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## Conference Call Transcript

ATAI - Q2 2010 ATA Inc. Earnings Conference Call

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## CORPORATE PARTICIPANTS

**Ed Job**

*CCG Investor Relations - IR*

**Kevin Ma**

*ATA Inc. - Chairman, CEO*

**Walter Wang**

*ATA Inc. - Director, President*

**Carl Yeung**

*ATA Inc. - CFO*

## CONFERENCE CALL PARTICIPANTS

**Ella Ji**

*Oppenheimer & Co. - Analyst*

**Jeff Lee**

*Signal Hill - Analyst*

**Adele Mao**

*OLP Global - Analyst*

**Michael Kass**

*Baron Capital - Analyst*

**Mark Skitovich**

*Piper Jaffray - Analyst*

## PRESENTATION

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**Operator**

Good day, ladies and gentlemen, and welcome to the ATA fiscal second quarter 2010 earnings conference call. My name is Noalia, and I will be your coordinator for today. At this time, all participants are in a listen-only mode. We will be facilitating a question-and-answer session towards the end of today's conference.

(Operator Instructions)

As a reminder, this conference is being recorded for replay purposes. I would now like to turn your presentation over to your host for today's conference, Mr. Ed Job. Please proceed.

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**Ed Job - CCG Investor Relations - IR**

Thank you, Noalia. Good morning and good evening and welcome to ATA's second quarter of fiscal year 2010 earnings conference call. With us today are ATA's CEO, Mr. Kevin Ma, President Mr. Walter Wang, and Chief Financial Officer, Mr. Carl Yeung.

Before I turn the call over to Mr. Ma, may I remind our listeners that in this call, management's prepared remarks contain forward-looking statements, which are subject to risks and uncertainties, and management may make additional forward-looking statements in response to your questions.

Therefore, the Company claims the protection of the Safe Harbor for forward-looking statements that is contained in the Private Securities Litigation Reform Act of 1995. Actual results may differ from those discussed today, and therefore we refer you to a more detailed discussion of the risks and uncertainties in the Company's filings with the Securities and Exchange Commission.

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In addition, any projections as to the Company's future performance represents management's estimates as of today November 9, 2009. ATA assumes no obligation to update these projections in the future as market conditions may change.

To supplement its financial results presented in accordance with US GAAP, management will make reference to certain non-GAAP financial measures, which the Company believes provides meaningful additional information to understand ATA's operating performance. A table reconciling non-GAAP measures to the nearest GAAP equivalent can be found on the earnings press release issued earlier yesterday.

For those of you unable to listen to the entire call, a recording will be available via webcast for 90 days at the investor relations section of ATA's website at [www.ata.net.cn](http://www.ata.net.cn). And now it's my pleasure to turn the call over to ATA's CEO, Mr. Kevin Ma. Mr. Ma, you may proceed.

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**Kevin Ma - ATA Inc. - Chairman, CEO**

Thank you, Ed. Welcome, everyone, and thank you for joining us today. We are pleased with the progress we are making on the execution of our strategy, despite a difficult economic environment and recent measures to control the spread of the H1N1 virus, which caused the postponement of some of our tests.

During the quarter, our core testing service business performed strongly, with revenue up 88.8% over the same period of last year. In addition to the strong organic growth of our tests on behalf of the Securities Association of China, we also benefited from a solid performance of our new service offerings.

As some of you know, in the March quarter we launched important new initiatives leveraging our technology and distribution platforms in the areas of HR assessment and language learning targeted at the significant market opportunities we see in the enterprise and consumer segments. We are very pleased to report that in the fiscal second quarter both our HR Select and Test of English for International Communications have contributed a total of RMB8 million to our revenue, or 19.3% of total revenue in a seasonally weak quarter.

As part of our effort to leverage our technology to broaden our service offering, we are also pleased to report the soft launch in October of our Cambridge Young Learners English language initiative in six provinces, with the nationwide launch now expected to happen in December.

We are very excited with the early results from our enterprise and consumer-focused initiatives, which highlight the significant opportunity ahead for developing our testing service business to penetrate the broader private enterprise and the consumer segments of the market. We believe these initiatives provide a solid foundation for our profitable growth in the years ahead.

Revenue from our test-based education business declined 41.2% in the quarter. As we disclosed in the past, we have shifted resources from our test-based education service business to focus on our HR assessment and language business, which we believe is a more attractive opportunity, with higher margins and where we enjoy strong and sustainable competitive advantages. As a result, we are expecting revenue from our test-based educational business to continue to decline.

Turning to our test preparation business, we saw a decline 81.5% in revenue because there were no sales of NTET software, as the postponement of the NTET exam deadline led to pushback of Ministry of Education budget to purchase preparation software for tests. Going into the seasonally strong December quarter, we expect this business to recover and online test-preparation solutions pickup.

As we move into our fiscal third quarter, we remain cautious, due to the potential impact of H1N1 virus on our testing business. As the winter December quarter is our highest volume test quarter, if the virus causes further disruption in the gathering of masses at school campuses, then our large-scale test operation may be affected.

In addition, while we are seeing encouraging early signs of business development in HR Select, TOEIC and Cambridge Young Learners Program, we think the revenue development cycles do take a long period of time and the full potential of these efforts will become more visible into the next fiscal year. With that, I will now turn the call over to Walter who will provide you with a business update, and Carl, who will discuss our financial results for the quarter in more details.

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**Walter Wang - ATA Inc. - Director, President**

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Thank you Kevin, and welcome to everyone joining us on the call today. Despite a difficult environment, we are pleased with our results this quarter, which came in within our guidance. We are also pleased with the progress we made to expand our service offering and lay the foundations for our growth in the quarters ahead.

In the computer-based testing segment, we delivered 0.7 million tests this quarter, down 49.1% over the same period of last year. The reason of the decline of test volume is because we delivered close to 1 million exams at very low per test price last year, such as provincial high school tests. Average revenue per test was up 270.9%, driven by a higher-value mix of tests, including HR Select, TOEIC and Security Professional exams.

During the quarter, we successfully delivered the third National Securities Practitioner and Securities Broker exams on behalf of the Securities Association of China, as well as Futures Association of China, to 426,000 candidates, up 94.9% from last year. These exams were successfully delivered in 1,436 sites across 39 cities, demonstrating our ability to deliver large-scale tests across our extensive test center network and offering convenience to candidates, while safeguarding the integrity of the exam.

We also successfully delivered HR Select exams to 84,000 candidates on behalf of Agriculture Bank of China and People's Insurance Company of China, among others. We have so far registered 32,000 companies and converted 14 companies to paying companies, including the Agriculture Bank of China, People's Insurance Company of China, Accenture China, China Telecom, among others. We remain optimistic that HR Select will become an important growth driver for our business in the quarter ahead.

As Kevin mentioned, we see limited market potential for our test-based education program offering and thus have shifted our marketing efforts to our higher-margin testing and test preparation services. In the quarters ahead, we expect testing and test prep to eventually account for most of our revenue.

In line with our expectation, we did not have any NTET test preparation software sales in the quarter, and do not expect meaningful sales of software in the near future. This is because the deadline of the NTET test itself has been postponed and government budget demand for the training tool, our NTET software, has also been pushed back. However, we are optimistic about growth from our online preparation solutions in the quarters ahead. We also continue to believe that we can grow our online test preparation solutions by targeting the continuous professional training requirements of professionals in the securities industry.

Operationally, we are still making a strong effort to build a sales team to unfold the vast opportunities behind the private sector including HR Select, TOEIC and Cambridge Young Learner English. These efforts will cause margin pressure in the near term as cost builds ahead of revenue ramp-up but the achievements we have had so far in the short few months of launch for those programs give us encouragement about what we can achieve in the next few years. With that, I will now turn the call over to our CFO, Carl Yeung, who will go over our financial results in more detail.

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**Carl Yeung - ATA Inc. - CFO**

Thanks, Walter. Our second quarter results came within our guidance: Total net revenue was down 19.6% year-over-year to RMB41.6 million, or \$6.1 million. Net revenue from testing services was up 88.8% to RMB26.8 million, or \$3.9 million for the quarter.

The number of tests delivered was down by 49.1% year-over-year to 0.7 million tests. Average price per test delivered was up 270.9% to RMB36.2, as we have continued to shift our mix to higher-value tests, targeted at the securities industry and corporate customers.

Net revenue from test preparation and training solutions was down 81.5% in the period to RMB3.9 million, or \$0.6 million, from RMB21.2 million as we recorded no sales of NTET software in the quarter. Net revenue from test-based education services was down by 41.2% to RMB6.4 million, or \$0.9 million in the second quarter.

Gross profit was down 54.3% year-over-year to RMB15.7 million, or \$2.3 million. Gross margin declined to 37.8% from 66.5% in the comparable period last year. The gross margin decline was mostly driven by the absence of high-margin NTET software sales, as well as amortization of TOEIC royalties and capitalized software costs. We expect gross margin to continue to be under pressure for our seasonally slow months as impact of amortized cost are greater in these quarters.

Total operating expense increased by approximately 28.6% year-over-year to RMB32.9 million, or \$4.8 million, primarily driven by general and administrative expenses required to support the launch of HR Select, TOEIC and Cambridge Young Learners service offerings.

General and administrative expenses increased by an estimated 16.7% year-over-year to RMB16.2 million, or \$2.4 million. This increase was primarily the result of higher compensation expense. Sales and marketing expenses were up by 61.6% to RMB11.2 million, or \$1.6 million, primarily due to higher compensation and marketing expenses to support the launch of HR Select and other testing service promotions.

Research and development expenses increased by 15.5% year-over-year to RMB5.5 million, or \$0.8 million, primarily due to increased headcount and higher compensation expense. Loss from operations was RMB17.2 million, or \$2.5 million. Net loss for the quarter was RMB16.4 million, or \$2.4 million, compared to net income of RMB8.3 million in the comparable period last year.

Basic and diluted loss per ADS were RMB0.37, \$0.05, and RMB0.74, or \$0.11, respectively. Net loss excluding share-based compensation expense and foreign currency exchange gain or losses, which is non-GAAP, was RMB15.2 million, \$2.2 million for the quarter, equivalent to RMB0.68, \$0.06 per ADS -- per basic and diluted ADS.

As of September 30, 2010, ATA had cash of RMB233.7 million, equivalent to \$34.2 million, working capital of RMB260.6 million, equivalent to \$38.2 million, and no debt. Shareholder's equity at the balance sheet date was RMB377.1 million, or \$55.2 million. CapEx for the second quarter of fiscal year 2010 were RMB53.3 million, or \$7.8 million, mainly for the closing of the acquisition of our Beijing operating office space.

Now, turning over to outlook, for the fiscal third quarter 2010, we expect net revenues will be in the range of RMB76 million to RMB80 million, representing year-over-year growth in the range of 12% to 18% -- 12% to 18%.

ATA expects net revenues for the fiscal year ended March 31, 2010 to be in the range of RMB225 million to RMB240 million, which is expected to represent a 3.4% to 10.3% growth over fiscal year 2009. As we mentioned in our press release issued prior to the call, we have lowered our guidance for the full year as we expect measures to prevent the spread of the H1N1 virus to affect our testing service business during the winter months as well as a more conservative view towards immediate revenue build behind our new private sector efforts. This is ATA's current and preliminary view, which is subject to change. Now I'll turn the call back over to Walter for some closing

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**Walter Wang - ATA Inc. - Director, President**

Thank you, Carl. Our results for the quarter reflect our decision earlier this year to focus resources on our testing as well as test prep business and our commitment to aggressively broaden our service offering to capture the opportunities we see in the corporate and consumer markets. Clearly, this effort has required us to scale our operations ahead of ramping up revenues from these new initiatives, which impacted our margins.

As we look to the future, we are confident that we are well positioned with the right service offering and the right strategic focus to capitalize on the large computer-based testing opportunity in China. With that, we would now like to open the call to your questions. Operator?

## QUESTION AND ANSWER

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**Operator**

(Operator Instructions).

Your first question comes from the line of Ella Ji with Oppenheimer.

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**Ella Ji - Oppenheimer & Co. - Analyst**

Hi. Good evening, guys. Your full-year guidance, revenue guidance, was lowered by about RMB35 million to RMB40 million. I'm just wondering if you can give us a breakdown of how much of that is from your government factor testing services, versus how much is from the new private sector services?

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**Carl Yeung - ATA Inc. - CFO**

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Okay, sure. Ella, it's good to hear from you again. It's been some time. We are lowering our guidance at the top and bottom of the range by RMB35 million to RMB40 million, and this is in the light of us expecting about potentially 600,000 test takers being displaced from the government testing site. This includes -- this spreads across some of our test services for the banking sector, as well as for the Ministry of Labor. So a total of about RMB16 million to RMB17 million is around that from there.

And then, because what we are seeing from the decline of test based education program is probably going to be going down a bit faster than what we originally know earlier in the year, we want to trim some of our numbers there, not by a lot, by about RMB4 million to RMB5 million for the second half.

And then the remaining is just we don't know how far the virus will impact, because just as we go into the colder months, the virus may take off. And then if that does happen, because we launch our testing services in school campuses, where a lot of people gather together, some campuses or these gatherings may be forced to be closed. So we just want to sort of move our numbers even further a bit lower to be conservative.

Of course, there's about RMB12 million to RMB13 million where we want to trim away from the private sector side, as instead of being a passive launch, we had the soft launch of the Cambridge Young Learners Exam -- Cambridge Young Learners Program, not exam. It's a learning product. So that revenue would probably be pushed back starting into December and then HR Select, it's actually on track for the first half of the year, according to what we have planned, but we just want to be a bit more conservative, since we were moving guidance anyway.

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**Ella Ji - Oppenheimer & Co. - Analyst**

Okay, thanks. I just want to clarify, so about RMB16 million to RMB17 million lower the guidance from government sectors.

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**Carl Yeung - ATA Inc. - CFO**

Yes.

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**Ella Ji - Oppenheimer & Co. - Analyst**

And about RMB4 million to RMB5 million in the private sector?

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**Carl Yeung - ATA Inc. - CFO**

In the test based education business.

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**Ella Ji - Oppenheimer & Co. - Analyst**

I'm sorry?

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**Carl Yeung - ATA Inc. - CFO**

RMB5 million from the test-based education sector.

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**Ella Ji - Oppenheimer & Co. - Analyst**

Oh, okay, I see. I see. And then about RMB12 million to RMB13 million in the Cambridge Young Learning Program, and the rest will be you're being more conservative, expect some impact from H1N1.

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**Carl Yeung - ATA Inc. - CFO**

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Right.

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**Ella Ji - Oppenheimer & Co. - Analyst**

Yes, okay, got you, thank you for the color. So about your TOEIC revenues, I see it's actually down quarter-over-quarter, but the average price was increased, so can you talk -- can you give us some color about seasonality wise how should we think about that?

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**Carl Yeung - ATA Inc. - CFO**

Yes, we obviously did not have TOEIC in the same quarter of last year, because we only got it in March of this year. The volume -- or the total revenue was down, but when we look at volume, compared to the same quarter last year, when the operation was in ETS hands, the volume was comparable, so we didn't see any drop in volume, and the revenue was comparable. So Q2 is a seasonally slower quarter for TOEIC, and then we expect that to pick up again into Q3.

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**Ella Ji - Oppenheimer & Co. - Analyst**

Okay, great. And then for your HR Select business, do you have any visibility in terms of for the remaining of the companies that have already converted, do you have any visibility of how much revenue potential does that represent.

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**Carl Yeung - ATA Inc. - CFO**

Yes, they will contribute a meaningful revenue on HR Select side, but we want to be a bit more conservative given that the service is new. We are still seeing some tweaks on how we want to service these customers in the best way. So we have upcoming clients and Walter can give us some color.

I have here, for example, Bank of China is probably going to be doing something in the second half, so there is going to be some meaningful revenue, probably not as big as Q2, because what we have done with Agriculture Bank of China is probably the largest we have done for any private sector client. But we are talking to them, to potentially expanding the current test title within Agriculture Bank of China to other areas of internal human resource testing. So, Walter, any additional color in terms of upcoming clients in the second half of fiscal 2010?

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**Walter Wang - ATA Inc. - Director, President**

We are almost -- we are closing the deal with Bank of China right now.

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**Ella Ji - Oppenheimer & Co. - Analyst**

Okay, thanks for the color. Lastly, I just want to see if you guys have any first takeaways for the new minister of MOE. How is that potentially going to impact your business? Thanks.

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**Carl Yeung - ATA Inc. - CFO**

We have to do a quick translation, and I can have our CEO answer that.

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**Kevin Ma - ATA Inc. - Chairman, CEO**

(spoken in Chinese).

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**Carl Yeung - ATA Inc. - CFO**

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The CEO's comment is there probably will not be any material impact to us.

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**Ella Ji - Oppenheimer & Co. - Analyst**

Okay, okay, good to know. Thank you very much.

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**Operator**

Our next question comes from the line of Jeff Lee with Signal Hill.

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**Jeff Lee - Signal Hill - Analyst**

Hi, good evening.

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**Carl Yeung - ATA Inc. - CFO**

Hi, Jeff.

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**Jeff Lee - Signal Hill - Analyst**

I wanted to clarify, so the reduction in expectations for banking in the Ministry of Labor, how much of that is related to H1N1, versus how much of it is just sort of slower demand in general and other unexpected factors?

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**Carl Yeung - ATA Inc. - CFO**

Yes. It's really hard -- it's very, very difficult to quantify. The reason is, when we go out and talk to these customers, when we go out and try to do publicity campaigns to attract more customers, their coordination has been done at the government side, so they have to do these public press releases, basically notices so that people know there are these tests out there. So when we try to do these marketing efforts with them, a lot of excuses or pushback came back in saying, well, we really don't want to have a lot of people gather to do these things, and then if there's outbreak and that source came from our test, we're going to be in trouble.

So it's very difficult to quantify that at the moment, but there has to be some impact from, for example, Ministry of Labor, where it's been doing some integration for the last year, so there must be some slowdown. But through all the conversations, the topic of this virus came up a lot.

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**Jeff Lee - Signal Hill - Analyst**

I see, Okay. And then can you talk about the outlook for new agreements? Is there any update on the Internet cafe or the security guard certification agreement. And then just sort of your general outlook for new agreements over the next two years or so?

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**Carl Yeung - ATA Inc. - CFO**

Sure. In terms of general outlook for new large-scale government-type tests, you probably heard that the new security guards regulation was approved by the [winjabao], so the regulation is out, so that's good news for us. And within that regulation there's an area of training and testing that is required by these security guards.

Now, what's a little uncertain within that is that there are no details within that specific regulation about specifics that outlines how their training should go, how the testing should go. There's no specific details. But we're working very closely with the authority to iron that one out and at the moment the good news is the regulation came out before the end of the year, is what we've been informed earlier by these regulators. But, looking at the timing, we need to iron out the details, because details were not released and approved. It may be March until we start to see a wider operation launch for the security guards. And then I'll leave the rest of the comments to Mr. Ma and Walter for any updates, since they're here.

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**Walter Wang - ATA Inc. - Director, President**

We are still under the negotiation with the Ministry of Culture to discuss the potential cooperation to certify the employees from the Internet cafe, but currently we are not -- we didn't see any chance that we can close this contract in the near future.

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**Jeff Lee - Signal Hill - Analyst**

Okay. Thank you. And then I wanted to ask about the expenses. Maybe you could give -- Carl, give more detail on what impacted gross margins this quarter and then what your expectations are for gross margins for the rest of the year.

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**Carl Yeung - ATA Inc. - CFO**

Sure. It's a bit more pressure when it's a seasonally slower month, as you know. Because ever since the third quarter last year, we had started to amortize, for example, the TOEIC acquisition costs, also amortize some of our new software development that we made last year. So that added about RMB4 million to RMB5 million in direct costs in a baseline scenario, so when a seasonally slower quarter comes, the testing business will see a bigger margin pressure.

But the key margin -- why margin dropped so much in this quarter compared to the same quarter last year, is because we did not have any sales of NTET software, and that software carries a margin of north of 90%, and we already discussed in the call why we don't have any sales there.

So in these seasonally lower quarters, for example, the upcoming fourth quarter, we expect margins to be lower than what we have seen in last year, but I think, given Q3 is a bigger quarter and that will probably neutral out some of these impacts, and we can probably sustain a gross margin of somewhere around 50% for the full year. And, hopefully, that margin will improve after Q4 into next fiscal year as Cambridge Young Learners Program, as HR Select, as TOEIC, picks up in revenue, because all three of those, when we initially designed the projects, carry a 55% to 60% gross margin.

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**Jeff Lee - Signal Hill - Analyst**

Okay, great, thank you. And then can you talk about other expenses, sales and marketing was up this quarter, which I assume was for HR Select, and G&A expense was also up sequentially. Can you just -- a little more detail on those two lines and your expectations for the rest of the year.

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**Carl Yeung - ATA Inc. - CFO**

Yes, sure. All three expenses, except for -- well, all three expenses were up year-on-year, and then quarter from last quarter, R&D was lower, but sales and marketing and G&A were still up. Sales and marketing is basically up, exactly like you said. It's really to support the launch of HR Select. Now, this is what our strategy is, is that given that 2010 is not going to be, to be very honest, we think it's not going to be a beautiful year, we want to make the commitment to develop these projects, so that 2011, our fiscal year 2011, can be very attractive.

So we are launching these advertising campaigns. We are launching our road shows to support the early development of HR Select, which I think so far we've seen pretty good progress. 32,000 companies is quite a feat for a new service launch.

Now, for the rest of the year, therefore, we will probably keep up with the sales and marketing expense, unless we hear back, we have a big pushback from our important shareholders and our Board of Directors. We can probably trim that down. We have a lot of flexibility in trimming that down, but at the moment we want to make that commitment to ensure the success of the programs.

In G&A, it's also up, but only marginally quarter-on-quarter. It was RMB14.9 million in Q1, and now it's RMB16.2 million. We added more people to support the operation, and mainly we want to add people at the higher end level, with more expertise in basically consumer battlefield. We've done pretty well in the past in terms of the government sector battlefield, but we really don't have much experience in the consumer battlefield. So, as you know, we hired Bennie Lin, which is a very important add to our senior management team, and he's adding some of his important people to help him launch these programs.

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So G&A is also going to be up. For the rest of the year, G&A is probably going to go even a bit higher, as we restructured some of our company's operation into a more sales-oriented operation, and that requires sort of more people with bigger titles, so that can probably creep into Q3 and Q4.

Now, it's the same story as sales and marketing. These are more discretionary. We don't need it to sustain the revenue for now, but we do want to make a commitment to build this business into a successful business and a sustainable business. So we will keep it -- we will keep going at it, unless there's a big pushback from our shareholders or our Board of Directors.

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**Jeff Lee - Signal Hill - Analyst**

Okay, great. That's all my questions. Thank you.

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**Carl Yeung - ATA Inc. - CFO**

Thanks, Jeff.

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**Operator**

Your next question comes from the line of Adele Mao with OLP Global.

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**Adele Mao - OLP Global - Analyst**

Hi. First of all, I would like to go back to the topic of HR Select. ATA successfully converted 15 trial accounts to revenue-generating customers. How many trial accounts were you targeting to convert in order for you to get to the 15? I just want to get a sense of the conversion success ratio.

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**Carl Yeung - ATA Inc. - CFO**

Sure. Our target conversion rate for the initial year is 1% of registered companies, and into next year our target is 3% of registered companies. Now, if you look at the success rate, it's not very high in the first year. The reason is because we still find that we lack a lot of the sales and marketing and the right headcount to close these accounts, because we've never really done that before 2009. So therefore it sort of links up with my previous comment about making the commitment to build the teams. So those are the numbers, Adele.

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**Adele Mao - OLP Global - Analyst**

I see. Okay. So does your current revenue guidance include the revenue contribution from HR Select?

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**Carl Yeung - ATA Inc. - CFO**

The updated one does, but it's a much more conservative number. Like I have discussed in the past before, I don't have a specific price tag in HR Select. I have a general number for Cambridge Young Learners plus HR Select. Now, Cambridge Young Learners moved back, so that piece of pie for the private sector side, we more conservatively moved that down. Right now, we are hoping that we can achieve another RMB5 million, RMB6 million for the rest of the year.

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**Adele Mao - OLP Global - Analyst**

I see, okay. Let's say that for the HR Select customer that you already converted, sort of what kind of visibility do you have once they say, OK, we're going to become a paid customer? How much sort of notice in advance? Can you see how many test takers are they going to sign up, and how many test titles are they going to do under your program?

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**Carl Yeung - ATA Inc. - CFO**

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Sure. There are two types of customers. One is the sort of small enterprise annual membership kind of thing, so that's simple. We just collect RMB3,800 from them and we just amortize it for the rest of the year. So it's very simple. Once they start paying, there's no question of visibility there. The visibility question is more applicable for these large-scale -- larger-scale, more unique HR services, basically, more customized solutions, such as the ones we have done for PICC and Agriculture Bank of China. And those probably take within the quarter they let us know how many people and then we just go and help them finish designing the test, set up the locations and then teach them how to use the systems and then get things going. So we have about a quarter's visibility.

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**Adele Mao - OLP Global - Analyst**

I see. That's helpful. Just for the quarter, regarding the sales and marketing expense that you discussed earlier, maybe you could break out for us how much it is from the launch of the HR Select, versus the regular sales commission?

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**Carl Yeung - ATA Inc. - CFO**

Sure. Additionally, we have about -- just in this particular Q2, about somewhere between RMB3 million to RMB4 million spent on HR Select.

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**Adele Mao - OLP Global - Analyst**

I see. Okay, thank you very much, Carl.

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**Carl Yeung - ATA Inc. - CFO**

So we can basically trim that down if we need to.

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**Adele Mao - OLP Global - Analyst**

Right.

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**Operator**

(Operator Instructions)

Your next question comes from the line of Michael Kass with Baron Capital.

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**Michael Kass - Baron Capital - Analyst**

Hi, thanks. I just wanted to get -- on this recent quarter, it seems like there was a mix in your shift obviously towards the TOEIC or HR Select, as the government -- some of the government lines were very weak. And I just think you said that you thought you could get to a 50% gross margin, that that was the design when you rolled out these new tests.

And I'm wondering, is there something about the startup that they're -- I mean, if the overall gross margin, I guess my question relates to with the absence of the NTET software revenue, it kind of looks like perhaps your gross margin is not a 50% plus type number. Could you just explain how you get from the high 30s back to the 50s and what's happening right now that's causing it to go below that on the gross margin?

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**Carl Yeung - ATA Inc. - CFO**

Sure, Michael. Thank you for your question. It's really because we have a small quarter, which is typical for Q2, and the quarter, we did RMB41 million in revenue, compared to the normal larger quarters. For example, my guidance for Q3 is between RMB76 million to RMB80 million, which doubles basically or revenue. So when a quarter such as this, just RMB41 million comes in, and what we're expecting for Q4 as well, when

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that comes in and when we have additional amortized cost such as TOEIC, license fee and also some software that we have been amortizing that added about RMB4 million in our base costs, direct costs, without doing anything, that does impact our margins.

So it does that when the quarter is slower. But when we go back into these RMB70 million, RMB80 million quarters, the result impact of the RMB4 million base direct cost from these amortizations don't affect it that much and we can get our margins back up, across the 50 line. So when we pull the rest of the year across and we have the first quarter at 55.9%. This quarter is at 37.8% and the next quarter will be north of 50% and then the final quarter will be sort of lower than 50%, we'll probably be able to sustain 50%.

And, for the full year, our guidance is at RMB225 million to RMB240 million, and looking at the mix, TOEIC and sort of this private sector slide, added together, is only accounting for 11% to 12% of our revenues, probably, for the full year. So that stuff that's designed to have 55% to 60% margin, with a sort of just about 10% contribution to revenue, will not take us into 55% or 60% this year. But it will have a much more positive impact into fiscal 2011, when we hope to have a much bigger revenue size for those.

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**Michael Kass - Baron Capital - Analyst**

Okay, thanks a lot.

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**Operator**

And our final question comes from the line of Mark Marostica with Piper Jaffray.

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**Mark Skitovich - Piper Jaffray - Analyst**

Hi. It's actually Mark Skitovich for Marostica. Just I was hoping to get, Carl, some further clarification on the HR Select sales model. Specifically, what is your sales headcount today and how do you see that trending over the next six months, if you can maybe quantify what you expect to see that number to be six months from now? And then what revenue capacity will that number support? And then also sort of the same question on the marketing side, what kind of marketing dollars are you spending today and sort of how does that trend sequentially over the next couple of quarters, thanks?

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**Carl Yeung - ATA Inc. - CFO**

Actually, I have the headcount sort of landscape and expectation sort of -- I'll have Walter drive that response. I'll first answer your sales and marketing dollars first. We're looking at about spending competitors the last year, where we didn't have these things. The addition of anywhere between RMB2 million to RMB5 million per quarter, in terms of sales and marketing additional.

So there is that impact, but that's all very discretionary, and we can move that up, move that down to the next two quarters, depending on the shape of what I hear back from the investment community. So, Walter, why don't you give Mark a bit more color in terms of headcount for HR Select.

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**Walter Wang - ATA Inc. - Director, President**

We are working on hiring more talent for the HR Select team. And in the near future, probably we think two or three months, we are going to hire 40 to 50 more people for the HR Select team.

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**Mark Skitovich - Piper Jaffray - Analyst**

Okay, and what --

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**Carl Yeung - ATA Inc. - CFO**

Now how many?

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**Walter Wang - ATA Inc. - Director, President**

I'm sorry.

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**Mark Skitovich - Piper Jaffray - Analyst**

What's the number today, and then sort of what sort of revenue number would that total, the additive 40 to 50, support?

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**Walter Wang - ATA Inc. - Director, President**

To date, for the HR Select team, we have 35 people, and we are going to hire ten to 15 more people.

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**Mark Skitovich - Piper Jaffray - Analyst**

Okay. And then just final question, separately, on the Internet cafe front. How would you characterize your discussions with the Ministry of Culture? Is it still progressing? Are you seeing sort of a declining progression there? I mean, how would you characterize that and sort of your confidence or visibility in that ultimately getting done? Thanks.

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**Carl Yeung - ATA Inc. - CFO**

We are in the progress to discuss with the Ministry of Culture, but the progress for this project is not that optimistic. So it's really hard for me to give you a very clear potential for the project now.

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**Mark Skitovich - Piper Jaffray - Analyst**

Okay, fair enough. Thank you.

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**Operator**

Ladies and gentlemen, this concludes your question-and-answer session. I would now like to turn the call back over to Mr. Carl Yeung for closing remarks.

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**Carl Yeung - ATA Inc. - CFO**

With that, thank you. And on behalf of the entire ATA management team, we want to thank you for your interest and participation on this call. ATA will be attending the Signal Hill Education conference in Baltimore on the 12th of November, as well as the BMC conference in New York on the 19th and 20th of November. If you have any interest in visiting ATA, please contact our investor relations representatives in the US at 1-646-213-1914. Again, I'd like to thank all of you for joining us on the call today. Operator?

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**Operator**

Thank you for your participation in today's conference. This concludes your presentation, and you may now disconnect.

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