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CONFERENCE CALL PARTICIPANTS

Glen Santangelo *Jefferies - Analyst*

PRESENTATION

Glen Santangelo - *Jefferies - Analyst*

While Stan and Ron get settled, I'll just introduce myself. I'm Glen Santangelo at Jefferies. We don't have official lead coverage of the dental sector, but for some of you that know me for a while know I have covered the company for over a couple of decades and we've had some transition at Jefferies.

So I'm going to be doing the introduction today, and we're trying to get back up to speed in dental as fast as possible. So if you could just bear with us for a little bit, that would be most kind. So welcome Stan Bergman, who I think everyone knows is the 30-year CEO of Henry Schein at this point, you went public in '95. And to his left is Ron South, the Chief Financial Officer of the company. So thank you guys for joining us. Obviously, a lot to talk about, so why don't we can we just get right into the Q&A.

QUESTIONS AND ANSWERS

Glen Santangelo - *Jefferies - Analyst*

Perfect. Okay. All right now, listen, I appreciate that 1Q results are a month old now, but this was your first full quarter since the fourth quarter sort of cyber-attack. You know, I figured we could start off Stan or Ron, whoever wants to answer by giving us a quick summary of those 1Q trends and maybe discuss what pieces of your business maybe returned a little bit faster than you thought? And maybe what pieces maybe you're taking a little bit longer relative to the issues you saw in 4Q?

Stanley Bergman - *Henry Schein Inc - President, Chief Executive Officer, Director*

So maybe Ron can give you the math and then I'll provide some comments.

Ronald South - *Henry Schein Inc - Chief Financial Officer, Senior Vice President*

Yeah. So in terms of the math on the first quarter, we did call out 300 basis points to 400 basis points of some headwinds that we still had on merchandise sales that we attribute to kind of the lingering effect from the cyber incident.

Some of that is as we recover episodic customers and the definition of an episodic customer is one who didn't have a kind of a consistent purchasing pattern, likely didn't have a relationship with a rep and therefore, was more transactional and was doing more of their buying through the website. When the website went down, they went someplace else and we're still trying to regain some of those customers -- a lot of those customers we have regained and some of those customers, we were still regaining over the course of the quarter.

Stanley Bergman - *Henry Schein Inc - President, Chief Executive Officer, Director*

So let me just build on what Ron mentioned, there are three legs to our business. There's the distribution part that was impacted by the cyber incident. And as Ron mentioned, essentially the challenging part of that business is these episodic customers. Having said that, our larger customers were mostly back, having bought everything from us that they could.

But we mentioned in the call, that that was going in a very, very good direction and the same is applicable to our midsized customers and a lot of our smaller customers that have a relationship with a field sales consultants or a tele-sales representative.

In that business we have seen quite a bit of movement towards midsize manufactured products and even some of the larger suppliers that have adjusted the pricing from the significant increase in pricing that we saw in the '22 and '23 period, a lot of movement towards generics on the medical side and to our own brands.

This is good from a profit point of view. But if you look at the sales, it can be slightly misleading. It's the episodic customer challenge. And glove pricing was still going down a bit, units have stabilized. So essentially, that business in the North American arena is relatively stable. There are a couple of parts of the world that are a challenge and a couple of parts of the world that are not -- they are in pretty good shape, but overall, the consumables and equipment businesses are pretty stable.

The second leg is our specialty businesses. Our implant business, of course, there was quite a bit of acquisitions in 2023. Part of that's left to analyze, but parts of the world were growing nicely, for example, in Europe, Germany, where we have the number one market share in terms of implants, bone regeneration products. There was a slight challenge in the US where the market is not growing significantly and we're bringing out a new product.

So it was a little bit of a holdback until the new product comes out. But essentially, we believe we're gaining market share on a global basis, on a US basis in the implants and bone regeneration space. Likewise, in the endodontic space, the growth was a little bit more, it was actually quite good. And we continue to believe we're growing market share in endodontics. In orthodontics it's very small. We also introduced a new orthopedic line.

The third leg, Glen, is our value-added services, two-thirds or so of that is software. Those businesses are all doing very well, although they did have a slight challenge because of the Change situation. We, within 48 hours, had an alternative system clearing claims on behalf of our customers, but they had some issues in collecting some of the fees.

I think that's largely dealt with although there are still are some issues in that area because Change is not fully back on the payment side, not on the claims processing side, but we have an alternative system. So, all three legs by and large showed pretty good stability. And there's some challenges in each from a mathematics point of view. But overall, I think our margins were pretty good. Gross profit grew.

Glen Santangelo - *Jefferies - Analyst*

Okay, that's a good summary. So, a lot to unpack there. Maybe let's start on the consumable trend, I mean, essentially, if we look back at 1Q, I think the global sales number was down, I think 3.7%, Ron and in your opening remarks, you seem to suggest the cyber incident. Did you say 300 to 400, I didn't hear.

Ronald South - *Henry Schein Inc - Chief Financial Officer, Senior Vice President*

Yeah, 300 to 400.

Glen Santangelo - *Jefferies - Analyst*

But I thought on the call you maybe said 200 basis points, but let's assume most of that decline is still residual effect from the cyber incident. But when I remove that right, the utilization trends still seem like it's flat to sort of modestly down. How do we think about that on a go-forward basis and how do we reinvigorate growth in that business?

Ronald South - *Henry Schein Inc - Chief Financial Officer, Senior Vice President*

Certainly a couple of other factors to consider there, too, is that also in the quarter we did quantify about a 60-basis point effect of lower PPE revenues. And we've had kind of ongoing headwinds with PPE revenues driven by glove prices in the market.

And this year, we expect to continue to have those headwinds. They just won't be nearly as pronounced as they have been say, in '23 versus '22 or '22 versus '21. But we do expect that to be likely the most significant effect we have in any given quarter, it was going to be in the first quarter, just the nature of how the pricing dynamic has worked since the beginning of '23. So, there was 60-basis points that can be attributable directly to just market conditions on pricing, primarily on pricing of gloves.

Glen Santangelo - *Jefferies - Analyst*

Right. So, I think again, not to put words in your mouth, but you're kind of making the case that ex-cyber incident, ex the PPE sort of headwind, we're dealing with a consumable number that's basically flattish.

Ronald South - *Henry Schein Inc - Chief Financial Officer, Senior Vice President*

That's correct. And I think what you see with consumables is that it tends to move with patient traffic. Patient traffic has been a little flat. Q1 did have some other challenges around patient traffic, including some weather conditions in January. The flu infection rate was a little higher in January and that increases cancellations in dental offices.

So we did see kind of see some softness at the beginning of the quarter that did get better as the quarter progressed. But yes, I mean right now in merchandise, the consumable merchandise growth is going to be largely driven by ultimately by patient traffic to the dental office and that churn that comes with that of merchandise of consumable merchandise is part of that.

Stanley Bergman - *Henry Schein Inc - President, Chief Executive Officer, Director*

Let's make sure that we stress here. I don't think we have deflation per se in dentistry. I don't think price competition is a significant issue. There always has been, but there has been a movement towards lowering the price of certain products by some of the manufacturers that took them too high during '22 and '23 and a switch towards lower [priced] (added by company after the call) manufacturers and corporate brand. Those do not impact profits, but that dynamic is in there and it's not like a general deflation. Certain manufacturers understanding they went too high, particularly on equipment side.

Glen Santangelo - *Jefferies - Analyst*

So despite those prices coming down, it does not impact profit your profitability?

Stanley Bergman - *Henry Schein Inc - President, Chief Executive Officer, Director*

No.

Glen Santangelo - *Jefferies - Analyst*

Okay. All right. Stanley, in your comments, you sort of talked about the fact that you believe the equipment market is stable. I think the results in 1Q were essentially flattish, I mean, are you anticipating flattish for the full year? And can you maybe elaborate a little bit more on which categories might be you're having more traction with, maybe which categories need some improvement?

Stanley Bergman - *Henry Schein Inc - President, Chief Executive Officer, Director*

Glen, we gave some guidance that indicated essentially that the traditional equipment market is relatively flat, good growth to be expected from the digital side. It's really hard to give indications going forward of exactly what that meant -- what that will mean. Equipment sales are heavily weighted towards the back third of the year, but essentially in the United States, there is a demand for traditional equipment. It's very similar to what it was last year.

And there is a significant increase in demand for digital products and we believe the pricing of digital products, particularly the scanners, DI, has stabilized and the unit growth is there. There seems to be more interest now in the mills, the chairside mills and a significant interest in 3D printing. So those items all go into the mix.

Europe is different. It's a bit of a mixed bag. Germany has some pricing issues because some of the key manufacturers went too high and there are imports coming into Germany from other parts of Europe. But essentially, the demand is pretty stable. And in Europe in general, France, there's some issues because the DSO world has had to adjust to some legislation, but essentially the equipment market is stable. It's hard for us to give you a readout of what's going to happen in the last three or four months of the year certainly when we gave comments at the end of the first quarter.

Ronald South - *Henry Schein Inc - Chief Financial Officer, Senior Vice President*

And Glen, Stan made a great point on the standard equipment. We did say that the balance of the year on standard equipment is expected to be relatively flat. But I think it's very important to look at that specific market and the growth that it has experienced since pre-pandemic, you go back to 2019 and you look at kind of standard equipment demand, the pandemic did generate a lot of demand for new chairs.

There's renovations. There's a lot of dental offices that we're building out, adding chairs, so there was very good growth. There was some pent-up demand. There was a little bit of supply chain issues that created some lumpiness in standard equipment, but we had multiple quarters of double-digit growth in standard equipment, which we knew was not a long-term sustainable process, but we're now working off a much higher base of standard equipment. So, the fact that it's running a little flat now, when you look at it over the long term, it's still a pretty good trajectory for us.

Glen Santangelo - *Jefferies - Analyst*

And Stanley, you also talked about tech and value-added services, right continues to be a growth business for you. I mean, predominately on the software side, what sort of color can you give us some on that business? And should we think about -- or I guess how should we think about a normalized growth rate for that business? That's always been a tough one, so to predict.

Stanley Bergman - *Henry Schein Inc - President, Chief Executive Officer, Director*

I'll leave that to Ron to give the normalized growth rate because I'm not sure exactly what guidance we've given. But conceptually, we are growing the installed base because of our pretty well received cloud-based system, it's in the US and entirely outside of the US, very well received.

But it's moving from a sale of equipment of software that's sold with the computer versus the SaaS model, we get a monthly fee, but the growth in this business is quite good. And particularly with the add-ons, including AI, we've got some good AI products that are selling quite well. Several of these systems are being tested in the DSOs now, and we expect to see a big movement with a couple of DSOs on the AI side.

We have some very exciting new software on interoperable on assessment of insurance claims, while the patient is in the chair, coupled with a new Google application, similar to almost a Uber environment where you will be able to search for a dentist who is available immediately in your area that accepts your insurance and get the rating of the dentist right away.

The system was shown at our Thrive event last month in Vegas and it's available. And we expect as installed base of users of the system grows, it will likely become the most popular system in dentistry for making online appointments and there's many others features that have been added to our software.

We've also invested on the service side. And transition services, we've got a very nice business now that is in the buying and selling of practices. We've done a lot in claims processing businesses in that area. We have consulting services for dental insurance, consulting the providers. All of these are quite profitable and are providing stickiness to our general business.

And connected to our practice management system or to the distribution business or indeed our specialty businesses, but Ron, what guidance have we given on --

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Ronald South - *Henry Schein Inc - Chief Financial Officer, Senior Vice President*

Specifically, around technology and value-added services in our Investor Day last year, Glen, we pointed out that our assumed market growth within that kind of combined segment is 8% to 12%. And a lot of that is driven by, as Stanley said, kind of transition to as we add more customers to cloud-based software, but also we have revenue cycle management tools that are becoming increasingly important to our customers.

There's other kind of add-on services that help drive some of that growth. So that's kind of the long-term market growth that we expect to see in the market, and we think we can participate in that market growth and perhaps take some market share along the way over the long term.

Glen Santangelo - *Jefferies - Analyst*

Yeah, that's a real differentiator for the company because I think people want to tend to look at you within the context of all your dental peers. And there's a number of them that are sort of going through some challenges right now.

And, you know, for example, 30% of your business is in medical right, and that's holding up, you know, relatively well. We talked about technology and sort of value added services. But, you know, Stanley, I can give you a minute to just talk about, you know, the performance of your portfolio and how you think that maybe differentiates you from your peers, which maybe is underappreciated.

Stanley Bergman - *Henry Schein Inc - President, Chief Executive Officer, Director*

A minute Glen for me to say anything is very difficult.

Glen Santangelo - *Jefferies - Analyst*

What's that?

Stanley Bergman - *Henry Schein Inc - President, Chief Executive Officer, Director*

A minute, you know me very well, I don't do a minute. But I will say to you that I think the biggest misunderstanding about Henry Schein is to associate Henry Schein with the brand we've had for 90 years of being a pure distributor. Yeah, we have a great distribution business, but today over 40% of our profits are coming from our specialty businesses where we own our brands, very good brands. We manufacture and we do our own R&D and the software business.

So those businesses work in complement with our distribution business because that's where we get the leads. And those businesses also give our distribution businesses leads. But I think when you mention to investors, Henry Schein, oh yeah, the biggest distributor of products to office-based practitioners, to dentists, and to physicians, that is true.

But today, over 40% of our profits are coming from these high growth, high margin distribution specialty businesses and software businesses. And we add to that another 10%-plus from products that are distributed under our own brands.

In the distribution business, well over half of our business is coming from areas other than distribution of products under other manufactured brands. So I think that's not quite understood. And we've shown pretty good growth in all three of these legs.

Glen Santangelo - *Jefferies - Analyst*

And so let's maybe talk about Bold One, right. And this is your strategic plan for longer term sustainable, high-single digit or low-double digit growth. I mean, you're not that far into it. So can you talk about your progress you've made since the launch, how you feel it's going in areas that are surprising you positively or negatively?

Stanley Bergman - *Henry Schein Inc - President, Chief Executive Officer, Director*

Yes. So, we undertook an analysis for our Board at the halfway mark, which was as of the end of June 2023, 18 months and really, we're doing very, very well. We actually did well in the third quarter and then we had the cyber incident in the fourth quarter. But if we ex out the cyber incident, I think you will see that we've done pretty well on our key goals for our strategic plan. We have a setback there. We're doing well on recovering on the distribution side, but overall, we are delivering quite nicely on the Bold Plus One, Glen.

Glen Santangelo - *Jefferies - Analyst*

Okay. I mean, yeah, it's unfortunate, obviously, you had the setback in December and you made obviously a lot of incremental progress in 1Q. Ron, do you feel comfortable with the company? I'm asking you for anything specific on 2Q, but do you feel comfortable that the company continues to make that operational progress?

Ronald South - *Henry Schein Inc - Chief Financial Officer, Senior Vice President*

Yeah, I mean, it's still a bit of a ramp up process for us, I would say, but we're still working to increase market share and recover market share that we may have lost to the episodic customers that I was referencing earlier. We are excited about the second half of the year. We expect some benefit from a newly launched implant product that we are waiting on FDA approval on any day now that we think will be very well-received in the market.

We have some of the new technology products that Stanley mentioned, we think that can help drive the ongoing recovery in distribution. Some of these new products and new services we think can help drive revenue growth in the back half of the year that should exceed what we see in the first half of the year. And I think earnings will follow that pattern.

Glen Santangelo - *Jefferies - Analyst*

Right. Maybe that's what I wanted to talk about too, I mean on EBITDA, I think you're calling for growth of 15% this year. Anything particular you want us to think about in terms of operating expense or anything specific on the cadence that you want to call out yet?

Ronald South - *Henry Schein Inc - Chief Financial Officer, Senior Vice President*

I think the EBITDA pattern will be similar to that of earnings. We wanted to highlight EBITDA this year because we do have some below-the-line items that we did know would create a little bit of a headwind for us.

From an EPS standpoint, we did take on more debt last year, we did $1 billion in acquisitions, it's by far the most we've ever done. So the balance sheet's a little more leveraged than it has been historically. So it's a little more interest expense. And then point two was on the tax side was adding another kind of 100 basis points to 200 basis points of effective tax rate on it. So, we wanted to be sure we could highlight EBITDA, so that we could still have what we thought was a strong indication of the overall health of the overall growth of the business.

Glen Santangelo - *Jefferies - Analyst*

And Stanley, anything quick on capital allocation? I mean you generate a substantial amount of cash flow. How do you prioritize repo versus debt paydown versus internal or external investments, sort of given where the stocks trading, I mean, as you know, coming off the cyber incident, does it look more attractive to you? I mean, do you rethink the allocation strategy at all?

Stanley Bergman - *Henry Schein Inc - President, Chief Executive Officer, Director*

Our philosophy has been pretty stable since we went public. We've been buying stock. I mean, right now the stock price is very attractive, but we also want to keep some money to pay down debt, so that we can ensure that our balance sheet remains exciting. And these acquisitions, we're not likely to do another year of $1 billion.

We've got lots of add-on opportunities. The pipeline and acquisitions has never been fuller. And we're not buying necessarily another big dental distribution company. And there's parts of the world where we have areas where we don't have a distribution coverage, but essentially it's to add on to our value-added services, software businesses, and of course, to our specialty businesses.

And so there's lots and lots of opportunity. There are a few opportunities also to buy out a minority interest in some of our joint ventures that will be accretive. So, there's plenty for use of the cash. But we also want to maintain, as we have for 29 years, a pretty conservative balance sheet.

Glen Santangelo - *Jefferies - Analyst*

We're essentially out of time, but I want to give you the last word. I don't know if there's anything either you want to leave with investors to close.

Stanley Bergman - *Henry Schein Inc - President, Chief Executive Officer, Director*

Well, I would say that it is important to understand that Henry Schein is not purely a distributor of branded products manufactured by others, if that's the view and we're compared to other distribution companies, it's a mistake. I'd also be careful to not compare us to others in our industry. There have been a lot with some of our suppliers, other comparables, their expectation gaps. And we've had a steady progress of growth and delivery of expectations for almost three decades.

Glen Santangelo - *Jefferies - Analyst*

Awesome. Stanley and Ron, thank you very much. Much appreciated.