometimes you do get into product portfolio transition issues. We saw that a little bit. And as well we think some customers are kind of contemplating the impact of X-ray on their business. To a certain extent X-ray -- or in certain applications X-ray can do some of the things that metal detectors and check weighers do, particularly metal detectors. And we think some customers are kind of evaluating what that means to them and that's maybe hesitating on some of the spending in addition to the concerns that I already described with that food. Product inspection is about a 70% food market.

Richard Eastman Robert W. Baird - Analyst

Okay. And then would you mind just giving the percentage of sales in the quarter that came from the three business segments?

Bill Donnelly Mettler-Toledo Intl. - CFO

Laboratory was 46%; industrial, that's the base industrial as well as the product inspection was 40%; and retail was 14%.

Richard Eastman Robert W. Baird - Analyst

Okay, excellent. And then last thought -- Bill, could you just help us for one second with how do you see your net interest expense or income number playing out for '06 with the debt and cash position as it was at year-end?

Bill Donnelly Mettler-Toledo Intl. - CFO

Okay. If I look out to the full year and, just a reminder to people, when we implemented the dividend reinvestment act we borrowed in Europe and we're depositing cash that will be used to fund our share repurchase program for the next couple years. And I would estimate an interest expense for 2006 approaching 19 million and other income line, which is principally interest income, in the 5 million, maybe a little bit more area for the full year. And that's -- we built in a little bit the current yield curve there.

Richard Eastman Robert W. Baird - Analyst

Okay. And then -- that'll be fine. Great, thank you.

Operator

Darryl Pardi, Merrill Lynch.

Darryl Pardi Merrill Lynch - Analyst

How much of the revenue growth in Q4 in 2005 was from pricing?

Bill Donnelly Mettler-Toledo Intl. - CFO

We would estimate between 75 and 100 basis points, but I wouldn't back that out to make a pure volume calculation because, of course, there are so many different productlines within the Group.

Darryl Pardi Merrill Lynch - Analyst

Alternatively are you arriving at that saying your net effective price increases across the portfolio were 75 to 100 basis points?



Bill Donnelly Mettler-Toledo Intl. - CFO

Correct. So price increases minus discounts.

Darryl Pardi Merrill Lynch - Analyst

Okay. The laboratory business in North America you mentioned was strong and you mentioned it was strong across the product portfolio. But were there any one or two customer groups that were particularly strong or do you see strength across the served markets?

Robert Spoerry Mettler-Toledo Intl. - Chairman, President, CEO

Both growth rate across the productlines and also the industry segments we serve.

Darryl Pardi Merrill Lynch - Analyst

Okay. China is -- you forecast to be the second-largest market next year. What percentage of sales was it in '05?

Bill Donnelly Mettler-Toledo Intl. - CFO

Just to maybe talk in number terms, it was -- China was for the full year 8%.

Darryl Pardi Merrill Lynch - Analyst

And Germany is about 10, is that correct?

Bill Donnelly Mettler-Toledo Intl. - CFO

Well, Germany is actually -- Germany customers are actually a little bit less. If you look -- if I pull out the impact of the Germany OEMs and what they export out of the country it comes to be a little bit less. I think to get to 10% you have to include German OEMs and their exports around the world.

Darryl Pardi Merrill Lynch - Analyst

Okay.

Bill Donnelly Mettler-Toledo Intl. - CFO

As you know, there are a lot of big German engineering companies.

Darryl Pardi Merrill Lynch - Analyst

And as you enter '06, what percentage of sales are being manufactured in China?

Bill Donnelly Mettler-Toledo Intl. - CFO

It's got to be 18% or so.

Darryl Pardi Merrill Lynch - Analyst

And as you add capacity where do you think that will get to over the next two to three years?

Robert Spoerry Mettler-Toledo Intl. - Chairman, President, CEO

That target building is in facility. We -- industrial and retail products are going to be at capacity. We should have new premises up and running in April '07 and we'll double the capacity for the industrial and retail businesses.

Darryl Pardi Merrill Lynch - Analyst

Okay. I guess an alternative way to ask the question is how quickly do you think you'll fill that capacity?

Robert Spoerry Mettler-Toledo Intl. - Chairman, President, CEO

It's hard to say, but based on past growth we had we believe it's going to be sufficient for the next five to ten years. But it's also building and designing in such a way that it can be easily expanded in case we need it earlier.

Darryl Pardi *Merrill Lynch - Analyst*

Okay, thanks.

Operator

[Vadit Khanna], Argus Partners.

Vadit Khanna *Argus Partners - Analyst*

Good morning. I just had a question on the pricing increases for '06. Are you saying, Robert, that that's pretty similar to what you're seeing in '05 and it's not unusual because of the 1% increase? Or is there something unusual that's allowing you to get this pricing?

Robert Spoerry *Mettler-Toledo Intl. - Chairman, President, CEO*

I think we'll do a little better than in past years. And we said two things -- we have certainly made a much bigger effort to have all the price increases in place by 1st of January this year. And then internally we're doing a better job of the managed discounts of salespeople and discounting behavior. So I think the net realized number is going to be slightly better than in the past.

Vadit Khanna *Argus Partners - Analyst*

Okay. And then I just had a question on the lab business -- the strength in the lab business. Are you seeing that just as an upgrade cycle or is it just new lab construction or what's driving the --?

Robert Spoerry *Mettler-Toledo Intl. - Chairman, President, CEO*

Our business is mainly a replacement business. And I think of the many new products we have is of course always a trigger to the replacement cycle. And we have really an excellent offering of new products on the lab side which, frankly, I hope is also going to help us this year because it always takes a while until you have fully launched a productline and every customer knows about it.

Vadit Khanna *Argus Partners - Analyst*

Right. And then just my last question on Europe. It seemed like a lot of your other peers seemed to have had stronger European results and I'm just wondering if you've seen any improvement as you've gone into '06 or is it pretty similar?

Robert Spoerry *Mettler-Toledo Intl. - Chairman, President, CEO*

Our European improvement I don't think was much different from what it was here in general. Of course we have a few big projects which may -- in P&L for example, 2004 really strong in Q4 and made a difficult comparison. But our European business I think is greatly improving. We have seen an uptick last year and we will continue an uptick this year.

Bill Donnelly *Mettler-Toledo Intl. - CFO*

We're assuming a 3 to 5% growth, we talked about, which would be more than what we achieved this year.

Vadit Khanna *Argus Partners - Analyst*

And that confidence is based on what, Bill? The improvement for '06, is that just because you've seen some order activity or what's causing that?

Robert Spoerry *Mettler-Toledo Intl. - Chairman, President, CEO*

Just quoting activity, lead generation -- these are all indicators.

Bill Donnelly *Mettler-Toledo Intl. - CFO*

New products and various other new initiatives.

Vadit Khanna *Argus Partners - Analyst*

Okay, great. Congratulations on a great quarter.



Robert Spoerry Mettler-Toledo Intl. - Chairman, President, CEO

Thank you very much.

Operator

[Herb Tanner], [Tanner] Capital.

Herb Tanner Tanner Capital - Analyst

Good morning, gentlemen. Bill, thank you for a superb quarter. Could you give us a little more color on Spinnaker as it relates, A, to the increase in lab business and, B, in addition to a cost reduction capability, is it generating leads?

Robert Spoerry Mettler-Toledo Intl. - Chairman, President, CEO

Yes. The primary objective of Project Spinnaker is to improve of the organic growth of the Company. Of course at the end of today I want to be totally transparent. There are many, many things affecting the organic growth of the Company. For example, of course the economy and the industry cycle, but then also new product launches and of course our own sales and marketing program. So if you were to ask me how much Spinnaker -- how much is new product that's going to be a difficult question for me to answer. But there are other ways I can check the effectiveness of Project Spinnaker. And you asked about lead generation.

Lead generation is actually way of year on year. We probably had 40 to 50% more leads last year than the previous year and we want to do the same this year again. But then also maybe to a another part of your question, yes, Spinnaker also has productivity improvement elements. In the past, for example, we (indiscernible) those leads to salespeople. Today, in most market organizations we have several marketing departments which do prequalify leads and so that makes the salespeople use leads in a much more effective way and freeing them up from a lot of calling and letting them have o more time in front of customers.

So there is a lot of good evidence that really Project Spinnaker is working well. And maybe a soft factor which I would not want to underestimate, it aligns all the Company's objectives behind one common target. And it aligns all the (indiscernible) business lines, product lines, market organizations in the very same direction and I think that adds long-term a very tremendous positive benefit for the Company.

Herb Tanner Tanner Capital - Analyst

We're seeing it currently aren't we?

Robert Spoerry Mettler-Toledo Intl. - Chairman, President, CEO

We certainly have seen benefits of that in 2005. Spinnaker, as I have said many times in the past, is also [churning]. We are working on selected topics at this point in time, but we have an inventory of ideas which we will activate at the right point in time, mainly once we are really (indiscernible) of those first ideas and it's time to move on to the next one. But we of course want to do this in a very controlled manner.

Herb Tanner Tanner Capital - Analyst

Thank you very much and continued good fortune. I appreciate it.

Operator

This does conclude our Q&A session. I would now like to turn it over to Mettler-Toledo's managers for closing remarks.

Robert Spoerry Mettler-Toledo Intl. - Chairman, President, CEO

I'd like to thank you again for joining us this morning. As you certainly feel from our comments, we are very pleased with our performance in the fourth quarter and also the entire year 2005. I think we have a realistic outlook for the coming year, we are cautiously optimistic on the markets and we believe that we can continue to grow the Company.

Our foundation for the future continues to be rooted in the hallmarks of our franchise, a franchise which can be described by market leadership, global presence, a diversified customer base and also product portfolio, leading technology and the culture of delivering the



highest quality products and services around the globe. I think with continued focus on execution we will be well-positioned for growth this year and beyond in the future. Again, thanks a lot for joining us this morning and we wish you a very pleasant day. Bye, everybody.

Operator

Ladies and gentlemen, this does conclude your presentation. At this time you may disconnect and have a wonderful day.

DISCLAIMER

Thomson Reuters reserves the right to make changes to documents, content, or other information on this web site without obligation to notify any person of such changes.

In the conference calls upon which Event Briefs are based, companies may make projections or other forward-looking statements regarding a variety of items. Such forward-looking statements are based upon current expectations and involve risks and uncertainties. Actual results may differ materially from those stated in any forward-looking statement based on a number of important factors and risks, which are more specifically identified in the companies' most recent SEC filings. Although the companies may indicate and believe that the assumptions underlying the forward-looking statements are reasonable, any of the assumptions could prove inaccurate or incorrect and, therefore, there can be no assurance that the results contemplated in the forward-looking statements will be realized.

THE INFORMATION CONTAINED IN EVENT BRIEFS REFLECTS THOMSON REUTERS'S SUBJECTIVE CONDENSED PARAPHRASE OF THE APPLICABLE COMPANY'S CONFERENCE CALL AND THERE MAY BE MATERIAL ERRORS, OMISSIONS, OR INACCURACIES IN THE REPORTING OF THE SUBSTANCE OF THE CONFERENCE CALLS. IN NO WAY DOES THOMSON REUTERS OR THE APPLICABLE COMPANY ASSUME ANY RESPONSIBILITY FOR ANY INVESTMENT OR OTHER DECISIONS MADE BASED UPON THE INFORMATION PROVIDED ON THIS WEB SITE OR IN ANY EVENT BRIEF. USERS ARE ADVISED TO REVIEW THE APPLICABLE COMPANY'S CONFERENCE CALL ITSELF AND THE APPLICABLE COMPANY'S SEC FILINGS BEFORE MAKING ANY INVESTMENT OR OTHER DECISIONS.

©2019 Thomson Reuters. All Rights Reserved.

