

01-May-2012

Open Text Corp. *(OTEX)*

Q3 2012 Earnings Call

CORPORATE PARTICIPANTS

Greg Secord
Vice President-Investor Relations

Paul J. McFeeters
Chief Financial Officer

Mark J. Barrenechea
President & Chief Executive Officer

OTHER PARTICIPANTS

Richard Tse
Cormark Securities, Inc.

Kris Thompson
National Bank Financial Brokers

Blair H. Abernethy
Stifel Nicolaus Canada, Inc.

Stephanie Price
CIBC World Markets, Inc.

Sera Kim
GMP Securities LP

MANAGEMENT DISCUSSION SECTION

Operator: Ladies and gentlemen, thank you for standing by. And welcome to the Open Text Corporation Third Quarter Fiscal Year 2012 Financial Results Conference Call. At this time, all participants are in a listen-only mode. Following the presentation, we will conduct a question-and-answer session. [Operator Instructions]

I would like to remind everyone that this conference call is being recorded today, Tuesday, May 1, 2012 at 5 PM Eastern time.

I will now turn the conference over to Mr. Greg Secord, Vice President, Investor Relations. Please go ahead, sir.

Greg Secord
Vice President-Investor Relations

Thank you, and good afternoon. With me today is Open Text's President and CEO, Mark Barrenechea as well as our 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 an 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 that we will refer to in this call. Within the next 48 hours, we will also post a summary table in the Investor Relations section of our website that highlights Open Text's historical trended financial metrics.

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

Thank you, Greg. Turning to the financial results, I will highlight our third quarter fiscal year 2012. Total revenue for the quarter was \$292 million, up 11% compared to \$263 million for the same period last year. Regionally, the Americas contributed 53% and EMEA 38% and Asia Pacific 8%.

License revenue for the quarter was \$61 million, down 10% compared to \$68 million, reported for the same period last year. Customer support revenue for the quarter was \$166 million, up 16% compared to \$142 million in the previous year. Our customer support renewals continue to be approximately 92%.

Services and other revenue in the quarter was \$65 million, up 25% compared to \$52 million in the same period last year. Gross margin for the quarter before amortization of acquired technology was slightly lower this quarter at 71% compared to 73.3% in the same period last year. The lower margin was primarily due to a lower proportion of license revenues and the impact of Global 360 and Metastorm.

The pre-tax adjusted operating margin was \$73.6 million this quarter compared to \$64.1 million Q3 last year, an increase of 15%. Adjusted net income increased 11% to \$59.2 million this quarter from \$53.4 million in the same quarter last year. Adjusted earnings per share was \$1.1 on diluted basis, up 11% from \$0.91 per share for the same period a year ago. GAAP net income for the third quarter was 35 million or \$0.59 per share on a diluted basis, compared to 36 million or \$0.61 per share on the diluted basis for the same period a year ago. There were approximately 59 million shares outstanding on a fully diluted basis for the third quarter. Sequential effect of foreign currency movement on adjusted earnings per share for Q3 was a negative \$0.01.

Total revenue on a year-to-date basis was 902 million, up 21% compared to 748 million for the same period last year. Regionally, the Americas contributed 53%, EMEA 38%, and Asia-Pacific 9%. License revenue on a year-to-date basis was 216 million, up 14% compared to 190 million reported for the same period last year. On a year-to-date basis, customer support revenue was up 20% and service and other revenue was up 30% over the previous year-to-date results.

Pre-tax adjusted operating income on a year-to-date basis was 245 million, compared to 211 million for the same period last year, an increase of 16%. Adjusted net income on a year-to-date basis increased 15% to 201 million from a 176 million from the same period last year. Year-to-date adjusted earnings per share was \$3.43 per share on a diluted basis, up 13.6% from \$3.02 per share for the same period a year ago.

On a year-to-date basis, GAAP net income was 117 million or \$2 per share on a diluted basis, compared to 95 million or \$1.63 per share on a diluted basis from the same period a year ago. Adjusted tax rate for the quarter in the year is 14%. The same as it was for the last fiscal year. Operating cash flow was 97 million, compared to 82 million in the same quarter last year. Operating cash flow before the impact of specialty charges was 100 million, compared to 87 million in the same period last year.

We incurred special charges in the quarter in the amount of 5.1 million relating to our restructuring plans and another 1.4 million relating to acquisition and integration costs. We expect to incur an additional 5 million relating to further restructuring actions in the fourth quarter of fiscal 2012 to the first quarter of fiscal 2013.

On the balance sheet at March 31st, 2012, deferred revenue was 303 million, compared to 237 million as of December 31st, 2011 and 266 million at June 30th, 2011. The increase in deferred revenue in the current quarter is due to higher percentage of customer maintenance contracts being renewed at December 31st.

Accounts receivables was 176 million, compared to 155 million at the end of last fiscal year. Day sales outstanding were 54 days as a March 31st, 2012, compared to 49 days at June 30th, 2011 and 49 days at the end of Q3 of fiscal 2011. At March 31st, 2012, our head count was approximately 4600 employees and is comprised of 1250 in R&D, 770 in customer support, 980 in services, 970 in sales and marketing, and 630 in the G&A.

There is no change to our pre-tax adjusted operating model for this quarter and expect our annual operating net margin model to continue 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 operating model. We anticipate that this will improve for 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 & Chief Executive Officer

Thank you, Paul, and welcome, everyone, to our fiscal '12 Q3 earnings call. I have much to go over today – the quarter, year-to-date results, remainder of the fiscal year, our market opportunity, changes I have made to the business to capture that opportunity, today's announced acquisition of EasyLink, and my priorities.

Let me start with the quarter and our year-to-date results. First and foremost, the quarter did not meet my standards on performance. While we had record earnings for a third quarter and our adjusted operating margins were in line, license performance was poor. And two out of three is not good enough.

With that said, we moved swiftly on sales execution issues, created a stronger organizational structure, generated record Q3 cash flows, announced the acquisition of EasyLink, and the OpenText opportunity has never been more compelling. Let me expand.

Q3 license performance was a disappointment due to sales execution issues within both our North America and BPM groups. First, the vacancies and turnover in the sales force have been increasing in the past quarters, has resulted in a meaningful undercapacity to deliver against our expanding expected license numbers.

Second, the merging together of our two acquisitions, Metastorm and Global 360, resulted in significant disruption in their performance. Further, these acquisitions were not being integrated into OpenText. I've taken swift actions on these execution issues.

We are expanding our quota-carrying sales force by over 20%, with the main focus being in the U.S., U.K., Germany, and emerging markets. We expect to have these positions filled over the next two to three quarters. The increased selling capacity will be cost-neutral and funded by efficiency gains and not impact our margin profile.

Further, we have not had a head of sales for over two years. I have initiated an external search for an industry veteran, who will have responsibility for all license, professional services and field operations. I am pleased with the candidates that have been identified, and we are looking forward to announcing this appointment when we complete the search.

As it relates to BPM, I have changed the leadership, and all BPM teams have now been fully integrated into their respective geographies or functions. This integration allows for the BPM sales force to fully leverage our global investments, strengths and scale, such as our installed base, professional services, demand generation, partners and operations.

And further, this expands our selling capabilities, because all OpenText account executives can now sell the BPM solution. In the first 30 days, I can already see improved pipeline and momentum.

As I highlighted on our Q2 earnings call, I would be focused on adjusted operating income. This remains my focus, while we build more predictability into our license performance. To that point, on a year-to-date basis, we're up 16% in adjusted operating income year-over-year. For full year FY '12, I see this financial metric remaining strong.

As for Q4, I am expecting our license performance to improve sequentially, but still not at the performance levels I'd expect longer-term. We have moved swiftly to take corrective actions and are confident that our organizational changes and enhancements will have a positive impact on our execution moving forward.

Let me transition. We are winning in the market and let me turn to customer wins within the quarter. BlueScope Steel, the leading steel company in Australia, New Zealand, has extended their use of e-mail archiving across their organization as part of an infrastructure consolidation program.

Sumitomo Heavy Industry in Japan is simplifying their business processes for outsourcing services within finance, HR, and procurement by leveraging our ECM software. NTT COMWARE in Japan is strengthening their information management foundation with our ECM solution. It supports their billing processes and outsourcing services. News International and Trinity in the UK, two leading media organizations have standardized their publisher solutions on our CEM software.

On the product, let me focus on two areas. We announced that Tempo is generally available in both the enterprise and express edition, a new offering that features easy sharing of content in private clouds. Both editions offer enterprise-level records management and security features. The end market for this product is very large and very excited and early indicators point to a high level of interest from both our existing ECM customers and new prospects.

We also announced Version 10 of our Extended ECM for SAP solutions. Version 10 includes support for SAP Customer Relationship Management and SAP Supplier Relationship Management applications.

Now let me turn to our market opportunity. Our opportunity is to grow from our strength in heritage and enterprise content management into a larger category of enterprise information management. We call this the EIM. This would expand our addressable market from approximately 5 billion to approximately 13 billion.

120 days into the business, this has become a shared vision and aspiration for the entire leadership team. At today's investor presentation, we define the five key markets for EIM. Our goal is to lead in each of these markets. Let me walk through them one by one.

ECM is a 4.6 billion market, growing at 9.9% CAGR. We have been focused in this market for 20 years and are the market leader. The market is far from mature and we have lots of room to grow and gain share. BPM is a \$2.6 billion market growing at 7.2% CAGR. We have been in this market for about one year. This is a strategic market for us and we are in it for the long-term.

Information exchange is a 3.2 billion market, growing at 11.4% CAGR. We've been in this market for over five years and our announced acquisition of EasyLink will create more strength in this market for us.

Customer Experience Management, also known as CEM, is a 1.35 billion growing at 14.3% CAGR. We have been in this market for five years and are a top four supplier today.

eDiscovery is 1.4 billion market, growing at 15.9% CAGR. We have some great assets in this market and will continue to focus on this area. E Suites of software fit naturally together in order to manage and gain value from big data, all the structured and unstructured information from the world's leading companies. Customers are looking to OpenText to solve these big data challenges. Information governance, information exchange, information processes, and information security and they want us to do this on premise, in the cloud and mobile.

The public web is less than 10% of content. The deep web, that is, corporate information inside the firewall, is greater than 90% of all the content and is now measured in Zeta bytes. Bid data on the deep web is the right place for OpenText to focus with enterprise information management.

We will be rolling out this expanded vision and new products and services expected in early FY '13 to our customers and partners, and we will be organizing an Investor Day in early September to walk investors through this strategy in detail. It will be a great opportunity to interact with the leadership team as we update you on our exciting market opportunity.

Let me take you through the organizational changes I've made in order to capture the EIM opportunity. Prior to Q4, we were operating under a hybrid business unit/general manager leadership model. This model served us well in the ECM market as we scale the business to \$1 billion in annual revenues.

On the first day of Q4, we transition the business to a functional model whereby we will have one leader for each of our key customer facing functions. This model will better support the business as we strive towards our next great milestone of \$2 billion annual revenues. Let me highlight the changes.

James McCurley now leads our worldwide customer service organization. Walter Koehler, now leads our worldwide professional services organization. Both Walter and James are OpenText veterans, and I'm confident in their ability to lead these groups. Each of our geography leaders Dave were in EMEA, Steve Best in the Americas and Graham Pullen in APJ are now focused on license and license growth. Steve Best replaces our previously year for the Americas. Steve is a world-class experienced sales executive and an OpenText veteran, so his transition into this role is natural and immediately impactful.

These changes will build a leadership team commensurate with the market opportunity, a business model that scales with greater ease and efficiency, functional accountability, and provide the attention and focus necessary to grow license sales and earnings. I'm pleased with our progress on forming a stronger organizational structure and leadership team, and we can now review – and you can now review our executive team on our website.

Let me turn to our other news of the day, our announced acquisition of Easylink. Easylink is headquartered in Atlanta, Georgia and is a global provider of cloud-based messaging services for a wide array of data types, facts, email, SMS, voice, EDI, and other data types. The trailing 12 month revenues were \$186 million, there were approximate 550 employees and with operations at approximately 20 countries. The revenue splits are 60% Americas, 23% APJ and 17% EMEA and they operate profitably. This acquisition will provide us additional scale and information exchange in the cloud.

Once we are together, we would also expect cross-sell opportunities between our mutual customers. OpenText has offered \$7.25 per share in cash for a purchase price of approximately \$310 million. The EasyLink Board of Directors has unanimously approved the transaction. The transaction is expected to close by mid-to-late summer 2012 subject to Easylink's shareholder approval, certain regulatory approvals, and customary closing conditions. Upon close, we expect the acquisition to be immediately accretive.

Let me end the prepared remarks with my key priorities. First, expanding our opportunity from the content experts to enterprise information management which would expand our addressable market from 5 billion to 13 billion with a blended growth rate of approximately 10%.

Second, we will measure our business against market growth rates. I'm focused on building a sales engine that grows and gains market share. Third, exploiting both organic and acquired opportunities to reach our next big milestone of 2 billion in annual revenues and capture the EIM opportunity. And fourth, and as I will continue to emphasize, we remain adjusted operating income focused with strong earnings and cash flow.

After my first 120 days on the job, I'm even more excited about the Open Text market and long-term growth potential. We're the market leader in ECM and this heritage positions us to be the market leader in EIM. Our pipeline of opportunities is strong. We're expanding our sales force, and I'm highly focused on putting the company in the best position to capitalize on our large and dynamic market opportunities. Our opportunities are unbounded.

With that, I will hand the call back to our operator for your questions.

QUESTION AND ANSWER SECTION

Operator: Thank you. Your first question comes from Richard Tse from Cormark Securities. Please go ahead.

Richard Tse

Cormark Securities, Inc.

Q

Yeah, thanks. So Mark, just to start off, you had -- I guess before you came on Board, kind of nice run over course of the year. So what happened that this quarter is sort of turned around here on your watch like, I know you are new to the job and I know you are making some changes. But it seems that the progression post acquisition is in the past has turned over very quickly in terms of their execution, but Metastorm and 360 haven't been as successful.

Mark J. Barrenechea

President & Chief Executive Officer

A

Well, I will continue to highlight that we had sales execution issues in North America and within BPM and as I said on the script, an accumulated deficit and sales capacity. And I have acted swiftly on the sales execution issues. I have transitioned the business to a functional model where we have one head of CS, one head of professional services, and our geographic leaders have transitioned from a general manager model to only focus on license. And we have OpenText to grow our sales, our license sales force capacity by 20%. So in short, we had leadership execution issues and an accumulated deficit and sales capacity.

Richard Tse

Cormark Securities, Inc.

Q

So just switching gears here in terms of the acquisition, my understanding that from your comments tonight is that Metastorm and the Global 360 haven't really been that successful in terms of the integration or the up-sell. So in the midst of that, why are you making decision here to take on another acquisition before that is actually integrated?

A

Well, let me take each of those -- the two parts I think to that question. The first is BPM. The changes we've made to BPM, and they are already showing positive results in momentum, is when we did the acquisition of BPM, we kept it as a separate unit. And we've kept it as a separate unit, in my opinion, too long. And there was somewhat of a culture clash between the two businesses.

So, we have integrated that now where CS is part of CS, PS is part of CS, and the license team is part of the field. We've also now turned on our entire sales force to be able to sell BPM. And I would expect significantly better results actually in Q4 on BPM than we had in Q3. We waited too long to do the integration, and it actually -- it maybe was not integrated at all. So, I changed that course to integrate.

So, I think we're on a good path. I can already see momentum, and I'm expecting quite a different outcome in Q4 and license. With that said, PS remains strong and our renewals remain strong within BPM.

As it relates to EasyLink, it's kind of a different story here. We have a mature business and our FDDD Group, fax distribution and documentation group, a very mature organization, been part of OpenText for quite sometime. And we see synergies between our business and EasyLink's business in the core messaging business.

Second is the ability to leverage the EasyLink infrastructure for moving a variety of our solutions into the cloud. So, the differences are -- its two major businesses coming together versus perhaps two rivals and two culture clashes.

Richard Tse

Cormark Securities, Inc.

Q

Okay. And just one final quick one. Just based on your experience with some of these changes, I'm sure you probably have implemented them in other organizations. How long, typically -- given on a quarterly basis, at full force here, is that one or two quarter even with the history then?

Mark J. Barrenechea

President & Chief Executive Officer

A

We're going to measure these in months, actually. On the CS side, we're off and running very hard. On the professional services side, the synergies are bringing together the PS teams has almost an immediate effect. On the licensed side, we're providing the field more focus.

Starting in Q3, our geographies had three things to focus on; our geographic leaders and today they have one, which is license. So, I would expect in Q4 our license performance to improve over Q3. And I would hope it would continue to improve into the year.

So, I'd be measuring the changes on the licensed side over the next two to three months given the -- two to three quarters over the capacity we're going to have. And I would think that the CS and PS changes are going to be in immediately impactful.

Richard Tse

Cormark Securities, Inc.

Q

Okay, great. Thank you.

Operator: Your next question comes from Kris Thompson from National Bank Financial. Please go ahead.

Kris Thompson

National Bank Financial Brokers

Q

Great. Thanks. Mark, on the EasyLink, can you just tell us how the technology will aid OpenText's competitive position against the usual suspects like IBM, EMC and HBN, maybe how it benefits your partnerships with SAP, Microsoft, and Oracle?

Mark J. Barrenechea

President & Chief Executive Officer

A

Thanks for the question, Chris. But first I would say as it will provide us additional scale and scale is always a good thing in a competitive environment. We also have different pieces of functionality between our distribution -- our messaging products and the EasyLink products. For example, we have archive capability that we can now offer or would be able to offer to EasyLink customers. We have BPM solutions that we can offer to EasyLink customers. EasyLink infrastructure will be beneficial to Open Text products where we can bring our FDD [ph] products into

the cloud and we're hopeful we can bring our ECM products and potentially Tempo products into the cloud into their global infrastructure.

Also, with our capital structure, there have been some geographies where EasyLink has not been able to invest, and we think we will be able to provide that investment to create a greater distribution. I'd say this really doesn't touch too much SAP, Microsoft, or Oracle, but it's rather within Open Text proper that it will be able to provide more products to EasyLink current customers, EasyLink infrastructure will be at a leverage for our products, and thirdly we see opportunity in other countries that they have not been able to get off the ground.

Kris Thompson

National Bank Financial Brokers

Q

Okay. That's helpful. And then just the IBM and EMC, did they provide similar solutions, or is it a different competitive landscape?

A

It's a different competitive landscape.

Kris Thompson

National Bank Financial Brokers

Q

Okay. Last for me, Paul. On the maintenance renewal rates, you mentioned they were 92%, but can you give us an idea of the robustness of the pricing in the market? Are you getting some price hikes their?

A

Paul J. McFeeters

Chief Financial Officer

Yeah, Chris. We're continuing to get some price increases on our renewals. We mentioned in the past perhaps pre-2008 we might have got into the sort of three to five range, now we're more in the 1% to 3% range. It's been consistently that for about the last two years.

Kris Thompson

National Bank Financial Brokers

Q

Okay. Thanks, guys.

Paul J. McFeeters

Chief Financial Officer

A

Thanks, Chris.

Operator: Your next question comes from Brian Freed from Wunderlich Securities. Please go ahead.

Brian Freed

Q

Good afternoon. Two quick questions. First, Mark, as you look to drive this shift to functional model, can you talk about any changes you've made to the sales incentive structure, either at the field or regional management level?

Mark J. Barrenechea

President & Chief Executive Officer

A

Brian, thanks for the question. We're going to complete fiscal year '12 before looking at the compensation plan. Our new fiscal year starts July 1st. And the changes come July 1 very simple. Our geographic leaders today have a basket of metrics. PS, CS, license, adjusted operating income, and other metrics. Come July 1st, they will have a licensed metric. So the model -- the compensation model will match the function. CS will be measured on the CS, PS will be measured on PS. And license will be measured on license. Everyone will always continue to have a margin component to what they do. So I am actually quite excited that the functional responsibility will be matched to the compensation plan more closely or rather perfectly aligned from July 1.

Brian Freed

Q

Okay. And then my second question for you, Paul, as you look at the shortfall, what is the relative split would you guess between the ECM business and North America and the BPM business?

A

Well, I'm not explaining a revenues, I guess I'll answer roughly 50-50.

Brian Freed

Q

Okay. Thanks.

Operator: Your next question comes from Blair Abernethy from Stifel Nicolaus & Company. Please go ahead.

Blair H. Abernethy

Stifel Nicolaus Canada, Inc.

Q

Thanks very much. Just a couple questions on the Q3. I wonder, if you'd just characterize the deals that the shortfall here. Was it more deals lost or slipped, and is -- what's your sense on the pipeline as you've entered Q4 versus as you entered Q3?

A

Sure. Blair, thanks for the question. Well, first and foremost, the execution issues are 100% hours, 100% under our control, and are 100% hours to fix. So they are all in our control. As you've probably saw in our investor deck within the quarter, we announced only one deal over \$1 million, compared to -- I think last quarter we had seven deals over a million, in Q3 last year, we had five.

So when I look at our pipeline, I always think of pipeline along five attributes. I think of it size, velocity, quality, conversion rates, and the age of opportunities within the pipeline, and where we struggled most was on the conversion of larger deals within the quarter in that sales execution.

We are not seeing competitive pressures. We certainly have seen some deals move clearly across quarter boundaries, but it's all within our control. There is no change to competitive dynamics.

Blair H. Abernethy
Stifel Nicolaus Canada, Inc.

Q

Okay, great. And in terms of the sales rep capacity, what is – how many quarter carrying reps do you have today?

A

So we breakout our total sales number, which is just a little under – Paul, is grabbing the number for me.

Paul J. McFeeters
Chief Financial Officer

A

970 in total.

A

Yeah. So 970 in total, and then 442 for our quarter carrying sales, which includes overlays. And we'll be expanding that by 20% effective immediately. And fund it within our current cost structure by efficiencies we've gained that will not impact our margin profile.

Blair H. Abernethy
Stifel Nicolaus Canada, Inc.

Q

Okay, great. And the last question for me, just on SAPs contribution in the quarter. In the past, SAP license contribution would be recognized one quarter in the rears. And I'm – sometimes that moves around a little. Can you just describe what they contributed to your business this quarter?

Paul J. McFeeters
Chief Financial Officer

A

Yeah, Blair, it's Paul. Well, it continued to be in excess of 10%. I just – has it has been for sometime, I just wanted to add a clarification note, which we haven't in the past is that a lot of our SAP transactions do involve the participation of our direct sales force. So we're looking at this now more as an influence as well as a partner led transaction. So while it's still in excess of 10%, I want to be clear that our direct sales force is also participating in these transactions.

Blair H. Abernethy
Stifel Nicolaus Canada, Inc.

Q

Okay. And just a follow on that, Paul. The SAP had trouble executing in North America. Did – was there any read through for Open Text in Q3?

Paul J. McFeeters
Chief Financial Officer

A

Blair, the execution issues for us in Q3 are 100% on us. 100% on us.

Blair H. Abernethy
Stifel Nicolaus Canada, Inc.

Q

Okay. Thank you.

Operator: Your next question comes from Stephanie Price from CIBC World Markets. Please go ahead.

Stephanie Price
CIBC World Markets, Inc.

Q

Hi, gentlemen.

A

Hi, Stephanie.

Stephanie Price
CIBC World Markets, Inc.

Q

Could you talk a bit more about the revenue and earnings contribution from Global360 and Metastorm in the quarter just given that you're talking about BPM as one of the factors for the miss in the license revenue.

A

Yeah Stephanie, we are just only breaking out this year as you know the contribution from Global360 and we are not segmenting our information in a queue, so not really going to be doing it here. As I mentioned earlier to a question about the miss, both Metastorm and Global contributed to perhaps a lower expectations than the – might have had is certainly that we might have had. It is still accretive. Both operations are still accretive, because as you know, we will take the cost out. And as we reported, our earnings have appeared to have gone up.

Operating 16% year-to-date net income 14% year-to-date. So they definitely have contributed to the accretive earnings. But on the revenue side, on the license again, Mark mentioned doing well on the CS renewals, doing well on professional services but due to sort of integrating those, they are responsible for what maybe procedures were missed there about 50% of that miss. That's the best I can answer the question without disclosing segmented information.

Stephanie Price
CIBC World Markets, Inc.

Q

Okay. And on the efficiency gains that are to pay for the salesforce increase in capacity, is that the \$5 million in restructuring you are talking about earlier?

A

Some of that is still -- that's what I was discussing in terms of the accretive of the acquisitions. That restructuring is still primarily 360, a little bit of what Mark referred to as efficiencies within the quarter. Some of that will be marked to Q4 and Q1 as I referred to in my remarks.

Stephanie Price
CIBC World Markets, Inc.

Q

Okay. And in terms of the ECM strategies that you've outlined Mark, could you talk about what acquisitions that you might need and what holes you still have to fill to sort of broaden up that strategy?

Mark J. Barrenechea

President & Chief Executive Officer

A

Thanks for the question. So again, we see five markets here. ECM, BPM, information exchange on the customer experience management, and e-discovery. These are the five markets that we see contributing to managing all the unstructured and structured big data inside the firewall. We are going to look opportunistically across those five sectors. As I highlighted on our last earnings call, I would be looking a bit more toward medium to larger size acquisitions that are more meaningful to the contribution as we look to capture this opportunity. And March [ph] shows our next big milestone of 2 billion in revenues. Each market is a little different. I mean ECM is more probably about functional components. BPM is still for scale. CEM is still sort of a defining market. We have some good starter assets in e-discovery but don't have the scale there yet. Hopefully, that's helpful, Stephanie.

Stephanie Price

CIBC World Markets, Inc.

Q

Okay, great. Thank you.

Operator: Your next question comes from Scott Penner from TD Securities. Please go ahead.

Scott Penner

Q

Thanks. Just looking at the consistence going in for license revenue versus what was reported is, call it a delta of about 14 million. And I know we're not exactly exact here. But I mean is it correct to think that probably 7 million of the misled, say, came from the BPM side and the others – the other was the sales execution in North America?

Paul J. McFeeters

Chief Financial Officer

A

Yeah, Scott, it's Paul. I did give approximately numbers. We – yeah, absolutely on the BPM because of the challenges of integrating those two together and not bringing [indiscernible] . It had a meaningful impact on – against our plan. I'm not going to stick together to street's numbers, were against our plan. And I gave a very kind of general range between that impact of approximately half and our on, call it, execution issues on the other front impact, against our own internal plan.

Scott Penner

Q

Yeah. No...

Paul J. McFeeters

Chief Financial Officer

A

I stick to your number.

Mark J. Barrenechea

President & Chief Executive Officer

A

And Scott, if I can, I'd like to add one component there to put in perspective the change we made, which is enormously positive. We went from a independent business unit called BPM with independent account executives selling their accounts to one sales force that can all sell BPM. So rough numbers, we went from 50 people with a license to sell to 500 people with a license to sell starting in Q4.

Now, we have a lot of training to do and a lot of education to do, so I'm not suggesting we 10x the sales force over a weekend, but adding 10%, 20%, 30%, 40% more capacity now is about training and awareness. And quarter over quarter in the first 30 days of Q4 I can see a lot more momentum.

Scott Penner

Q

Okay. Thanks for that, Mark. Just – when you outlined the EIM market in general, what additional competitors does that bring into the mix when you sort of expand what you consider to be your market opportunity?

A

Well, I think at the end of the day when you start looking at a category of between 10 billion and 20 billion, I would look towards both IMB and HP ultimately as our top competitors across these two segments.

Scott Penner

Q

Okay. And then, the acquisition of the Easylink, when I just took a quick look at their revenues, and it looks like the vast majority – well, the majority of their revenue comes from as they defined it, SAC services. So just want to get a sense whether this is a technology buy or a customer base expansion. And you think you can leverage down the road, or was it really about acquiring cloud capabilities?

A

I think it's a mixture of two things. We like their products and their offerings, both within their – across the board. And second, being able to add additional capabilities to that. We, obviously, have to complete the transaction. We have – we're targeting the summer for that. But we see our ability – we like their products and services and we see additional products and services we can add to their infrastructure.

Second is the cloud. Customers are asking Open Text to deliver on-premise in the cloud and mobile. And they are a global infrastructure. It's an infrastructure we would like to invest in and expand to be able to deliver the Open Text capabilities in the cloud. So we like their offering. We see things we can add to it. We like their roadmap, and we also like their infrastructure to be able to build out our cloud.

Scott Penner

Q

And just to be clear, of Blair's question earlier, the deals that you didn't have the execution on in the quarter are all of those deals still live in your pipeline?

Mark J. Barrenechea
President & Chief Executive Officer

A

I'm sorry, I don't understand the question.

Scott Penner

Q

The deals that decided for the execution issues in Q4, are those deals still live?

Mark J. Barrenechea

President & Chief Executive Officer

A

I'm sorry, I thought we were on acquisition deals versus our pipeline deals. Yeah, we didn't see an effect of economy. We didn't see an affect of deal shrinkage. It was execution. So a goodly portion of those deals are still active and we're still working on them.

Scott Penner

Q

Okay. How long do you think it will take you, Mark, to get the organization to on that 10% blended growth rate of the EIM business?

Mark J. Barrenechea

President & Chief Executive Officer

A

Yeah, we are on dual execution paths, right one is organic and the second is acquired. On the organic side, I would look toward an increased rate of growth, in FY '13, organically and FY '14 getting closer to market growth rates.

Scott Penner

Q

Okay. Thank you very much.

Mark J. Barrenechea

President & Chief Executive Officer

A

Thank you.

Operator: Your next question comes from Paul Steep from Scotia Capital. Please go ahead.

Paul Steep

Q

Great. Thanks. Mark, maybe we just to look back at EasyLink for a second. Maybe you could give us a little bit more color around the stability, the base and the business there. It seems like it's more of a services business. How much of that is under long-term contract that's fairly sticky for you folks?

Mark J. Barrenechea

President & Chief Executive Officer

A

I am sorry, Paul, just little difficult hearing the first part, this is EasyLink?

Paul Steep

Q

Yeah, EasyLink. How much of its contracted long-term or over sort of a one to three year period in terms of a recurring business?

Mark J. Barrenechea
President & Chief Executive Officer

A

I'm not sure it's disclosed in our Qs and Ks, their productivity [ph] of their contracts. So I'm going to have to go back and check their disclosures to confirm.

Paul Steep

Q

Okay. How much you...

Mark J. Barrenechea
President & Chief Executive Officer

A

Sorry. Go ahead, Paul.

Paul Steep

Q

How much of you business then would you try to sort of shift over? I guess, where I'm going with this is, on a revenue recognition basis, do we need to think about as you bring in a services business and a SaaS model. How much should we model in a change in the operating model going forward?

Paul J. McFeeters
Chief Financial Officer

A

Yeah, Paul, it's Paul. I mean, clearly, they are a public company agency now and so I think if you look at their financial reporting, I wouldn't think that ours – we would expect to continue to disclose that business along with the business that Mark referred to that we are already in, our Fax Distribution business, either separately on the face of the financials or disclosed in our MD&A. So I think the answer is, look how they report and assume that we'd be onboard in that kind of reporting view.

Paul Steep

Q

Okay. Fair enough. Last one for me would just be on BPM. 15% license decline, is that sort of the number we're tracking to at this point? I know we've talked a lot on the call about a disappointment here. That was sort of the number we talked about February 1. Is it sort of on that par into the back half?

A

Yes. Certainly, when we talked about on the acquisition of these, I think at that time we talked more about 10 to 15, so clearly on the license only it would be greater than that to date.

Mark talked about expectations much more positively going forward. But clearly, it was more than the 10 to 15 that we anticipated when we acquired them. Again, having said that, strong CS, strong PS not that far off the contribution of the accretive contribution we are expecting.

Because sales costs are fairly high in relations to license revenues. So I still want to point out that what we might have missed on license we made up for some of that on our earnings. That's why our earnings stayed strong

quarter-over-quarter and year-to-date over year-to-date. It was much closer in our expectation on the bottom line because of cost management and because of revenues from CS to PS.

Paul Steep

Q

Great. Thanks.

Operator: Your next question comes from Sera Kim from GMP Securities. Please go ahead.

Sera Kim
GMP Securities LP

Q

Hi, good evening. So just to clarify the last question, you're planning to breakout EasyLink services revenue either separately or in MDA once the acquisition closes?

A

Yes. I think it was on the size and then uniqueness that we will be doing that.

Sera Kim
GMP Securities LP

Q

Okay. In the past you had mentioned that you grow, like I know cloud is still really small – budding part of that your business. In the future as you grow your cloud business, would that all be all included together or would EasyLink just be segmented separately?

A

I would assume that we would be including all of our cloud businesses together.

Sera Kim
GMP Securities LP

Q

Okay. And just for clarification, earlier you mentioned that you are seeing immediate impact from consolidating in the BPM operations. So just keeping in mind that it does take time to wrap up sales capacity and to train them and whatnot, when do you think you will start to see positive impact in North America for license revenue growth?

A

Well, we are expecting – and we can see early signs of it that we will see a positive impact within this quarter. Quarter-over-quarter. Obviously, we would see more impact kind of rolling into FY 13. The business model change is instead of having two separate sales forces, one small, one large that all quota carrying account executives are able to engage their customers as an accounts for BPM opportunities. So I am expecting in Q4 an immediate impact of the change, the positive immediate impact of the change and even a more fuller impact in FY 13.

Sera Kim
GMP Securities LP

Q

Okay. So just to be clear, so there are two issues that cause your license sales weaknesses. One was issues on the BPM side but another was on execution issues in North America sales overall for license revenues, is that not correct?

A

Yes, so first was North America and BPM execution issues, and second was this accumulated deficit in sales capacity. So I put execution and sales capacity as two issues. Perhaps it's one A., North America, one B. BPM, and two the deficit of sales capacity.

Sera Kim*GMP Securities LP*

Q

So just addressing the deficit and sales capacity. What is the reason for the turnover that you have seen and how long do you think it will take to see a positive impact from the increase in sales capacity that you expect for the next couple quarters?

A

So, we've -- we are immediately expanding our sales force by 20%. We've opened those racks. We are looking primarily in North America, UK, Germany, emerging markets. We would expect over the next two to three quarters to have those positions filled.

Sera Kim*GMP Securities LP*

Q

Just last question. You mention that you didn't see any impact from the economy. So I'm just wondering if you can comment on the decline in Europe, was that related to the BPM issues, or was there anything else that was impacting that weakness?

A

Yes, I will talk about the economy in general and Paul can talk about anything within the geographies. We haven't seen any change in economic buying behaviors related to economies quarter-over-quarter. Europe is still cautious environment. That has not changed. One thing gets solved and another thing comes up, right, in Europe. So quarter-over-quarter we are still cautious in Europe, but we haven't seen anything to change that caution. Our licensed disappointment in Q3 is related to our issues and execution. Paul, anything you want to add in sort of geographic splits?

Paul J. McFeeters*Chief Financial Officer*

A

Geographic splits by and large remains similar to last quarters similar to year ago.

Sera Kim*GMP Securities LP*

Q

Thank you.

A

Thanks Sera.

Operator: Your next question comes from Eyal Ofir from Canaccord Genuity. Please go ahead.

Eyal Ofir

Q

Thanks. Thanks for taking my question, guys. First of all I will ask the easy one, I guess, for Paul. On the sales and marketing expense lines, I see that it's actually up sequentially and I guess that kind of -- I guess my thought process when we see license revenue down, so was this due primarily to the increased integration of the BPM into the sales organization and training, or is there anything else working in their?

A

It's a good question, Eyal. A little bit of what you said just to make the answer easy, yes. Also, we are getting in some cases some of the high-performing individuals are doing very well through the year, so it changes that mix a little bit. So its a combination of those two things.

Eyal Ofir

Q

Okay. And then, Mark for you, I guess there's two parts to my question. First off, on the BPM side you talk about, obviously, having the sales reps now trained to sell BPM. But when do you expect to get some of your partners trained on BPM and extend that in direct channel as well?

Mark J. Barrenechea

President & Chief Executive Officer

A

Certainly, a FY '13 effort. Right now we are focused on getting our own productivity levels up and -- again, I'm trying to say it as simply as I can. If we are going from roughly a 50 person sales force to a 500 person sales force who can go build pipeline and convert for BPM wins, that's our immediate focus is getting our worldwide sales force trained, effective to build pipeline and convert to revenue. In FY '13 when we complete that, we will then turn outside our four walls and look towards more partners. Our biggest opportunity right now is within the company getting our worldwide sales force now up to speed and trained.

Eyal Ofir

Q

Okay. And then you've also done some other internal changes like looking at the low producers and may be targeting them to the forward turnover, turn those guys over to maybe bringing external parties to take over.

Mark J. Barrenechea

President & Chief Executive Officer

A

When we complete the year, my philosophy is to certainly look at low performers, do some churn there, and bring in fresh talent inside the company. So, we will wait until the end of the fiscal year.

Eyal Ofir

Q

Okay. Last thing for you on the partnerships. When you look beyond BPM, you talked about the new markets you want to attack. Is there any new type of partners you're looking to attract, or should we assume it's going to be kind of what was seen to date in terms of partnerships?

Mark J. Barrenechea

President & Chief Executive Officer

A

I'd break that into two categories, technology partnerships of SAP, Oracle, and Microsoft and then distribution partners such as the system implementers. So, those remain our two big focus areas, the large tech partners and increasing the emphasis on system implementers.

Eyal Ofir

Q

Okay. So going forward, it should be a similar type of split, potential increase fixed focus on system integrators. That doesn't change when you look at the overall larger markets as you try to --

Mark J. Barrenechea

President & Chief Executive Officer

A

I would -- I kind of break them into three categories, the technology partners, system implementers, and then the sell-through relationships. Again, I'd work through them in priority of large tech system implementers and sell-through.

Eyal Ofir

Q

Okay. Thanks. I will pass it on.

Paul J. McFeeters

Chief Financial Officer

A

Operator, I think we have time for one more question.

Operator: Your next question comes from the line of Paul Treiber from RBC Capital Markets. Please go ahead.

Paul Treiber

Q

Hi. Thanks for taking my question. How should we think about license seasonality going forward? Do you think some of the changes you're implementing will do some of the historical seasonality or do you think it will actually increase it? And then regarding Q4 license, you expected that quarter-over-quarter, but do you think you think you will be able to see some year-over-year growth as well?

Paul J. McFeeters

Chief Financial Officer

A

I'll start off. I think the second part is for Mark, Paul this is Paul. It's hard now I think for us to make references to historical seasonality because in the last two years, as I know you know, its been less predictable or more volatile

on that. So to answer your question specifically, I don't know anything we are doing is going to change so much. There's definitely going to be seasonality to our business with of course Q4 and Q2 being stronger than Q1 and Q3, but as far as percentages up and down, I'm much more hesitant now to suggest we look at historical views and can't really tell you whether or not the increase or decrease of that seasonality will be more or less pronounced.

Mark J. Barrenechea

President & Chief Executive Officer

A

And Paul, on the second part of the question, we are certainly looking toward Q4 that sequential growth over Q3. We are not providing annual guidance or annual targets, but I will emphasize something I said in the script that I remain focused on adjusted operating income. And year-to-date we are up 16% and operating – adjusted operating income year-over-year. And for full-year FY 12, expect to see the financial metric remaining strong.

Paul Treiber

Q

Thank you. Mark, one last question. You have been at the company as you said for 120 days now, what's being the feedback that you are getting from partners, customers, employees, and other stakeholders on the new vision for the company? And has there been anything surprising that you can share, or is it mostly in line with your expectations?

Mark J. Barrenechea

President & Chief Executive Officer

A

Paul, I'd say that the reaction has been enormously positive. You know, we look at our heritage and strengths in enterprise content management. We have the expertise, we have the vision, we have the experts to be able to bring together an expanded market category. So I'd say across all stakeholders there has been a lot of enthusiasm and a great esprit de corp [ph] to go out and win and grow the business. So it's really quite empowering and refreshing to see such an esprit de corp.

Paul Treiber

Q

All right. Thanks, guys.

A

Thank you.

Operator: And I will now turn it over to Mr. Barrenechea for closing remarks.

Mark J. Barrenechea

President & Chief Executive Officer

Greg, over to you.

Greg Secord

Vice President-Investor Relations

Okay. Thanks everyone for your questions. As I mentioned earlier, the PowerPoint is posted on the website within the next 48 hours the financials will be there as well. Thank you all for attending the call, and good night.

Operator: Ladies and gentlemen, this concludes the conference call for today. Thank you for participating. Please disconnect your lines.

Disclaimer

The information herein is based on sources we believe to be reliable but is not guaranteed by us and does not purport to be a complete or error-free statement or summary of the available data. As such, we do not warrant, endorse or guarantee the completeness, accuracy, integrity, or timeliness of the information. You must evaluate, and bear all risks associated with, the use of any information provided hereunder, including any reliance on the accuracy, completeness, safety or usefulness of such information. This information is not intended to be used as the primary basis of investment decisions. It should not be construed as advice designed to meet the particular investment needs of any investor. This report is published solely for information purposes, and is not to be construed as financial or other advice or as an offer to sell or the solicitation of an offer to buy any security in any state where such an offer or solicitation would be illegal. Any information expressed herein on this date is subject to change without notice. Any opinions or assertions contained in this information do not represent the opinions or beliefs of FactSet CallStreet, LLC. FactSet CallStreet, LLC, or one or more of its employees, including the writer of this report, may have a position in any of the securities discussed herein.

THE INFORMATION PROVIDED TO YOU HEREUNDER IS PROVIDED "AS IS," AND TO THE MAXIMUM EXTENT PERMITTED BY APPLICABLE LAW, FactSet CallStreet, LLC AND ITS LICENSORS, BUSINESS ASSOCIATES AND SUPPLIERS DISCLAIM ALL WARRANTIES WITH RESPECT TO THE SAME, EXPRESS, IMPLIED AND STATUTORY, INCLUDING WITHOUT LIMITATION ANY IMPLIED WARRANTIES OF MERCHANTABILITY, FITNESS FOR A PARTICULAR PURPOSE, ACCURACY, COMPLETENESS, AND NON-INFRINGEMENT. TO THE MAXIMUM EXTENT PERMITTED BY APPLICABLE LAW, NEITHER FACTSET CALLSTREET, LLC NOR ITS OFFICERS, MEMBERS, DIRECTORS, PARTNERS, AFFILIATES, BUSINESS ASSOCIATES, LICENSORS OR SUPPLIERS WILL BE LIABLE FOR ANY INDIRECT, INCIDENTAL, SPECIAL, CONSEQUENTIAL OR PUNITIVE DAMAGES, INCLUDING WITHOUT LIMITATION DAMAGES FOR LOST PROFITS OR REVENUES, GOODWILL, WORK STOPPAGE, SECURITY BREACHES, VIRUSES, COMPUTER FAILURE OR MALFUNCTION, USE, DATA OR OTHER INTANGIBLE LOSSES OR COMMERCIAL DAMAGES, EVEN IF ANY OF SUCH PARTIES IS ADVISED OF THE POSSIBILITY OF SUCH LOSSES, ARISING UNDER OR IN CONNECTION WITH THE INFORMATION PROVIDED HEREIN OR ANY OTHER SUBJECT MATTER HEREOF.

The contents and appearance of this report are Copyrighted FactSet CallStreet, LLC 2012 CallStreet and FactSet CallStreet, LLC are trademarks and service marks of FactSet CallStreet, LLC. All other trademarks mentioned are trademarks of their respective companies. All rights reserved.