OWENS & MINOR INC/VA/
Form 10-K
February 28, 2008
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-K

x **Annual Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**
For the year ended December 31, 2007

¨ **Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**
For the transition period from to

Commission File Number 1-9810

OWENS & MINOR, INC.

(Exact name of registrant as specified in its charter)

Virginia	**54-1701843**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**
9120 Lockwood Boulevard, Mechanicsville, Virginia	**23116**
(Address of principal executive offices)	**(Zip Code)**

Registrant s telephone number, including area code (804) 723-7000

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
Common Stock, $2 par value	**New York Stock Exchange**
Preferred Stock Purchase Rights	**New York Stock Exchange**
6.35% Senior Notes due 2016	**Not Listed**

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer (as defined in Rule 405 of the Securities Act). Yes x No ¨

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 12(d) of the Act. Yes ¨ No x

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x No ¨

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant s knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. ¨

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act.

Large accelerated filer x	Accelerated filer ¨	Non-accelerated filer ¨

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ¨ No x

The aggregate market value of Common Stock held by non-affiliates (based upon the closing sales price) was approximately $1,419,767,893 as of June 29, 2007.

The number of shares of the Company s common stock outstanding as of February 21, 2008 was 40,928,579 shares.

Documents Incorporated by Reference

The proxy statement for the annual meeting of shareholders on April 25, 2008, is incorporated by reference for Part III.

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Corporate Officers, located on page 4 of the company s printed Annual Report, can be found at the end of the electronic filing of this Form 10-K.

Part I

Item 1. Business

The Company

Owens & Minor, Inc. and subsidiaries (Owens & Minor, O&M or the company) is the nation s leading distributor of medical and surgical supplies to the acute-care market, a healthcare supply-chain management company, and a national direct-to-consumer supplier of testing and monitoring supplies for diabetics. In its acute-care supply distribution business, the company distributes over 180,000 finished medical and surgical products produced by over 1,200 suppliers to approximately 4,100 healthcare provider customers from 45 distribution centers nationwide. The company s primary distribution customers are acute-care hospitals which account for approximately 90% of O&M s revenue. Many of these hospital customers are represented by integrated healthcare networks (IHNs) or group purchasing organizations (GPOs) that negotiate discounted pricing with suppliers and contract for distribution services with the company. Other customers include the federal government, for which Owens & Minor serves as a prime vendor for medical and surgical supply distribution services for the U.S. Department of Defense. On a more limited basis, the company serves alternate care providers including clinics, home healthcare organizations, nursing homes, physicians offices, rehabilitation facilities and surgery centers. The company typically provides its distribution services under contractual arrangements with terms ranging from three to five years. Most of O&M s sales consist of consumable goods such as disposable gloves, dressings, endoscopic products, intravenous products, needles and syringes, sterile procedure trays, surgical products and gowns, urological products and wound closure products.

Founded in 1882 and incorporated in 1926 in Richmond, Virginia, as a wholesale drug company, the company sold the wholesale drug division in the early 1990s to concentrate on medical and surgical supply distribution. Since then, O&M has significantly expanded and strengthened its national presence through internal growth and acquisitions, including the September 30, 2006, acquisition of certain assets of the acute-care medical and surgical supply distribution business of McKesson Medical-Surgical Inc., a business unit of McKesson Corporation. Additional information on the acquisition and the company s other acquisition activity is included in Note 2 of the consolidated financial statements.

The Acute-Care Supply Distribution Industry

Distributors of medical and surgical supplies provide a wide variety of products and services to healthcare providers, including hospitals and hospital-based systems, and alternate care providers. The company contracts with these providers directly under terms set by GPOs and IHNs. The medical/surgical supply distribution industry continues to grow as the aging population in the United States requires more healthcare services and as emerging medical technology leads to the development of new products and procedures. Over the years, healthcare providers have adapted their health systems to meet the evolving needs of the markets they serve. In order to manage supply procurement and distribution challenges, these providers have increasingly forged strategic relationships with national medical and surgical supply distributors. The traditional role of distributors in warehousing and delivering medical and surgical supplies to customers continues to evolve into the role of assisting customers in efficiently managing the entire supply chain.

Consolidation trends in the overall healthcare market have led to the creation of larger and more sophisticated healthcare providers, which increasingly seek methods to lower the total cost of delivering healthcare services. These healthcare providers face a variety of financial challenges, including the cost of purchasing, receiving, storing and tracking medical and surgical supplies. The competitive nature of the medical/surgical supply distribution industry mitigates distributors ability to influence pricing, keeping profit margins relatively modest. However, distributors have opportunities to help reduce healthcare providers costs by offering services designed to streamline the supply chain through inventory management, activity-based pricing, consulting and outsourcing services. These trends have driven significant consolidation within the medical/surgical supply distribution industry due to the competitive advantages enjoyed by larger distributors, which include, among other things, the ability to serve nationwide customers, buy inventory in large volume, and develop technology platforms and decision support systems.

The Acute-Care Supply Distribution Business

Through its healthcare provider distribution business, the company purchases a large volume of medical and surgical products from suppliers, stores these items at its distribution centers, and provides delivery services to its customers. The company has 45 distribution centers and three service centers dedicated to single customers, located throughout the continental United States, and one warehousing arrangement in Hawaii. These distribution centers generally serve hospitals and other customers within a 200-mile radius, delivering most customer orders with a fleet of leased trucks. Almost all of O&M s delivery personnel are employees of the company, thereby increasing the consistency of customer service. Contract carriers and parcel services are used in situations where it is more cost-effective. The company customizes its product pallets and truckloads according to the customers needs, thus enabling increased efficiency in receiving and storing the product. Sales, logistics, credit management and operations teammates are located at or near distribution centers to manage service to healthcare provider customers.

O&M strives to make the supply chain more efficient through the use of advanced warehousing, delivery and purchasing techniques, enabling customers to order and receive products using just-in-time and stockless services. A key component of this strategy is a significant investment in information technology infrastructure and services, which includes OMDirect^{SM}, an Internet-based product catalog and direct ordering system that facilitates communication with customers and suppliers. O&M also uses its technology and logistics experience to provide supply-chain management consulting, outsourcing and logistics services to customers through its OMSolutions^{SM} professional services unit.

Products & Services

The distribution of medical and surgical supplies to healthcare providers, including O&M s private label product line known as MediChoice®, accounts for over 95% of the company s revenues.

The company also offers its customers a number of complementary supply-chain management services, including inventory management, information management, strategy, logistics and clinical consulting, materials management outsourcing and resource management. Examples are as follows:

- OMSolutions^{SM}, O&M s supply-chain consulting and outsourcing business unit, provides supply-chain management consulting, materials management outsourcing and resource management to enable healthcare providers to operate more efficiently and cost-effectively. For example, OMSolutions^{SM} provides clinician-consultants who work one-on-one with hospital staff to standardize and efficiently utilize products, processes and technologies. Other examples of OMSolutions^{SM} services are receiving and storeroom redesign, conducting physical inventories, and configuration of periodic automatic replenishment systems.

- PANDAC® is O&M s operating room-focused inventory management program that helps healthcare providers reduce and control suture and endo-mechanical inventory. Detailed analysis and ongoing reporting decreases redundancy and obsolescence, and increases inventory turns, which in turn reduces investment in these high-cost products.

- SurgiTrack® is O&M s customizable surgical supply service that includes the assembly and delivery, in procedure-based totes, of supplies based on the operating room s surgical schedule. Through in-depth assessment, O&M provides customers with information in order to standardize products, reduce inventory and streamline workflow.

- WISDOM Gold^{SM} is O&M s Internet-based spending management solution, and analysis and reporting service that enables customers to gain deeper understanding and control over their supply procurement and contracting efforts. WISDOM Gold^{SM} consists of three components: WISDOM^{2SM}; a standard product master file (Gold file) that includes industry standard information, including catalog numbers, names and product codes; and an Internet-based contract management system that digitizes local and GPO contracts, maintains contract details in a central database, and synchronizes customers item files to their contract portfolios.

QSight is the technology platform behind O&M s new Clinical Supply Solutions Internet-based clinical inventory management tool that enables healthcare providers to accurately track and manage physician-specific inventories, medical/surgical inventories, and clinical assets in clinical specialty departments, such as cardiac catheterization labs, radiology and operating rooms.

O&M s Bone and Tissue Tracking system uses barcode technology to track all types of implants in a healthcare setting, enabling customers to comply with regulatory requirements, avoid costly expirations, and respond quickly to recalls.

Customers

The company currently provides distribution, consulting and outsourcing services to approximately 4,100 healthcare providers, including hospitals, the federal government and alternate care providers, contracting with them directly and through IHNs and GPOs. The company also provides logistics services to manufacturers of medical and surgical products.

GPOs and IHNs

GPOs are entities that act on behalf of a group of healthcare providers to obtain better pricing and other benefits than may be available to individual providers. Hospitals, physicians and other types of healthcare providers have joined GPOs to take advantage of improved economies of scale and to obtain services from medical and surgical supply distributors ranging from discounted product pricing to logistical and clinical support. GPOs negotiate directly with medical and surgical product suppliers and distributors on behalf of their members, establishing exclusive or multi-supplier relationships; however, GPOs cannot ensure that members will purchase their supplies from a particular distributor. O&M is a distributor for Novation, a GPO which represents the purchasing interests of more than 2,500 healthcare organizations. In 2006, the company executed a new five-year agreement with Novation. Sales to Novation members represented approximately 40% of the company s revenue in 2007 and 43% in 2006. The company is also a distributor for Broadlane, a GPO providing national contracting for more than 900 acute-care hospitals and more than 2,600 sub-acute-care facilities, including Tenet Healthcare Corporation, one of the largest for-profit hospital chains in the nation. Effective February 2007, the company executed a new five-year agreement with Broadlane. Sales to Broadlane members represented approximately 12% of O&M s revenue in both 2007 and 2006. The company is also party to a distribution agreement with Premier, a GPO representing more than 1,500 hospitals. Premier provides resources to support healthcare services, including group purchasing activities. Sales to Premier members represented approximately 19% and 15% of O&M s revenue in 2007 and 2006. The company s agreement with Premier is up for renewal in 2008.

IHNs are typically networks of commonly owned or managed healthcare providers that seek to offer a broad spectrum of healthcare services and geographic coverage to a particular market. IHNs are significant in the acute-care market because of their expanding role in healthcare delivery and cost containment and their reliance upon the hospital as a key component of their organizations. Because IHNs frequently rely on cost containment as a competitive advantage, IHNs have become an important source of demand for O&M s enhanced inventory management and other value-added services.

Individual Providers

In addition to contracting with healthcare providers at the IHN level and through GPOs, O&M contracts directly with individual healthcare providers and smaller networks of healthcare providers that have joined to negotiate terms.

Sales and Marketing

O&M s healthcare provider sales and marketing function is organized to support field sales teams throughout the United States. Local sales teams are positioned to respond to customer needs quickly and efficiently. Corporate account directors work closely with IHNs and GPOs to meet their needs and coordinate activities with individual members. The company also has an enterprise sales team that operates centrally and coordinates all the company s service offerings for customers of a certain size. The company s integrated sales and marketing strategy offers customers value-added services in logistics, information management, asset management and product mix management. O&M provides special training and support tools to its sales team to help promote programs and services.

Pricing

Industry practice is for healthcare providers, their IHNs or GPOs to negotiate product pricing directly with suppliers and then negotiate distribution pricing terms with distributors.

The majority of O&M s distribution arrangements compensate the company on a cost-plus percentage basis, under which a negotiated fixed-percentage distribution fee is added to the product cost agreed to by the customer and the supplier. The determination of this percentage distribution fee is typically based on purchase volume, as well as other factors, and usually remains constant for the life of the contract. In many cases, distribution contracts in the medical/surgical supply industry specify a minimum volume of product to be purchased and are terminable by the customer upon relatively short notice.

In some cases, the company may offer pricing that varies during the life of the contract, depending upon purchase volume, and as a result, the negotiated fixed-percentage distribution fee may increase or decrease over time. Under these contracts, customers distribution fees may be reset after a measurement period to either more or less favorable pricing based on significant changes in purchase volume. If a customer s distribution fee percentage is adjusted, the modified percentage distribution fee applies only to purchases made following the change. Because customer sales volumes typically change gradually, changes in distribution fee percentages for individual customers under this type of arrangement have an insignificant effect on total company results.

Pricing under O&M s CostTrack^{SM} activity-based pricing model differs from pricing under a traditional cost-plus model. With CostTrack^{SM}, the pricing of services is based on the costs to O&M of providing the services required by the customer. As a result, this pricing model more accurately aligns distribution fees charged with the costs of the individual services provided. In 2007, 32% of the company s revenue was generated from customers using CostTrack^{SM} pricing.

O&M also has arrangements under which incremental fees are charged for enhanced inventory management services, such as more frequent deliveries and distribution of products in small units of measure. Pricing for consulting and outsourcing services is generally based on the type and level of service provided.

Suppliers

O&M believes that its size, strength and long-standing relationships enable it to obtain attractive terms from suppliers and has well-established relationships with virtually all major suppliers of medical and surgical supplies. The company works with its largest suppliers to create operating efficiencies in the supply-chain through a number of programs which drive product standardization and consolidation for the company and its healthcare provider customers. By increasing the volume of purchases from the company s most efficient suppliers, the company provides operational benefits and cost savings throughout the supply-chain.

The company works very closely with its branded supplier base to enlist their participation in a variety of O&M supplier program offerings. O&M supplier programs provide for enhanced levels of support that are closely aligned with annual supplier objectives in the areas of product market share and sales growth attainment. O&M receives incentives from suppliers, including cash discounts for prompt payment, operational efficiency funding and performance-based incentives. Operational incentives are negotiated annually and are based on improved end-to-end supply-chain expenses realized by the suppliers. Suppliers participating in the company s supply-chain efficiency programs currently represent 58% of O&M s revenue.

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The company offers MediChoice®, O&M s private label brand of economical medical and surgical products and equipment. O&M partners with national name-brand manufacturers known for their quality and high service levels for the MediChoice® products to provide cost savings alternatives on over 1,400 highly commoditized products. MediChoice® supports a savings value and a comprehensive product portfolio for healthcare provider customers in combination with branded supplier partner offerings.

In 2007, sales of products of Covidien and Johnson & Johnson Health Care Systems, Inc. accounted for approximately 13% and 11%, respectively, of the company s revenue.

Information Technology

To support its strategic efforts, the company has implemented information systems to manage all aspects of operations, including order fulfillment, customer service, warehouse and inventory management, asset management, electronic commerce, and financial management. O&M believes its investment in and use of technology in the management of operations provides the company with a significant competitive advantage.

In 2006, O&M amended its agreement with Perot Systems Corporation to expand the outsourcing of its information technology operations and extend the agreement through 2014. This agreement includes the management and operation of information technology and infrastructure, as well as support, development and enhancement of all key business systems. The agreement provides for a major enterprise systems modernization project that will improve O&M s flexibility in serving its customers, and that will significantly increase systems capacity to support business growth. The company s relationship with Perot Systems Corporation began in 1998.

The company s technology strategy and expenditures focus on customer service, electronic commerce, data warehousing, decision support, supply-chain management, warehousing management, and sales and marketing programs, as well as significant enhancements to back office systems and overall technology infrastructure. O&M is an industry leader in the use of state-of-the-art electronic commerce technology to conduct business transactions with customers, suppliers and other trading partners. These capabilities in technology are built upon the foundation of the award-winning OMDirect SM Internet Order Fulfillment system, and the WISDOMSM knowledge management and decision support system.

Asset Management

In the medical/surgical supply distribution industry, a significant investment in inventory and accounts receivable is required to meet the rapid delivery requirements of customers and provide high-quality service. As a result, efficient asset management is essential to the company s profitability. O&M is focused on effective processes to optimize inventory and collect accounts receivables.

Inventory

The significant and ongoing emphasis on cost control in the healthcare industry puts pressure on suppliers, distributors and healthcare providers to manage their inventory more efficiently. O&M s response to these ongoing challenges has been to develop inventory management capabilities based upon proven planning techniques; to utilize a highly flexible client/server warehouse management system; to standardize product whenever possible; and to collaborate with supply-chain partners on inventory productivity initiatives, including vendor-managed inventory, freight optimization and lead-time reductions.

Accounts Receivable

The company believes its credit practices are consistent with those of other acute-care medical and surgical supply distributors. O&M actively manages its accounts receivable to minimize credit risk.

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Competition

The acute care medical/surgical supply distribution industry in the United States is highly competitive. The sector includes two major nationwide distributors: O&M and Cardinal Health, Inc. The company also competes with a smaller national distributor of medical and surgical supplies, Medline, Inc., and a number of regional and local distributors.

Competitive factors within the medical/surgical supply distribution industry include total delivered product cost, product availability, the ability to fill and invoice orders accurately, delivery time, services provided, inventory management, information technology, electronic commerce capabilities, and the ability to meet customer-specific requirements. O&M believes its emphasis on technology, combined with a customer-focused approach to distribution and value-added services, enables it to compete effectively with both larger and smaller distributors.

Direct-to-Consumer Supply Distribution Business

In 2005, O&M entered the direct-to-consumer (DTC) supply distribution business with its acquisition of Access Diabetic Supply, LLC (Access), a Florida-based distributor of diabetic supplies and products for certain other chronic diseases. The company s DTC supply business began operating under the trade name AOM Healthcare Solutions (AOM) in late 2007. AOM primarily markets blood glucose monitoring devices, test strips and other ancillary products used by diabetics for self-testing, mainly through direct-response advertising using a variety of media. AOM ships products directly to approximately 188,000 customers homes throughout the United States by mail or parcel service and manages the documentation and insurance-claims filing process for its customers, collecting most of its revenue directly from Medicare or private insurance providers, and billing the customer for any remainder. As a result, pricing is almost wholly dependent upon the reimbursement rates set by Medicare and private insurers. AOM does not manufacture products, but purchases its products from a number of suppliers.

The mail-order distribution of diabetic testing supplies is a fast-growing market that is experiencing rapid consolidation. The company s largest competitor in mail-order distribution, Liberty Medical, is the diabetes business unit of PolyMedica Corporation. Effective October 31, 2007, PolyMedica Corporation was acquired by Medco Health Solutions, Inc. The mail-order distribution industry, as a whole, competes with retail pharmacies, which are the most common distributors of diabetic supplies.

Other Matters

Regulation

The medical/surgical supply distribution industry is subject to regulation by federal, state and local government agencies. Each of O&M s distribution centers is licensed to distribute medical and surgical supplies, as well as certain pharmaceutical and related products. The company must comply with regulations, including operating and security standards for each of its distribution centers, of the Food and Drug Administration, the Occupational Safety and Health Administration, state boards of pharmacy, or similar state licensing and regulatory agencies. In addition, the DTC supply business must also comply with Medicare regulations regarding billing practices. O&M believes it is in material compliance with all statutes and regulations applicable to distributors of medical and surgical supply products and pharmaceutical and related products, including the Healthcare Insurance Portability and Accountability Act of 1996 (HIPAA), Medicare, Medicaid, as well as applicable general employment and employee health and safety laws and regulations.

Employees

At the end of 2007, the company had approximately 4,800 full-time and part-time teammates. O&M believes that ongoing teammate training is critical to performance, using Owens & Minor University, an in-house training program, to offer classes in leadership, management development, finance, operations and sales. Management believes that relations with teammates are good.

Available Information

The company makes its Forms 10-K, Forms 10-Q and Forms 8-K (and all amendments to these reports) available free of charge through the SEC Filings link in the Investor Relations content section on the company s Web site located at www.owens-minor.com as soon as reasonably practicable after they are filed with or furnished to the SEC. Information included on the company s Web site is not incorporated by reference into this Annual Report on Form 10-K.

Additionally, the company has adopted a written Code of Honor that applies to all of the company s directors, officers and teammates, including its principal executive officer and senior financial officers. This Code of Honor (including any amendment to or waiver from a provision thereof) and the company s Corporate Governance Guidelines are available on the company s Web site at www.owens-minor.com.

Item 1A. Certain Risk Factors

Set forth below are certain risk factors that the company believes could affect its business and prospects. These risk factors are in addition to those mentioned in other parts of this report.

Competition

The medical/surgical supply distribution industry in the United States is highly competitive. The company competes with another major national distributor, a smaller nationwide distributor, and a number of regional and local distributors. Competitive factors within the medical/surgical supply distribution industry include total delivered product cost, product availability, the ability to fill and invoice orders accurately, delivery time, services provided, inventory management, information technology, electronic commerce capabilities, and the ability to meet special requirements of customers. The company s success is dependent on its ability to compete on the above factors and to continually bring greater value to customers at a lower cost. These competitive pressures have had and may continue to have a material adverse effect on the company s results of operations.

Dependence on Significant Customers

In 2007, the company s top ten customers represented approximately 20% of its revenue. In addition, in 2007, approximately 70% of the company s revenue was from sales to member hospitals under contract with its three largest GPOs: Novation, Broadlane and Premier. The company could lose a significant customer or GPO relationship if an existing contract expires without being replaced or is terminated by the customer or GPO prior to its expiration (if permitted by the applicable contract). Although the termination of the company s relationship with a given GPO would not necessarily result in the loss of all of the member hospitals as customers, any such termination of a GPO relationship or a significant individual customer relationship could have a material adverse effect on the company s results of operations.

Dependence on Significant Suppliers

The company distributes approximately 180,000 products from over 1,200 suppliers and is dependent on these suppliers for the supply of products. In 2007, sales of products of the company s ten largest suppliers accounted for approximately 57% of revenue. The company relies on suppliers to provide agreeable purchasing and delivery terms and sales performance incentives. The company s ability to sustain adequate gross margins has been, and will continue to be, partially dependent upon its ability to obtain favorable terms and incentives from suppliers, as well as suppliers continuing use of third-party distributors to sell and deliver their products. A change in terms by a

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significant supplier, or the decision of such a supplier to distribute its products directly to hospitals rather than through third-party distributors, could have a material adverse effect on the company s results of operations.

Bankruptcy, Insolvency or other Credit Failure of a Significant Customer

The company provides credit, in the normal course of business, to its customers. The company performs ongoing credit evaluations of its customers and maintains reserves for credit losses. The bankruptcy, insolvency or other credit failure of any customer at a time when the customer has a substantial balance due to the company could have a material adverse effect on the company s results of operations.

Changes in the Healthcare Environment

O&M, its customers and its suppliers are subject to extensive federal and state regulations relating to healthcare, as well as the policies and practices of the private healthcare insurance industry. In recent years, there have been a number of government and private initiatives to reduce healthcare costs and government spending. These changes have included an increased reliance on managed care; cuts in Medicare funding; consolidation of competitors, suppliers and customers; and the development of larger, more sophisticated purchasing groups. Medicare has recently introduced competitive bidding in certain limited markets for the pricing of diabetic testing and monitoring supplies. Price changes from competitive bidding are to be in effect in mid-2008, though they will affect an insignificant portion of AOM s customer base. The company expects the healthcare industry to continue to change significantly and these potential changes, such as reduction in government support of healthcare services, adverse changes in legislation or regulations, and reductions in healthcare reimbursement practices, could have a material adverse effect on the company s results of operations.

Operating Margin Initiatives

Competitive pricing pressure has been a significant factor in recent years and management expects this trend to continue. In addition, suppliers continue to seek more restrictive agreements with distributors, resulting in lower product margins and reduced profitability. The company is working to counteract the effects of these trends through several margin initiatives, including consulting and outsourcing services, through the OMSolutions^{SM} business unit, and MediChoice®, the company s private label brand of select medical/surgical products. In addition, the company offers customers a wide range of value-added services, including PANDAC®, Wisdom Gold^{SM}, QSight and others, all of which enhance profitability. The company also works with suppliers on programs to enhance gross margin. If these margin initiatives fail to produce anticipated results, the company s results of operations could be materially adversely affected.

Reliance on Information Systems and Technological Advancement

The company relies on information systems to receive, process, analyze and manage data in distributing thousands of inventory items to customers from numerous distribution centers across the country. These systems are also relied on for billings and collections from customers, as well as the purchase of and payment for inventory from hundreds of suppliers. The company s business and results of operations may be adversely affected if these systems are interrupted or damaged by unforeseen events or if they fail for any extended period of time. In addition, the success of the company s long-term growth strategy is dependent upon its ability to continually monitor and upgrade its information systems to provide better service to customers. A third-party service provider, Perot Systems Corporation, is responsible for managing a significant portion of the company s information systems, including key operational and financial systems. The company s business and results of operations may be materially adversely affected if the third-party service provider does not perform satisfactorily.

Internal Controls

Pursuant to Section 404 of the Sarbanes-Oxley Act, management will be required to deliver a report in the company s Annual Report on Form 10-K for the fiscal year ending December 31, 2008, similar to the one

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delivered herein, that assesses the effectiveness of the company s internal control over financial reporting. The company also is required to obtain an audit report of its independent registered public accounting firm on the operating effectiveness of internal controls. The company has undertaken substantial efforts to assess, enhance and document its internal control systems, financial processes and information systems and will continue to do so in the future to prepare for the required annual evaluation process. Although the company believes it has adequate internal controls and will meet its obligations, there can be no assurance that it will be able to complete the work necessary for management to issue its report in a timely manner or that management or the company s independent registered public accounting firm will conclude that the company s internal controls are effective.

Item 1B. Unresolved Staff Comments

None.

Item 2. Properties

In February 2006, O&M relocated its corporate headquarters to a newly-constructed office building owned by the company, located in Mechanicsville, Virginia, a suburb of Richmond, Virginia. The company leases office and warehouse space from unaffiliated third parties for its 48 distribution and service centers across the United States; offices and shipping facilities for its DTC supply distribution business in southern Florida; and small offices for sales and consulting personnel across the United States. In addition, the company has a warehousing arrangement in Honolulu, Hawaii, with an unaffiliated third party, and leases space on a temporary basis from time to time to meet its inventory storage needs. In the normal course of business, the company regularly assesses its business needs and makes changes to the capacity and location of distribution centers. The company believes that its facilities are adequate to carry on its business as currently conducted. A number of leases are scheduled to terminate within the next several years. The company believes that, if necessary, it could find facilities to replace these leased premises without suffering a material adverse effect on its business.

Item 3. Legal Proceedings

As previously reported, in September 2004, the company received a notice from the Internal Revenue Service (IRS) proposing to disallow, effective for the 2001 tax year, certain reductions in the company s tax-basis last-in, first-out (LIFO) inventory valuation. The company filed an appeal with the IRS in December 2004 to contest the proposed adjustment. In December 2007, the company entered into a settlement agreement with the IRS for the 2001 tax year. In an effort to resolve outstanding issues in later years, concurrent with the settlement agreement, the company filed a request with the National Office of the IRS for permission to change its method of accounting for LIFO inventories for tax purposes. The settlement did not have a material effect on the company s results of operations or cash flows.

In addition to the foregoing matter, the company is subject to various other legal actions that are ordinary and incidental to its business, including contract disputes, employment, workers compensation, product liability, regulatory and other matters. The company establishes reserves from time to time based upon periodic assessment of the potential outcomes of pending matters. In addition, the company believes that any potential liability arising from employment, product liability, workers compensation and other personal injury litigation matters would be adequately covered by the company s insurance coverage, subject to policy limits, applicable deductibles and insurer solvency. While the outcome of legal actions cannot be predicted with certainty, the company believes, based on current knowledge and the advice of counsel, that the outcome of these currently pending other matters, individually or in the aggregate, will not have a material adverse effect on the company s financial condition or results of operations.

Item 4. Submission of Matters to a Vote of Security Holders

During the fourth quarter of 2007, no matters were submitted to a vote of security holders.

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Part II

Item 5. Market for Registrant s Common Equity and Related Stockholder Matters

Owens & Minor, Inc. s common stock trades on the New York Stock Exchange under the symbol OMI. As of February 21, 2008, there were approximately 5,400 common shareholders of record. The company believes there are an estimated additional 33,000 beneficial holders of its common stock. See Quarterly Financial Information under Item 15 for high and low closing sales prices of the company s common stock.

The following performance graph compares the performance of the company s common stock to the S&P 500 Index and an Industry Peer Group (which includes the companies listed below) for the last five years.

5-Year Total Shareholder Return

This graph assumes that the value of the investment in the common stock and each index was $100 on December 31, 2002, and that all dividends were reinvested.

(Data provided by Standard & Poor s)

	Base Period 12/2002	**12/2003**	**12/2004**	**12/2005**	**12/2006**	**12/2007**
Owens & Minor, Inc.	100	135.64	177.35	176.45	204.30	282.22
S&P 500 Index	100	128.68	142.69	149.70	173.34	182.86
Former Peer Group	100	109.91	108.25	141.91	141.45	150.87
Current Peer Group	100	111.98	113.29	142.05	141.88	149.12

The Industry Peer Group, weighted by market capitalization, consists of companies engaged in the business of healthcare product distribution. The Current Peer Group includes pharmaceutical distribution companies: AmerisourceBergen Corporation, Cardinal Health, Inc., and McKesson Corporation; and medical product distribution companies: Henry Schein, Inc., Patterson Companies, Inc., and PSS World Medical, Inc. In order to provide a more meaningful comparison, Patterson Companies, Inc. was added and Owens & Minor, Inc. was removed from the Current Peer Group.

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Item 6. Selected Financial Data

(in thousands, except ratios and per share data)

	2007	2006	2005	2004	2003
Summary of Operations:					
Revenue	**$ 6,800,466**	$ 5,533,736	$ 4,822,414	$ 4,525,105	$ 4,244,067
Net income	**$ 72,710**	$ 48,752	$ 64,420	$ 60,500	$ 53,641
Per Common Share:					
Net income basic	**$ 1.81**	$ 1.22	$ 1.63	$ 1.55	$ 1.52
Net income diluted	**$ 1.79**	$ 1.20	$ 1.61	$ 1.53	$ 1.42
Average number of shares outstanding basic	**40,250**	39,860	39,520	39,039	35,204
Average number of shares outstanding diluted	**40,656**	40,467	40,056	39,668	39,333
Cash dividends	**$ 0.68**	$ 0.60	$ 0.52	$ 0.44	$ 0.35
Stock price at year end	**$ 42.43**	$ 31.27	$ 27.53	$ 28.17	$ 21.91
Book value at year end	**$ 15.03**	$ 13.60	$ 12.84	$ 11.65	$ 10.53
Summary of Financial Position:					
Working capital	**$ 521,393**	$ 596,267	$ 405,684	$ 433,945	$ 385,743
Total assets	**$ 1,515,080**	$ 1,685,750	$ 1,239,850	$ 1,131,833	$ 1,045,748
Long-term debt	**$ 283,845**	$ 433,133	$ 204,418	$ 207,476	$ 209,499
Shareholders equity	**$ 614,359**	$ 547,454	$ 511,998	$ 460,256	$ 410,355
Selected Ratios:					
Gross margin as a percent of revenue	**10.5%**	10.8%	10.7%	10.2%	10.3%
Operating earnings as a percent of revenue	**2.1%**	1.9%	2.4%	2.4%	2.5%
Average inventory turnover	**9.7**	8.9	9.8	9.9	10.3
Current ratio	**1.9**	1.9	1.8	2.0	2.0

Item 7. Management s Discussion and Analysis of Financial Condition and Results of Operations

2007 Financial Results

Overview. In 2007, the company earned net income of $72.7 million, increased from $48.8 million in 2006, and $64.4 million in 2005. Net income per diluted share was $1.79 in 2007, as compared with $1.20 in 2006, and $1.61 in 2005. Net income for 2006 included a pre-tax charge of $11.4 million related to a loss on the early retirement of debt, as the company refinanced $200 million in debt. Operating earnings, which were $143.2 million in 2007, improved from $102.8 million in 2006 and $117.4 million in 2005. As a percentage of revenue, operating earnings were 2.1%, 1.9%, and 2.4% in 2007, 2006 and 2005. Operating earnings in both 2007 and 2006 were impacted by the cost of integrating the acquired acute-care distribution business of McKesson Medical-Surgical