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Open Text Corp. *(OTEX)*

Q2 2012 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Ladies and gentlemen, thank you for standing by. And welcome to the Open Text Corporation's Second Quarter Fiscal Year 2012 Financial Results Conference Call. [Operator Instructions] . This conference is being recorded today February 1st of 2012.

And I would now like to turn the conference over to Greg Secord, Vice President, Investor Relations. Please go ahead.

Greg Secord

Vice President-Investor Relations, Open Text Corp.

Thank you and good afternoon. I'd like to take this opportunity to welcome OpenText's President and CEO, Mark Barrenechea. Also with me today is Open Text's CFO, Paul McFeeters. As with our previous calls, we'll read prepared remarks, followed by a question-and-answer session. The call will last approximately one hour with a replay available shortly thereafter. I would also like to direct investors to the Investor Relations section of our website, where we have posted an updated PowerPoint.

Please note that during the course of this conference call, we may make statements relating to the future performance of Open Text that contain forward-looking information. While these forward-looking statements represent our current judgment, actual results could differ materially from a conclusion, forecast or projection in the forward-looking statements made today. Certain material factors or assumptions were applied in drawing any such conclusion, or while making any such forecast or projection as reflected in the forward-looking information.

Additional information about the material factors that could cause actual results to differ materially from the conclusion, forecast or projection in the forward-looking information, and the material factors or assumptions that were applied in drawing the conclusion while making the forecast or projection as reflected in the forward-looking information, as well as risk factors that may affect the future performance and results of Open Text are contained in Open Text's Form 10-K and Form 10-Q, as well as in our press release that was issued earlier today, each of which may be found on our website.

We undertake no obligation to update these forward-looking statements unless required by law. In addition, our conference call will include a discussion of certain non-GAAP financial measures. Reconciliations of all non-GAAP financial measures to their most directly comparable GAAP measures have been included in today's press release, which may be found on our website.

And with that, I'll hand the call over to Paul McFeeters.

Paul J. McFeeters

Chief Financial Officer, Open Text Corp.

Thank you, Greg. Turning to the financial results, I'll highlight our second quarter fiscal 2012. Total revenue for the quarter was \$321 million, up 20% compared to \$267 million for the same period last year. License revenue for the quarter was \$90 million, up 13% compared to \$79 million reported for the same period last year.

Maintenance revenue for the quarter was \$165 million, up 21% compared to \$137 million in the previous year. Services and other revenue in the quarter was \$66 million, up 29% compared to \$52 million in the same period

last year. Gross margin for the quarter before amortization of acquired technology remained relatively consistent this quarter at 73.8% compared to 74.7% in the same period last year. The decrease is primarily related to the initial write down in maintenance revenue of \$1.7 million due to the acquisitions of the Metastorm and Global 360.

Pre-tax adjusted operating margin before interest expense and stock compensation was approximately \$99 million this quarter compared to \$84 million in Q2 last year. Adjusted net income increased 15% to \$82 million this quarter from \$71 million in the same quarter last year. Adjusted EPS was \$1.39 on a diluted basis, up 14% from \$1.22 per share for the same period a year ago. The sequential effect of foreign currency movement on adjusted EPS for Q2 was a negative \$0.03.

The adjusted tax rate for the quarter is 14%, the same as it was for last fiscal year. Net income for the second quarter in accordance with GAAP was \$47 million, or \$0.81 per share on a diluted basis, compared to \$37 million or \$0.64 per share on a diluted basis for the same period a year ago.

There were approximately 58.7 million shares outstanding on a fully diluted basis for the second quarter. Operating cash flow was approximately \$45 million compared to \$40 million in the same quarter last year. On a year-to-date basis, operating cash flow was \$90 million compared to \$89 million in the same period last year, cash flow year-to-date has been impacted by three days of additional DSO [ph] propagating (4:40) a timing difference of approximately \$12 million, and changes in working capital of \$8 million.

On the balance sheet at December 31, 2011, deferred revenue was \$237 million compared to \$266 million as of June 30, 2011, and accounts receivable was \$167 million compared to \$155 million at the end of last fiscal year. Days sales outstanding were 47 days as of December 31, 2011 compared to 49 days at June 30, 2011 and 44 days at the end of Q2 of fiscal 2011.

During the quarter, we closed our financing by way of a term loan A of \$600 million and an available operating line of \$100 million. Our pricing on the term loan A is LIBOR plus 2.50% with no floor on LIBOR. If our debt to EBITDA ratio reaches 1.5 to 1, our rate drives to LIBOR plus 2.25%. Our current ratio is 1.8. Our net additional cash was \$314 million after repaying the previous term loan B in the amount of \$285 million and a revolver in the amount of \$49 million.

There was no change to our pre-tax adjusted operating model for this quarter and we expect our annual operating net margin model continue to be in the range of 25% to 30%. Our recent acquisitions continue to have an impact on the overall operating margins in FY '12, as we continue to bring them up to Open Text's operating model. We anticipate that this will improve through the year, but will not be fully on target until fiscal '13. The full details of our operating model are available on our website.

Now, I'll turn the call over to Mark.

Mark J. Barrenechea

President and Chief Executive Officer, OpenText Corporation

Thank you, Paul, and welcome everyone to our FY '12 Q2 earnings call. Let me start with saying, I am thrilled to join Open Text as CEO and be located out of Waterloo, Ontario. I come to Open Text with 20 years of leadership experience in the high-tech industry, primarily in enterprise software. These 20 years include being President and Chief Executive Officer at Silicon Graphics, Executive Vice President and Chief Technology Officer at Computer Associates, as well as Senior Vice President of Applications Development and a member of the executive management team at Oracle. These previous leadership experiences place me in a unique position to bring Open

Text to the next level of success. I'd like to spend the time today on two things: an overview of our strong Q2 results, as well, my initial observations on Open Text, including our strategic opportunity and my initial set of priorities.

Let me start with the quarter. Q2 revenue was \$321.5 million with license revenue of \$89.7 million and an adjusted earnings of \$1.39. All three results were record highs for Open Text. I am very pleased with the quality of Q2 revenue. License revenue grew 37.8% quarter-over-quarter and 13.3% year-over-year. Further, nearly 50% of our license revenue was sourced from new customers. The Americas contributed 53% of total revenue, EMEA performed well in a tough economic environment with a 40% contribution and APJ, albeit on a smaller base, had strong growth, while contributing 7% of total revenues. The maintenance business was strong and our professional services margins have improved for three quarters in a row. There were seven transactions over \$1 million and 22 additional deals over \$500,000.

The integration of Metastorm and Global360 is proceeding as planned and we expect to see revenues this fiscal year more in line with our historical acquisition models, which is a 15% revenue decline in the first year of combined operations. Overall, our business performed well, despite continuing economic uncertainty in many parts of the world.

Also within the quarter, we held our Annual User Conference, Content World, in Orlando, Florida. It was another successful event for us with over 1,400 attendees. We also made several important product announcements during the quarter with the underlying theme of access to information.

Let me spend a moment and walk you through these. First, Tempo. Tempo client/server edition is a new module integrated into our core ECM Suite. It is a no-training-required, thus easy to use secured document sharing product that allows enterprise users to share and manage content on smartphones, tablets, PCs or laptops, while synchronizing information across these devices. It has the attributes for the cloud, but inside the firewall. Tempo goes GA this quarter.

We also released OpenText Portal Site Management, so users can gain access to SAP ERP content through one piece of software. We also released OpenText Auto-Classification for unstructured data, giving organizations a powerful way to manage the retention and disposition of high-volume, low-touch content such as social media, email, office documents and legacy content. We took our business process management software on mobile, allowing organizations to initiate, approve and participate in BPM processes for many devices.

We also announced major enhancements to Version 2 of OpenText Web and Social Analytics, which allows for deep real-time web usage and social interaction insights, so customers can identify actionable trends and optimize their online initiatives. It was a good product quarter, but even better customer quarter.

Hydro One in Canada is simplifying their customer care and field service processes with our ECM software. Peabody Energy in the U. S. has extended their core ECM usage into email management. Salzgitter AG, a leading European steel and technology company has extended their ECM usage with our SAP Vendor Invoice Management software. Taco Bell's web presence is now powered by our Web Experience Management software and opened -- and hosted at OpenText. Tenet Healthcare Corporation, one of the largest investor-owned healthcare delivery systems in the United States, purchased the OpenText ECM Suite as a resource to enhance their document and records management functionality and efficiency. Volkswagen Finance in China is employing our ECM Suite for dealer contracts management.

I wanted to spend time on customers from the quarter, because these examples illustrate our strategic opportunity and ultimately why I joined OpenText. There are four reasons that convinced me OpenText will lead the market.

Number one, ECM is far from mature. OpenText is best positioned to continue to gain share over EMC and Documentum and IBM and FileNet. We view Microsoft as a partner today, as we build products on top of SharePoint and Web Experience Management is essential as we orchestrate content together, both inside and outside the firewall. Core ECM is clearly important to us and the market is far from mature.

Number two reason, process-enabling core ECM. We call this BPM and as you know we have made two strategic acquisitions in this space. Three, delivering packaged applications that are content centric not transaction centric. There are many enterprise applications that will benefit from a content centric orientation such as invoice management, expense management, claims processing, contract management, loan processing, field service, search and many more. The style of these applications require a foundation of ECM and BPM.

Longer term, as categories evolve, the market will include ECM, BPM and DI. OpenText is uniquely positioned to not only capture these opportunities, but also create them. We have 4,600 employees focused on ECM and BPM proven products, global operations and scale in 31 countries. Many markets we have either lightly penetrated or not touching at all, strong financials and a stellar customer base to build upon. And perhaps most importantly, OpenText employees are the experts in content management. What I see inside that perhaps you can't see outside is the amazing passion and talent at OpenText.

Further, we have strong partnerships with core application providers and unique technology that open these platforms for content, processes and applications. Our relationship at SAP is strong, our relationship with Microsoft continues to emerge and our relationship with Oracle is an untapped opportunity.

Let me transition to our FY '12 financial model, go forward operations, an initial view of my priority. As for the FY '12 financial model, I feel confident in our previously announced pre-tax adjusted operating margin target. As for operations, my priorities are pretty straightforward, grow the business, improve our efficiency and continue with strong earnings.

As for growing the business, we need a multi-path execution strategy with a strong emphasis on license growth. This means an optimized direct go-to-market sales force companioned with a world-class channel, increased emphasis on large technology partners that expands our distribution capabilities, selectively filling territory coverage, a stronger presence in key markets and verticals such as U. S. Federal, U. S. Commercial, Japan, the BRICs as well as manufacturing. I also see opportunity where we can add more value to customers in our maintenance offering. We will continue to acquire.

Let me just spend a little more time on the channel. OpenText is well positioned to have a larger and more robust channel in partner program. First through Tier 1 ERP providers, second through significant Tier 2 application providers, and third a larger SI and FSI network.

As we're improving our efficiency, best-in-class businesses get more efficient year-over-year. 30 days into OpenText, I can already see a path to releasing unlocked value and some of our processes and approaches to running the business. As we unlock that value, we unlock dollars that can be reinvested back into the business. Strong earnings and cash flow remain a priority.

In summary, we are in the right double-digit market. ECM, BPM, archiving, fax, text analytics, et cetera. Our target model R&D expense is between 14% and 16% of total revenues. We are in the right markets with the right spend. But there is a disconnect between market growth rates, our spend and our growth. To me that is the opportunity. And the basic solve is an optimized selling model and separating growth products for sustaining margin products, so as a company, we have more focus while maintaining operating margins. For all these reasons, the future has never looked better for OpenText.

Before I open the call for questions, I want to recognize the incredible contribution from John Shackleton in his many years of service here at OpenText. We all wish him the best in his future endeavors.

With that, I'd like to open the call for your questions.

QUESTION AND ANSWER SECTION

Operator: Thank you. We will now begin the question-and-answer session. [Operator Instructions] We have a question from the line of Richard Tse with Cormark Securities. Please go ahead.

Richard Tse

Analyst, Cormark Securities, Inc.

Q

Yeah. Thank you. A couple of quick questions here. Mark, how would say your style in the outset differs from John's and the priorities that you're focusing on?

Mark J. Barrenechea

President and Chief Executive Officer, OpenText Corporation

A

Well, again, I would keep style aside for a moment.

Richard Tse

Analyst, Cormark Securities, Inc.

Q

Right.

Mark J. Barrenechea

President and Chief Executive Officer, OpenText Corporation

A

And I think we'll just talk about the opportunity and the priorities. We can come back to style.

Richard Tse

Analyst, Cormark Securities, Inc.

Q

Yeah.

Mark J. Barrenechea

President and Chief Executive Officer, OpenText Corporation

A

I'd just like to reinforce the opportunities that I see here in the first 30 days. Number one continues to be core ECM share gains. It's going to be a unifying narrative for us. We're competing very effectively against IBM in EMC, and you're going to see us dial up in this market for core ECM market share gains. Second, the BPM market. Again, third, if I look at what we're doing with SAP and Microsoft, we're probably under 10% penetrated in their installed bases. So we're just in the first inning of a nine-inning game of continuing to build an ecosystem around the core ERP providers. And I look at our distribution capability; there is just opportunity in key verticals. You look at the public sector; this should be in the top three verticals of what we do. Manufacturing isn't highlighted as a key vertical at all. And then when you kind of drive down in Japan, you have Commercial and Federal, these are opportunities for us that we're just not connecting at scale, our product to the customers. So that's the opportunity that in my first 30 days seems to be pretty clear.

Richard Tse

Analyst, Cormark Securities, Inc.

Q

All right.

Mark J. Barrenechea

President and Chief Executive Officer, OpenText Corporation

A

Yeah, in terms of priorities, I think I can state this pretty simply, it's earnings and license growth. And that quickly deconstructs into delivering a solid FY '12, balancing organic growth with acquired growth, while continuing to be margin focused. That might be a stronger emphasis on that balance for us leading with acquisitions. And probably a stronger orientation towards strategic operations, which you're going to hopefully translate into improved efficiency and certainly our out of the gate hope is that we can unlock some value and free up dollars, so we can reinvest in the business without affecting our margin profile.

Richard Tse

Analyst, Cormark Securities, Inc.

Q

And is your bonus structure similar to the one that John had as outlined in your circulars?

Mark J. Barrenechea

President and Chief Executive Officer, OpenText Corporation

A

I think my comps been filed already on file, so you can take a read of that.

Richard Tse

Analyst, Cormark Securities, Inc.

Q

Okay. And then sort of a -- little bit of a loaded question here, but I know you've gone through your priorities, but if you had to change like a single thing right now in terms of what you've seen in the past 30 days, what would that be?

Mark J. Barrenechea

President and Chief Executive Officer, OpenText Corporation

A

I would say a stronger emphasis on the core ECM market. Again, we're competing very effectively against EMC and IBM. We released an investor deck today, I don't know if folks had a chance to see it, if not, please go to our website, we added a slide in there that sort of shows the overall trend of IBM and EMC and us. We're on uptick, they're on a down tick. So if there is one thing, I'd say increasing the narrative around gaining share in the core market because it's far from mature.

Richard Tse

Analyst, Cormark Securities, Inc.

Q

That's great. Thank you very much.

Mark J. Barrenechea

President and Chief Executive Officer, OpenText Corporation

A

Thank you.

Operator: Thank you. And our next question comes from the line of Brian Freed with Wunderlich Securities. Please go ahead.

Brian S. Freed

Analyst, Wunderlich Securities, Inc.

Q

Okay. Thanks for taking my call and congratulations Mark. So, looking forward to continuing to deal with you.

Mark J. Barrenechea

President and Chief Executive Officer, OpenText Corporation

A

Thanks Brian. You're not going to ask me an E&O question today. Are you?

Brian S. Freed

Analyst, Wunderlich Securities, Inc.

Q

No, no. But I did want to just -- since I'm pretty familiar with your background and you mentioned Oracle is a currently promising but as yet untapped opportunity, given your history with Oracle can you talk a little bit about how you think you might be able to leverage those past relationships and that past history to move Oracle into a tapped opportunity and a revenue producing partner?

Mark J. Barrenechea

President and Chief Executive Officer, OpenText Corporation

A

Sure. Great question, Brian. Well, first of all the relationships are there. I've spoken to the leadership team at Oracle already. And the door is open for us. And if I make a contrast to the SAP relationship, because I think it will open up or maybe make a little clearer the opportunity with Oracle, is -- one of the reasons our SAP relationship has been very strong is that it first starts off with our products. Our products are well integrated and differentiated from Travel Expense Management, Vendor Invoice Management. We add clear value to customers. And third we are very well aligned in our field organizations, from senior leadership down to individual AEs, Account Executives, throughout the world. So, compelling product, clear alignment, education down to the AE level. When I look at the Oracle opportunity, we still have a little work to do in our product to have that bright line value and differentiation. The door is open for us to build that strategic alliance to help Oracle customers. But it's sort of a tale of two different stories. One is a more mature product versus a less mature product. But Oracle is certainly very interested in working with us.

Brian S. Freed

Analyst, Wunderlich Securities, Inc.

Q

Okay. Thanks.

Operator: Thank you. And our next question comes from the line of Kris Thompson from National Bank Financial. Please go ahead.

Kris Thompson

Analyst, National Bank Financial Brokers

Q

Great. Thanks Mark and welcome to Canada.

Mark J. Barrenechea

President and Chief Executive Officer, OpenText Corporation

A

Thank you.

Kris Thompson

Analyst, National Bank Financial Brokers

Q

I just wanted to chat a little bit about the December quarter. A lot of people were a bit paranoid about lower than normal budget flush. It looks like you guys have managed to escape that. I mean, how did you guys escape that crisis? And in your recent discussions with customers do you think spending is going to slow a little bit in Half 1? And maybe you could just give us an idea of the spend into Half 1 and Half 2 of the calendar year, if you don't mind?

Mark J. Barrenechea

President and Chief Executive Officer, OpenText Corporation

A

Sure. I wasn't obviously here through Q2. But I can give you a sense of what I'm seeing my first 30 days in. The first is why customers are considering us. And I can already see a very strong clustering of reasons. One, compliance and regulation, the need to manage bigger and unstructured data, information security remains top of mind, mobility cloud and reducing cost by globalizing and standardizing on best practices. So in my first 30 days with the sales force and customers, you can already see a very strong buying consideration with OpenText solutions, and I think that pairs very well to uncertain economic times.

Now in a tougher economy, look, we're going to control what we can control and what we control is where we place our team, what verticals we go after, what opportunities we try to develop, spending more time and insight in pipeline. I don't see any change in economic environment quarter-over-quarter, but I'll tell you that the clustering of why folks are considering OpenText seem pretty compelling both in an up or in a down economy.

Kris Thompson

Analyst, National Bank Financial Brokers

Q

Okay. That's helpful. And you did mention the Tempo solution in your prepared remarks. Can you just give us an idea of the pricing model for that solution and the client interest so far and maybe if you could provide some materiality to your revenue profile going forward, so we get our heads around it? If that's really going to be a big driver this year or is it a few years away still?

Mark J. Barrenechea

President and Chief Executive Officer, OpenText Corporation

A

Sure. So in terms of the approach to pricing, Tempo is an additional charged-for module on top of ECM. So it's not part of ECM EULA or bundle, Yapta, the initial version of Tempo is an additional module on top of that already deployed and paid for license, so it's a additional revenue. We don't give guidance for the year. Paul, may want to comment on the go forward looking revenue, but right now there are no revenue projections for it or no change to our model for the year.

Kris Thompson

Analyst, National Bank Financial Brokers

Q

Okay. Fair enough. And just one more from me actually, Paul, just on the CapEx, it looked a little bit hotter than I was expecting in the quarter, did you have some more CapEx in the Waterloo for your new building there, are you done and what's the normal maintenance level of CapEx going forward on a quarterly basis?

Paul J. McFeeters

Chief Financial Officer, Open Text Corp.

A

Yes. Kris, we do have our final CapEx for the Waterloo building was in this quarter about \$4 million. So if you back that out that will be our normal run, we CapEx in about the mid-\$20s as our ongoing operating CapEx. So

this year we picked up that additional floors, as I said, that should be pretty well it for Waterloo now going forward.

Kris Thompson

Analyst, National Bank Financial Brokers

Q

Okay. Thanks for taking my question, guys. All the best.

Mark J. Barrenechea

President and Chief Executive Officer, OpenText Corporation

A

Thanks.

Operator: Thank you. And our next question comes from the line of Scott Penner from TD Newcrest. Please go ahead.

Scott Penner

Analyst, TD Securities

Q

Thanks. Just, first of all, Paul, on the charge this quarter is a little less than I was expecting. I was expecting more around the \$15 million mark. Maybe you could just talk us through whether there is some still to come and what the cash outflow was for this quarter?

Paul J. McFeeters

Chief Financial Officer, Open Text Corp.

A

You mean on special charges?

Scott Penner

Analyst, TD Securities

Q

Yeah, yeah.

Paul J. McFeeters

Chief Financial Officer, Open Text Corp.

A

Yeah, it was \$5 million, the cash out flow was \$4 million -- \$1.4 million for the quarter. I would say for the balance of the year approximately \$7 million, and most of that could show up as a charge in Q3. But the cash for the balance of the year will be something less than that because a lot of that \$7 million now is for facilities, which flows out overtime. So cash for the balance of the year probably about \$4 million and then the balance of about \$6 million through the end of fiscal year.

Scott Penner

Analyst, TD Securities

Q

Okay. All right. Mark, if I could just ask, you made just a comment on the integration of the BPM assets and I just want to be clear on what you said. I think you said a 15% revenue decline in the first year of operations. I think the guys here were saying about 10% decline on the license revenues; just I wanted to clear that up?

Mark J. Barrenechea

President and Chief Executive Officer, OpenText Corporation

A

Yeah, 15% license revenue reduction.

Scott Penner

Analyst, TD Securities

Q

License revenue, okay. And, Paul, do you have the revenue and I guess earnings contribution from Global 360?

Paul J. McFeeters

Chief Financial Officer, Open Text Corp.

A

The revenue is \$20 million. From a GAAP standpoint, we lost about \$2 million, but from an adjusted standpoint it was accretive about \$0.06.

Scott Penner

Analyst, TD Securities

Q

Okay. And then, just, I guess lastly from me, Mark, just on that the integration of the BPM businesses, there was a timeline laid out where first it was the integration of the two Global 360 and Metastorm separate from the mother ship, and then it would be integrated and cross-selling would come from that. I just wanted just kind of set some expectations as to when we should assume that we're going to start to see some really significant cross-selling opportunities come in then really contribute to the revenue side?

Mark J. Barrenechea

President and Chief Executive Officer, OpenText Corporation

A

My expectation would be with kickoff FY '13 with a worldwide sales force, better trained, better equipped, building pipeline and starting to see some wins. So I'd like to see the junction of FY '13 with BPM fully integrated.

Scott Penner

Analyst, TD Securities

Q

Okay, that's helpful. Just lastly the margin on the professional services was quite a bit higher than it was last quarter and quite a bit higher then, I think, most people were expecting. You said last quarter that I guess the company was feeling a little pinched on professional services capacity, I just want to know if you could update us on how you're feeling about that and whether the margins likely to come back down to the 20% level?

Paul J. McFeeters

Chief Financial Officer, Open Text Corp.

A

I think our longer-term projection is in that range. We certainly, obviously showed good margins, we had full utilization. And as you know in the past Scott, we had provided services at the below optimum rates for certain acquisition, situations, and we didn't really have any of that experience this quarter. From a capacity standpoint, as you can see, yes, we would continue to look to hire in that area, which is of course good news. But I think sustainable margins are more in that 20% range that we've discussed in the past.

Scott Penner

Analyst, TD Securities

Q

Okay. Thanks. I'll pass the line.

Operator: Thank you. And our next question comes from the line of Mike Abramsky with RBC Capital Markets. Please go ahead.

Mike Abramsky

Analyst, RBC Dominion Securities, Inc.

Q

Yeah, thanks very much. Hi Mark, and welcome.

Mark J. Barrenechea

President and Chief Executive Officer, OpenText Corporation

A

Thank you Mike.

Mike Abramsky

Analyst, RBC Dominion Securities, Inc.

Q

Hey, just to Mark, maybe you -- welcomed to hear your comments on why you joined and how you looked at the company and those are very positive. I was wondering, based on your experience and knowledge of knowing the software companies you worked with but others, and also what you see going forward as a kind of global environment. Do you have any thoughts that you are formulating on where OpenText maybe needs to be sured-up to reduce risk to the business model and maybe bring its model more to maximize the opportunities ahead of it?

Mark J. Barrenechea

President and Chief Executive Officer, OpenText Corporation

A

Well, Mike, I'll start with the first -- why I joined. But this is a very good company, going to great. And I've tried to find that one-liner, and the best one-liner I have is a Snapple ad in the U. S, which is the best stuff on earth just gets better. I view this as a very good company. And the opportunity to bring the business to the next big milestone of \$1 billion to \$2 billion, while having amazingly strong earnings, felt like a real good match with my skill sets in the market opportunity. So I'm thrilled to be here and those are the some of the basic reasons I joined.

In terms of the opportunity, my initial thoughts here remain and I don't mean to be repetitive, but when you look at the core market, the core ECM market, it's far from mature. I know it's an existing market, but there will be a leader that emerges with fair market share ownership, the leader in the market gets the lion share of the profits. We're best position to go capture that market opportunity.

Second is content, has to be process-enabled and bringing on two strong assets like Metastorm and Global 360 to have that second pillar of our go-to-market with BPM is pretty appealing. And then third is you look at what Oracle and SAP have achieved in the scale of their companies, it's all around transactional-based applications. But there is a view that as applications get more mobile, more social, on newer type of devices, can there be a class of applications that emerge, that are more content-centric from case management to loan processing, to things such as field service? And that looks like a real opportunity to me, outside looking in and as well as now inside looking out. So those are some of the reasons I joined and some of the things that make me pretty excited about the opportunity.

Mike Abramsky

Analyst, RBC Dominion Securities, Inc.

Q

Okay. That's helpful. And OpenText is traditionally traded at a discount to peers, I think, it may be fair to say partially because of some lack of visibility to organic growth, given the acquisition-centric model as well as other decisions taken such as lack of guidance. And I'm not asking because I'm sure you're unprepared at this point to state whether you're going to change policy or not. But I just wondered if you felt that, with your focus on organic growth that you think some of those issues that have led to those decisions may become more easier or different in the future?

Mark J. Barrenechea

President and Chief Executive Officer, OpenText Corporation

A

Fair enough, Mike. Well, as you know, we're not providing guidance, but we do provide a target model today. And Paul and I have -- we're not going to change any of the metrics or sort of key disclosure around elements for FY'12. But as we get into FY '13, Paul and I will evaluate if there are other ways we want to describe the business going forward. But for FY '12, this quarter -- through the end of the fiscal year, we're not going to change any of the metrics we set out on.

Mike Abramsky

Analyst, RBC Dominion Securities, Inc.

Q

Okay. And then lastly, do you think we should set up for any expectations for either investments or impacts to growth in margins that could be transitional related to you're coming on board with some of the plans that you've seen either short-term or longer-term?

Mark J. Barrenechea

President and Chief Executive Officer, OpenText Corporation

A

Well, I've amplified two statements I've made, right. As we look towards strategic operations, I can already see opportunity to start to unlock some value and free up dollars. And those freed up dollars, I'm going to look to reinvest, right. So they're neutral to the model. And we're going to continue to have a strong emphasis on our operating margin targets. Regardless of the strategy we go down.

Mike Abramsky

Analyst, RBC Dominion Securities, Inc.

Q

Okay. Thank you.

Operator: Thank you. And our next question comes from the line of Paul Steep with Scotia Capital. Please go ahead.

Paul Steep

Analyst, Scotia Capital Markets

Q

Great. Thanks. Welcome, Mark.

Mark J. Barrenechea

President and Chief Executive Officer, OpenText Corporation

A

Thank you, Paul.

Paul Steep

Analyst, Scotia Capital Markets

Q

Hi guys, my first question sort of falls on what we've just been discussing, going back over the call here, so far you've talked a lot about unifying the narrative, dialing up the emphasis in core ECM. I guess, the question will be, what you need to do there? You talked a little and I would read from your prior statement that the investment bubbles aren't going up, maybe they shift around a bit. What also is sort of the timing, when do you think you'd be in place that you'd be ready to run your new Play Book?

Mark J. Barrenechea

President and Chief Executive Officer, OpenText Corporation

A

Well, it's going to be, for the most part, pretty steady as you go in FY '12. We have five months left FY '12. Right. We're here in early February. So been on board for 30 days, I am going to continue to listen, assess, gain perspective. We're going to take an evolutionary approach here through FY '12 and I'd look towards our FY '13 plans of where we may dial certain things up or dial things down. So I want to send sort of a clear message that it's steady as you go in FY '12, I want to make sure here in the early days, I don't lose the opportunity to talk to as many employees, as many customers, as many analysts, as many investors as I can to keep forming the opinion on our priority. These are my initial views. So it's steady as you go in FY '12, some evolutionary change will happen in FY '12, look towards FY '13 where we dial certain things up and certain things down.

Paul Steep

Analyst, Scotia Capital Markets

Q

Okay. Just, I guess, tag on to that point or the other question, it sort of got raised from your comments here. You talked more about, I guess, focusing in and highlighting growth products versus sustaining market products?

Mark J. Barrenechea

President and Chief Executive Officer, OpenText Corporation

A

Sure.

Paul Steep

Analyst, Scotia Capital Markets

Q

When do you think, we sort of talked about, is this sort of -- we'll revisit these things come June and get more feedback from you prior to then or what should people expect?

Mark J. Barrenechea

President and Chief Executive Officer, OpenText Corporation

A

Yeah. I think this will start to get into the cadence of the business almost right away, actually. So let me spend a little time on that, I talked about optimize selling and sort of separating growth and sustaining value. Now on the direct side, on how we go to market on the direct side, there are certainly some coverage gaps that I'd like to see balanced. And the planning for that and the adjustment for that, we're not going to wait for a long time to do. U. S. Commercial, U.S. Public Sector, I look at the New York Tri-State area, Japan, India as areas that are deserving more coverage, either direct or indirect. I'm evaluating the channel on our indirect business. And as you segment this, we obviously have our technology partners as SAP, Oracle, Microsoft. We have business transformation partners like Accenture and Deloitte, there are others to add there. In EMEA, Atlas, Origin and T-Systems, others to add there. In the U. S. Raytheon and Northrop, but there is a good list of top six at that size I would like our channel team to start opening some doors with. And in APJ, we're just starting on a channel with Tata, TCS, Wipro and Infosys as well as Mitsubishi in Japan.

So when I talk about the optimized selling model, it's really kind of picking higher value areas that we'd like to be in and balancing our investments and starting to elevate the channel in our ecosystem. And on separating the growth versus sustaining value I'd like our sales organization really to major in the majors. And majoring in the major is focused on license growth, but the customer service organization to major on sustaining value. And as we sort of start to separate that gradually, that gives the sales force more focus, easier opportunity to train SEs, easier ability for SEs to understand the core products and hopefully increase our win rate.

Paul Steep

Analyst, Scotia Capital Markets

Q

Fair enough. I guess the last one, just to make sure. All that was great and helped clarify things. Last one, you sort of flag, is it fair to sort of state out of your comments tonight, you talked about balancing acquisitions versus organic growth in the next year that really we're going to likely see an evolution here and you're going focus on these fundamental changes, and we're unlikely to see any sort of big deals unless something fantastic sort of falls out of the sky on us?

Mark J. Barrenechea

President and Chief Executive Officer, OpenText Corporation

A

Well, yes, it's two things there. I want to emphasize evolution versus revolution. And let me just comment on acquisitions, right. Acquisitions are a clear core competency of the business and we will continue to acquire. As I look at the basic categories that are interesting, I think of three categories that are interesting and one category that's a little less interesting. Of the three categories that are interesting are those opportunities where we can gain core market share. Second would be relevant market segments, BPM was a relevant market segment that we entered via acquisition. Of course, we have a third category, which I wouldn't take off the table, but a little less prominent right now are those transformative acquisitions. The category I'm much less interested in is small point technology buys.

Paul Steep

Analyst, Scotia Capital Markets

Q

Okay. Great. Thanks a lot.

Operator: Thank you. And our next question comes from the line of Thanos Moschopoulos from BMO Capital Markets. Please go ahead.

Thanos Moschopoulos

Analyst, BMO Capital Markets (Canada)

Q

Hi. Good afternoon. Welcome on board, Mark.

Mark J. Barrenechea

President and Chief Executive Officer, OpenText Corporation

A

Thank you.

Thanos Moschopoulos

Analyst, BMO Capital Markets (Canada)

Q

As we look at the deal streams in the past quarter, good volume of larger deals and good mix of revenue coming from new customers. Are there any one or two areas that really stood out in driving that, be it transactional ECM through the SAP relationship or SharePoint related solutions? Was there one or two big factors in that strength or was it sort of across-the-board, across the product portfolio?

Mark J. Barrenechea

President and Chief Executive Officer, OpenText Corporation

A

Well, I would start with maybe geography and then drill below that. If we just run by the numbers, APJ and Latin America were certainly strong and I would say that was driven by an SAP relationship in ecosystem. Certainly the U. S. held their own within the quarter. And within Europe, I would say that the two GOs that stood out for us,

contributing well was Germany and France, and I look at that probably more as core market gains versus ecosystem partners.

Thanos Moschopoulos

Analyst, BMO Capital Markets (Canada)

Q

Okay. And then, in terms of product areas, are there any -- you mentioned that you see core ECM as a good opportunity. Any other specific areas that you think will be instrumental in driving accelerated growth going forward?

Mark J. Barrenechea

President and Chief Executive Officer, OpenText Corporation

A

Certainly core ECM, BPM and I would also put out there our WCM products as well.

Thanos Moschopoulos

Analyst, BMO Capital Markets (Canada)

Q

Okay. And then, finally, just a question for Paul. We saw the maintenance margin come down a little bit relative to the prior quarter. Is there any dynamic there we should be aware of?

Paul J. McFeeters

Chief Financial Officer, Open Text Corp.

A

No. Not particularly in a trend area. I would say, from our own perspective, I think, it's trending pretty much to where we think or do point that to come down a little bit. I think just a little different balance under our third party software in that mix and that varies from quarter-to-quarter.

Thanos Moschopoulos

Analyst, BMO Capital Markets (Canada)

Q

Okay. That's great. I'll pass the line. Thank you.

Mark J. Barrenechea

President and Chief Executive Officer, OpenText Corporation

A

Thank you.

Operator: Thank you. And our next question is from the line of Sera Kim with GMP Securities. Please go ahead.

Sera Kim

Analyst, GMP Securities LP

Q

Hi. Good evening, and welcome to OpenText. Just wondering, in terms of the geographic areas, you talked about seeing strength in France and Germany. Are there any areas of specific concern that you're seeing as we look ahead in the pipeline? And then I'm also wondering if you can comment on emerging markets and what your strategy is there? Do you still expect to use partners like SAP to penetrate those markets or are you looking to add direct representation in those areas as well?

Mark J. Barrenechea

President and Chief Executive Officer, OpenText Corporation

A

Sure. Thanks Sera for the question. I'd say if there is one area where I'm spending a little more time than others that continues to be Europe. Certainly not a surprise for anyone. And 40% of our Q2 revenues came from EMEA.

Certainly, probably one of the tougher economies out there right now. What I'd certainly liked about our business in Europe is that we have more scale in Germany anywhere else, and it's the best economy in Europe. And to a large degree, because we have a lot of revenues and costs matched, we have some natural hedging built into our business in Europe.

So certainly I'm spending more time thinking about Europe than any other geography as an area to be watchful of. In terms of the BRICs, Brazil, Russia, India, China, we're doing well in Brazil. We have a good team there, we have good partnerships there, and it's certainly a highlight for us for everything in Latin America. India is an untapped opportunity for us, we have over 300 employees in India because we have a large R&D facility there and we haven't really tapped into yet that ecosystem from TCS, Infosys and Wipro. And certainly with my Oracle background, I have a lot of contacts and a lot of relationships and lot of experience in that market. I'm not as educated on Russia, on our business in Russia yet. And in China, we had a nice win within the quarter, and we'd certainly be leveraging our SAP relationship there.

So two out of three, I go Brazil and India. I'm quite enthused about Russia, I'm not educated yet, and we had a nice win in China and are certainly trying to build off our SAP relationship.

Sera Kim

Analyst, GMP Securities LP

Q

Okay, great. And just last question, I guess, earlier in the call, you mentioned some coverage gaps, in I think you said, U.S. Federal, Commercial and Manufacturing. What's your go-to-market strategy in those areas to help you increase your penetration?

Mark J. Barrenechea

President and Chief Executive Officer, OpenText Corporation

A

Sure. So we just take U. S. Federal, we just hired a new leader of U. S. Federal, based out of the D. C. area and comes with a lot of experience both in the DoD and the intelligence communities in the U. S., and starts with leadership and focus. So we just hired a nice leader there, as well as a lot of customers buy indirect through FSIs. So new leadership as well as working with the federal system implementers who participate or drive a lot of the solution architecture.

In Japan, it's a market that we historically haven't done an acquisition in, we built that team organically. I think they need a little more attention and perhaps a little more investment. In Japan, through the years I hope will really emerge as a top contributor for us. I think that's good old fashioned execution and prioritization on a country like Japan.

Sera Kim

Analyst, GMP Securities LP

Q

And what percentage of revenues is coming from Japan and where do you want it to go?

Paul J. McFeeters

Chief Financial Officer, Open Text Corp.

A

All of APJ, Sera, is about 7% and I would say Japan is probably less than half of that.

Sera Kim

Analyst, GMP Securities LP

Q

Okay. Great. Thank you.

Operator: Thank you. And our next question comes from the line of Eyal Ofir from Canaccord Genuity. Please go ahead.

Eyal Ofir

Analyst, Canaccord Genuity Corp.

Q

Thanks for taking my question, and welcome aboard, Mark.

Mark J. Barrenechea

President and Chief Executive Officer, OpenText Corporation

A

Thank you.

Eyal Ofir

Analyst, Canaccord Genuity Corp.

Q

So just, kind of very high level. As you're looking out into the pipeline, obviously you talked about some of the opportunities in Europe and Germany specifically and I'm assuming you're still seeing a lot of stuff in the U. S. Can you just talk about geographically where you're seeing the biggest opportunities in your pipeline, and what gets you excited in some of the more emerging areas?

Mark J. Barrenechea

President and Chief Executive Officer, OpenText Corporation

A

Well, I would just sort of re-emphasize what I said, right. I mean we have a strong America's business and looking at U. S. Commercial and U. S. Federal, certainly, is of high interest and high impact. We sought opportunities clearly in Canada as well, building out even more in the public sector here in Canada, both at the provincial as well as the federal level, and making sure that our top contributors in Europe, U. K., Germany and France, are getting all the support that they need. So I'd say those are the majors for me right now in terms of the pipeline in the second half of the year.

Eyal Ofir

Analyst, Canaccord Genuity Corp.

Q

Okay. And in terms of the products that are driving some of the pipeline, is it primarily core ECM or are you starting to see some of the new products launched late last year starting to come into the pipeline, such as Tempo, and what kind of feedback have you gotten so far from some of the new products from customers?

Mark J. Barrenechea

President and Chief Executive Officer, OpenText Corporation

A

Yeah. I'm going to probably have to defer that to our next call. Certainly, what I'm seeing most of the pipeline right now, 30 days in, really revolve around ECM, BPM, WCM, and again I'm majoring in the majors right now as I work through our 4,600 person company. So that's certainly what I'm seeing the most of. In terms of Tempo, we're just selling GA. The initial reaction is very favorable. Now this is an easy to use, easy to install, no training required module that works across multiple devices. It feels very much like almost a consumer application in its ease of use. So there's a lot of excitement and enthusiasm around the offering. And our first target is going after the installed base and trying to extend share and license within the installed base. Our second version of the product would be more focused around bringing new customers to the OpenText family. So quite a bit of interest and enthusiasm, beautiful UI and operating module, first target is the installed base, second version of the product will be targeted more towards expanding the installed base.

Eyal Ofir

Analyst, Canaccord Genuity Corp.

Q

Okay. Thank you. And I guess just one last question from me. You talked about your kind of approach to growing in emerging markets, but if you exclude India and China, when you look at APJ and obviously Japan as well, are you looking into more [ph] because it's foreign, (51:24) more direct sales there, like, increase the head count or are you still focused on leveraging the current partner ecosystem?

Mark J. Barrenechea

President and Chief Executive Officer, OpenText Corporation

A

APJ is traditionally an indirect business. And I would sort of classify my first observation that we're following a very good model in APJ, which is where you have a direct assist selling force. So we have direct account executives in APJ, they have partners there opening doors. We go in to direct assist in a selling model. So APJ is typically, given the size of the geography, much more of a channel orientation versus building a direct sales force. Having said that, I think there are some select places where we do want direct sales reps, such as Japan.

Eyal Ofir

Analyst, Canaccord Genuity Corp.

Q

Okay. Thanks. I'll pass the line.

Operator: Thank you. And our next question comes from the line of Blair Abernethy from Stifel Nicolaus. Please go ahead.

Blair H. Abernethy

Analyst, Stifel Nicolaus Canada, Inc.

Q

Thank you, and welcome aboard, Mark.

Mark J. Barrenechea

President and Chief Executive Officer, OpenText Corporation

A

Happy to be here. Thank you.

Blair H. Abernethy

Analyst, Stifel Nicolaus Canada, Inc.

Q

Just two questions, I guess, one on the government vertical side and your thoughts there, and then secondly organic growth. On the government vertical side, could you just give us your sense of the selling environment out there now, obviously with all the macro concerns in Europe and the goings-ons, how was your Q2 in Europe on the government side and how are their budgets looking in 2012?

Mark J. Barrenechea

President and Chief Executive Officer, OpenText Corporation

A

Well, I have no problem saying I don't know an answer to something. And particularly on the government side in Europe, I'm not as close to that. So, Paul, I don't know if you have any view of that, but 30 days in, I'm not as close to that on the EMEA government side.

Paul J. McFeeters

Chief Financial Officer, Open Text Corp.

A

Yeah. I would say the overall government vertical stayed about the same as the previous quarter, and we do have good representation from Europe and from the UK. So it would have been a steady business. We didn't break it down by geography other than the overall vertical is 11%.

Blair H. Abernethy

Analyst, Stifel Nicolaus Canada, Inc.

11%.

Q

Paul J. McFeeters

Chief Financial Officer, Open Text Corp.

World-wide.

A

Blair H. Abernethy

Analyst, Stifel Nicolaus Canada, Inc.

Okay. Great. And secondly, Mark, just on if you look out over the next year, what do you think are the highest impact steps or areas that you can go after to help step-up the organic license growth in the business?

Q

Mark J. Barrenechea

President and Chief Executive Officer, OpenText Corporation

I know I'm probably going to sound like a broken record, but number one, core ECM share market gains. Number two, is getting our worldwide sales force trained, educated, well equipped to be able to sell business process management. I'd say those are the two big ticket items for us as we look at organic growth.

A

Blair H. Abernethy

Analyst, Stifel Nicolaus Canada, Inc.

Great. Thank you. And Paul just on the quarter -- any large deals like deals over \$2 million or \$3 million?

Q

Paul J. McFeeters

Chief Financial Officer, Open Text Corp.

No. The \$1 million dollar plus deals were -- there was no single large deal in that place.

A

Blair H. Abernethy

Analyst, Stifel Nicolaus Canada, Inc.

Okay, great. Thanks very much.

Q

Operator: Thank you. And our next question comes from the line of Michael Nemeroff from Morgan Keegan. Please go ahead.

Michael B. Nemeroff

Analyst, Morgan Keegan & Co., Inc.

Hi, guys. Thanks for taking my questions. Mark, congratulations on the job. I'm looking at the presentation on the web and one of the growth drivers, it says BI, I mean, and I joined the call a bit late. Could you expand on this intelligence and how do you think that's going to drive some core growth going forward.

Q

Mark J. Barrenechea

President and Chief Executive Officer, OpenText Corporation

A

Sure. Thanks for the question, Michael. Yeah, I walked through sort of what we looked at the immediate opportunities, core ECM business process management, sort of a second phase of content centric applications and even longer term looking at the content category evolving into more of an information category that encompasses ECM, BPM and beyond. So our immediate opportunity obviously is in our core market in BPM, our medium-term application is in longer term as the category evolves. So we're going to consider looking at partners, building or buying, as this category evolves. I don't see this as a short-term contributor to revenue, but more as a directional statement as where we think the category is going to go. We'll follow the evolution of the category and start to think about whether we're going to partner, build or buy.

Michael B. Nemeroff

Analyst, Morgan Keegan & Co., Inc.

Q

Great. And then, just a couple of quick ones for Paul. I was wondering, if you wouldn't mind giving us the revenue contribution from Metastorm in the quarter, and then also, what the license contribution from the BPM businesses was total? And then also I just have a question on deferred revenue, it seemed to be down a little bit, a little bit more than I was expecting, if you can comment on that please?

Paul J. McFeeters

Chief Financial Officer, Open Text Corp.

A

Sure, Mike. Well, I'm going to hesitate on the first question because, as you know, we don't separate the revenues on [ph] nano-global (57:01) we have, because we have in our Q. Perhaps I'll help you out a little bit more than that typically. I mean, we are, as Mark indicated, we're about expecting a 15% drop in license revenue in the first year as opposed to previously announced maybe 10%. So I would say if you had the last quarter, we're down a little bit from that, not significantly. It was also accretive, I mentioned, [indiscernible] (57:56) accretive by \$0.06 and our results in that range of accretive to adjusted earnings. That's probably the most disclosure I presented on that one.

Deferred revenue continues, our renewal rates do continue to be at 92%, it's where we think it should be. As you know, deferred revenue decreases every quarter, and I know you know that, and you said it was down a little bit more than you thought. It's in line with what we're expecting, we're not seeing any change in our historical [ph] mill rates (56:54) in that 92% range.

Michael B. Nemeroff

Analyst, Morgan Keegan & Co., Inc.

Q

Okay. Great. I'll pass it along. Thanks very much.

Operator: Thank you. And at this time, I'd like to turn the conference back over to Mr. Secord for closing comments.

Greg Secord

Vice President-Investor Relations, Open Text Corp.

Thank you. And thank you everybody for joining us. Just a reminder, OpenText will be presenting at a couple of conferences in the quarter, including the Stifel Financial Conference on February 9, in Greater LA area and the Morgan Stanley Conference on February 27th in the San Francisco area. And with that, we thank you all for joining us and we'll talk to you next quarter.

Operator: Ladies and gentlemen, this does conclude our conference for today. We thank you for your participation. And at this time, you may now disconnect.

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