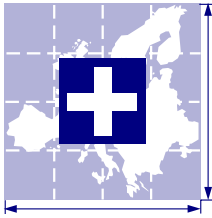


13 June 2005



Dental Implant Update

Feedback from Dr. Niznick Site Visit in California – A Serious & Dynamic Operation

**Medical Technology
Health Care Distribution & Technology**

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Highlights of This Issue

- On 10 June 2005 we performed a **site visit** of **Dr. Niznick's dental implant facility** in California, U.S. to be able to make a better assessment of the potential threat upon his re-entry to the dental implant by way of a new aggressive business model.
- **Non-compete clause** – we understand that Niznick's non-compete clause expires on 8 January 2006, but could be delayed based on a legal challenge by Zimmer Dental on a potential breach of contract. It appears the final final ruling must be made by December 2006 (i.e. within 6 months of the appointment of the arbitrator). Hence by December it should be clearer as to whether Dr. Niznick will be able to re-enter the dental implant market with high quality but discounted implants that will only be sold via the internet; the worst case scenario appears to be a delayed re-entry by the amount of time the arbitration panel believes the contract was breached by.
- Depending on what starting point the arbitration panel may choose for breach of contract (i.e. hiring of first employee, pre-marketing activities etc.) we estimate that Niznick's *Implant Direct* (we believe this could eventually be the company name based on the employee uniforms) could be delayed until 1H 2007.
- **Facilities** – our factory tour of the facility (previously used by Zimmer Dental) highlighted a **very modern** and **newly equipped operation** that housed over **55 staff** of which around 35 appear to be experienced ex Zimmer Dental employees; these had previously worked for Dr. Niznick before the sale of his Paragon Dental Implant company to Centerpulse (Note: Centerpulse was purchased by Zimmer in June 2003). While the production floor is awaiting some additional equipment for increased capacity, the existing machines, which can run virtually unsupervised, are **building inventory** of the various product lines.
- At random we took dental implants from the production line and viewed them under a microscope and were impressed with the precise engineering and the attention to detail. We would be surprised if any of the premium dental implant companies are achieving a materially higher level of quality than the *Implant Direct* facility. All implants go through a quality department where they are checked for abnormalities as well as metal residue that may have not been fully removed during the production process.
- **Product Portfolio** – our discussions with regulatory department has indicated that at present *Implant Direct's* product portfolio consists of **7 product lines** which equates to **~500 different inventory line items**; we estimate this could expand to ~800 by the time the company is entitled to legally enter the market. We also understand that *Implant Direct* will be submitting its products for **regulatory approval** in both the U.S. and Europe in September 2005, which should result in 510k and CE Mark approval by December of the same year. With the **rough implant surface** being created from the same blasting process as Zimmer Dental, we believe this is unlikely to raise concerns amongst regulators.

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Refer to important disclosures on page 3. Analyst Certification on page 2. Price Objective Basis/Risk on page 2.

- **Targeted Companies** – while the product portfolio is clearly targeted at any customer wishing to buy a quality implant at a discounted price, it does appear, based on the product design to slightly favour existing Zimmer Dental and Nobel Biocare customers. With respect to Zimmer, we believe the existing customers will be able to use their existing drill sets with *Implant Direct* implants.
- **Packaging** – the package design, which is nearing completion, appears to be sufficiently user friendly not to put the company at a competitive disadvantage.
- **Internet Portal** – during our site visit we also had the opportunity to ‘drive’ the internet portal from which customers are expected to place their orders. Given that *Implant Direct* will not have a direct sales force, we found the portal particularly useful in forming a view on the future success of the business.
- While we are not a **fan of the colour schemes** and the **general feel** of the internet portal (i.e. it does not look sophisticated enough for our liking), we have to admit that it offers a high degree of user friendliness with respect to getting **product information** and **placing orders**. We also believe that the **on-line feature comparisons** between the products of *Implant Direct* and offerings from Nobel Biocare, Straumann, Zimmer Dental and 3i will make interesting reading for potential new customers. Overall however, we feel that the portal in its current form does not give justice to the underlying product quality of *Implant Direct*.
- **Tactile Technologies** – we also took the opportunity to get an update on the Dr. Niznick’s recent acquisition of a 60% interest in Tactile Technologies, which is developing an interesting navigation system for precise placement of dental implants. The patented technology uses electronic bone mapping through tiny needles that sense bone and uses wireless communications to guide implant placement using 3D CT scan. The potential advantage of this system is that a **guide can be manufactured in the dentists’ office** rather sending it away to be fabricated and then returned to the dentist; we feel this product could be sufficiently competitive to offer an alternative to Nobel Biocare’s *NobelGuide* product and could potentially provide other companies, by means of a license, with interesting ‘guide’ technology; as a matter of fact we would not be surprised if Straumann is currently doing some due diligence on this technology.
- **Cash Burn** - with over 55 people currently employed at *Implant Direct* we estimate that Dr. Niznick’s monthly cash burn is comfortably above US\$250,000; hence with the non-compete clause expiring at the earliest in January 2006, we estimate at least another

~\$2 million needs to be spent before any revenues are generated. Should the arbitration panel rule in favour of Zimmer and result in a non-compete extension until late 2006/early 2007 than this amount could easily accelerate to US\$5 million.

■ Conclusion

- Following our site visit of *Implant Direct* we are of the view that the operation run by Dr. Niznick needs to be considered as a **serious** and **dynamic business proposition**, with the success largely dependant on the ability to sell solely through the internet as well as the ability by premium companies like Nobel Biocare and Straumann to be sufficiently innovative and speedy in rolling out differentiated products.
- Following a strong round of new innovative product launches in conjunction with an insight into its product portfolio at its World Conference last week, we believe **Nobel Biocare** (Buy: CHF264.5; C-1-7) is **sufficiently innovative** to stem-off potential threats from discount operators including the potential re-entry of Dr. Niznick in January 2006.
- With respect to **Straumann** (Neutral: CHF268.5; C-2-7) we believe the lack of product pipeline within its dental implant franchise puts the company more at risk than Nobel Biocare. However, with the company holding its ITI World Congress this week in Munich, Germany, we may get an update on the product pipeline, including data on its potentially improved SLA implant surface (SLActive).
- We will continue to monitor Dr. Niznick’s progress to see how successful his ‘low priced internet only’ strategy can be and the impact it may have on the **pricing stability** of the dental implant industry.

Price Objective Basis and Risk

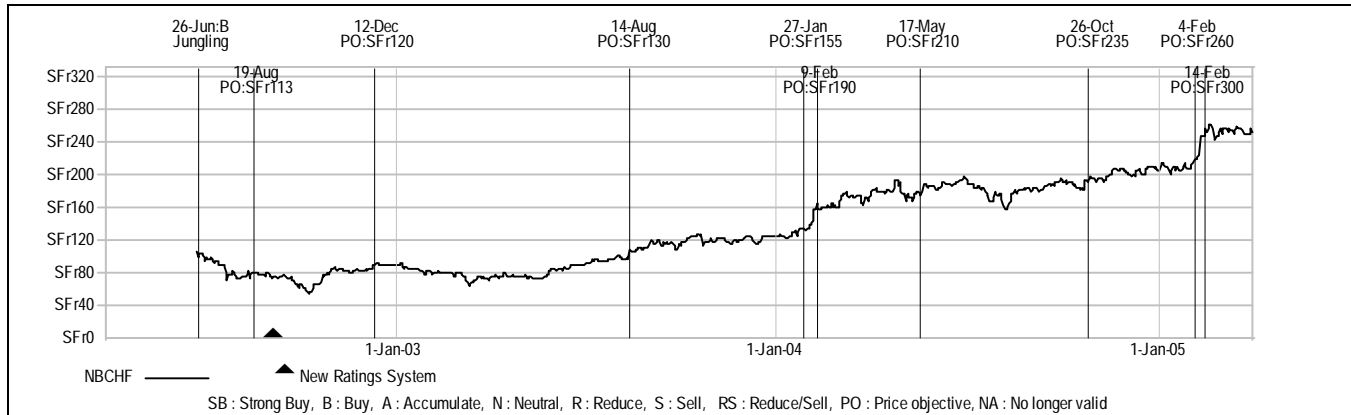
- For **Nobel Biocare (C-1-7)** our 12-month price objective equates to CHF300 per share, which is in line with our DCF valuation which uses a WACC of 8% and a terminal growth rate of 3%. Key risks to our valuation include the inability by management to further raise operating margins, a slowing dental implant market, inability to maintain high-teens sales growth as well as foreign exchange.

Analyst Certification

I, Michael Jüngling, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

Important Disclosures

NBCHF Price Chart



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Investment Rating Distribution: Health Care Group (as of 31 March 2005)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	81	41.54%	Buy	32	39.51%
Neutral	103	52.82%	Neutral	23	22.33%
Sell	11	5.64%	Sell	1	9.09%

Investment Rating Distribution: Global Group (as of 31 March 2005)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	1060	39.91%	Buy	368	34.72%
Neutral	1379	51.92%	Neutral	403	29.22%
Sell	217	8.17%	Sell	44	20.28%

* Companies in respect of which MLPF&S or an affiliate has received compensation for investment banking services within the past 12 months.

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