

# FINAL TRANSCRIPT

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## **LTM - Q3 2010 Life Time Fitness Earnings Conference Call**

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*Life Time Fitness, Inc. - CEO, Founder, Chairman of the Board*

**Mike Robinson**

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## CONFERENCE CALL PARTICIPANTS

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**Michael Lasser**

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## PRESENTATION

**Operator**

Good day ladies and gentlemen, and welcome to the Q3 2010 Life Time Fitness earnings conference call. My name is Jeremy and I will be your operator for today. At this time, all participants are in listen-only mode. Later, we will conduct a question and answer session. (Operator Instructions). I would now like to turn the conference over to your host for today, Mr. John Heller, Senior Director of Investor Relations and Treasurer. Please proceed, sir.

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**John Heller** - *Life Time Fitness, Inc. - Sr. Dir. of IR, Treasurer*

Thanks, Jeremy. Good morning, and thank you for joining us on today's conference call to discuss the third quarter 2010 financial results for Life Time Fitness. We issued our earnings press release this morning. If you did not obtain a copy, you may access it at our website, which is [lifetimefitness.com](http://lifetimefitness.com).

Concurrent with the issuance of our third quarter results, we have filed a Form 8-K with the SEC, which also includes the press release. On today's call, Bahram Akradi, our Chairman, President, and CEO, will discuss key highlights from our third quarter and our operations. Following that, Mike Robinson, our CFO, will review our financial highlights. Once we have completed our prepared remarks, we will answer your questions until 11.00 AM Eastern Time. At that point in the call, Jeremy will provide instructions on how to ask a question.

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I will then close with a tentative date of our fourth quarter 2010 earnings call. Finally, a replay of this teleconference will be available at approximately 1.00 PM Eastern Time today. Today's conference call contains forward-looking statements and future results could differ materially from those statements made.

Actual results may be affected by many factors, including the risks and uncertainties identified in our SEC filings. Certain information in our earnings release and information disclosed on this call constitute non-GAAP financial measures, including EBITDA and free cash flow. We have included reconciliations of the differences between GAAP and non-GAAP measures in our earnings release and our Form 8-k. Our required information about our non-GAAP data is included in our Form 8-K. With that, let me now turn the call over to Bahram Akradi. Bahram?

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**Bahram Akradi** - *Life Time Fitness, Inc. - CEO, Founder, Chairman of the Board*

Thanks, John. I am excited to provide you with my thoughts and perspective on our third quarter of 2010. Late last year, the Company put in place a number of strategies to allow us to win in this challenging environment. A year later, we can say that those strategies are working.

Our same-store sales, operating margins, revenue per member and attrition rate all improved for the quarter and year-to-date compared with 2009. We believe this is a direct result of the efforts of our team and the effectiveness of the substantial investments we have made in the business. We are determined to demonstrate our value proposition and connect with our members in the best -- and connect with our members in the best way imaginable. Attrition for the quarter was down 100 basis points versus a year ago, bringing our trailing 12-month rate to 37.1%. This is down from 40.6% the same time last year. We're pleased with the results as we relentlessly drive towards our goal of 36%. That said, with the continuing economic headwinds, we have never had to work harder to attract and retain members. To accomplish this, we have been proactive on many fronts.

We have invested heavily in our value proposition with enhanced program and service offerings and mind-blowing value pricing in our cafes, spas and member activities. We have invested in member engagement and connectivity ensuring that new members get involved and stay connected to the club in ways that matters to them. In fact, we have brought over 500 people from across the company to Minneapolis today and tomorrow for what we call our Company's Inside Expo, which allows us -- which allows our key center leadership to gain first-hand reinforcement of many initiatives and businesses we have available to our membership to drive the value and engagement we believe is so critical to our success.

While this is a significant cost, we firmly believe it is the right thing to do in this environment. In summary, our value proposition and engagement initiatives are progressing well. Now, on the other hand, we continue to see persistent difficulties in attracting and retaining new members without substantial effort. We have had to keep enrollment fees low to attract new members and invest heavily in programming to see improvement in retention. As we have said all year, we don't expect this to change anytime soon. However, over the last two years, we have run our business with the expectation of headwinds and we believe our results demonstrate that we are winning, and we also firmly believe we can continue to win.

Our revenues for the quarter were strong, growing over 10% above a year ago. This growth is coming primarily from our in-center businesses. This performance is driven by our value proposition -- by value pricing and engagement initiatives centered around children's activities which peak during the summer months. While these revenues come at lower margin than our dues, we believe that an increased use of our services is key in keeping memberships connected and engaged, which is reflected in our improved retention rate.

We are pleased with our revenue growth, which was over 8% top-line year-to-date. We consider mid to high single-digit growth, a reasonable rate through 2011. As we think about our growth beyond that, our expectations are unchanged from last year. Long-term, our goal is to grow our top-line at least low double digits per year and leverage that growth with higher net income and EPS growth. We expect this growth to come not only from new club offerings, but also from the investment we are making



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in our businesses. In conclusion, while I still am not bullish on the consumer environment, I have never felt better about the Company and our management team.

Since the economic downturn, we have executed on almost every aspect of our plan. Attrition has improved. We have strengthened our balance sheet, and we have brought the Company to a free cash flow positive, while continuing to grow the businesses. We will continue to examine every aspect of our business to find better, more creative and less capital intensive ways to grow our business and drive member involvement. With that, I will turn the call to Mike Robinson, our Chief Financial Officer. Mike?

**Mike Robinson** - *Life Time Fitness, Inc. - CFO*

Thanks, Bahram. As Bahram indicated, we continued to show solid improvement in several key operating and financial metrics. Let me start with some additional details on attrition and retention. For the quarter, our attrition rate was 9.6%, as compared to 10.6% last year. This includes approximately 40 basis points of improvement related to our change in methodology that went into affect on April 1st. That is, we no longer count those potential members that elect to cancel during their 14-day trial as members or attritions.

We continue to shoot for an internal goal of 36% or better total year attrition over the next several quarters, and to continue the momentum we established in the first nine months of this year. We expect this improvement to get more challenging as we go against more difficult retention comparisons. What is inherent in our guidance, which I'll talk about in a few moments, is about a 50 to 60 basis point improvement over last year's 10.8% fourth quarter results. This includes approximately 30 basis points for our methodology change.

Early experience shows the Q4 retention improvement will be more challenging due in part to lagging attrition from the typical end of summer pool season and the beginning of school membership movements. Our improvement in attrition lead us to be slightly ahead of our net membership growth expectations in the quarter. We finished the quarter with 622,698 memberships. This is a 5.4% increase from the third quarter of 2009. While down approximately 9,000 memberships since Q2, it is much better than the 17,500 membership loss from Q2 to Q3 2009.

For the third quarter, we grew the net balance of flex memberships by approximately 9,000 units to approximately 63,000 total units. Our membership activity lead to total revenue of \$238.3 million for the quarter, which is up 11.2% from last third quarter. Our main revenue drivers include growth of our in-center revenue stemming primarily from our mind-blowing value pricing initiatives in our spas, cafes and kids activity programming, and our ramp of the two large centers we've opened so far this year and the three large centers we opened in 2009. The total number of open centers at September 30, 2010 was 89 compared with 84 at September 30, 2009. Of the 89 centers, 53, or 60%, are our large current model and 66, or 74%, of all of our centers have been open three years or more, which we classify as mature centers.

We now operate 8.7 million square feet of health and fitness centers. Membership dues grew by 7.2% for the quarter, which outpaced our membership growth of 5.4%. Our goal is to continue to have dues growth in excess of membership growth. We accomplish this by improving our average dues via selling more memberships at higher priced centers, providing more valued upgrade opportunities and upgrading more memberships to couples and families. We had very little price increase in the first nine months of 2010. Our powerful dues annuity stream accounts for 66% of our total revenue.

In-center revenue continues to perform well. In-center revenue grew by 17.5% in the quarter. The growth was across the board, including our kids' programming which peaks in the summer months. Personal training, which was up 16%, and life spa, which was up 24% leading the way. Again, we are strategically driving this growth through lower price points on many services to drive volume and enhance member connectivity and involvement, and thus improve member retention. Our revenue metrics continue to show improvement during the quarter. Third quarter same-store sales was 6.6%, the strongest growth since early



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2007. And our 37 month mature same-store sales came in at 4%. Both of these metrics, as expected, showed improvements sequentially driven by in-center revenue.

With respect to revenue per membership, we generated \$374 per membership, which was up 4.4%. This was driven by a slight mix increase and our in-center businesses. In-center revenue per membership of \$112 was up 11.9% in the quarter. For perspective, this comes off \$112 second quarter, thus tying the record for the highest quarterly in-center revenue per membership in our history. We believe this is further evidence of our connectivity with our members, as well as the new programs and changes in program pricing. Our members are reacting favorably to our mind-blowing value proposition and our onboarding connection through our affinity program called to our Life Time Bucks. I'd like to move to some discussion on our cost structure.

Overall operating profit margin in Q3 improved 40 basis points to 19.1% from 18.7% in Q3 2009. Center operating costs were up about 140 basis points due primarily to the same three drivers we've seen all year. First, we continue to incur a higher membership acquisition cost as we use lower promotional enrollment and administrative fee pricing to stimulate new member demand. Second, our strong in-center revenue growth comes at lower margins. And finally, we continue to make investments in our centers to enhance the member experience and improve retention.

These investments range from the expanded hours of operations for various programs to more fitness class offerings to the reward and retention affinity programs like Life Time Bucks. Marketing and advertising costs were down 10 basis points due to our controlled promotions and more effective marketing. We kept these costs lower to help offset our planned use of lower enrollment fees, which result in the higher net membership acquisition cost.

Central overhead costs and G&A were flat as a percentage of revenue at 4.5%. The dollar increase is a reflection of some of the limited investment in overhead structure to help drive the retention and connectivity initiatives at our centers, as well as opportunities to grow other healthy way of life-related businesses. G&A is 50 basis points lower year-to-date reflecting our continued focus on efficiency. We also saw leverage in other operating expense as we had a reduction in construction-related expenses incurred last year that was partially offset by costs associated with the acquired athletic events, such as the Chicago Triathlon. We continue to see significant leverage and depreciation and amortization as we continue to grow well ahead of square feet expansion. Now I'd like to move to a quick capital structure update.

We've continued to de-lever our balance sheet. The key driver to this is the continued power of our cash flow from operations, which totaled \$45.4 million for the quarter, up \$5.1 million from Q3 2009. And was \$146.1 million year-to-date, up over \$7 million from our 2009 year-to date results. We also generated our seventh consecutive quarter of free cash flow. For the quarter, we generated \$7.5 million of free cash flow, and year-to-date we're at \$60 million. This excludes approximately \$15 million in cash spent on acquisitions year-to-date. These small purchases in Q2 and Q3 include a small fitness center in Houston, two marquee events businesses, the Chicago Triathlon and associated races and the Leadville 100 Mountain Bike Race series, and a yoga instruction training curriculum. They had a very small revenue and net income impact on our net results. These acquisitions continue to broaden our strategic offerings as a healthy way of life company. Debt is up \$3.1 million in the third quarter; however, we've been building our cash balance in anticipation of retiring approximately \$70 million of mortgage debt at maturity next year.

Our cash balance grew another \$9 million in the quarter, and has grown \$27 million since December 31st last year to \$33.5 million. As of September 30, we have \$382 million outstanding, including letters of credit on our \$470 million revolver. That leaves over \$120 million in cash and revolver availability. Our net debt to total capital came down 110 basis points from the second quarter to 42.4% at the end of the second quarter, which compares favorably to the 47% at the beginning of the year. Our covenant calculations for the quarter continue to show significant improvement in significant room versus our covenant limits and we remain well positioned for the debt maturities near term.

Our focus remains on de-levering the balance sheet. We continue to monitor the various debt markets, however, our baseline assumption is that we do not answer into any significant new financings in 2010. By the way, we now have 37 owned facilities with an asset cost on our balance sheet well in excess of \$750 million with no mortgage financing. Regarding capital expenditures,



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we paid for approximately \$38 million of CapEx in the third quarter and our year-to-date total is \$86.1 million. This is comprised of approximately \$60 million for growth and \$26 million for maintenance and infrastructures. Currently, we have one center left to open this year. This large center is planned for December and will be in Centennial, Colorado, a suburb of Denver.

For 2010, we expect to spend approximately \$110 million to \$130 million on capital expenditures for club growth and maintenance CapEx. This will be comprised of approximately \$80 million to \$95 million for growth CapEx and \$30 million to \$35 million for maintenance and infrastructure support. We've increased our CapEx spend expectations \$10 million as we have moved up our construction timing on some of our planned 2011 and 2012 openings. This capital expenditure expectation excludes the acquisitions we've completed so far this year.

Now, I'd like to give you some other key P&L highlights. Interest expense net of interest income decreased slightly sequentially \$6.8 million from \$6.9 million in the second quarter.

Our tax rate for the quarter was 40.2%, which was higher than the 36.8% in Q3 2009. As a reminder in 2009, our lower tax rate was due to a reduction in tax accruals resulting from a favorable outcome from a federal tax audit. We expect our effective tax rate in 2010 to be at or slightly above 40%. Our EBITDA margin decreased to 29.1% as compared to 29.7% for Q3 2009 due primarily to the increase in in-center operating expenses. Our net income for the quarter was \$23.4 million, which was 13.3% growth over Q3 2009. Our net income margin increased 20 basis points to 9.8%. Weighted average fully diluted shares totaled 41.3 million shares for the third quarter. We expect our average diluted shares to increase slightly over the rest of the year.

Overall, we achieved diluted EPS of \$0.57 in the third quarter compared to \$0.51 Q3 2009. A few balance sheet variances to note include a decrease of approximately \$3 million in pre-creation expenses and other current assets from the second quarter due primarily to a reduction in prepaid insurance and other prepaid accounts as we work through the year. Deferred membership origination costs, both short and long-term, as well as deferred revenue, continue to decline due to the low enrollment fee pricing and the result in increase in membership acquisition costs from the commissions and related direct expenses in excessive enrollment fees, which we expense in the period incurred.

Other assets increased to about \$5 million since Q2 due primarily to the small acquisitions we made in Q3. Current maturities of long-term debt have increased to above \$77 million as we reclassified the Starwood or formerly Teacher's Mortgage Debt to current as it is due and payable July 1st, 2011. As I stated earlier, we plan to pay this mortgage debt off with cash and cash flow from operations. Accrued expenses have increased about \$4 million in the quarter related primarily to increases in accrued real estate taxes. Before I move to our updated guidance, as a reminder, we have a senior management restricted stock performance incentive plan in place for 2011 and 2012. The 50% and 100% performance EPS hurdles to earn the incentive requires significant performance improvement over the 2008, 2009 results, and must fully absorb up to \$20.6 million of compensation expense associated with the grant.

Since we believe these targets to be aggressive goals in excess of our current baseline expectations, we have not recognized any compensation expense associated with the grant, nor has any share amount been included in our diluted -- in our total diluted shares. We re-evaluate the probability of achieving these goals each quarter. We have not included any expense or additional share count in our guidance. Let me discuss our updated financial guidance for 2010. While pleased with where we are at this far through the year, it is important to note that we have hard work ahead of us in this environment, including a challenging quarter for member retention and dues growth. Therefore, we expect our revenue will grow to \$900 million to \$910 million, up from \$890 million to \$905 million.

We brought our guidance up \$5 million to \$10 million based primarily on our in-center revenue results. We anticipate our net income will grow to approximately \$81 million to \$83.5 million, up from previous guidance of \$79 million to \$81 million. We expect our diluted EPS will grow to \$1.98 to \$2.04, up from \$1.92 to \$1.98 per share. While we expect total year operating margin to show good improvement, incorporated in this guidance is some operating margin decline in Q4 as we expect increase pre-sale expenses and marketing expenses for our Q4 and early 2011 center openings.



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We will also continue executing on our value proposition and connectivity initiatives, and the results in investments we are making, such as the Expo Bahram mentioned earlier, to differentiate Life Time Fitness to position us for further improvement in this environment. As we look to 2011, we plan to give our usual next-year guidance on our February call. However, as we are currently in the planning process, here are some things we expect. We expect the same economic headwinds and thus plan to sustain or potentially grow the programs and investments we are making to further differentiate Life Time Fitness, its value proposition and the connectivity, engagement and retention initiatives.

We currently plan to open three large centers next year, including on Syosset on Long Island, New York in Q1. We plan to continue our prudent balance sheet management targeting to de-lever to approximately a 2 to 1 EBITDA leverage ratio. We believe this will deliver mid to high-single digit revenue growth and modest net income leverage. Most importantly, it will continue to position our company very well for growth and margin expansion as we look to the future. That concludes our prepared remarks regarding the third quarter 2010 financial results. We are pleased to take your questions now.

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## QUESTIONS AND ANSWERS

### Operator

(Operator Instructions). Our first question comes from Scott Hamann from KeyBanc Capital Markets. Please proceed.

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### Scott Hamann - KeyBanc Capital Markets - Analyst

Good morning, guys. Just a question on the membership dues spread. It seems like it kind of narrowed a little bit this quarter. Is there any flexibility you had in price increases or how should we think about that trend developing in the next several quarters?

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### Bahram Akradi - Life Time Fitness, Inc. - CEO, Founder, Chairman of the Board

This is Bahram. We have no intention of increasing any of our rack rate on any of our clubs. I think there might be one or two clubs that we will make adjustments. Other than that, at large, we're going to keep the rack rate the same. We might make some adjustments on the members that are paying substantially below the rack rate, but it's going to be a very, very small adjustment in the number of people who would get that.

And the increase in the dues, in my opinion, is going to be primarily a function of members who are paying below the rack rate attritioning out, being replaced by the people coming in with a full rack rate since we are not discounting for 26 and under and some of the other stuff. So I do see an increase in our dues revenue still gapping the membership count in at least in the next several quarters, I think you should continue to see some of that, but it's not a surprise for it to narrow down since we have not been doing any rack rate increases at all for almost a couple years.

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### Mike Robinson - Life Time Fitness, Inc. - CFO

Especially given the environment. Obviously we watch -- we meet, and Bahram and his team meet, weekly. In fact, in some cases daily looking at price and in other variations. And in this environment, from a rack rate perspective, we still don't feel that it's conducive to take rate up.

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### Scott Hamann - KeyBanc Capital Markets - Analyst

Okay. And then just a follow-up on center ops, Mike, can you talk about the 150 basis point de-leverage that you talked -- you talked about some of the buckets. Can you quantify what some of those buckets were and how they've changed over the last

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couple of quarters? How much is mix really impacting it? How much is this spending really impacting it? And how do you expect those buckets to change as we go over the next several quarters?

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**Mike Robinson** - *Life Time Fitness, Inc. - CFO*

Sure. I mentioned three elements to this. The first element is higher member acquisition costs that come from the fact that our commissions and other direct-related selling expenses are in excess of enrollment fees. That's been high all year. We expect it to remain high in the next quarter. It hasn't moved significantly, meaning that it's just been high. Again, it's been the single largest factor in the -- in that center operating margin degradation. As we lap that and go into next year, I would expect that it's going to get better just from a simple arithmetic perspective. But until -- it's going to depend really economically into whether we actually see some improvement in that.

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**Bahram Akradi** - *Life Time Fitness, Inc. - CEO, Founder, Chairman of the Board*

We don't see it getting worse.

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**Mike Robinson** - *Life Time Fitness, Inc. - CFO*

The second area is the fact that our in-center revenues have grown at double-digit rates. In fact, 17.5% top line growth in the second quarter. That's the highest growth rate of the -- in the three quarters we've had this year. And those -- those revenues have come in at a lower margin, significantly lower margin, than reduced margin. And with some of the pricing changes, the strategic pricing changes that we have made in center to drive more of these engagement initiatives, that margin rate on those services has actually come down.

So over the three quarters, we've seen that as an increasing amount of that center operating expense dues degradation. The third area are just all of the things that we're doing at the club level to improve the value and the member experience. And those things range from expanded hours in certain areas to more and more classes to the use of affinity programs. And those have grown from the first quarter to the second quarter to the third quarter. And in this environment, we continue to expect that we're going to invest in those types of value differentiators into the future.

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**Operator**

Our next question comes from Michael Lasser from Barclays Capital. Please proceed.

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**Michael Lasser** - *Barclays Capital - Analyst*

Good morning, thanks a lot for taking my question. On the increase in in-center revenue and all the effort that's going on to boost that spending, how are you able to discern the return on some of those initiatives, because theoretically as you worked into -- as attrition peaked up and you worked into more committed members, their in-center revenue spending is higher so you would have gotten some growth by virtue of that. So I'm just trying to understand where the recent growth has come from and how you are getting a return on those expenditures?

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**Bahram Akradi** - *Life Time Fitness, Inc. - CEO, Founder, Chairman of the Board*

I'm going to take this one for you. The first and most important thing is to offer the right product that matches our branding and positioning that we want to establish for Life Time for the customer. So the driving factor in the decision-making is delivering the best possible product in each area of the interest of our customer. Next, we work on trying to make sure that comes at a

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mind-blowing value, and then we work on making sure we have some level of margin on that new revenue so we are not continually adding revenue with no margin if it's in-center. And the decisions are fairly easy because we're focusing on the customer and making sure we give them what they want. While I am answering your question, I am going to elaborate on a little more for everybody else.

We keep talking about economy being tough, macro economics being tough; it's really a function of the heavy, heavy unemployment. As you guys all know, that's a headwind for membership-type business. We have two choices. We can reduce dues, cut prices like everybody else, and cut services and programs, or, at Life Time, as always, we have chosen to do the right thing by customer. Instead, we have decided to add value not by cutting prices, but by adding programming, just like Mike said, adding more free-time on the climbing walls that adds labor for us, adding more time in the pools for the families to be able to get in the pool areas. That adds more labor around lifeguards and people maintaining the facilities.

So altogether, we are more than satisfied with our strategy. We would like to continue on, we will continue on, on improving the programs for our members, as long as we continue as always and meet our internal budgets, internal goals. We feel like we're on track. We set goals, we achieve our goals, and those goals are both based on achieving our internal budgets and numbers. And two, most importantly, achieving the customer satisfaction we are looking for. So if you are trying to come at this just from the number standpoint, what decision can we make to increase the margin, if it's not the right decision for the customer, we are not going to make that decision here.

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**Michael Lasser** - Barclays Capital - Analyst

Thanks a lot for the detail. One quick follow-up question. Can you reconcile some of the comments about -- well, three new centers next year, but also accelerating the longer-run outlook for center growth and that's why CapEx is being -- moving up for this year?

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**Bahram Akradi** - Life Time Fitness, Inc. - CEO, Founder, Chairman of the Board

Mike will take that.

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**Mike Robinson** - Life Time Fitness, Inc. - CFO

Yeah. The reconciliation right now, we added about \$10 million to our CapEx guidance for this year. That's just simply moving the opening dates for planned 2011 openings up a few months. What that does is accelerate some of the construction costs that will occur in 2010. That same comment reflects on a center that we looked at and have the ability to start the construction a little earlier for 2012. So there is some construction expense that will occur, and we will absorb in the fourth quarter of this year for that.

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**Operator**

Our next question comes from Tony Gikas from Piper Jaffray. Please proceed.

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**Anthony Gikas** - Piper Jaffray - Analyst

Hey, guys. A couple questions. Could you just comment a little bit on how you expect interest expense to trend through the next year? Second, how quickly can you start to ramp new center openings and have you been working on new site selection and that sort of thing? And then third question, just the ad and marketing spending Q4, will that follow the continued trends to be down a little bit?

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**Mike Robinson** - *Life Time Fitness, Inc. - CFO*

I'm going to take number one and number three, Tony, and let Bahram talk about the second one. Interest expense should -- it will trend a little bit lower as you move through 2011, although I don't expect debt levels to change too much here in the short-term as we build our cash. So short-term, I don't expect that they're going to trend too much lower. But once we payoff at midyear the Starwood, we should see it trending a little bit lower.

**Bahram Akradi** - *Life Time Fitness, Inc. - CEO, Founder, Chairman of the Board*

Until we refinance.

**Mike Robinson** - *Life Time Fitness, Inc. - CFO*

Yeah, until we would refinance our revolver. Your question on marketing spend, like I said in the prepared comments, we would expect that to go up a little bit in the fourth quarter. And the reason we expect that is we've got pre-sale activity. We're hot and heavy in the pre-sale activity in Centennial and Syosset, which -- and that pre-sale just opening. So there'll be quite a bit, especially in a market like Long Island where we've got -- it's really the first -- we've got two in New Jersey, but the first one in Long Island. So we'll be certainly spending some awareness dollars in that market. So I would -- you should expect that to go up in the fourth quarter. Bahram?

**Bahram Akradi** - *Life Time Fitness, Inc. - CEO, Founder, Chairman of the Board*

And the -- we still have a full team of people working on a whole laundry list of deals we're working on. We have many deals queued up. We could start an unplanned construction for a particular club literally within months. So we have the ability to ramp up as we see it appropriate, Tony, with our managing of our total objectives, which includes the balance sheet, the refinancing and all of those things where we are in a really, really good spot. And as soon as we want to step up on the opening of clubs, we can do that.

**Operator**

And our next question comes from Ed Aaron from RBC Capital Markets. Please proceed.

**Edward Aaron** - *RBC Capital Markets - Analyst*

Thanks. Good morning everybody.

**Mike Robinson** - *Life Time Fitness, Inc. - CFO*

Good morning, Ed.

**Edward Aaron** - *RBC Capital Markets - Analyst*

I just wanted to follow-up on comments you made in your prepared remarks about your preliminary look at 2011. Did I hear right that you're targeting mid to high single digit growth for next year? And if so, is that a little bit different from what you hinted at last quarter?

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**Mike Robinson** - *Life Time Fitness, Inc. - CFO*

I think we said in the high -- not really, not really; it's not intended to.

**Edward Aaron** - *RBC Capital Markets - Analyst*

Okay. And then I wanted to focus also just a little bit on some of the seasonal dynamics. Do you think -- when you think about the drivers of your business from a membership perspective, being retention versus acquisition, it seems like a lot of your progress internally has been on the retention side whereas the acquisition piece feel tougher with the environment being what it is. As you look forward to the next couple quarters, particularly after Q1, would it be fair to say that the business becomes seasonally more dependent on acquisition than retention, and if so, how should we think about how your level of furthering your term progress in that respect.

**Bahram Akradi** - *Life Time Fitness, Inc. - CEO, Founder, Chairman of the Board*

I don't see a lot of change in the trends you guys have seen. We have seen the last two or three years, initially, if you look at just a pure health club business when beautiful summer months exist in whatever type of the market or the months that people can be outside comfortably, you will see a little bit of a slow down in the traffic. In our particular business model, we have kind of a winter season, which people come in and we have the summer season around our big pools that we get families joining, kids out of school, and some people just join for that 90 days. That's the impact -- that increased impact we see in our attrition on end of the 3Q and beginning of the 4Q is really function of people deciding to join with their mind made that they're going to join for four months or three months or something like that.

So I don't see any change in the pattern of membership in terms of what comes in, what goes out. 2010 has been, as we have mentioned numerous times, a very, very challenging year. We have a team of folks in here, including myself, we maneuver on enrollment fees, promotions for the salespeople, release of marketing material we can be agile with, on literally weekly basis or sometimes even twice a week. And, therefore, we feel that with that same level of intensity and agility, we can continue to perform as good as we have performed in 2010, in 2011. I don't expect it to be radically different one way or the other, unless we see a robust change in employment going from 9.5% or whatever it is today to 7.5%. I think then we will get some wind on our back. I am really, really happy with our team and our results based on this difficulty. And in a sick way, I almost like this tough economy that exists out there because it's allowing us to sharpen our skills and get much tougher. And so as soon as we have some tailwind, I think we will see some good results kind of pouring in. Until then, we are just committed to winning in the environment that exists today without getting tired of it. If it lasts two more years, so be it.

**Edward Aaron** - *RBC Capital Markets - Analyst*

I have one more follow-up and then I will jump back in the queue. Thank you.

**Operator**

Our next question comes from Greg McKinley from Dougherty. Please proceed.

**Gregory McKinley** - *Dougherty & Company LLC - Analyst*

Yeah, thank you. I don't know if you are able or willing to quantify for us this morning, but you talked about the cost membership acquisition exceeding enrollment fees. I think you've quantified that in your case in the past. Can you give us a sense for what that net P&L hit has been this year, because I think you recognize that as a period expense when you sign up that member?

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**Mike Robinson** - *Life Time Fitness, Inc. - CFO*

That's correct, Greg. Just to remind people what Greg is referring to is in the K in 2008, I think we had about \$6 million worth of costs in excessive enrollment fees. In 2009, that number was in the \$8 million to \$9 million range, and year-to-date, this year, it's in the \$10 million to \$12 million range.

**Gregory McKinley** - *Dougherty & Company LLC - Analyst*

Okay. And given your expectations for year-end membership, would you expect that to migrate meaningfully higher yet here as we go through the fourth quarter?

**Mike Robinson** - *Life Time Fitness, Inc. - CFO*

No, we expect it to be in the same range that we've been seeing in the first three quarters.

**Gregory McKinley** - *Dougherty & Company LLC - Analyst*

Okay. But year-to-date, we're \$10 million to \$12 million?

**Mike Robinson** - *Life Time Fitness, Inc. - CFO*

That's -- that's correct. Now on a year-over-year basis, it's probably a little bit worse because I think we had a little better performance last year.

**Gregory McKinley** - *Dougherty & Company LLC - Analyst*

Okay. And then it's just for context for that initial framework you provided us for 2011, are you making any assumption changes in that particular item?

**Mike Robinson** - *Life Time Fitness, Inc. - CFO*

The only assumption change we are making there is in an affect we lap this comparison and it becomes fairly flat year-over-year. Does that make sense to you? Meaning, no increase or decrease on that cost in excess.

**Bahram Akradi** - *Life Time Fitness, Inc. - CEO, Founder, Chairman of the Board*

We don't see that we have to go lower on the enrollment fee, but we do not want to budget going higher on the enrollment fee.

**Operator**

Our next question comes from Sharon Zackfia from William Blair. Please proceed.

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**Sharon Zackfia** - *William Blair & Company, L.L.C. - Analyst*

Hi, good morning. I had a few questions. I guess most of them center around members. Does it seem fair to assume in your guidance for the fourth quarter that you expect membership to decline again sequentially?

**Mike Robinson** - *Life Time Fitness, Inc. - CFO*

No, we don't expect it to grow substantially, but we don't expect it to decline either.

**Sharon Zackfia** - *William Blair & Company, L.L.C. - Analyst*

And then just on attrition, I followed the company for awhile, and usually the third quarter is seasonally the highest in terms of attrition. And if you kind of back out what you're facing on a year-over-year basis, it implies attrition being up sequentially in the December quarters. So just curious if there's something you're seeing in the business with the seasonality for attrition is changing so much.

**Bahram Akradi** - *Life Time Fitness, Inc. - CEO, Founder, Chairman of the Board*

Yeah, Sharon, That's a good question. Even myself, I was under the impression that last year's fourth quarter should have been lower than the third quarter, but, in fact, last year 4Q attrition was about 20 basis points higher than the 3Q last year. And it's really nothing more than a delayed reaction, as Michael suggested, on some of the people who want to drop out in the month of September. They actually drop out their membership, but they fall off on October 1, so they use the club part of September. So that would help us favorably in September versus a higher expectation of attrition and unfavorably in October. But really, it all evens itself out. I really wouldn't dwell on -- so much on if it drops in one month or the other, we're more focused on trying to take the trailing 12 months or the annual attrition rate totally down.

You know, just to continue our improvement. I think we can continue to improve on that 37.1% here in the fourth quarter, albeit, it will be a small improvement, very small. And then we're not done with ideas that we are still baking and trying to implement in continuing to improve attrition until we -- like we said earlier, we really want to hit that 36% bad. And we continue to work on that. I think we can get there pretty positively.

**Sharon Zackfia** - *William Blair & Company, L.L.C. - Analyst*

Okay. And then last question, and Mike, I apologize if you talked about this, but as we think about you ramping up growth in 2012 and beyond and some of that CapEx gets pulled forward, what is the thought process between owning versus leasing going forward? And should we expect a massive acceleration in CapEx in 2012, or will it be more moderate?

**Mike Robinson** - *Life Time Fitness, Inc. - CFO*

I don't think you should expect a massive increase in CapEx. I think -- as I've been talking about keep it to investors before, if we sat at this table in the next two or three years, it wouldn't surprise me if we'd be seeing a split that might even be closer to 50/50 on lease versus owned over that time period, assuming we can find the right locations in the right demographics and the right type of graphics to be able to do that. So I would not be modeling in significant increases in CapEx. Our next question comes from Brent Rystrom. Please proceed.

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**Brent Rystrom** - *Felti & Company - Analyst*

Just a real quick thought, from the perspective of the increase expenses relative to the customer enhancement and services and stuff, when do you feel that you'll start to anniversary that uptick? I know it will probably persist high for a while as a percent of sales, but when do you feel you kind of anniversary that?

**Bahram Akradi** - *Life Time Fitness, Inc. - CEO, Founder, Chairman of the Board*

Brent, this is a good question. I think at this point, we are in the process of innovation and testing and implementation of ideas, and we are -- we're still trying to build a program that is really -- it's a whole different business than traditional health club business. And that's the ultimate goal of this company, to build a truly different type of business we call healthy way of life company. That requires us to think about our business from the point of view of our customer, not the gym customer, but really a customer who is interested in running, a customer who is interested in yoga, a customer who is interested in weight loss and so on. We are super excited about what we are doing. We are very, very comfortable with our strategy. And the early indications of adoption by both team members and members who are discovering what we are doing in this space.

Our goal, best way I can put it, is to achieve the guidance that we give you guys. We will, Mike and I, since the day we have made a commitment to go public, we have had in mind to deliver what we promise to the street in terms of guidance. And then if we're trying to innovate new things, test new things, we try to do that in the context of making sure we still hit the numbers we guide for. So with that said, we are not 100% capable of estimating exactly -- if we're going to invest more or we're going to stop investing, we're still trying to figure out what are the best ways to achieve that satisfaction for each group. I think ultimately, this will lead us to a company that is much more evolved than everybody thinks about it in terms of just the best gyms in the United States or something like that.

And so all I can say to you is that it's not 100% possible to tell you we will lap that because it's not just an increase in adding a few hours for certain programs. We're actually building businesses that may have potentials outside of the four walls of our clubs, as well. And while we are making that early investment, we are just paying for it with the over-performance on our day-to-day operation, not paying for it risking not hitting our numbers.

**Brent Rystrom** - *Felti & Company - Analyst*

Maybe a different way to put it is it sounds like it will be dilutive from an expense perspective for some time. Does it become accretive by the back half of next year?

**Bahram Akradi** - *Life Time Fitness, Inc. - CEO, Founder, Chairman of the Board*

I will respond to you this way, it seems to be dilutive if you're looking at it from a margin standpoint. We might find ways to ramp up revenue as we're building some new business model, new business opportunities in each of these categories. But like any new start-up, you don't expect to immediately be profitable with some of those. And some of them will be immediately profitable. So I think we will be able to -- our goal is to grow our membership base, our customer base, grow our revenue. Our goal is to hit the EPS that we guide you to, and hopefully beat it. But meanwhile, we want to make sure we have the opportunity to latitude inside of our four walls of our corporate office to make decisions that for the ultimate good of the company and our customer.

**Operator**

(Operator Instructions). Our next question comes from Ed Aaron from RBC Capital Markets.

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**Edward Aaron** - RBC Capital Markets - Analyst

Thanks for taking the follow-up. Bahram you mentioned earlier in the call when you were talking about the responses that you could have to the current environment that the one route that you could go would be to reduce dues and prices like everyone else, I think is what you said. And it just kind of prompted me to think just from an industry perspective, what are you really seeing on that front? Is there -- are you observing a lot of deep discounting by your peers right now?

**Bahram Akradi** - Life Time Fitness, Inc. - CEO, Founder, Chairman of the Board

Well, I don't want to speak for single club operators and/or small regional operators, but on a national basis, the bulk of people in the health club or gym business are moving towards less programs and less services, and regardless of what their rack rate may be, you can buy memberships between \$15 and \$20 a month, remember. We have studied that market, we know that market, I had designed clubs two or three years ago that we could have executed in that space and opening boxes that would obviously do the same thing.

We feel that we can build better, more attractive, 15,000 to 20,000 square foot boxes than anybody else, and at more cost effective ways, but it's a space where there is no barrier to entry, and you are really deviating from your culture of being a top-notch customer service business. Then, you need to manage kind of a cost managing company, and that's not the culture we build here. So we chose very firmly we're not going to do what we see other people are doing. We see other players giving four people a \$60 a month combined rate for four people, or we see people selling memberships for nearly two years for \$300 online, and we really don't feel like that's the space that we're in, and we don't need to kind of play the same set of rules.

**Edward Aaron** - RBC Capital Markets - Analyst

Thanks for the color.

**Operator**

Mr. Heller, there are no more questions at this time.

**John Heller** - Life Time Fitness, Inc. - Sr. Dir. of IR, Treasurer

Thank you for joining our call today. We look forward to reporting to you our fourth quarter 2010 results, which tentatively have been scheduled for Thursday, February 17, 2011 at 10.00 AM Eastern Time. Until then, we appreciate your continued interest in Life Time Fitness. Thank you and goodbye.

**Operator**

Ladies and gentlemen, that concludes today's conference. Thank you for your participation. You may now disconnect. Have a great day.

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