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XRAY - Q4 2013 Dentsply International Inc Earnings Conference Call

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OVERVIEW:

XRAY reported 4Q13 reported net income attributable to Co. of $74.4m or $0.51 per diluted share. Expects 2014 adjusted diluted EPS to be $2.45-2.55.

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PRESENTATION

Operator

Good day and welcome to the DENTSPLY International fourth-quarter year-end 2013 earnings conference. Today's conference is being recorded. At this time I would like to turn the conference over to Mr. Derek Leckow, Vice President of Investor Relations. Sir, you may now begin.

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

Thank you, Lisa, good morning, everyone. Thank you for joining us to discuss DENTSPLY International's fourth-quarter and fiscal 2013 results. I'm here with Bret Wise, Chairman and CEO; Chris Clark, President and CFO; and Jim Mosch, Executive Vice President and COO. we will have some prepared remarks and then we have allocated the balance of our time for your questions.

I hope you had a chance to review our press release issued earlier this morning. I would like to point out that a copy of the release and a set of supplemental slides and the Regulation G information relating to any non-GAAP financials are available for download in the Investor Relations section of our website, www.DENTSPLY.com, under the heading Events and Presentations.

I would like to remind everyone that the Safe Harbor language and US GAAP reconciliation contained in today's press release also pertains to this conference call. We may make forward-looking statements involving risks and uncertainties; these should be considered in conjunction with the risk factors and uncertainties that are described in the release and in our SEC filings.

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

A recording of this call in its entirety will be available on our website. With that I would now like to turn the call over to Bret Wise. Bret.

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

Thank you, Derek. Good morning, everyone, thanks for joining us here on our year-end call. As Derek noted, I have some opening comments about the market and our performance, then I'm going to turn the call over to Jim for an update on operational topics and then Chris will provide a deeper dive on the results.

I would like to begin by putting some context around overall performance for 2013. We came into the year expecting, or hoping perhaps, that the global dental market would continue to accelerate as we moved through the year.

At the same time we had several key areas that we needed to execute including numerous new product launches to come out in the year, completing the sales and marketing integration of our implant business and continuing the recovery of our orthodontics business.

As the year progressed it became clear that the market acceleration that we had expected or hoped for would not materialize, particularly in Europe, and this created a barrier to hitting our growth goals for the year. Despite this we are pleased with our ability to execute on operating margin expansion, again, overcoming the slow sales environment and Europe, we had some major headwinds from currency in that regard and also the Medical Device Tax that was implemented in the US.

On the implant integration, we completed the combination of the marketing units as planned, but really encountered much more disruption than anticipated in Germany. And in orthodontics our recovery progressed in what has become a very competitive and in many ways a disruptive market.

All told, we accomplished several key goals last year including growing cash flow generation, but we fell short of our initial growth objectives at the start of the year.

On our actual results we finished the year at just under $3 billion in revenue, growth was lower than our long-term trend line due in part to the slow condition I mentioned in Europe, but also due to the Company specific matters that I also alluded to a moment ago.

Growth ex PM came in at a positive 2.1% for the year and that is comprised of constant currency growth at 2% with the currency translation essentially being unchanged on a net basis across all our countries. Internal growth for 2013 was a positive 1.9%, that was comprised of positive growth in each of our geographic regions. The highest in the US at a positive 3.8%, while Europe was positive 0.2% and rest of world came in at positive 2.7%.

On this 2.1% top-line growth we had adjusted earnings per share growth of a positive 5.9%, that is on stable to slightly improving operating margins. And again, that overcame the slower growth and the headwinds we had in Europe. This 5.9% earnings gain came on top of a 9.4% gain in 2012.

Shifting to the fourth quarter, total growth ex PM was a positive 1.5% with our internal growth positive 0.8% and constant currency growth was a positive 1.1% and that is against a pretty difficult comp of internal growth last year and the fourth quarter of a positive 5.9%.

In the US we had internal growth of 2.5%, up against a 5.9%, in the prior year and in rest of world we had internal growth of 2.5% against a 12.1% comp in the fourth quarter 2012.

Europe had a negative 1.1% internal growth in the quarter, but absent the German implant business where we had a -- we had a tough comp because we were coming up against a pre-integration period Last year. So absent the German implant business the European business was up low-single-digits.

On the 1.5% top-line growth in the quarter adjusted EPS was up 9%, and that is on top of a 10% gain last year in the fourth quarter. There are several moving parts in the quarter and Chris is going to cover those in more detail. But overall I think this was a good earnings outcome even after considering a lower tax rate, which mostly offset currency headwinds and, again, Chris will give you more of those details.

On market conditions, the US market at retail was probably growing low single digits in Q4, while we believe Europe was down slightly. In the use our expectation is that economic growth should continue to accelerate in 2014 and the dental market should also pick up, probably in the range of about 100 basis points normalized for the impacts in the baseline for the device tax in the US.

I would like to add that we have seen some weakness in the US early in 2014, which may be attributable to some pretty severe weather in the Midwest and the East Coast. And of course we hope that will level out over the coming months or over the first half of the year.

In Europe there are some interesting data points including some stability or even growth late in 2013 in the southern countries of Europe which of course is an encouraging sign and one that we haven't seen for some time. Overall we are expecting dental markets to accelerate in the EU also by about 100 basis points or perhaps a little bit more in 2014.

In the rest of world territories for us currency weakness is a major barrier present with numerous markets in those categories suffering material currency devaluations versus the US dollar, the euro and the Swiss currency. As our rest of world territories are generally important markets we view this as a risk and thus we're not expecting any significant acceleration in these markets overall in 2014.

Our building blocks for 2014 take these market conditions into account, but also a pretty solid innovation pipeline that we have coming into the year and of course an improved capital structure over what we had a year ago. We are also very focused on improving the operating leverage of our business and generating operating margin expansion, improved as it turns and cash flow.

Likewise we are also mindful of the headwinds we face from currency and tax for the next year. Based on these factors in the aggregate we are targeting adjusted earnings in the range of $2.45 to $2.55 per diluted share for 2014 and we view this as a reasonable expectation given the points I have noted here. I would like to now turn the call over to Jim for an update on some of our operational matters including the innovation pipeline. Jim.

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

Thank you, Bret. I would like to comment on a few operational items and then turn it over to Chris for the financial review. Overall our primary objectives and operations have been on scientific research and in combination with strong clinical evidence which supports our commercialization of innovation. Ultimately this drives better patient outcomes and clinical efficiency.

In 2013 we made good progress on this objective and I'm confident our pipeline will drive continued commercial success in 2014. Close secondary objective has been on improving our operating platform to allow for margin expansion even in slower growth environments. I have a few brief comments on both of these areas.

Overall the businesses have been focusing on commercializing some key internally developed innovations; innovations in the chair science consumable category with new composite products such as TPH Spectra is gaining market share in the large composite category. With two new innovations in this area, SDR, which is a bulk flow restorative, and now TPH Spectra, we have a competitive portfolio with clear procedural advantages.

In other restorative categories we launched Aquasil Ultra Cordless in Q4; we are gaining momentum in this new category, which simplifies the restorative procedure by eliminating the use of a retraction cord. We also entered the large and growing fluoride varnish category by launching both a white and clear varnish solution and went from absent in the space to strong number three share position in one year.

Outside of our internal development we did complete a small transaction to support our consumables business in late 2013 with the acquisition of Triodent and New Zealand-based manufacturer of a line and restorative dental consumables. Triodent is known for its innovative and patented sectional matrix system which has been well accepted by clinicians globally and it is very complementary to procedures involving key restorative products such as our SDR.

Success in the dental specialty segment is also heavily dependent on innovation. And I am pleased with our pipeline. Recent examples include the continued success of our endodontics portfolio providing comprehensive state-of-the-art solutions for root canal therapy. Over the past three years we have changed the game in this specialty with newly introduced reciprocating file systems, WaveOne and Reciproc which alter the potential of one file endodontics.

These solutions combined with GuttaCore a non-carrier-based [Thermafilling] material providing superior [operation] and greatly enhances the ease and efficiency of endodontics. In addition, last year when we introduced ProTaper Next, the next generation in Rotary endodontics providing superior flexibility, improved cleaning and shaping and a unique patented swaggering motion which ensures that the file maintains root canal integrity.

Clinicians can feel this difference with a vial and we're having good commercial success and positive feedback from leading global opinion leaders. These are just a few quick examples of innovation in our pipeline. Overall I feel good about our forward-looking pipeline and our ability to bring innovation to the marketplace in each of our product portfolios.

In regards to our implant business, we are now two years plus for the acquisition, and with the last of 19 subsidiaries fully integrated in early 2013, the integration from a high level is complete. Our focus has now turned to business effectiveness, new product development, executing our market strategy and continuing to drive synergies.

We have executed well on our synergies despite market-related headwinds. We have made good progress with (inaudible) in-sourcing of ASTRA TECH implants. We are on schedule and completed 50% of our in-sourcing in 2013 and expect to complete 90% of our in sourcing plan by the end of 2014. Overall I think we've make good progress in positioning the business for strong earnings leverage as the market and volumes recover and begin to grow.

Lastly, I would like to add that we have been focused on how to better leverage our cost structure so that we can expand operating margins even in a lower growth environment. This has included leveraging manufacturing assets as well as maximizing the leverage of our related overhead structure.

We were pleased to see operating margin expansion in 2013 despite the slow environment in Europe and the implementation of the Medical Device Tax in the US. Our early success in this effort is encouraging and I see room for meaningful improvement going forward. With that I would like to turn it over to Chris Clark. Chris.

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

Thank you, Jim, and good morning, everyone. I would like to provide some detail on both our fourth-quarter and also our full-year results by reviewing key elements of our income statement and also providing some additional color on both the balance sheet and cash flow.

For the fourth quarter sales excluding precious metals grew 1.5% compared to prior year including 80 basis points of internal growth, 30 basis points benefit from recent acquisitions and favorable currency translation of 40 basis points.

Gross profit rate on an adjusted basis in the fourth quarter was 56.5% of sales, excluding precious metals, which was an improvement of 20 basis points versus prior year despite the negative headwind of between 40 and 50 basis points from the Medical Device Excise Tax in the US, as we had mentioned previously.

SG&A expenses on an adjusted basis were 39.3% of sales excluding precious metals in the quarter, identical to our rate in the fourth quarter 2012. Operating margin for the quarter improved by 10 basis points to 17.2% of sales excluding precious metals on an adjusted basis compared to 17.1% in the fourth quarter last year reflecting the gross margin and SG&A impacts I just described.

Overall we are pleased to deliver some operating margin expansion in a low growth environment despite the headwind we faced from currency and to a lesser extent the Medical Device Tax.

Currency represented a significant headwind to earnings in the quarter of slightly over $0.03 per share due largely to the significant weakening of the currencies in Canada, Russia, Australia, Latin America and the Asia-Pacific region. As those currencies weaken our cost of products in local currencies rises creating gross profit headwinds as we import goods into these markets from the US and from Europe.

Our reported tax rate for the quarter was 14.3% while our operating tax rate was 20.8% in the quarter, which represented a 130 basis point improvement compared to our average rate for the first three quarters of the year and a 350 basis point improvement over the operating rate in the fourth quarter of 2012. Or about a $0.03 per share impact. This improvement in rate basically offset the currency headwind we experienced in operating income that I previously mentioned.

Net income attributable to DENTSPLY International on an as reported basis in the fourth quarter was $74.4 million or $0.51 per diluted share compared to $126.8 million or $0.88 per diluted share in the fourth quarter of 2012. These results include a number of items which we have listed in schedules in the release, including an exceptionally large one-time tax benefit in 2012.

On an adjusted basis net earnings grew to $87.9 million from $81.4 million in the prior year quarter and adjusted diluted EPS grew 9% to $0.61 per diluted share. Of course this 9% EPS growth rate includes the offsetting impacts of currency taxes as I described earlier.

Transitioning out to the full-year 2013, sales excluding precious metals grew by 2.1% compared to prior year, including 1.9% internal growth and a 10 basis points tailwind from both acquisition and currency translation. As Bret indicated, our US internal growth for the year was 3.8% which we believe to be stronger than underlying market growth.

European internal growth was positive 0.2% in a flat to down market while internal growth in the rest of world regions was 2.7%. Internal growth within the developed countries in this region was flat for the year in aggregate and, on the other hand, our global internal growth rate for emerging markets was mid to upper single digits for the year. For the year the US comprised 34% of our global sales while Europe represented 45% and the rest of world region 21%.

Gross profit on an adjusted basis for 2013 was 57.4% of sales excluding precious metals, which was a decline of 50 basis points versus last year's 57.9%. Again, we estimate the negative headwind of approximately 40 to 50 basis points from Medical Device Excise Tax in the US.

SG&A expenses on an adjusted basis 39.8% of sales excluding precious metals, that is an improvement of 70 basis points compared to last year's 40.5% and reflects the impact of our cost reduction and integration efforts.

You will notice that restructuring and other costs totaled $13 million for the year and including just over $8 million for the fourth quarter primarily for investments we've made to realize these synergies and efficiencies.

Operating margin for the improved by 10 basis points to 17.6% of sales excluding precious metals on an adjusted basis compared to 17.5% last year. And again, in delivering this modest improvement we had overcome both the currency issues and the Medical Device Tax, so we're generally pretty pleased with operating leverage in the business that is generating under really slower than ideal market growth conditions.

Net income attributable to DENTSPLY International on and as reported basis for 2013 was $313.2 million, or $2.16 per diluted share compared to $314.2 million or $2.18 per diluted share in 2012. These results also include a number of items which we've listed in the schedules in the release including the exceptionally large one-time tax benefit in 2012 that I mentioned earlier.

On an adjusted basis net earnings grew to $341.2 million from $319.2 million in 2012. And adjusted earnings per share grew 6% to $2.35 per diluted share from $2.22 per diluted share in 2012. Our results for the year include a negative impact from currency of between $0.05 and $0.06 per share due to the factors I described earlier. This was offset by favorability in our operating tax rate in 2013. We see some upward pressure on our tax rate going into 2014 which I will discuss in a moment.

Moving on to cash flow, our operating cash flow for the year was a record $417.8 million, that is up 13% from $369.7 million last year. And this improvement largely reflects latent cash and tax benefits associated with recent acquisitions.

Our cash flow performance allowed us to take a more balanced approach to capital deployment as we move through the year including reducing our net debt to capital ratio from 39% at the beginning of the year and 51% immediately following the ASTRA TECH acquisition in August 2011 to 35.2% as of December 2013.

In addition we announced the acquisitions of the Triodent and QAHR businesses in November and finally we were also increasingly active in repurchasing shares to offset dilution from equity plans and we repurchased just under 1 million shares in the fourth quarter at an average cost of $47.65 per share. For the full year the Company repurchased approximately 2.7 million shares.

Inventory's now stand at 114 days which is down five days compared to September and up eight days compared to December 2012. As we mentioned previously, have strategically increased inventory in a few businesses as part of transition plans associated with anticipating operating changes.

We anticipate inventory may continue to increase slightly through midyear to support these efforts before returning to more normal levels as we move through 2014 and 2015.

Accounts receivable days were 56 days at the end of December, down eight days from prior quarter and up three days compared to December 2012. Capital expenditures for the year totaled $100 million for the quarter, consistent with our most recent projections. Depreciation was $82 million for the year while amortization was $46 million.

Finally as Bret stated, we are establishing our 2014 earnings per share guidance at $2.45 to $2.55 on an adjusted basis. Our guidance reflects the impact of the incremental currency headwind of approximately $0.04 per share, largely due to the weakening of the second-tier currencies I mentioned earlier.

In addition, we currently anticipated an operating tax rate for 2014 that will be in the range of 22.5% to 23% which represent an earnings headwind of up to $0.05 per share compared to our 2013 rate of 21.7%. There may be some opportunity to improve on this as we move through the year so we will have to see.

Our guidance reflects the anticipated impact of both of these items as well as our assessment of continued above market performance and a modest strengthening of market conditions. That completes our prepared remarks. We appreciate your support and we would be now glad to answer any questions you might have.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions). Jeff Johnson, Robert Baird.

Jeff Johnson - *Robert W. Baird - Analyst*

Wanted to start first just on a couple of your specialty businesses, in endodontics and implants if you could at all give me any insight. Kind of where you expect share to go this year? I think we feel like those markets could grow low- to mid-single-digits this year, but where do you think your share specifically in those two markets could go this year?

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

Well, I'm going to answer that in part and then I am going to ask Jim to talk about maybe some technology that we have in the market or coming. I think that in 2013 it was a pretty disruptive year for our implant business. We did complete the integration in the largest country for that business, which was Germany, but also Japan.

I think the business is now very focused on creating a kind of competitive advantage that it needs to and, thus, I am hopeful we can start to grow share their again as well.

On other things in the specialty business without orthodontics which is still in a recovery mode, you know we've recovered some of the lost share that we had following the disruption in Japan but I think I have commented earlier in the year in several cases that is a very competitive market right now with us trying to elbow our way back in and the competitors trying to defend their market share. I think that we will continue to take some market share back in that category, it is just a question of how fast we can take it back.

In endodontics, that is a business that is very much driven by innovation. We've brought out some kind of game-changing innovation over the past few years that have allowed us to grow share in that marketplace, and we have got some pretty interesting things in the pipeline. So that is a market I think we continue to have some competitive advantage.

Jim, do you have anything to add on those?

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

Yes, absolutely. Jeff, I think from a standpoint of the implant business as we have mentioned, we are now eclipsing two years. And I think what has probably happened more than anything is this business has really stabilized and moved beyond the integration. And we can just see the activity level and the focus and the competency at our field level, really around the world. And I think that is really proving that I think our business strategy is sound and this organization is performing at a much better level.

At the same point in time, we have done some things from the standpoint of how we've improved that business model. We have done some consolidation of our ES Healthcare and our materialized dental business into ATLANTIS. Those products are now -- you are able to order those via ATLANTIS Web order, at least the ES products. We are manufacturing bars and bridges at ATLANTIS, and we are integrating the implant Guided Surgery products with the ATLANTIS products.

So we are seeing some real opportunities to offer a lot of value to our customers. And we believe that this, along with some product innovations in the implant area, will really help us to move forward.

As it relates to Endo, as Bret said, we have launched a lot of new products over the last couple years; products like WaveOne, Reciproc, ProTaper Next. And I think what I would emphasize about these products versus traditional products is that what they really do is they simplify and expedite the endodontic procedure. They reduce the number of files used. They allow the clinician to get a high-quality result in less time. And those have been extremely well received in the marketplace.

And even though we have had successes in those launches in the last year, we continue to see share gains as a result.

Jeff Johnson - *Robert W. Baird - Analyst*

Great, that is helpful. Thanks, Jim. And, Bret I guess one last question for you just from a high level. It has been a few years since we've seen any kind of double digit EPS growth out of you guys. It sounds like now in 2014 tax and currency will probably create a little more impact than I think any of us were expecting.

But where do you think fundamentally dental markets can get to back to -- maybe 3% to 5% growth -- knowing where you are at in your different business lines and all of that. What do you think fundamentally is your longer-term EPS growth potential as we cycle through maybe some of these macro issues and what have you?

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

Well, I think the fundamentals about the dental market and the competitive position that we have has not really changed. Meaning if we can see these markets from return to kind of pre-recession levels, let's, call it 4% to 6% growth for the marketplaces, and our business model is in really good shape to get the kind of operating leverage that we have historically gotten.

So I think -- and you throw on top of that some earnings gains from redeploying the cash that we generate, I think those kind of earnings gains long-term are clearly possible and of course in those environments we would be striving to hit those.

In the current environment we have a US market that is growing low-single-digits, we have a European market that is probably -- I mean realistically it is probably still flat. We are kind of expecting that both the US and the European markets are going to accelerate by about 100 basis points, maybe a little bit more in Europe this year.

Although even with those accelerations that is not back to the longer-term trend line. So we are pleased that even in a tough environment this year with currency headwinds, device tax, this, that and the other thing we still grew operating margin a little bit.

I think we have been working very hard to get a cost structure in place that will allow us to have the kind of earnings leverage that maybe we saw historically if we get back to a market that can grow in that 4% range and we can grow a little bit faster than that through innovation and so forth.

Operator

Steve Beuchaw, Morgan Stanley.

Steve Beuchaw - *Morgan Stanley - Analyst*

First of all, I wonder if -- Bret and maybe Jim, if you could spend another minute on the impact of the weather that you called out, clearly a US centric issue. How much of the impact of weather would you say came along in the fourth quarter? How much are you embedding in your expectations for the first quarter? And which areas of the business might be more or less weather sensitive?

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

Well, let me take a shot at that. This is always difficult because we don't really have great data on what happens in the dental operatory when we have a blizzard or we have an ice storm, etc. But I will say that the weather that we had -- this is mainly a first-quarter issue, not a fourth-quarter issue.

But the weather that we had on the East Coast and into a lesser degree and the Midwest in January and the early part of February was pretty severe. I mean, we had probably the economy shut down for 90-million-plus people at some point due to the recent storms. And that does have an impact on dentistry because the operatory is closed, so dentistry doesn't get done during that period of time.

The data points that we have is we looked at -- we have looked at growth in the various regions throughout the world -- or excuse me, not throughout the world, throughout the country and compared them the ones that were weather-related and the ones that weren't weather-related and there is a pretty big divergence in growth here early in the year.

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Now hopefully because dental ailments don't self correct they keep getting worse, hopefully that will level out over the next few months as people that had their appointment canceled or canceled their appointments because of weather, end up back in the dental operatory later to get those same ailments corrected.

So too as it looks like a temporary thing, it was pretty notable.,,, in the first let's say five weeks of the year. And again, we are hoping that will level out this we move through the year. You have anything to add to that?

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

No, I think that covers it.

Steve Beuchaw - *Morgan Stanley - Analyst*

Thanks, that is very helpful. And then one quickly on SG&A. Jim, just following up on your comments in the prepared remarks. The SG&A control in 2013 was fairly remarkable keeping it fairly flat in dollar terms. Can you give us any color on what you are expecting in terms of SG&A growth? Is there a reacceleration in 2014? And maybe along the same lines speak to how much runway there is in terms of the cost control efforts that you have implemented thus far? Thanks so much.

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

Yes, Steve, it is Chris. I will take a stab at that. Yes, in short, we are pretty pleased with the SG&A leverage we are able to generate. And as Jim mentioned, and as I think I mentioned as well in our comments, that has been a clear focused strategy for us, obviously on the integration efforts but also frankly and terms of our (inaudible) businesses as well.

And again, we do believe that as a lower growth environment we need to focus a little bit more on manufacturing operating margin improvements. We obviously have focused the businesses and business has been focused heavily on doing that we are pleased with the performance they delivered on that in 2013.

As we move to 2014 we would expect to get some additional leverage associated with some of the structural moves we made later in the year. I mentioned the restructuring charges and that is not atypical for us. I mean as we move through the year we typically move forward as we identify opportunities to make the business more efficient we'll take restructuring charges from time to time.

So I think we would expect to continue to be able to get some improvement on the SG&A line moving forward. I'm not going to speculate in the context of what a ratio may be. But we typically do look for SG&A rates to grow basically below what the sales growth rates are and we're pleased with the ability to do that in 2013.

Steve Beuchaw - *Morgan Stanley - Analyst*

Okay, thanks, everyone. We will see you in Chicago.

Operator

Robert Jones, Goldman Sachs.

Robert Jones - *Goldman Sachs - Analyst*

I was hoping you guys could share a little bit more around your assumptions relative to 2014 guidance around capital deployment specifically. You guys have done a nice job of getting the debt ratios back to a more normal level. Pre-ASTRA TECH I know buybacks were certainly a bigger part of the EPS growth story. Anything you can share with us on how you are thinking about capital deployment and repurchases specifically in 2014?

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

Yes, sure, Robert, it is Chris. We will take a stab at that as well. I think we have been commenting on recent calls about the fact that we are really trying to take a far more balanced approach to capital deployment and we think that we would be deleverage now to a position which really allows us to do that. And I think that is certainly our expectation as we move through 2014.

Specifically relative to share count, we certainly don't anticipate shares to be the headwind that they were year on year in 2013; if anything they are going to be a little bit of help.

On top of that, obviously we did some acquisitions that could give us a little bit of a lift here next year and we expect some modest accretion from the particularly the largest one being internalization of the minority interest line that internalizing that into the base business, if you will, as we went through 2014.

So I think that you will continue to see us do a balanced approach and relative to some share buybacks, again, a little bit of a lift maybe from that. But also focusing on acquisitions and also deleveraging a little bit as well.

Robert Jones - *Goldman Sachs - Analyst*

So I guess just because the last couple of years haven't really been a normal buyback year, I mean is there any just range you can give us if we think pre-ASTRA TECH? Is it fair to think of $150 million-ish as a level that you guys are comfortable with executing against as debt ratios are, like you said, more stable?

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

Yes, I think, Robert, a fair amount of that depends on some of the acquisition opportunities that may present themselves throughout the year. So I really hesitate to give you a number on it. But I guess what I would say is that, again, our capital deployment strategies are to ensure number one we don't go backwards relative to share count in terms of dilution.

And again, I anticipate having a slight benefit, if anything, from that line moving forward in 2014. But I guess, again, we are going to look deploy capital to make the business stronger and then also look to return cash to shareholders if that is the -- if we don't find good ways to do that.

Robert Jones - *Goldman Sachs - Analyst*

Got it, got it. And then I guess just my follow-up. I know you guys aren't giving specific guidance by geography, but if I heard you correctly, Bret, it sounded like you were saying you expected the European market to expand around 100 basis points.

Just given the growth for the Company and 2013 was affected by some very Company specific events like the salesforce integration for example, is there any sense you can give us on just general range of where you could see DENTSPLY growing in Europe in 2014 above that 100 basis points that you called out for the broader market?

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

Well, we don't give guidance on internal growth either in total or by region. Europe obviously is a large region for us, over 45% of our sales are in that region. So any improvement in that region we get pretty good leverage on in our P&L. And of course we haven't really had improvement in that region for the last three years.

But I think the reason we called out what we expect the market to do with respect to both European market and the US market next year was to send a signal that we are expecting those markets to accelerate a little bit and we would expect to get our fair share, or perhaps a little more, depending on the innovation pipeline when -- if in fact those markets do accelerate. So again we don't give specific guidance on internal growth by region, but we were trying to signal that we would expect some improvement there.

Robert Jones - *Goldman Sachs - Analyst*

Got it. Thanks for the questions.

Robert Jones - *Goldman Sachs - Analyst*

Got it. Thanks for the questions.

Operator

Brandon Couillard, Jeffries.

Brandon Couillard - *Jefferies & Co. - Analyst*

Bret, could you elaborate on what you saw in the fourth quarter between each of the sub segments? I'm talking about like implants, healthcare, lab, chair side consumables? And then in the US, I believe last call you said you expected a draw down in inventories. Did that materialize and was that effect in that negative year-over-year versus the buy ins last year that you saw in the fourth quarter?

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

Okay, let me take a stab at the first question; I will let Chris field the second question. Overall in Q4 we had internal growth of 0.8%, but we had low-single-digit growth in consumables in the specialties; we had kind of mid-single-digit growth in the medical line; and we had negative growth in the lab business.

We don't give a lot of color within those categories, although I will give you a little bit of color on implants and in the future I would like to stick to dealing with the specialties in total.

But with respect to implants we were slightly negative on implants in the quarter with Germany and without Germany we were slightly positive on implants and the quarter and that was led by the US market and the rest of world markets whereby of course Germany is ended and Europe, Europe was negative for us in the quarter. So that is kind of the general trends within each of those categories for the fourth quarter.

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

Relative to the dealer inventories, Brandon, again, we commented on the fourth-quarter call last year that there were a number of factors kind of going about ways that we thought the net impact of all of that was probably inflating internal growth in the quarter by up to a full percentage point.

And the largest factor that we mentioned at the time was really the fact that the dealers get heavy inventory levels in the US in Q4 after our price increase and in some cases even increased them further in advance of the January 1 price increase last year.

This year we ran up against that fourth-quarter base issue and we also saw dealers, as expected, push their inventories down towards more towards normal levels, if you will, after increasing them in advance of our October price increase this past year.

So as expected we really saw a pretty large divergence between retail sales and the wholesale sales in the quarter in the US and ,again, that is as we expected. And we think in general at this point channel inventories in aggregates are back down more towards normal levels, if you will? And that has probably got some give and takes across some of the individual businesses. But I think that the aggregate comment holds.

Brandon Couillard - *Jefferies & Co. - Analyst*

Thanks. And then one more for Chris. Could you give us a sense of what your net interest expense expectation is for next year? And then some view around operating cash flow and CapEx? That would be helpful. Thank you.

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

Sure. From a net interest expense for the year we will have a little bit of a benefit in terms net interest -- in terms of the interest expense from deleveraging. But unfortunately that is going to be slightly offset from -- as a result of lower interest income as we have reduced some of our derivative positions. So net of that is going to be essentially flat.

In terms of cash flow for the year, obviously we had a pretty significant investment in working cap, in particular inventory this year as we mentioned. We would expect that to obviously not repeat as we move through particularly in the second half of next year and move forward. So I would expect a little bit of a left there.

And I guess in terms of capital we entered last year guiding frankly and the 130 range, we ended up at 100, that was really timing related as a couple of key projects anything for 2014 I would expect something back again guiding in the probably $130 million range.

Brandon Couillard - *Jefferies & Co. - Analyst*

Super. Thank you.

Operator

Glen Santangelo, Credit Suisse.

Glen Santangelo - *Credit Suisse - Analyst*

Bret, I just want to follow up on some of the comments you previously made around Europe. If we were to strip the implant business out of your Europe sales for a second, is it fair to say that in aggregate the business was in positive territory on an organic basis this quarter?

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

Oh, yes, it was. And we have had 16 running quarters of positive growth in Europe, this was the first one we went negative. But absent implants and in particular absent the German implants, yes, we would have been positive low-single-digits.

Glen Santangelo - *Credit Suisse - Analyst*

And so embedded in that I am guessing you are suggesting that you continue to take some market share. Because was the market you think flat or better? Or you think the market is still in negative territory and you are just taking share? Because I'm just trying to reconcile that back to your comment that you expect the European market to expand 1% next year.

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

Yes, I think the market was flat plus or minus maybe a half a point. The data we have on the European market is not as good as we get in the US market, but just looking at all the data points in total we would say that European market was flat in the fourth quarter, we were up low-single-digits. That is entirely driven by the innovation platform that we have and we would expect that to continue.

Glen Santangelo - *Credit Suisse - Analyst*

And then maybe just one sort of follow-up question on the guidance. It kind of sounds like you don't have any capital deployment sort of baked into that guidance and you are suggesting you are going to take a balanced approach. Could you maybe give us some sense for what the acquisition pipeline looks like at this point in time?

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

Yes, I'm going to pass -- let Chris take that.

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

Yes. I think from an acquisition standpoint there are a lot of discussions happening, again we were pleased to be able to complete two small deals in November. I commented as well that an additional acquisition benefit that we will have in 2014, relates to the internalization of that minority interest line, which is going to certainly bring -- that brings about $0.03 per share in terms of additional accretion.

So again, I think that there is no doubt that we will continue to look at acquisitions beyond what we have already done as opportunities. Obviously those are binary, they happen when they happen. And are we optimistic we can get some done? Sure. But at this point in time I think our guidance reflects what we have already done.

Glen Santangelo - *Credit Suisse - Analyst*

But just to confirm, you are comfortable with the leverage you are at now, so there is no plans to further deleverage it? As we think about the use of free cash flow it should either be to do acquisitions or share repurchase?

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

I think we have got some opportunity again, I think, Glen, the way to think about it would be a gradual -- really a balanced approach. We may see some additional gradual deleveraging to provide additional dry powder for the future. But I think that is going to be in the context of a balanced approach relative to share repurchases and acquisition.

Glen Santangelo - *Credit Suisse - Analyst*

Okay, thank you.

Operator

John Kreger, William Blair.

John Kreger - *William Blair & Co. - Analyst*

Just a couple of questions on what you are assuming in guidance for 2014. I know you don't like to give specific revenue targets, but would it be reasonable to assume that on a consolidated basis you could do perhaps 3% or better for the year given your comments about some market growth improvement?

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

Yes, I don't want to give specific guidance on internal growth for next year or for the current year 2014. But again in the guidance comments when we said the market -- we were expecting markets to accelerate in the US and Europe, we would expect to get our fair share of that. And then secondly, the wildcard would be this rest of world region where we have had these major devaluations.

I'm not sure what will happen in those countries. But I think that adds some risk to the equation certainly at this point. But to the extent we see market acceleration happening we would expect to get our fair share or more of that.

John Kreger - *William Blair & Co. - Analyst*

Great, thanks, Bret. And perhaps a follow-up. What sort of pricing are you assuming you can get in 2014?

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

Yes, John, our price increases were generally taken back in October. We are pleased in terms of basically at this point what it looks like in terms of what has stuck. And again, I would guide that in the range of probably 1.5%, pretty consistent with where we have been in the past.

John Kreger - *William Blair & Co. - Analyst*

Great, thanks. And then one last one. Bret, if you look at the implant market more broadly what are you seeing in terms of the three different sort of broad price points? And are used sort of comfortable with your offering across those three price points?

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

Let me take a stab at that, I don't know if Jim will have anything to add or not. Obviously the three price points for implants is there is a premium segment out there which includes a vast array of technologies, everything from digital treatment planning to drill guides to customized abutments, implants, etc., it is a pretty broad category. There is kind of a mid-tier sector and then there is kind of a low-tier sector -- we participate in the premium sector only at present.

I think that, particularly in Europe where the economy has been really, really horrible, premium implants have had a lot of pressure and in that environment I think, as in every area of dentistry, lower-cost products sometimes gain some share.

I think over the long term in this -- in what is a pretty technical discipline within dentistry we are going to see people want to use the most advanced technologies and that is where our focus has been. Jim, do you want to comment further on that?

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

Sure. Yes, John, from the standpoint of the implant business globally, we continue to focus on the premium category. We believe that there continues to be a lot of opportunities for differentiation. We have plans for innovation in that area, some of the things I mentioned earlier as it relates to digital technology. And I think the impact that they can have to offer a lot of value and more simplicity for the clinician will continue to focus on.

As it relates to the value segment, we continue to monitor and analyze that closely. There is no question we can see the visibility of that segment in the emerging markets. In the more developed and more premium markets, we continue to watch that closely as well.

And I think the challenge that we see is that while there is certainly a lot of dialogue in that segment, the difference between a premium and a value implant of $50 to $75, how that would influence the cost of treatment at the patient level of $2,500 to $3,000 is just a little bit uncertain at this point in time. And we continue to monitor that to understand really what is going to be the driver in the market.

John Kreger - *William Blair & Co. - Analyst*

Very helpful, thanks.

Operator

(Operator Instructions). Steven Valiquette, UBS.

Steven Valiquette - *UBS - Analyst*

Just a quick question on operating margin and leverage. You talked about some opportunities on the manufacturing side for operating leverage in 2014, that seems to be incorporated into the guidance. I guess the question is, is the operating margin expansion specifically tied to your expectations of accelerated market growth and key geographies in 2014? Or do you think you can achieve the operating margin expansion from your various initiatives even if the market improvement does not materialize? Thanks.

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

Yes, Steve, it is Chris. Bottom line is there is no doubt that a more robust market certainly helps us in terms of operating margin leverage to our P&L. So our guidance includes obviously an estimated operating margin based on what we are estimating market growth to be and basically our sales performance to be.

So there is no doubt that that obviously helps a bit. That said, we are also cognizant, as I mentioned before, that in lower growth environments we need to focus on manufacturing the operating margin via efforts of our own and I commented I think previously in terms of what that entails.

And we are very focused on that, committed to that and we've taken a number of actions last year that will obviously help us as we move forward this year. And we have got additional focus on that as we move through 2014.

Steven Valiquette - *UBS - Analyst*

Okay, so I guess just tied into that, so like in the last quarter you just had about 10 bps of operating margin expansion that was a little bit lower than what we saw in the middle of 2013. And obviously the growth organically kind of slowed down a little bit in the top-line in the fourth quarter.

It sounds like there's additional things you can do though in 2014. So it is not like the run rate exiting 2013 is the proper assumption for what you are capable of, is that the way to think of it?

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

Yes, obviously I think there is no doubt the fourth quarter additional sales growth would help. But there are a couple of other significant factors on our operating margin, currency is a very significant factor. When you talk about currency in terms of the headwind of about $0.03 in the quarter in terms of basically operating profit on slightly positive translational impact on the top line, I think you can kind of see how that can have an enormous impact.

So again, I think there are some aberrations there in the fourth quarter. But again, as we move forward we have a lot of efforts in place to continue to improve in this area and as we get any lift from the market that helps us further.

Steven Valiquette - *UBS - Analyst*

Okay, got it. Thanks.

Operator

Jon Block, Stifel.

Jon Block - *Stifel Nicolaus - Analyst*

I have got maybe one or two sort of clarifications and then one or two follow ups. So first sort of clarification question. Chris, the tax rate step up that you mentioned in 2014, is that permanent? Should we think about that as permanent or something specific as 2014?

And then the FX headwind for $0.03 that you called out on the quarter, where was that relative to where you were in late October? I think it might have only been a penny additional relative to where you were in mid-October, is that correct?

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

Yes. So let me handle that one first. Yes, the FX was a penny -- incremental penny worse than what we had guided on the -- or indicated or suggested on the third-quarter call for the fourth quarter. And the bulk of that change again was in what I will call the second-tier currencies, which in aggregate for us comprised about 25% of our sales.

And as you look at it through 2013 there's about a little over a 10% devaluation in that basket of currencies versus the major currencies of the US dollar, euro and Swiss. So that is a big impact for us obviously in the quarter. And obviously it is causing the bulk of the headwind for 2014.

Relative to the operating tax rate, really what is driving that is mix. Obviously the International tax System is pretty complicated overall forecast and estimate. But I think the primary variable for us is geographic mix of income.

And in short we had a mix benefit or tailwind in 2013, if you look and compare that rate to 2012's rate you will see that it really was an improvement in 2013 versus 2012, but we don't, at this point, expect that to repeat or to fully repeat in 2014. So again, it is really more driven based on our mix estimate in terms of income.

Jon Block - *Stifel Nicolaus - Analyst*

Okay, great.

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

And I would add to that just longer-term, whether we can then get the rate back down again in future periods I think is yet to be seen. There is a lot of tax planning that we do. And so and you have seen that rate move around a little bit from year-to-year. So I don't know that this is a permanent change as much as it is a mix change for 2014.

Jon Block - *Stifel Nicolaus - Analyst*

Okay, perfect. That is very helpful. And then just the other sort of clarification question. You mentioned the rest of the world, obviously you are getting a headwind from the currency devaluating relative to the USD and I guess the euro as well. Just for clarity purposes, should we think about -- I think you mentioned flat growth is that in rest of world or is that in the emerging component of rest of world when we think about growth in 2014?

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

Well, I'm going to start this and I think Chris will finish it. But when you look at our rest of world category it includes basically three developed markets and then the rest are emerging markets. The three developed markets are Canada, Australia and Japan, all three of which took a major currency devaluation in 2013, late 2013. So even the developed countries in that category got hit hard by currency.

Then when you look at the developing components of rest of world, of course -- and Chris can give you more statistics on this -- essentially all of those countries took a pretty major development or excuse me devaluation in the fourth quarter. So it is both components that are getting hit.

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

Yes, and I think in terms of growth I think the comment we made, Jon, was that the developed countries and that rest of world region the sales were essentially flat for the year. And emerging markets overall for us were up mid-single to high single digits for the year.

Jon Block - *Stifel Nicolaus - Analyst*

All right and maybe last one I will take the rest off-line. But just specific to the German implant business, can you guys take a step back and just sort of discuss how comfortable you are that maybe some of the weakness?

And I think the weakness may have been stretching up for longer than originally anticipated that that's specific to the sales force reorg instead of sort of the market fundamentals and where we hear of value guys getting more aggressive? So can you maybe tease that out for us in Germany, what is sort of salesforce reorg noise that will be in the rearview mirror shortly versus underlying market fundamentals?

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

Yes, Jon, this is Jim Mosch. From the data that we see from our competitors and also industry data there is an indication that the implant market in Germany is down overall. So that is not been helpful in the year.

With respect to our integration activities, we are very comfortable that that organization has stabilized. It probably took us a couple of quarters longer than we would have liked, but these were two large organizations. And I think when you merge two organizations, if one is a lot larger than the other one essentially absorbs the other. When they are the same size you have got to combine them.

And therein lies the complexity of our German integration. But we have seen sequential improvement in Germany and we are seeing a nice uptick so far in Q1, albeit this is compared to a post integration quarter in 2013. But we are comfortable that that organization has stabilized and that we will move forward favorably.

Jon Block - *Stifel Nicolaus - Analyst*

Great, thanks for your time, guys.

Operator

And that does conclude today's question-and-answer session. Mr. Leckow, I will turn the conference back over to you for any additional comments or remarks.

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

Okay, thank you very much for your interest in DENTSPLY, that concludes the conference call. If you have any other questions please give me a ring, I'm available for follow-up. Goodbye.

Operator

And this does conclude today's conference and we thank you for your participation.
