



**ATA Inc. Fiscal 2014 First Quarter Financial Results Conference Call
TRANSCRIPT**

August 9, 2013 at 8 a.m. ET

SPEAKERS

Carolyne Yu – Senior Associate, The Equity Group

Benson Tsang – Chief Financial Officer & Chief Accounting Officer, ATA

Kevin Ma – Chairman and Chief Executive Officer, ATA

Q&A PARTICIPANTS

Mark Marostica, Piper Jaffray

Ella Ji, Oppenheimer

Operator:

Greetings. Welcome to the ATA Incorporated fiscal 2014 first quarter financial results. At this time, all participants are in a listen-only mode. A brief question and answer session will follow the formal presentation. If anyone should require operator assistance during the conference, please press star-zero on your telephone keypad. As a reminder, this conference is being recorded.

It's now my pleasure to introduce your host, Carolyne Yu of the Equity Group. Thank you, Ms. Yu. You may begin.

Ms. Carolyne Yu:

Thank you, operator, and good morning, everyone. Thank you for joining us.

Copies of the press release announcing ATA's fiscal 2014 first quarter results are available at the IR Section of the Company's website at www.ata.net.cn.

As part of this conference call, the Company has an accompanying slide presentation available on the Company's website. You are also welcome to contact our office at 212-836-9600, and we would be happy to send you a copy. In addition, a replay of this broadcast will be made available at ATA's website for the next 90 days.

Before we get started, I would like to remind everyone that this conference call and any accompanying information discussed herein contains certain forward-looking statements within the meaning of the Safe Harbor Provision of the Private Securities Litigation Reform Act of 1995. Although the Company believes that the expectations reflected in its forward-looking statements are reasonable as of today, those statements are subject to risks and uncertainties that could cause the actual results to differ dramatically from those projected. There can be no assurance that those expectations will prove to be correct.

Information about the risks associated with investing in ATA is included in its filings with the Securities and Exchange Commission, which we encourage you to review before making an investment decision.

The Company does not assume any obligation to update any forward-looking statements as a result of new information, future events, changes in market conditions, or otherwise, except as required by law.

Regarding the disclaimer language, I would also like to refer you to slide two of the conference call presentation for further information.

All U.S. dollar amounts in this conference call relating to financial results for the Company's most recent quarter ended June 30, 2013, are converted from RMB using an exchange rate of 6.1374 RMB to 1 U.S. dollar. All historical conversions are accurate as of the time reported, unless otherwise noted. The Company reports its financial results under U.S. GAAP in RMB, and all percentages calculated in the presentation are based on RMB unless otherwise noted.

For those of you following along with the accompanying PowerPoint presentation, there is an overview of the Company on slide three. The Company's CFO Mr. Benson Tsang will provide an overview of operational and financial highlights for First Quarter 2014, beginning with slide four. The Company's Chairman and CEO Mr. Kevin Ma will then provide closing remarks.

With that, I'll turn the call over to ATA's CFO, Mr. Benson Tsang. Please go ahead, Benson.

Mr. Benson Tsang:

Thank you, Carolyne, and good morning, everyone.

Today we will provide an overview of our financial and operating highlights for First Quarter 2014 and discuss our outlook and growth strategies for the remainder of Fiscal Year 2014.

Slide five shows some operating highlights for First Quarter 2014. During the period, we delivered 2.1 million billable exams, which is about the same number of exams ATA delivered in the prior-year period. The majority of these exams were for the China Banking Association, which continued to experience increased volumes, and the Securities Association of China.

We also made some progress with our security guard exams, having renewed our contract in Shanghai as well as signing new contracts and beginning pilot exams in several other provinces.

With regards to our private sector business, we entered into strategic partnerships with a few different educational institutions and companies as part of an effort to introduce TOEIC to a larger audience.

During the period, ATA also delivered recruitment and assessment exams for various banks in China, including the Agricultural Bank of China, Hua Xia Bank, and Shanghai Rural Bank.

On the right-hand side of the presentation is a map of our extensive nationwide network of 2,810 test centers, which enables ATA to deliver large scale exams simultaneously and cost effectively for our clients. We believe we are the only provider of this kind of large scale testing solution in China.

Now I would like to discuss our financial highlights for the quarter on slide six. We achieved year-over-year growth in net revenues and gross profits for First Quarter 2014 and beat consensus estimates on both the top and bottom lines for the quarter.

We streamlined operating expenses during the period but continued to face some challenges with weaker demand for the SAC exam, which we began seeing in the later part of Fiscal Year 2013 and continued into First Quarter 2014. However, low volumes of the revenue from the SAC exam were in line with our expectations for the period.

As a result of our adjustments in marketing strategy and continued efforts to expand the private sector business, ATA grew revenues from HR Select and TOEIC 38.6 percent to RMB20.2 million in the First Quarter of 2014.

With an encouraging start to the fiscal year, the company is reiterating its revenue and non-GAAP net income guidance for Fiscal Year 2014, which Kevin will expand upon later in the call.

On slide seven, we show our First Quarter 2014 results compared with our analysts' estimates. We were pleased to have exceeded market consensus estimates for the period.

On the next slide, we break out revenues for First Quarter 2014 by our businesses, which can be broken down broadly into two areas, testing services and test preparation and training solutions.

At about 91 percent, our core segment of testing services was a significant percentage of our total revenue in the 2014 first quarter. Testing services include exams ranging from professional certification exams in various industries such as securities and futures to exams resulting from our private sector business, which include TOEIC and HR Select exams.

On the next slide, we have provided a breakdown of the company's financial results for the quarter. Gross profit increased 2.8 percent to RMB48.1 million from RMB46.7 million in the prior-year period.

Gross margin for First Quarter 2014 was 52.2 percent compared to 53 percent in the prior-year period. The decrease in gross margin was primarily due to a year-over-year decrease in SAC exam volumes, which resulted in lower contributions as a percentage of revenue.

Net income increased 78.7 percent to RMB9.4 million from RMB5.3 million in the prior-year period.

Diluted earnings per ADS were RMB 40 cents in First Quarter 2014 compared to RMB 22 cents in the prior-year period.

On slide 10, we provide a supplemental chart of quarterly numbers adjusted for share-based compensation expense and foreign currency exchange gain and losses. I would like to highlight that, excluding these items, adjusted net income for First Quarter 2014 increased 14.5 percent to RMB11.1 million from RMB9.7 million in the prior-year period.

Diluted earnings per ADS during First Quarter 2014 on a non-GAAP basis was RMB 40 cents, or equivalent to US\$0.06.

We continue to be supported by free cash flow and a solid balance sheet, which we have highlighted on slide 11. As of June 30, 2013, we had about US\$43.5 million in cash. We have no long-term debts

or short-term borrowings, and continue to follow the strict cost structure that has served us well over the past several years.

Finally, I would like to provide some projections for Second Quarter 2014. Based on existing exam schedules, we expect second quarter net revenues will be in the range of RMB 36 million to 46 million.

Please keep in mind that this guidance is based on our internal growth projections, and we will continue to evaluate our projections on an ongoing basis.

With that, I would like to turn it over our Chairman, Mr. Kevin Ma, for concluding remarks.

Mr. Kevin Ma:

Thank you, Benson.

We were encouraged by the growth in TOEIC and HR Select in First Quarter 2014, as well as the progress made with the security guard exams. At this point in time, ATA is in a unique position to capitalize on the competitive job landscape in China. Statistics show that nearly seven million students will graduate in 2013.

In an increasingly competitive environment, trusted and fair assessment tools will be critical in helping job candidates stand out from the crowd, and helping employers find the best employees.

Slide 14 shows our annual guidance for Fiscal Year 2014, which Benson mentioned earlier. We are reiterating the Fiscal Year 2014 guidance provided in May and expect the net revenue to be between RMB403 million and RMB423 million, and non-GAAP net income to be between RMB 37 million and RMB 47 million.

We continue working to execute on our growth strategies and remain committed to providing our test takers and clients with valuable quality certification and skill assessment services. We list our initiatives on slide 15.

In fiscal year 2013, ATA was selected to be the service provider that would transition the highly regarded CPA exam from paper-based format to computer-based. We continue working to secure more contracts like this, and believe our strong track record will help us to do so.

We also continue to enact our new mobile testing system, which has been very well received thus far.

Our client, Cambridge ESOL, has agreed to use MTS for its global junior English exams in four markets by the end of this year. We recently helped them administer one sitting in Hong Kong, and are preparing for upcoming exams in Latin America and Europe.

This technology creates limitless opportunities for ATA outside of China, and we expect to begin realizing the benefits of our investments in the coming quarters.

ATA continues to generate excess cash flow and will continue to use these funds to nurture healthy, organic growth.

With that, operator, let's open it up for any questions.

Operator:

Thank you. We will now be conducting a question and answer session. If you would like to ask a question, please press star, one on your telephone keypad. A confirmation tone will indicate your line is in the question queue. You may press star, two if you would like to remove your question from the queue. For participants using speaker equipment, it may be necessary to pick up your handset before pressing the star keys. One moment, please, while we poll for questions. Thank you.

Our first question comes from the line of Mark Marostica with Piper Jaffray. Please go ahead with your question.

Mr. Mark Marostica:

Yes. Um, good morning, uh, and thank you for --or good evening, actually, and thank you for taking my question.

The first question I have is in regards to your guidance for the year. And I was wondering if you can give us an update as to what's implied in terms of any new pipeline exams that may be driving that guidance at this point.

And then, you know, presuming that typically your guidance doesn't include anything brand new, you can also give us a sense of what that pipeline of the public test looks like. Thanks.

Mr. Benson Tsang:

Thank you for your question, Mark.

Uh, regarding our annual guidance, as we mentioned earlier, we still maintain our guidance of 403 to 423 million for Fiscal Year 2014.

The original guidance, when we prepare, we anticipate we have, single-digit growth in our traditional business, the public sector, and we do anticipate about 20 to 25 percent growth in our private sector. And based on what we see right now, we still feel comfortable we can achieve that growth, and that is the main reason we maintain our guidance.

As far as the new contracts, many of the new contracts are in the private sector. And, at the moment for our Q3, we can actually see a pipeline of 110 million RMB. As a result of that, we feel pretty strongly, 403 to 423 million is very achievable.

Mr. Mark Marostica:

Okay. Thank you, Benson, for that color.

Also, the security guard exams seemed to shine this quarter. And, I'm curious if that was above your expectations, uh, and also what your guidance implies for the full fiscal year for revenue from the security guard exam, and whether or not that could be a source of potential upside to your guidance.

Mr. Benson Tsang:

Security guard exam, uh, last time we share to the Streets, we anticipate a minimum of 30 percent growth on an annual basis. And by Q4 2013, we signed seven cities and seven contracts to deliver for the security guard examination. And I'm very happy to tell you at this moment we already have 18 contracts with 18 cities. And in 17 cities, we are delivering the test as we speak.

And in terms of revenue, last year we deliver--generated about five million RMB revenue from the security guard exam, and we anticipate this year 30 percent is, uh--is very comfortable. And we do anticipate the contribution from security exam probably will be in a range of 50 percent plus.

Mr. Mark Marostica:

Okay. Very good.

On the headcount side, I know this has been a focus for the company. Go over your current headcount plans for the year and whether there will be any focused increases in headcount in any areas that you'll be looking at.

Mr. Benson Tsang:

At the end of last year, uh, in the last quarter, we shared to the market we are in the process of restructuring the company in order to make it a very cost-efficient structure to propel the business going forward.

As a result of the restructure, we downsized about--close to 60 people. And the current headcount, at the end of Q1 we are about 465 people. And according to our current plan, we did budget for approximately--the headcount could go up to 500 people. But, the way we'll add the people is basing on the actual need and the value the new staff can bring into the company.

So, we do not think we will reach the 500 headcount by the end of Q2. If, uh, we will hit 500, it will--probably mid Q3 or towards the end of Q3.

Mr. Mark Marostica:

Okay, great.

And then, one last question, following up on Mr. Ma's statements around the Cambridge relationship. It seems that you're getting some momentum there, and it's going well.

Just trying to get an idea of what the revenue potential is here, if you could help frame it for us. It sounds like this year is more of a year focused on trialing the system and rolling it out on a select basis. But trying to get a sense for, you know, how many locations, regions you will have in place by the end of the year for the new MTS and the ESOL exams, and then, um, what we could be looking at by the end of next year as well. So, any update there would be helpful.

Mr. Benson Tsang:

Sure.

Currently in 2014 fiscal year, uh, we budgeted about--up to 10 million RMB will be mainly as investment costs to build up the MTS system and fulfill all the requests of Cambridge.

In the revenue side, we did not really budget for anything. And in term of the status right now, uh, we confirmed with Cambridge we will deliver a showcase test for Cambridge in Hong Kong and Spain, towards the end of August.

If the examination is to the satisfaction of Cambridge, Cambridge has confirmed will roll out the MTS system to four countries and city, which include Mexico, Argentina, Spain, and Hong Kong.

But, of course, uh, within those three countries, there may be more than one city will grow out the MTS test. But, the final decision will be advised--will be determined and will be advised by Cambridge. And the timeframe for that will be September or October. That will be, again, depending on the final direction from Cambridge.

And what we understand, if everything works well, Cambridge has indicated they would like to roll out this MTS system on a global basis. And the timing will--probably will be January 1, 2014. But based on the current rollout schedule, if everything works well, there is a fair chance that everything will start in Q4, uh, calendar year 2013.

As far as revenue, as I mentioned earlier, we did not budget anything for 2014. And if we can actually start rolling out the program earlier, we do anticipate we'll get some revenue from this particular system.

But, at this moment we are not able to give a good estimate what the amount will be. But, whatever we will be getting from Cambridge, uh, it will be additional to our revenue guidance. For 2014--.

Mr. Mark Marostica:

Okay—

Mr. Benson Tsang:

--Uh, for 2014, calendar year, I may not be able to give you a firm sense of the revenue figure, but I can give you it in terms of the number of tests we may be delivering.

Just for the young learner English, uh, Cambridge will have over a million tests a year. But, with regard to the rollout program, we do not anticipate will roll out in one go covering the whole country, uh--the whole world. We believe Cambridge will have a rollout program for different countries and different cities. So, probably it would take like four years to roll out to cover the whole world. So, that's what we get so far from Cambridge.

Mr. Mark Marostica:

And then, one last follow up, uh, on Cambridge. Give us a sense of the feedback you're getting from Cambridge on the MTS system so far with the Hong Kong test that you've done. Thank you.

Mr. Benson Tsang:

Uh, yeah. So far, they are very happy with the result, and that is the reason why they confirm Hong Kong and Spain roll out in end of August and also confirm the schedule for September or October. So, uh, at the moment, I think the feedback is very positive, and, uh, we are building on this and--to build the relationship with Cambridge.

Mr. Mark Marostica:

Okay, thank you. I'll turn it over.

Mr. Benson Tsang:

Thank you.

Operator:

Thank you. As a reminder, to ask a question, you may press star, one on your telephone keypad.

The next question is from the line of Ella Ji of Oppenheimer. Please go ahead with your question.

Ms. Ella Ji:

Thank you. Good evening.

So, first of all, I wonder if, Benson, you could comment on the latest trend we are seeing at the financial securities exam. Are you seeing the downward trend being stabilized?

And also, I wonder if you still maintain the expectation that, on a full-year basis, the SAC is likely to see a flat year-on-year expectation?

Mr. Benson Tsang:

Ella, thank you for the question.

Um, regarding the financial security, let me just emphasize one point first. From our perspective, we look at financial industry mainly include three examinations—financial securities, banking association, and financial futures.

Of these three tests, of course financial future is relatively a small test. And this year, Q1, SAC exam compared to Q1 2013, it came down a bit. In term of number of tests, it came down about 80,000 tests, but, uh, it was in line with our expectation for 2014.

And for the banking exam, it actually grew about 8 percent in term of volume and also in term of the revenue. So, overall for Q1, we were basically all in line with our budget, our expectation.

And in Q2, traditionally there is no examination for banking, and there's only examination for financial securities. And in Q2, we anticipate there will be short of about 70,000 tests in financial securities as compared to Q2 2013.

And overall for the rest of the year, on a total basis, we continue to expect banking association exam will continue to see growth. And on the combined basis, we still feel comfortable the financial sector, will be able to achieve the single-digit growth for both 2014. And as a result, we maintain our guidance of 403 to 423 million.

Ms. Ella Ji:

Uh, got it. Is it fair to say that, uh, you know, the, uh, strength you are seeing in the banking association test is still more than offset the weakness in the financial securities, and therefore you are able to achieve a single digit growth in the--of test takers? Is that a fair statement?

Mr. Benson Tsang:

Yes, we anticipate the growth in banking association will continue in 2014. And we also believe the shortcoming in Q2, the financial security exam, could be just for Q2.

We anticipate at the moment the, uh--the number of tests to be delivered in Q3 and Q4 in the financial security exam will go up--back to our 2014 expectation, which is--should be in the range of 400 to 450,000 tests per quarter.

Ms. Ella Ji:

Got it. Thank you. And then, my next—

Mr. Benson Tsang:

Thank you—

Ms. Ella Ji:

—question is regarding your guidance. So, 1Q you did pretty well. You beat your guidance range. Um, but, it appears 2Q's guidance is relatively low. It looks a year-on-year decline. Uh, however, you maintain the full-year guidance. So, I wonder if you can give us some details behind the numbers. Is there any shift between the quarters that you are seeing? Thank you.

Mr. Benson Tsang:

Sure. There are two main reasons for the Q2 guidance. The first reason I just mentioned. There was a shortfall in the financial security test in term of the volume, and the impact for that approximately--about three million RMB.

And then, another reason for the Q2 guidance is there were a shift of two tests from Q2 to Q3. One test is in relation to mutual fund, and the other test is related to a private sector client, and the total for those two projects are totaling to about 10 million to 12 million RMB.

And let me emphasize we did not lose the contracts. And these two contracts, at the current indication from our clients, we will deliver them in Q3. And as a result of that, I mentioned earlier we do anticipate we will have a very strong Q3, and we anticipate another record-breaking Q3 in 2014 financial year.

Ms. Ella Ji:

Excellent. And then, my, uh, third question is, uh, if you can comment on the tests in your--still in your pipeline. What's--you know, uh, do you expect to roll out any new tests in the remaining of this year?

Mr. Benson Tsang:

Sure. In term of new tests, uh, the private sector will have a number of them. As you know, in the private sector we basically base on the content provided by the clients. And what they want us to deliver, we'll help them to deliver them. But, those are normally like smaller scale type of tests.

And in terms of in the public sector, currently there are different tests we are pursuing. And all of them are with the government-controlled or regulated association. And I think there are three we are very close to concluding the contract. And, uh, unfortunately, I am not able to disclose too much detail at the moment, but we do anticipate we should be able to conclude one or two during this financial year and will start seeing the contribution probably towards Q4 of this financial year. And one of the projects that I mentioned is actually--is a paper-based examination to be converted into computer-based examination.

Ms. Ella Ji:

Great. And just to confirm that you have not expected any, uh, of these potential tests in your full-year guidance. Is that right?

Mr. Benson Tsang:

Correct.

Ms. Ella Ji:

Okay.

And last question is with regards to your R&D expenses. I wonder, you know, for example, for the new MTS technology, are you pretty much done in terms of the R&D work, or do you still need to, uh, spend some money in developing, uh, or, you know, like running the R&D with regard to this new technology?

Mr. Benson Tsang:

Our current plan, the 10 million RMB we set aside for 2014 financial year, we anticipate this amount will be adequate to fulfill a majority of the request from Cambridge this year. And the amount we spent thus far in Q1, uh, does fulfill all the requests so far.

But, we also do anticipate, as we roll out the program with Cambridge, there will be more demands and requests. So, we do anticipate we'll continue to spend some money.

And also let me highlight, the majority of the expenses included in the R&D is actually our engineers. So, the engineer will maintain--will be, uh--will remain our employee to support the Cambridge or the MTS system.

Ms. Ella Ji:

Great. Thank you so much. You have answered all my questions.

Mr. Benson Tsang:

Thank you, Ella.

Operator:

Thank you.

There are no further questions at this time. I'd like to turn to floor back to management for closing comments.

Mr. Kevin Ma:

Thank you again to all of you for joining us. We look forward to speaking with you again during our Second Quarter 2014 financial results call in November.

As always, we welcome any visitors to our office in Beijing. Thank you.

Operator:

This concludes today's teleconference. You may disconnect your lines at this time. Thank you for your participation.