Sharps Compliance Corp.
Third Quarter Fiscal Year 2009 Earnings
April 28, 2009

Operator: Greetings, ladies and gentlemen, and welcome to the Sharps Compliance Corp. third quarter fiscal 2009 earnings release conference call. It is now my pleasure to introduce your host, Ms. Deborah Pawlowski, IR for Sharps Compliance Corp.

Deborah Pawlowski: Thank you, Jen, and good afternoon everyone. We appreciate your participation in our third quarter fiscal year 2009 earnings conference call. You should have a copy of the news release detailing Sharps' financial results that was put out earlier this morning and is actually the first major testament to the value of Sharps' solutions and services. If you do not have the release, you may obtain a copy from the Company's website at *sharpsinc.com*. On the line with me today are Sharps' Chairman and CEO, Dr. Burton J. Kunik, and Executive Vice President and Chief Financial Officer, David Tusa. Burt and David will provide their planned comments, and then we will open it up for questions. Also, if you are listening via the webcast, you do have the ability to submit questions online.

As you are aware, we may make forward-looking statements both during the call and in the following question and answer session. These forward-looking statements are not guarantees of future performance and are subject to risks and uncertainties as well as other factors that could cause the actual results to differ materially from what we discuss here. These risks and uncertainties are available for you in the press release itself as well as in the Company's filings with the Securities and Exchange Commission.

So, with that, let me turn the call over to Dr. Kunik to begin the review and discussion.

Dr. Burton Kunik: Thank you, Debbie, and welcome, everyone, to our fiscal fear 2009 third quarter earnings teleconference call. As Debbie mentioned, our third quarter results were extraordinary, and we believe, just the beginning of the potential growth we could realize from the sale of our proprietary medical waste management solutions. Importantly, beyond our first major government contract, through the nine-month period, we have had excellent growth in the retail, professional, and pharmaceutical markets as well.

We successfully launched our U.S. Government contract and are currently ahead of schedule with implementation. You may recall, we announced February 2, 2009, that we were awarded a contract to provide our Sharps Medical Waste Management System to an agency of the United States Government. The total contract is valued at approximately $40 million, and it is expected to be executed over a five-year period. We received the purchase order for $28.5 million for products and services to be provided during the first contract year ending February 1, 2010, of which we recorded $2.9 million of revenue during the quarter ended March 31, 2009. The following four option years represent payment for program maintenance.

The U.S. Government contract represents a significant milestone for the Company. We are pursuing additional opportunities of similar size and nature as we actively market our medical waste management solution, which is designed to be an integral part of government and commercial emergency preparedness programs to various federal, state, and municipal agencies. We've been very pleased with the response and interest to date. Additionally, we are marketing the system to large corporations and industrial facilities, who we believe will also see the value of our service offering. Our sales and management team are poised to continue the momentum we have generated and are focused on growing this sector.

On the pharmaceutical front, we expect to launch our next Patient Support Program with a major manufacturer during the quarter ending June 30, 2009. The program will be an integral part of addressing a new indication for an existing self-injected drug. We expect the program to contribute approximately $500,000 to our fourth quarter fiscal 2009 revenue. We continue to make significant progress with other pharmaceutical manufacturers, and as the leader in the mail-back industry, we believe we have a strong competitive advantage to capture a significant portion of this new market.

In the latter part of 2008, we launched a new solution to address the problem of how to dispose of unused prescription medications for consumers. The RxTakeAway™ is designed for retail pharmacies, alternate care facilities, community programs, and individual consumers to provide a safer and cleaner environment. In addition to the adverse effects on our water systems from these medications, improperly disposed of prescription medications are believed to be one of the leading causes of accidental poisonings of our children in the United States. The RxTakeAway™ product comes in a wide variety of sizes, including a special use envelope and 10- and 20-gallon products. The return packaging is prepaid to be easily shipped to our treatment facility. We've been receiving very encouraging feedback from our customers, and we're developing some real traction in the market.

With that overview, I'd like to turn the call over to David for review of our financial performance and a more detailed description of the earnings release.

David Tusa: Thanks, Burt. Good afternoon, everyone, and thank you for participating in our call. I'm sure everyone has seen the earnings release by now. As you see from our review, we generated $6 million in revenue, which is more than double for the $2.9 million in revenue recorded the prior year period. Burt mentioned the increase was driven primarily by the $2.9 million we recognized in the third quarter from the sale of our Sharps Medical Waste Management System under our government contract. The increase in the third quarter was also positively impacted by strengthened billings in our healthcare, professional, and hospitality market. The increases were somewhat offset by a decline in the pharmaceutical market which, as many of you know, is a very lumpy market for us, and revenue can be dependent upon the timing of the implementation of the Patient Support Programs.

For the nine-month period ended March 31, 2009, revenue increased 35% to $13.6 million, compared with the prior year period. Of this $3.5 million increase, $2.9 million of it was related to the government contract. Strength in the retail pharmaceutical and professional markets also contributed to the increase in the revenue year-over-year for the nine-month period.

The retail market billings represent sales of our flagship product, the Sharps Disposal by Mail System® to clinics and in the retail setting, as well as support of the cost-effective disposal of syringes used during the flu shot season. The retail market also reflects products that are part of the community programs where the mail-back is obtained through the retail pharmacy. Pharmaceutical market billings, as many of you know, are in support of patient compliance and support programs by major pharmaceutical manufacturers. We wrap an array of services around the product, such as fulfillment, inventory management, and data services. The sales in the pharmaceutical market are much lumpier and a bit more difficult when you compare year-over-year. The professional market represents sales in the doctor's office, dentist's office, and vets, where our product gets used as an alternative to a pickup service.

Gross margins for the quarter increased significantly to 59% and for the year-to-date period are at 49%. The increases in the gross margin are attributable to the significant operating leverage that's inherent in our business as the revenue grows at a rate in excess of our expanded infrastructure. We expect the gross margins for our fourth quarter, which is the quarter ended June 30, 2009, to be near the same 60% level.

SG&A expense was $1.4 million for the third quarter. That's up about $270,000 over the prior year period. For the nine-month period, SG&A was $4 million, which is up about $0.5 million over the prior year. About one-half of those increases in the SG&A is attributable to our non-cash stock option or stock-based compensation expense. Additionally, we had higher personnel costs that drove the increase in the SG&A. The SG&A for our fourth quarter ended June 30, 2009, is expected to be about the same level, $1.4 million. As we look forward into 2010, the SG&A should probably be about $6 million, which is approximately a 5% increase over the current run rate level.

Operating income for the quarter was $2 million, or 33.2% of revenue, versus an operating loss for the prior period of about $100,000. For the nine-month period ended March 31, 2009, we generated operating income of $2.4 million, or 17.4% of revenue, compared with the prior year operating income of $471,000, or 4.7% of revenue. The significant operating margin is a result of SG&A increasing at a much lower rate than the increase in our revenue; it's the operating leverage which I mentioned earlier.

On a bottom line basis, net income was $1.3 million, or $0.09 per diluted share for the third quarter of FY 2009, compared with a net loss of $0.01 for the prior year. Net income was $3.5 million, or $0.25 a diluted share, for the nine months ended March 31, 2009, compared with net income of $538,000, or $0.04 per diluted share, over for the prior year nine-month period. The net income for the nine-month period includes $1.8 million, or $0.13 per diluted share, related to an income tax benefit that we recorded in the December quarter, which ended December 31, 2008. As mentioned in our prior call, the $1.8 million is related to the net operating losses that the Company had generated since the inception. We took the benefit of that in the December quarter because of the confidence we had in the ability to generate future taxable income.

The Company's balance sheet at March 31, 2009, remains very strong, actually stronger than ever. Working capital is $3.6 million, total assets approach $12 million, and equity is over $8 million, all on zero debt.

As Burt mentioned, the government contract is $40 million, of which $28.5 million is expected to be earned in the first contract year, ending February 1, 2010. The remaining $11.5 million will be earned over the following four-year period as maintenance. We recognized $2.9 million from the government contract in this current third quarter. We expect to recognize an additional $3 million in the quarter ended June 30, 2009. That totals about $6 million for fiscal year 2009, between the third and the fourth quarter. Based on our current production schedule, we expect to recognize revenue of about $11.5 million in the first quarter of fiscal year 2010, which ends September 30, 2009, and an additional $11 million in the second quarter of fiscal year 2010, which is the quarter ended December 31, 2009. The remaining $11.5 million of the contract over the next four years will be recognized as maintenance.

We're limited in the amount of information we can disclose about the new U.S. Government contract, including the name of the agency. Therefore, I request that you respect the confidentiality surrounding the contract when we get to the question and answer session later.

I want to share with everybody something we talk about here in the Company, as a barometer of the level of growth that this Company has seen over the last five years. We currently have under lease and under ownership about 150,000 square feet of facility and office space. We expect that to be about 200,000 by June 30th, as the operations portion of the house moves into a new manufacturing and distribution facility. This represents a ten-fold growth in the facility and office space over the last five years. This increase in space is not only driven by the needed growth in the business, but also by a real shift in our business from the customers and the market demand for our vendor-managed inventory opportunities in the pharmaceutical manufacturing and government sectors.

As I mentioned on the February 2009 conference call, we received a favorable term sheet on our line of credit from JPMorgan Chase to increase it from $2.5 to $4.5 million. We're waiting for our government customer to sign off on a security agreement, and once that documentation is received, we will be able to close on that line of credit. The line of credit is similar to our current one, which is a traditional line of credit with a borrowing base and interest at prime, which is currently 3.25%.

We have completed the application process for listing on NASDAQ. We meet all requirements other than the $4.00 stock price. NASDAQ requires a closing bid price at $4.00 or above for a few days, and then we'll be eligible for listing on the NASDAQ. We already meet all other requirements related to the NASDAQ listing.

As Burt mentioned, we're well ahead of schedule and performing very well on the government contract. We have a number of our key personnel, along with Burt, focused on the sale of additional Medical Waste Management Systems to federal and state level opportunities. It is very evident that we're filling a need in the marketplace for this cost-effective and comprehensive solution to medical waste disposal outside the hospital setting. It's a very exciting time for the Company, our employees and our shareholders. I look forward to sharing this excitement with you and more of the Sharps Compliance story with current and prospective shareholders in mid to late May when I'm going to get back on the road to re-launch our Investor Relations program.

Operator, we're ready to open up the line for questions.

Operator: Thank you. Our first question comes from the line of Ben Lichtenberg with Noble Financial.

Ben Lichtenberg: Gentlemen, good work. I have two questions. I'll ask each one separately, please. I'm quite impressed with what you just said a few minutes ago, David, about your expected 2010 SG&A to be just moving upwards modestly. I think you mentioned 5%, which is probably just inflation-impacted, but really no increase that I can see, for the warehouses, for your new salespeople, or to service your maintenance on your big government contract and other new business. Can you draw a parallel there?

David Tusa: Sure, and that's a good question, Ben. We've been building out the infrastructure for this Company over the last few quarters. If you noticed, over the last couple of quarters, the SG&A's been about $1.4 million. Now, we will have an increase and some shift of some SG&A dollars going into 2010 because we do plan on hiring more sales personnel. On a net basis, we will be up at least three to four, maybe even five people from the sales standpoint. But the basic infrastructure that we have in place right now that we've been building pretty much over the last year, we believe, will be sufficient to be able to handle a much larger Company, including warehouse space and basic infrastructure.

Ben Lichtenberg: So, it's already there. The warehouses and expenses are already built in, the maintenance of the government contract's already built in, and there may be some new salespeople but, presumably, there'd be a significant benefit to that if and when they're at it.

Question two. You had a press release a couple of hours ago regarding the Product Stewardship Institute. Is that just a credibility bit of information, or is there some real ultimate economics to that?

Dr. Burton Kunik: Well, long term, it's going to probably guide the direction of where much of the consumer medical waste and pharmaceuticals are going to go. So being an integral part of that team is important to us so that we can help guide what's going to take place, and be a part of the discussion and the conclusions. It's a very influential group and so, I can't define the economic benefit, but it certainly ought to help us be prepared for where the market goes as time goes by.

Operator: Our next question comes from the line of Bruce Nakfoor with 3000 Partners.

Bruce Nakfoor: Great job. I have a two-part question on the future pipeline of the private and public sectors. If you could break down the anticipated cycle times now that you've achieved this government contract with the public sector? Does that roll over into the state and municipal levels, having achieved a federal approval? And then, on the private side, are you're seeing any real traction or significant growth from legislation in that sector as well?

Dr. Burton Kunik: What we are seeing is when we go visit other government agencies is that it's truly an unmet need. We see a lot of excitement and they're glad to see us and, respect what we bring to the table. We're ready to move to the next step. But, in terms of government, even large corporations, the time frame for that is uncertain. You can't expect to put any numbers down. But, everywhere we've been has been very, very positive, and we expect good results. It's an unmet need that's been identified, and the government agencies certainly recognize that. I think that our opportunities certainly should be there, and it's just the time frame of how long it takes for it to materialize. Did I answer your question completely?

Bruce Nakfoor: Not on the private side, but back to the public for a second, do you anticipate less cycle time? Is it affecting at all the state and the municipal discussions you're having?

Dr. Burton Kunik: Yes, I definitely think it would accelerate the cycle time; but, more importantly, I think the state of our preparedness to manage the new government contract should be as good or better than anybody else in the country today. That, in itself, says we're ready. "If you're ready, we're ready," and that accelerates the cycle time, and our presentations are very well done because we're already in the business.

Bruce Nakfoor: And on the private side? Specifically, the pharma side?

Dr. Burton Kunik: On the pharma side, we're gaining traction in that marketplace and gaining respect for all that we bring to the table. There is no one else out there who brings to the table all the elements that we do relative to the product design, the fulfillment, and data collection. We are doing well there, and we expect to continue to do well.

Operator: Our next call comes from Walter Young with Thompson Davis.

Walter Young: I have two questions. One of them is, can you explain how your service is proprietary? I understand that nobody else is doing it now, but what would keep someone else from entering the market? I'll ask my next question after that.

Dr. Burton Kunik: Are you talking in terms of things that we offer in the government contract or on the pharmaceutical side, or what?

Walter Young: The government contract mostly. But you made a comment earlier that it was a proprietary service, and I'm trying to understand how you would protect that from competition?

Dr. Burton Kunik: It is a proprietary service, such that we've designed data collection systems, methodologies of managing fulfillment, and other things that are not being done anywhere else as we are in those markets. I wouldn't say that somebody couldn't come in and do something that would be as good as what we're doing, but hopefully we can stay ahead of the curve. We're sitting here with the opportunity and working with the major pharmaceutical manufacturers in the country as well as the government contracts. We should be the best that you can be, and be at the top of the best offerings out there. That's exactly where we are, and intend to stay. We should be competitive and our proprietary elements should continue to grow as we increase our offerings through the government contracts and the pharm and any other markets as well.

David Tusa: Let me help with that one, too, Burt. Walter, it's a really good question about differentiators and proprietary nature. We've got a number of things, one in particular is the vertical integration nature of the Company. When you're dealing with large customers, vertical integration is just incredibly important. Over the last couple of years, by wrapping proprietary services, whether it's our tracking system, data services, fulfillment services, or the inventory management services, we've made it a much stronger offering. Maybe there will be competition at some point, but we think we're very well positioned with those items that I just mentioned in securing the large contracts. I know it's been something that's been very important for us, especially on the pharma and on the government side.

Walter Young: I guess what I was getting to is, I had heard you all in the past say a lot of times, that it's a requirement that you own the facility, which would certainly make you proprietary. But there can only be so many people that could put this vertical integration together.

David Tusa: Well, that's true. It's very important. As far as the closed-lid nature of the offering, it's part of the vertical integration, and we have everything under one entity under our control so we can assure the proper collection, the tracking, and the disposal of the medical waste.

Walter Young: My next question is about the legislation that is probably coming. It, as usual, starts in California and comes this way. When I think about doctors and veterinarians, and people like that, it appears to me that they are already trying to do the appropriate thing. My question is, how soon and to what degree would legislation improve your core business?

Dr. Burton Kunik: Legislation is definitely a big driver, and you're absolutely right, healthcare facilities are regulated and they are doing what they're supposed to be doing. In that market, we feel we are a more cost-effective way for many people to use our products rather than a pickup service. As far as the consumer market goes, there is a lot of new legislation out there both on sharps disposal and on unused medications in many states. There are seven states now that have made it illegal to throw a syringe in the garbage at home or office, or anywhere. That's impacting the people and their needs.

In California, there's another bill now that requires the manufacturer of self-injected drugs to address providing disposal for it. And so, yes, legislation is definitely a good driver, and I understand there's going to be more activity relative to reimbursement on a federal level for disposal of used syringes from consumers. I think you're going to see a lot of it due to the momentum created by making sure that consumers used syringes and unused medication get out of the solid waste drains. It's quite strong across the country, and we're in the leading role in providing a service for that.

Walter Young: Are there any ranges that you could say that you would predict would be the add-on business that would come from this type of legislation for your core business?

David Tusa: When you really stand back and look at this industry, we think there are over 2 to 3 billion syringes disposed of outside the hospital setting every year. If you do the math on those and assume that all those were disposed of using a mail-back, that is a greater than $1 billion-dollar industry. Things like legislation clearly help; but as a company moves more toward the proper disposal of syringes, then we think that we're going to be able to get our fair share of that market opportunity.

Walter Young: No ranges that you could give us?

David Tusa: That's tough. It's tough to look at it from a range standpoint. This is a growing market, a growing industry. It's an emerging industry, and as we continue to penetrate this industry and sign larger deals, it may become more and more evident. It's just difficult to put a number to it.

I want to go back to Bruce's question on the pharma side, quickly. Bruce, as I mentioned in the earnings release, we have one more pharma deal that we're looking to wrap up by June 30th. There are others. What's interesting about this pharmaceutical manufacturing market is that it's very important that the pharmaceutical manufacturers are getting on board and supporting their patients with our compliance program. What is really important is that as we do more and more of these pharma deals, we find is that the pharmas also like to use us as a marketing opportunity, an opportunity to be able to get the word out that they're doing the right thing in supporting the patients and protecting the environment. We're seeing more and more of that, and so we're encouraged that this pharma market will continue to grow.

Deborah Pawlowski: I have a question from the web. It's from Mr. Stephen Walker of Walker and Associates. His question is, "Have you been contacted by any agencies concerning the swine flu outbreak?

Dr. Burton Kunik: In reference to what we already are doing, there's a confidentiality issue involved in that. I certainly think it speaks to the opportunity with what we are involved with right now. We have been in contact with some retail settings that are concerned and are using the Medical Waste Disposal relative to solve ways for some of their items they're disposing of. We are in contact, and I think it really does point out how important that part of the market that we're working in is right now and the opportunities that come up.

Operator: Our next question comes from the line of John Sauder with Passel.

John Sauder: Hello. I'd like to ask about the credit facility with JPMorgan. Why do you think you need it, given your strong working capital position, and under what conditions would you proceed with drawing on it?

David Tusa: That's a good question, John. We would use that line of credit for working capital purposes. I'll give you an example. As of March 31st, we had no debt on our balance sheet, but we drew down about $0.5 million of that here this week to assist us from a working capital standpoint. The other reason would be for expansions, if we wanted to expand further. It could be for acquisitions, for potential additional lines of business or a different product or services that we could sell to our existing customer base. We want to be sure that we have the capital necessary to be able to fund any kind of expansion. It's nice to have, and we have a great relationship with our bankers. It's nice to have the dry powder.

Operator: Our next question comes from the line of Matt Kantrowitz with RedChip Companies.

Matt Kantrowitz: Hi, Burt, David. I want to ask about the RxTakeAway. What kind of traction are you getting with pharmaceutical chains and clinics, and when do you think you might see some significant revenue coming out of that?

Dr. Burton Kunik: Well, it really is getting some traction in terms of the interest level, and now we're starting to get some customers. We have pilots in some cities right now with a, drugstore/grocery store chain. We have orders that we're working on with assisted living. It's really growing, and the need for that is just tremendous. I think there's been a full page in both *USA Today* and even the *New York Times* about getting drugs out of the waste stream away from kids. So, this thing's really getting a tremendous amount of traction, and people are being concerned. All the government agencies and organizations are trying to move this thing forward to put regulations and solutions in place to get rid of the unused medications in everybody's medicine cabinet as well. We've had some very serious meetings that we're not ready to discuss right now, but we're positioned to manage this process with them. We are prepared to manage this program from the aspects of receiving it, disposing of it, and tracking it for any customer that wants to work with us. I think it's going to be a great market, and I think we're perfectly positioned to be a major player in it.

David Tusa: Matt, as you've seen, we have three sizes. We have the envelope product, which is a product that would be used at the consumer level. We also have a 10- and a 20-gallon product that would be used in a facility that may be taking back some unused medications. We've also developed DrugTracer, which is an add-on to our SharpsTracer. That's a proprietary system that we're using to track the proper disposal of the unused medication product.

Matt Kantrowitz: Yes, because you definitely have the infrastructure there. I'm just wondering what's been the holdback thus far? Is it the cost, that they just don't want to get involved unless they have to, or is it that they're waiting for one to sign on, like the government project, and then more will come. Why are they dragging their feet thus far?

Dr. Burton Kunik: It's all about who's going to pay for it. If you went to the top, you could say the pharmaceutical manufacturer in terms of product stewardship, should be responsible but they're not coming to the table either. And so, then who is going to pay for it? That's the big issue. The different places that we're working with have different methods of funding it, from government grants to waste companies to all different methods. I think that as the industry matures there will be several good solid sources to make it a sustainable program.

Matt Kantrowitz: I really like what you are doing with the PSI and the relationship with the EPA, it's a good step forward, and it's something I like to see. Thanks a lot, and good quarter.

Dr. Burton Kunik: Thank you, Matt.

Operator: I would like to turn it back to management for any closing comments.

Dr. Burton Kunik: Thank you. We successfully launched our first large-scale government contract and are aggressively pursuing additional opportunities to implement our solutions for other government agencies as well as corporations. The pipeline of opportunities for all our products and services continues to be strong. Looking forward, we will capitalize on our leadership position for managing medical waste in the many markets outside of the hospital setting, and we expect to continue to win new customers and expand our business. Once again, thank you for joining us today on our fiscal year 2009 third quarter earnings teleconference call.