FINAL TRANSCRIPT

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LTM - Q4 2008 Life Time Fitness Earnings Conference Call

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PRESENTATION

Operator

Good day ladies and gentlemen and welcome to the fourth-quarter and full-year 2008 Life Time Fitness earnings conference call. My name is Erica and I will be your coordinator for today.

At this time, all participants are in a listen-only mode. We will facilitate a question-and-answer session towards the end of this conference. (Operator Instructions) I would now like to turn the presentation over to your host for today, Mr. Ken Cooper, VP of Finance. You may proceed, sir.

Ken Cooper - *Life Time Fitness - VP, Finance*

Thanks Erica. Good morning and thank you for joining us on today's conference call to discuss the fourth quarter and full-year 2008 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.

In a moment, Bahram Akradi, our Chairman and CEO, will discuss his thoughts on our performance in 2008 and our expectations for 2009. Following that, Mike Robinson, our CFO, will review financial highlights in greater detail, including specifics on our 2009 expectations. Once we have completed our prepared remarks, we will take your questions until 11:00 AM Eastern time.

At that point in the call, Erica will provide instructions on how to ask a question. I will close with a tentative date of our first-quarter 2009 call and our annual shareholders meeting. Finally, a replay of this teleconference will be available on our website at approximately 1:00 PM Eastern time today.

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Before I turn the call over to Bahram, I would like to remind everyone that this call contains forward-looking statements and future results could differ materially from the forward-looking statements made today. Actual results may be affected by many factors including the risks and uncertainties identified in this morning's earnings release and in our SEC filings.

Concurrent with the issuance of our fourth quarter and total year earnings results, we have filed an 8-K with the SEC. Certain information in our earnings release and information disclosed on this call constitute non-GAAP financial measures, including EBITDA.

We have included reconciliations of the differences between GAAP and non-GAAP measures in our earnings release and our form 8-K. Other required information about our non-GAAP data is included in our form 8-K. With that, let me turn the call over to our Founder and CEO, Bahram Akradi.

Bahram Akradi - *Life Time Fitness - Chairman and CEO*

Thanks Ken. 2008 was a bittersweet year for our Company. We had many significant accomplishments. We also had tremendous challenges and overall, it did not meet our expectations.

There are things we did well and some things we did not perform to our satisfaction. We spent significantly more money on marketing and member acquisition costs to offset rising attrition rates. Meanwhile, we grew our memberships during this tough time.

We introduced some targeted membership initiatives that helped bring in membership counts and market share. They worked. Yet they reduced our incremental average dues.

The combined effect of the higher acquisition and marketing costs with lower average dues resulted in a revenue shortfall that dropped to the bottom line and lowered our fourth-quarter earnings significantly below our expectations. This is obviously something we are focused to change.

Radical macroeconomic change in the second half of the year did not allow us to react and adjust our marketing acquisition costs accordingly and as quickly as we would have liked. We are changing this at this time.

We are already deep in process to adapt and improve our marketing efficiencies and acquisition cost to better match with the new conditions, while we are still committed to achieve our membership goals and increase our market share. Additionally, we are making micro adjustments to the new membership programs we just introduced to make sure we achieve an average dues rate consistent with our internal goals.

However, we are not stopping here. From our corporate office to the field, we have prompt and strong measures in place to identify and eliminate unnecessary costs without damaging the member experience we want to deliver or the brand we have worked hard to create. We will be mindful to not cut muscle, but we will also not tolerate waste or inefficiency.

As it relates to our center growth plan, we have a number of centers under development construction. These centers will be constructed at a rate that will be comfortably and safely within the boundaries of our cash flow generated by operations and our current credit facilities, not any faster.

As it relates to future growth prospects, all I can tell you today is that we will be extremely cautious and selective in what, where and when. As the visibility to credit markets gets better, we will be more clear with our expansion plans. Now I would like to end my comments on a great note.

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Our achievements in 2008 were many. We opened 11 state-of-the-art centers in a number of new and existing markets. We saw the success we can have on the East Coast with the initial ramp of our Florham Park club which opened in November and the early results of the Berkeley Heights club that opened a few weeks ago.

We finished the remodels of nearly all our recently acquired clubs, which brings these clubs back to the forefront within the communities they serve. We generated a 7% increase in our in-center revenue per membership and nearly 5% increase in our revenue per membership for the year.

We rolled out one of the most expansive member-only websites available to customers in the health club space. We have presented over 50 Healthy Way of Life events such as indoor triathlons to customers.

We delivered over $270 million of debt and sale leaseback capital. There was much to be proud of.

In closing, we firmly believe in our business model. It has proven to be resilient and successful.

Our most valuable asset, our membership base, maintains strong usage levels and our feedback from our members continues to get better. We are a very profitable Company and we intend to stay that way.

With that, I will now turn it to Mike Robinson, our Chief Financial Officer. Mike, here you go.

Mike Robinson - *Life Time Fitness - CFO*

Thanks Bahram. I would like to start with just a few thoughts on the impacts from the economy. At Life Time Fitness, we believe the economy is a factor, it is not an excuse.

Accordingly, as I continue my comments, you will not hear many references to the economy. Rather, I will provide you with specific thoughts and candid explanations on trends and results. As I am providing details on our fourth-quarter and full-year 2008 performance, I will provide 2009 guidance throughout my comments as appropriate.

For the fourth quarter, total revenue was $194 million, up 13.4% from last fourth quarter. We were up 17.4% for the year to $769.6 million.

Our revenue growth in the quarter continues to be driven by two main factors, including membership dues growth of 14.5% for the quarter and 17.2% for the year. Although the gap between dues growth and membership growth is the lowest in the past several years, membership dues growth is still greater than our membership growth at 13.6%.

Membership dues came in under our internal expectations for the fourth quarter, primarily as a result of the enrollment of more individuals then typical and the introduction of lower price dues programs, including a membership level targeted at an underserved demographic, individuals 21 to 26 years old, and a team member friends and family program.

In-center revenue grew by a 13.1% in the quarter and 19.7% for the year. We did see deceleration of growth of personal training, LifeCafe and LifeSpa in the fourth quarter.

For instance, personal training grew over 20% for the year but the fourth quarter growth was closer to 10%. As we have seen throughout 2008, spa growth was our most affected business, growing slightly in the fourth quarter and 6% for the year.

In 2009 we expect the in-center businesses will continue to grow as we ramp our membership levels and the accompanying in-center activity in the immature clubs. However, we also expect in-center revenue per membership to reflect the same trends we saw late in 2008, namely flat to negative comparisons.

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Let me also take a minute to provide some highlights on other revenue metrics. Memberships at December 31, 2008 totaled 567,110 which is an increase of 13.6% from last fourth quarter. Our membership growth rate was up from the 13.2% growth rate in the third quarter.

For a perspective on our membership growth, our clubs in ramp are growing pretty much according to plan. A club like Florham Park is performing about 10% ahead of our internal plan.

A club like Vernon Hills in Chicago is about where we expect. A club like City Center in Houston is below plan as we have not been able to get up yet from the effects of Hurricane Ike this summer.

Mature club memberships have come down slightly. But this has been partially offset by the performance of our acquired clubs that had remodels completed.

For 2009 we expect membership growth in the mid-single digits commensurate with our unit growth rate. With respect to revenue per membership, we generated a 30 basis point increase to $345 in the quarter.

For the year, revenue per membership grew 4.9% to $1427, which is approximately $119 per month. For 2009 we expect this to be flat to down slightly given recent trends and the membership mix shift we saw in the fourth quarter.

Our in-center revenue per membership was roughly the same as last fourth quarter at $93. For the year, in-center revenue per membership grew 7% to $414 or about $35 a month.

We saw our membership base continuing to use our fee-based programs and services due to their effectiveness. However, clearly, our members have taken pause in what we feel less is their most discretionary dollar. We expect in-center revenue per membership trends to be flat to down also in 2009.

We were flat on same-store sales for the quarter and we were down by 5.2% on our 37-month mature same-store sales. This was driven by lower membership levels, dues mix and lower in-center sales.

For the year, we generated growth at 2.8% for 13-month same-store sales and we were down 2.8% for the 37-month metric. For 2009 we expect recent trends to continue with potentially negative comps.

Before moving to margins, I want to make some comments regarding any regional impacts we're seeing. Predominately center performance has held up well, with usually one to two centers in a market showing more signs of lower revenue and profitability than others. These clubs are typically on the low-end of the demographic range for us.

In the fourth quarter, using same-store sales and attrition rates as our proxy, we did see more pressure in markets such as Detroit, Houston and Phoenix. While this is consistent with what we have seen in other consumer businesses experienced for the most part, we are still looking closely at these markets, in particular, to monitor performance levels.

Moving to our margin analysis, let me start with a discussion of the $0.08 charge per share that we incurred in the fourth quarter. These costs totaled approximately $5 million pretax and resulted primarily from the reduction in future center development.

On the employee front, we laid off approximately 100 team members, mainly in construction, development and our training teams. This resulted in approximately $0.01 per share of cost between G&A and center operating expenses.

For site development, we are typically pursuing many sites for possible club openings. Once deemed probable, these costs are capitalized and reflected within other assets. We made the decision to remove several of these sites from the development consideration.

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This resulted in approximately $0.5 per share or a little over a $3 million pretax of additional G&A expense in the quarter. Lastly, we have assets which we have made available for sale where we took a lower of cost or market adjustment.

We recognized approximately a $0.02 per share or a little over $1 million pretax charge to reflect current market value, primarily in depreciation expense. The clubs operating margin decreased to 15.1% from 22% as compared to the prior fourth quarter.

For the year, our operating margin has decreased to 19.1% from 21% in 2007. The main drivers of this margin decrease in the quarter were the charges I just discussed, roughly $4 million of incremental rent due to the sale leasebacks and rent on clubs recently opened and incremental membership acquisition costs. This was offset slightly by approximately $1 million of lower depreciation that went away with the sale leaseback transactions.

As we look to 2009, we expect lower operating margins driven primarily by lower center operating margins coming from higher member acquisition costs, the recent dues mix trends and increased occupancy costs from the sale leasebacks that we did in August and September 2008. As a reminder, we will incur approximately $17 million of annual rent from those two transactions. We offset approximately $4 million of depreciation annually due to these transactions as well as lower incremental interest expense.

Further, we expect G&A leverage to come in 2009 as we maintain a very flat organization. This has been a hallmark of ours for the past five years. Marketing is expected to be relatively flat as a percentage of sales.

We expect depreciation expense as a percentage of revenue to be up, driven by the completion of the remodels of the seven leased centers, higher center investments and the deceleration of growth rates in comparison to the CapEx increase. Interest expense net of interest income increased to $8.2 million from $6.4 million last fourth quarter as we grew our new center base and our corresponding average debt balance during the quarter.

For the year, total interest expense was $29.5 million as compared to $25.4 million last year. We anticipate interest expense to increase in 2009 as our average debt balances are higher compared to the prior year and we recognize lower capitalized interest as we reduce our construction in progress.

Our tax rate for the quarter was 39% as compared to 39.7% last fourth quarter. For the year, our tax rate was 39.7% compared to 39.9% for 2007. We expect our 2009 effective tax rate to be approximately 40%.

Net income for the quarter was $13 million compared to $19.1 million last fourth quarter, down 31.7%. Our net income margin for the quarter decreased to 6.7% from 11.1%. For the year, net income was $71.8 million, up 5.6% and our net income margin has decreased to 9.3% from 10.4%.

Total weighted average diluted common shares was 39.2 million shares for the fourth quarter. For the year, our average diluted common shares totaled 39.3 million. We expect our total 2009 share count to be approximately 40 million shares.

Based on our 2008 fourth quarter weighted average share count, our diluted EPS for the quarter was $0.33, down from $0.48 in the fourth quarter last year. For the year, our EPS is up 3% to $1.83.

Moving to operating data, our 2008 attrition rate was 42.3%. Accordingly, we changed our estimated average life of a membership in the fourth quarter to 30 months.

The number of open centers at December 31, 2008 was 81 compared to 70 at December 31, 2007. Our current number of open centers is 83 with our Berkeley Heights New Jersey and Atascocita or Lake Houston Texas centers opening in early February.

Of the 83 centers, 50 or 60% are our large current model and only 55% of all centers have been opened three years or more which we classify as mature clubs, mature centers. In 2008, we grew our square footage 18.7% to 8.1 million square feet as

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compared to 6.8 million square feet we had at the end of 2007. In 2009 we plan to grow approximately 6 to 8% or 500,000 to 700,000 square feet.

EBITDA totaled $50 million in Q4, down 6.8% from the last fourth quarter. For the year, EBITDA was up 12.1% to $221.5 million.

EBITDA margin for the quarter was 25.8%. Our EBITDA margin for the year was 28.8% which is down 130 basis points from 2007, primarily due to the sale leasebacks during the year and the charge discussed earlier.

Cash flow from operations totaled $183.1 million in 2008 which grew 28.8% from the $142.2 million generated in 2007. This 28.8% improvement in our operating cash flow compares favorably with our EBITDA growth rate of 12.1% and was driven by favorable cash tax treatment from accelerated depreciation on assets placed in service in 2008.

Cash flow from operations in the fourth quarter totaled approximately $39 million compared to approximately $35 million in the fourth quarter of 2007. Cash outlays for capital expenditures for the quarter were $104 million.

For the year we paid a total of $464 million in total capital expenditures. During the fourth quarter, our overall debt balances grew by approximately $66 million to $713 million as of December 31. Our net debt to capital ratio was 52% for the fourth quarter as compared to 50% for the third quarter.

In capital structure news, our entire team is very proud of our achievements in 2008 as we raised in excess of $270 million of capital in the form of debt and sale leaseback transactions. Although the credit markets remain very difficult, we still see some semblance of activity.

In December we added a single club mortgage and some equipment leasing. In addition, we're working on several other mortgages and a sale leaseback transaction.

Generally, we're dealing with local banks and investment groups on these deals. We are focused on finding the best use of capital for the Company. From a cost perspective, we believe it will be within our expectations and goals. If not, we stand ready to slow down our new club growth even more.

As of December 31, we had approximately $55 million in cash and availability on our revolver. And as of today, we have 33 large centers with an asset cost on our balance sheet well in excess of $500 million with no mortgage financing against it.

During the pre-earnings call on February 5, I commented on our revolver credit facility covenants. Because of the flexibility we have and the timing of capital expenditures and the strength of the cash flow delivery of our business, I am comfortable with our covenant position.

We have room in these covenants even at the low-end of our guidance. However, I am comfortable in telling you that if we are directionally headed toward the low-end of our guidance, we will be slowing our CapEx spend even further.

Before I move to our 2009 guidance discussion, I would like to make a few balance sheet comments. Accounts receivable was up $1.6 million for the year and $800,000 sequentially from the third quarter. This increase is related to the growth in our corporate businesses.

As you know, we do not have accounts receivable on our core business, that being memberships, as all members are on EFT and we recognize only cash received as revenue. Pre-paids and other current assets are down $5 million for the year and are down $4.5 million sequentially from the third quarter. This was driven by a reduction in land that we intended to sale in the next 12 months of approximately $5 million during the year and as a result of sales completed and transfers to long-term land held for sale and a projected sale did not occur.

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Other assets are up $7 million for the year but down $6.2 million sequentially from third quarter. This year-over-year growth is related to increased property held for sale, both transfers from other current assets as well as property purchased in 2008.

The sequential reduction is driven by a decrease in development cost capitalized for future center development which was part of the charge I previously discussed. Accrued expenses decreased $0.8 million from last year-end and more than $9 million sequentially from the third quarter. The sequential change is driven primarily by changes in accrued taxes.

Preferred revenue reduced 5% year-over-year. This is a direct reflection of the lower enrollment fees we're currently charging to attract new memberships.

Deferred membership origination cost grew 11% year-over-year. Deferred origination costs are growing at a much slower rate than previously because we are experiencing more direct cost in excess of our enrollment fees which we expense immediately.

With that, let me turn our attention to our guidance for 2009. First, from a development perspective, we currently plan to open up to six centers in 2009. The total number we open will be dependent on our cash flow and the credit environment.

We have the flexibility to change our CapEx spend and will proceed with prudence. We've already open two of these centers, one in Berkeley Heights, New Jersey and the other in Lake Houston Atascocita area of Houston, Texas.

We have control over the timing of construction of these centers. The actual number of centers we will open will be dependant on our operating cash flow and debt levels. If we are able to maintain our strong operating cash flow or bring in additional cost-effective financing, we will continue on our build schedule.

I know you are all looking at a downside scenario, as are we. To the extent our operations take drastic changes to the negative, we are in a position to open up one more club and then hold indefinitely on the remaining clubs under construction. As we look to 2010, we will use the same cautious approach.

Regarding our specific financial guidance, our revenue guidance is 8 to 12% growth which equates to approximately 830 to $860 million. We expect net income of approximately 60 to $68 million. This results in diluted EPS guidance of $1.50 to $1.70 per share.

Our CapEx guidance is approximately 150 to $200 million in 2009, of which we expect approximately 35 to $40 million will be the maintenance of our existing club base. This works out to be approximately $3.50 per square foot for our centers and about $10 million in corporate initiatives.

Total new construction CapEx will be approximately 110 to $160 million. We plan to fund these capital expenditures with cash from operations and our revolving line of credit. Please keep in mind, we could reduce this CapEx spend well below these guidance numbers if necessary.

That concludes our prepared remarks regarding our fourth-quarter and full-year 2008 financial results. On behalf of our entire executive team, I want to thank our national base of team members who deliver upon our member experience and business operation expectations.

We all remain very excited about the future of Life Time Fitness. We are pleased to take your questions now.

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QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Paul Lejuez, Credit Suisse.

Paul Lejuez - *Credit Suisse - Analyst*

Can you guys maybe talk about a club -- just to use as an example, a club that was performing well that has suddenly turned on you and one that you're disappointed in? You don't have to name it. Just want to try to get an understanding about the kind of revenue declines that you have seen in that club.

How attrition changed? How were you able to cut the staff, if at all, at this point and what happened to the four-wall EBITDA, just so we have an understanding of the types of declines we might be seeing at what might have previously been a strong club?

Mike Robinson - *Life Time Fitness - CFO*

I'm not going to point to a specific club, but I will give you a general idea. We talked about a few of these in the past.

A club might be seeing somewhere between 5 and 10% lower revenue coming from a few percent drop in membership levels. As you go from that level down to EBITDA where we expect a mature club to be delivering in the high 30% EBITDA margins, that club is probably now delivering in the low 30% EBITDA margins.

Key changes include things that we have talked about before. We are seeing an attrition rate that may have been running in the mid 30s up to over 40% and the replacements that we are able to in new memberships coming in are coming in at a little bit lower average dues. And so those are the big drivers for that.

I do want to stress thought that as we look up and down all of our open clubs, the margin rate that we are seeing is still what I would call a very good margin rate. Again, like I mentioned, it's still at -- the EBITDA margin rate we are seeing is still above 30% in those clubs and in this environment I think we're pretty proud of that. Bahram, any thoughts?

Bahram Akradi - *Life Time Fitness - Chairman and CEO*

Nope.

Paul Lejuez - *Credit Suisse - Analyst*

That attrition rate that you gave is a weighted average. So presumably there's some clubs that are above that. I'm just wondering, how many of them are at a 50% attrition rate, for example?

Bahram Akradi - *Life Time Fitness - Chairman and CEO*

That is a great question. Very, very few and those are clubs that the bulk of our membership is a single membership.

The single membership clubs have always had a higher attrition, just the nature of the single member has the highest attrition, then the couples is a little less and then the family is the lowest in terms of attrition. So the clubs that have had single population at-large, they were probably in the past in the 40s and now they are over the 50s. But there is very few of our clubs are that way.

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Paul Lejuez - *Credit Suisse - Analyst*

Okay, thanks. I will turn it over to the next person.

Operator

Scott Hamann, KeyBanc Capital.

Scott Hamann - *KeyBanc Capital Markets - Analyst*

In terms of the enrollment fees kind of falling into center ops, can you quantify what the actual impact was for the fourth quarter and the full year and kind of in this environment where I assume you're going to keep enrollment fees pretty close to zero, what your expected impact would be for 2009?

Bahram Akradi - *Life Time Fitness - Chairman and CEO*

I'm going to give you the color first and Mike is probably going to give you some numbers. This is Bahram.

During the 2008, as I have mentioned since the day we went public, during recessionary time, the easiest thing to do is just lower the enrollment fee and allow people to get in and try to keep them in our particular case through our great programs, great experience and programming. In 2008, we saw deterioration in attrition and then unfortunately in the fourth quarter, instead of us being able to reign that back in, it ramped up dramatically and the entire fourth quarter just kept getting worse instead of getting better.

So, what we have done is generally lowered initiation fee and increased the marketing cost to go ahead attract new members to replace. Having spent the number of years I've been in the business, I have no problem knowing that we can continue to get more memberships into the door via more aggressive marketing, more aggressive promotions.

It is not where I would like us to be and it is not where I would like us to end. We would really like to be able to normalize the attrition to a level where we don't have to spend nearly as much on member acquisition. To that effect, some of the changes we made, some of the moves we made in the late 3Q and 4Q were very quick changes to deal with a very radical change in the macroeconomic and therefore the results were a little less than our expectation.

Of course they have huge impact on the P&L, but we have been working literally seven days a week this year on making, as I mentioned in my comments, micro adjustments on how these promotions run, how we work on the marketing and how we work on the enrollment fees so that we are putting the proper controls in place and therefore I don't believe we have as much of a risk on the upside down scenario that we experienced latter half of -- particularly more aggressively in the second half of last year in the cost of acquisition versus the enrollment fee. So that is in my opinion going to be completely under control unless the macroeconomics get dramatically worse again and we would have to make additional shifts and I can't talk to that.

But if things stay the way they are now, not getting worse, I believe we will be able to control that better. Now I'm going to give it to Mike to give you some numbers that he might want to share with you.

Mike Robinson - *Life Time Fitness - CFO*

What you are specifically referring to is what is the effect on center operating expense and the driver for that is when you reduce the enrollment fees and those enrollment fees go below the commissions that we spend or the commissions that we pay to our salespeople, rather than defer those direct costs, we expense the excess. For last year for the total year, that ran about

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roughly 1%. It was about roughly a 1% drag on your center operating expense and that did increase in the second half of the year.

Scott Hamann - *KeyBanc Capital Markets - Analyst*

Okay, thanks Mike. And then just on CapEx, if things do worsen up here pretty quickly, I know you can trim back your growth plans. How much -- you probably incurred some expense or capital expenditure in the past for these two clubs that are already opened. So how much above the 35 to $40 million of maintenance CapEx could you get that number down to for the full year?

Mike Robinson - *Life Time Fitness - CFO*

I think we could get the full year down to well below $100 million.

Scott Hamann - *KeyBanc Capital Markets - Analyst*

Okay, thank you.

Operator

Karen Howland, Barclays.

Karen Howland - *Barclays Capital - Analyst*

You talk about how some of your initiatives this past quarter as far as lowering your dues levels drove membership growth, but you are now kind of reverting that, presumably no longer offering those initiatives to drive higher member growth. Can you talk about I guess the profitability of those members versus the loss of members entirely? I would think in this market environment you would continue to try to drive member growth even if it is at a lower profit level.

Bahram Akradi - *Life Time Fitness - Chairman and CEO*

Let me take that Karen. I did not tell you we are eliminating the promotion. What I did say is that we would make micro adjustments. I think we can do better.

We may have given discounts in places we don't need to give to get the memberships that we have gotten. And in certain areas, we need to continue to give those discounts to get those membership counts.

So, it is just having a little more time now that things have settled, the dust has settled, to go through club by club, market by market as I have done with my marketing team all of the last two or three weeks and really comb through our facilities one club at a time, one market at a time to make sure we can think through much more with much more detailed thought process and focus rather than kind of a one block introducing a membership type. We're not going to eliminate them. We're just going to micro adjust it so we can get better yield where we can get it and still get the membership and use those same prices where we need to use them to continue to get the membership count. Does that answer your question?

Karen Howland - *Barclays Capital - Analyst*

It does. It sounds like you are going to be continue to be promotional to try to drive membership growth but perhaps a little bit more strategic.

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Bahram Akradi - *Life Time Fitness - Chairman and CEO*

A lot more strategic.

Karen Howland - *Barclays Capital - Analyst*

Okay. And then, are there any cash costs associated with pushing if you do decide to go from the six centers that it sounds like you are tentatively planning to three centers this year? Are there any costs of deferring that growth?

Mike Robinson - *Life Time Fitness - CFO*

What you would do is you would slow the construction growth of those other centers, so that you have some slight carrying costs, but it is not significant.

Karen Howland - *Barclays Capital - Analyst*

When you say not significant, is it less than $5 million?

Mike Robinson - *Life Time Fitness - CFO*

It would be less than $5 million or so.

Karen Howland - *Barclays Capital - Analyst*

Okay, great. Thank you.

Bahram Akradi - *Life Time Fitness - Chairman and CEO*

We only have four clubs that we are -- as a Mike had said, three to four clubs that are remaining for this year's opening schedule right now. We are moving very, very cautiously under construction of those facilities and we are watching the credit market and the internal cash flow.

Again, as we have repeatedly said, we have the control on slowing those furthermore, or ramping them up a little bit more if the total comfort of the cash is available either through future financing or great cash flow operation. Otherwise, we just want to keep a certain amount of cushion in our dollars that we have available to us.

Karen Howland - *Barclays Capital - Analyst*

Final question. I know you said that center operations margin should continue to deteriorate throughout the course of this year. If I think about operating expense per center, is there any reason that that would stabilize? Or should that continue because of the higher rent expense, that should continue to grow as well?

Mike Robinson - *Life Time Fitness - CFO*

Well if you've got -- on a per-center basis, again, if you spread those occupancy costs across all the centers rather than the specific centers that were there, you are going to see on average cost increase in center operating expense. So that will stabilize

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as we anniversary that in the August/September time period and then the other drivers to that increase in the cost side have been in 2008 membership acquisition costs.

As Braham talked about there, that grew through the year. So I would be expect it to be a little bit of a pressure on that early in the year. But again, as we start to anniversary that, that would stabilize also and hopefully come down as we work hard on a number of the initiatives there.

Karen Howland - *Barclays Capital - Analyst*

Great, thank you very much.

Operator

Jaison Blair, Rochdale.

Jaison Blair - *Rochdale Research - Analyst*

A couple of quarters ago, you guys mentioned that something -- you thought that approximately 25% of your membership base was categorized as inactive. Would you say that number still kind of stands?

Mike Robinson - *Life Time Fitness - CFO*

No, that number -- we don't discuss the actual split of that. But given the usage patterns that we continue to see at our clubs, we believe that that level is actually coming down and it makes sense that it would be coming down.

Jaison Blair - *Rochdale Research - Analyst*

I guess the question I have for you is that quarter-over-quarter, from the third to the fourth quarter, your average memberships per unit dropped from 7053 to 6833, which is a pretty sizable -- I guess it's about 3%. Your average dues per membership were also down about 3%, in-center membership was down about 12% and I continue to hear from management about that you have a high level of variable costs, that there are lots of levers you can pull.

And I think that there are a lot of number crunchers who think, boy, we could reduce all the costs out of the business. But as Bahram said, you are really unwilling to cut the muscle, which I agree with. Because as soon as you really start to cut advertising expense, my guess is your churn -- it's harder to replace.

However, during the quarter, the average -- the sports fitness family recreation operating expenses were only down slightly from $211 in the third quarter per membership to $209. Now some of that may be the sale leaseback you did in the third quarter, but I guess I was expecting to see that number drop further, especially given the decline of in-center revenue.

And then the other piece -- I guess the other question is, you talked about being more efficient with your advertising, which -- that was up double digits year-over-year. So if you could kind of help me figure out -- the data is not pointing to that you have got all these levers to pull and all these variable costs. The data is saying that your cost per membership were pretty stable while your revenues per membership have started to come down a bit.

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Mike Robinson - *Life Time Fitness - CFO*

I think there's a lot of points in there. Let me try to address those, one or two at a time here.

From a big picture, from a 30,000 foot perspective, you are right. The biggest driver that we saw outside of the charges that we took, outside of the sale leasebacks and the expense there that sits in the center operating expense, the biggest driver that we saw was the fact that our incremental revenue per membership or our incremental dues came down and that is going to put pressure on those margins, especially if most of that cost base, it is built based on usage.

So if the members are using the clubs at the rates that they continue to use the clubs and the membership growth is there, then we are much more limited -- and not to say that we don't have opportunity -- but we are much more limited in some of the cost reductions that we can -- or the variable cost portion of the business. So the big driver to this is that we have seen average dues come down a bit, mainly driven by the programs we introduced later in the year but our usage levels remained high.

Let me go back to a couple of statistics you talked about earlier and I think the first one you threw out was the average members per center. And when I talk about that, I always caution people about that because that is -- because of the number of open centers that came in, for instance, we opened four centers in the fourth quarter, we opened three centers in the third quarter, those as you would well expect, have membership rates or levels of membership that are significantly below the averages. When you open centers like that, that is going to draw those averages down.

So, I just caution people to make sure that when you are looking at a number of these statistics, that you keep the timing of club openings, the fact that these clubs take three years or so to ramp-up et cetera all are going to affect some of those numbers. But big picture, Jason, I think it is important to say that you are correct.

There has been more stress on that operating margin really coming from outside of some of the things I talked about before, coming from the fact that usage levels remain high yet we saw some incremental reduction in average dues. And those are things that Bahram talked about earlier, that part of that is driven by the environment that we are in and there are things that we will be doing, have been doing to try and moderate that.

Bahram Akradi - *Life Time Fitness - Chairman and CEO*

Let me add a little color about your advertising comment. As I mentioned, I don't particularly took any credit for being efficient in marketing in the last five months or so.

We basically had to react to what was going on out there and threw a lot of money at marketing, threw a lot of money at promotions, paid a lot of money in commissions to try to bring in a significant number of memberships to offset the significant membership loss. To generate 13% membership growth, you just can't be doing that in this environment unless you're spending a lot of money.

That money eats away at your margin. Look, I don't think that these are particularly fun times or business as usual. I think you are very, very astute and you're making great comments.

But the focus on our advertising efficiency and control of the acquisition cost and the balance of where we deliver the discounts and where we don't; I think those things are the things that now that things have settled down, we have the ability to actually get focused on bringing more excellence in our thought process than we utilized in the 4Q. So, I feel great about the actions we're taking.

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I am cautious about the environment ahead. I think we'll have a very, very challenging environment ahead in regards to acquiring members and keeping members. We have, as Mike mentioned, our utilization report shows higher utilization in our clubs than the years past. Yet we have lower number of members in certain clubs in our facilities.

So, therefore, to your question, is there are more nonusers who are paying dues or less, I can tell you for fact there is probably significantly less nonusers paying dues today than there may have been one year ago this time. But I think we're getting close to a point where it doesn't get -- I believe most of our members are using the club as they are paying dues.

So, we feel optimistic that with our current adjustments we're making, we're going to be able to maintain a very profitable Company. Margins that they are good, not near as good as what they were one year ago or two years ago, but then again we have to be realistic about what we're dealing with out there.

Jaison Blair - *Rochdale Research - Analyst*

If I could just follow-up. Have you projected at the low end of guidance where your coverage ratios will be in '09?

Mike Robinson - *Life Time Fitness - CFO*

Obviously, I run sensitivities all the time and as I've made comments in the prepared remarks, I feel very comfortable that our covenants at the low end are well with then our covenants packages. I also said that if we felt things were going toward that low end, we would be slowing down our CapEx spend even more and that that would also help protect those covenants.

Jaison Blair - *Rochdale Research - Analyst*

Thank you for addressing my questions.

Operator

Hardy Bowen, Arnhold & Bleichroeder.

Hardy Bowen - *Arnhold & Bleichroeder - Analyst*

Bahram, can you comment on the state of the industry, what you see elsewhere and also your experience in January? Do you think things are the same, getting better, getting worse?

Bahram Akradi - *Life Time Fitness - Chairman and CEO*

Yes. January was I believe not only for us, but also for some of the other people in the industry I've talked to, a very robust membership sales month. We spent a lot of money in marketing and we had strong promotions in place.

In many cases, many of our clubs, two, three, four, five, six years old, we sold probably more membership units then we have sold ever before. So, January was a robust month, but I would not hang my hat on January going forward for the rest of the year.

There could be a lot of a phenomena about January. It could be that members were -- people were so scared of spending money November, December, in January they came in, they kind of did their resolution and said my health is the most important thing to me, run in and joined the club. That enthusiasm can wear off by late February, who knows.

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We had a great January. I can't undermine that at all. But -- and business -- the utilization of the clubs, literally when I go through our clubs even as early as yesterday, day before, parking lots are packed. People are coming in. Some of our clubs were shuttling people back and forth from crossover parkings.

So I don't think that the consumer has walked away from the exercise whatsoever. They just -- they are dealing with pinching stuff everywhere they can, but I don't think this is one of those spaces that they will easily let go.

Hardy Bowen - *Arnhold & Bleichroeder - Analyst*

I guess it is hard to tell if the connectivity programs are beginning to get some traction in this kind of an environment. But what can you say about them so far?

Bahram Akradi - *Life Time Fitness - Chairman and CEO*

As I mentioned in my first portion of our talks, we have just launched our web and member based web. It is truly, in my opinion, at the baby stages. While we're getting a lot of attraction from members coming in utilizing it, I think it is just way early.

We are focusing on creating a true healthy way of life destination for our members. So it's their social place, their country club, their health club, their resort with our pools, et cetera. I think we can provide substantially more value to the consumer then anybody else.

If they took what we offer them (technical difficulty) but if they took what we offer them per list of amenities, if they looked at the quality of service, the quality of the place and their experience, they are paying significantly less relative to those things than they are paying elsewhere. So I am bullish on our product.

I think this year, this spring, this summer we are going to position this as a place you can stay and take a vacation in our clubs for a lot less money than going on a vacation. So we're going to buy as fight as hard as we can to make sure our customer gets that message both by what we tell them and by how we deliver.

I believe we will win long-term as we have this far. Again, we just do not like the deterioration in the margins we have had in the last six months and we are certainly all over it to try to correct that.

Hardy Bowen - *Arnhold & Bleichroeder - Analyst*

I don't think too many other retail trade companies like it either. In the Northeast, it seems the clubs are working, if anything, better than expectations. Do you plan to look for more sites in the Northeast proportionately?

Bahram Akradi - *Life Time Fitness - Chairman and CEO*

Right now we are still working hard on our pipelines and trying to find locations. I think, that real estate is at a state of flux. Our opinion is that we're going to see deterioration in the real estate prices.

I don't think that is quite there yet. So we do not want to get pregnant getting into deals for two reasons. One, as I mentioned, we don't want to get pregnant into any new deal that we are not already substantially committed, just because we don't know what the macroeconomics is going to bring and what the credit facilities -- what the credit market is going to be like.

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But at the same time, we are looking. I also think we will find opportunities in existing space that would be substantially below costs that you could start from scratch. We will work on those type of facilities as I have done them for years in the past and this would not be anything new for us to do.

In our club in Fairfax, Virginia does phenomenal returns and it was about a 60,000, 70,000 square foot facility with it in line 400,000, 500,000 square foot shopping center. And we're going to find all sorts of opportunities where we haven't had in the past years to allow us to grow. But I want to be very, very clear that all of this will not -- none of this will come at us taking a chance of spending dollars that we should be saving in this credit market.

Hardy Bowen - *Arnhold & Bleichroeder - Analyst*

So you have to wait a bit for the real estate to come down in price?

Bahram Akradi - *Life Time Fitness - Chairman and CEO*

We believe that will happen. We are not rocket science. We're Houdinis. We could be wrong, but I believe that will happen.

Hardy Bowen - *Arnhold & Bleichroeder - Analyst*

Okay, sounds good.

Operator

Rachel Chow, Morgan Keegan.

Rachel Chow - *Morgan Keegan & Co., Inc. - Analyst*

Can you just comment a little bit more about this membership shift? It used to be I think [50]% individual and [15]% in family. Now how significant this shift will be?

Mike Robinson - *Life Time Fitness - CFO*

Well what we have talked about -- and it varies by club. But generally across -- we've generally seen about 50, 55% individual and somewhere around 30% couple and about 15% family or so, just generally in that. In the fourth quarter, we saw the individual memberships increase and they are probably running more in the 60% range than they were previously.

Bahram Akradi - *Life Time Fitness - Chairman and CEO*

Let me give you something. I would really be cautious on trying to extrapolate anything out of the last three or four months into a long-term projection. Let me just tell you why I feel that way.

The market shifted so radically. We introduced a bunch of different programs, promotions, membership types et cetera to kind of combat that. We did not have, in my opinion, the appropriate levels of controls and right execution at each center.

So I don't feel comfortable that we necessarily can take what happened and extrapolate it into what it should be. If I take one more quarter, this next 45 days, with all the controls that we are putting in place, all of the new micro adjustments we're making,

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I feel like I would be much more comfortable talking about any detailed numbers in terms of what happened, how we of course correct it and then what to expect.

Unless our execution, in my opinion, is near our desired levels, I don't want to read into it that this is what is going to happen long-term. So I have to just excuse -- I have to apologize for the fact that we acted and we acted promptly.

But as you do that, sometimes you have to come back and do some micro adjustments, course corrections to make sure it is in fact giving you the results you want and not some other side effects that you did not want. I think we have had a lot of those side effects.

Rachel Chow - *Morgan Keegan & Co., Inc. - Analyst*

I got you. The last question is going forward, are you considering opening like a smaller center with fewer amenities, just downsizing and lower the cost of construction et cetera so make it more affordable?

Bahram Akradi - *Life Time Fitness - Chairman and CEO*

That's a great question. Now you're asking me to tell you what I don't want to tell any of my competitors what we're doing. But I will answer you like this.

Over the last -- since 1983, since I been in this business, I personally have built clubs as a little as 14,000 square feet and as large as 300,000 square feet. Initial stages of my career, every center we built was a smaller facility inside of existing space.

So, we have the total capability of taking advantage of the appropriate market. I believe in the near future, the next two to three years, there is going to be opportunities beyond -- with no kind of -- significantly multiple times what there has been in the past three or four years, five years, in the areas of finding smaller boxes that you could get into with much, much lower occupancy cost.

So I'm not going to give you any sort of a direction of what we will do. I will tell you that we're examining, studying every other possibilities and we will take appropriate actions at the right time.

Rachel Chow - *Morgan Keegan & Co., Inc. - Analyst*

Got you. Thank you very much.

Operator

This concludes the question-and-answer portion of the call. I would now like to turn it over back to Mr. Ken Cooper for closing remarks.

Ken Cooper - *Life Time Fitness - VP, Finance*

Thank you for joining us on our call today. We look forward to reporting to you our first-quarter 2009 results which tentatively has been scheduled for Thursday, April 23, 2009 at 10:00 AM Eastern time.

Our annual shareholder meeting will also take place on that day in the afternoon at our corporate office in Chanhassen, MN. Until then, we appreciate your continued interest in Life Time Fitness. Thank you and good bye.

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Operator

Thank you for your participation in today's conference. This concludes our presentation. You may now disconnect and have a wonderful day.

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