

ATA

TRANSCRIPT

ATA Inc.

June 2nd, 2011

Q4 Fiscal Year 2011 ATA Inc. Earnings Conference Call



PARTICIPANTS – CORPORATE

Kevin Ma

Chairman & Chief Executive Officer

Walter Wang

President

Benson Tsang

Chief Financial Officer and Chief Accounting Officer

Adam Prior

Vice President of The Equity Group

PARTICIPANTS – CONFERENCE CALL

Mark Marostica

Piper Jaffray

Ella Ji

Oppenheimer

Operator:

Welcome everyone to 4QFY2011 ATA Inc. earnings conference call. All lines have been placed on mute to prevent background noise. After the presentation, there will be a question and answer session. Please follow the instructions given at that time if you would like to ask a question. For your information this conference call is being broadcast live over the Internet.

Webcast replay will be available within an hour after the conference is finished. Please, visit ir.ata.net.cn.

I would like to introduce Adam Prior, Vice President of The Equity Group. Mr. Prior, please begin.

Adam Prior:

Thank you, operator, and good morning, everyone. Thank you for joining us. Copies of the press release announcing the fiscal 2011 fourth quarter and year-end results are available at the IR section of ATA's website at www.ata.net.cn.

As part of this conference call, the Company also has an accompanying slide presentation available in PDF format at the IR portion of the Company's website, which can be accessed under the webcast tab or also on the future events calendar. You are also welcome to contact our office at (212) 836-9600, and we would be happy to send you a copy. In addition, 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 USD amounts in this conference call, relating to the Company's most recent financial results, are converted from RMB using an exchange rate of RMB6.5483:USD1. 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.

I would now like to take a moment to outline the format for today's call. The Company's President, Mr. Walter Wang, will open up with an operational overview. The Company's CFO, Mr. Benson Tsang, will then discuss the financials. The Company's Chairman and CEO, Mr. Kevin Ma, will then conclude with a discussion of growth strategy in fiscal 2012. For those of you following along with the accompanying PowerPoint presentation, there is an agenda and overview of the Company on slide three. And Mr. Wang will be beginning on slide four.

With that, I would now like to turn the call over to ATA's President, Mr. Walter Wang. Please go ahead, Mr. Wang.

Walter Wang:

Thank you, Adam. Fiscal 2011 was a strong year for our Company. We believe that ATA is well positioned and appropriately capitalized to safely expand on our leading market position in China's computer-based testing industry. Given that this is a year-end call, I would like to briefly discuss ATA's history and growth, note a few operational highlights, and then turn it over to Benson. I apologize to those of you who may have heard some of this background information before.

ATA is the market leader in China's computer-based testing and related services industry, providing testing services to individuals all over China, in various industries including IT, banking, teaching, securities, and others. A recent example of our success occurred in March, where over the course of one weekend, ATA delivered approximately 654,000 tests for the Chinese government's Securities Regulations Examination. This is the highest total number of tests ATA has administered in any given weekend over the Company's history.

Since inception, we have successfully delivered over 31 million billable exams, without a single instance of a security breach. This is an achievement that all of our employees are proud of. During fiscal 2011, we continued to expand our service offerings and testing capabilities, and we currently have a daily capacity of potentially delivering 1 million tests.

And on slide five, we list a few of our key clients, which include global brand names such as Dell, Deloitte, and P&G, as well as important associations and ministries in China that are setting industry standards, rules, and regulations by requiring professionals in these industries to pass certification and licensing exams.

We feel that this slide is a testament to our solid performance, and while I will not say that clients stay with us forever, I will say that once a client has started computer-based testing with us, it is very difficult for them to change service providers.

On the next slide we highlight our continued geographic expansion. This map illustrates our nationwide network of over 2,000 test centers, which allows for large-scale testing throughout the country. We have a presence in every province in mainland China. We are not aware of any comparable size network in China.

Moving to the next slide. Over the past six years, we have grown significantly, in both net revenues and tests delivered to individuals throughout China. In the red boxes, we have highlighted a few of the key milestones for each year. Of note, during fiscal 2011, the four largest China state-owned banks all became customers of ATA's HR Select service.

On slide eight, you can see a few key highlights for the year and quarter. ATA delivered approximately 6.9 million billable tests in fiscal 2011, an increase of 19.9% from fiscal 2010. This led to strong financial results, which included double-digit growth on the top line and a return to profitability. During the fourth quarter, we also improved each of our operating metrics during what is seasonally a weaker period.

And for a noteworthy recent accomplishment, on May 14th, a free pilot of the National Security Guard Qualification Test was held for the first time in Shaanxi province. The test was successfully administered in four cities, including Xian, Yulin, Ankang, and Xianyang. A total of 674 candidates from security service companies took part in the test. The computer-based test leveraged ATA's advanced delivery platform, test administration and delivery services, test site monitoring technology and data analysis services. We were proud to have received high praise not only from the test sponsor but also from test candidates, who gave favorable responses to the computer-based test platform for its convenience and ease of use.

Our business can be broken down broadly into two segments, which you can see on slide nine. First, our core testing services. These specific types of exams range, from professional certification exams in various industries, such as banking, securities, etc., to our newer HR Select service, where we assist with tests for hiring and internal assessment at different companies, and the TOEIC exam as well.

ATA is also involved in online test preparation and training for professional development and for English language education. This is where we package our testing services together with comprehensive training content and online delivery platform.

On the whole, we continue to develop our platform. Our Chairman will go into our future growth plans and outlook shortly, but right now I would like to turn it over to Benson for a review of the financials. Benson.

Benson Tsang:

Thank you, Walter. I will try to keep my statements brief. We are very pleased with our results for the quarter and year. Our Company reported solid operating results across the board, which included strong cash generation and stable growth.

On slide 11, we show in USD that ATA has exceeded the market's consensus estimates for the past four quarters, in terms of net revenues, gross profit, net income, and diluted EPS per common share. We are confident that our Company can continue this trend and have listed on this slide ATA's covering analysts at OLP Global, Oppenheimer and Piper Jaffray.

On the next slide you will see a breakdown of the Company's financial results for the quarter. The Company's net revenues increased 5.3% year over year during a seasonally weaker period. Gross profit for the 2011 fourth quarter increased 29.6% to RMB22.4 million, or US\$3.4 million, from RMB17.3 million in the same period last fiscal year.

Gross margin increased to 45% in fourth quarter 2011 from 36.6% in the prior-year period, primarily due to an impairment of the prepaid royalty fee in the prior-year period related to the Company's partnership with Microsoft.

Operating expenses for fourth quarter 2011 decreased 44.9% to RMB30.5 million, or US\$4.7 million, from RMB55.3 million in the same period last fiscal year, primarily due to significant decreases in general and administrative expenses as well as a one-time bad debt provision related to the Company's NTET tutorial platform that was taken in the prior-year period. We also substantially reduced our loss from operations and net loss.

On slide 13, we provide more detailed information about our revenues, both by year and then by quarter. Note the seasonality in our business model. Quarterly analysis of our business model has shown that we have a highly seasonal business model that reflects the testing calendar in China.

Fiscal 3Q, which runs from October to December, is typically our strongest, while fiscal 4Q, which runs from January to March, is typically a weak quarter. In general, fiscal 1Q and 3Q tend to have higher revenues than fiscal 2Q and 4Q because of how tests are scheduled.

Keep in mind, that as test schedules change, ATA's revenues associated with the corresponding exams will adjust accordingly. Our expectation is that contributions from HR Select, while still a relatively small portion of our revenue, will help to offset the inherent lumpiness of our business from quarter to quarter.

This is further displayed in our next slide, where we break out our fiscal 2011 revenues by segment. The testing services Walter discussed earlier are ATA's core business, which accounts for approximately 80% of revenues. The specific types of exams range from professional certification exams in various industries, such as banking, securities, etc., to our HR Select service, where we assist with tests for hiring and internal assessment at different companies, and TOEIC exams.

ATA is also involved in online test preparation and training for professional development and education in the English language. This is where we package our testing services together with comprehensive training content, online delivery platform, etc., and we generally charge these testing-related services on a per-head-delivered basis.

We have noted to many of you in meetings and in past calls that trailing 12-month results are a true indicator of our business. We are very pleased with our return to profitability in fiscal year 2011. You can see the full fiscal year results on slide 15.

We reported 24% revenue growth and over 50% gross margin for the year, which we feel is a testament to our highly scalable method of delivering computerized testing services. We expect continued gross margin improvement in fiscal year 2012 due to improved economies of scale with our testing center partners, greater inroads with banking and financial institutions, and more streamlined operations.

On slide 16, we outline the improvement in our operating costs as a percentage of revenue. We have continued to optimize our sales cycle, where we often spend considerable time educating and providing information to prospective clients regarding the use and benefits of our products and services.

We continue to be supported by strong free cash flow and a solid balance sheet, which we have highlighted on slide 17. Cash generated from operating activities in FY2011 was RMB62.1 million, or US\$9.5 million. As of March 31, 2011, we had over US\$40 million in cash and no long-term debt.

We believe we have sufficient funds to meet both our short-term and long-term liquidity needs and capital expenditure requirements to achieve our expansion plans, including internal growth initiatives.

As some of you may have seen the other announcement we made yesterday, which speaks to our Company's ability to produce free cash flow, thereby allowing us to return capital to our loyal shareholders. Yesterday, we announced that ATA's Board of Directors has declared a special cash dividend of US\$0.215 per common share, or US\$0.43 per ADS.

The total amount of cash distributed in the dividend is expected to be approximately US\$10 million. The dividend will be paid on or around August 1, 2011, to all shareholders of record as of the close of business on June 30, 2011.

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

Kevin Ma:

Thank you, Benson. ATA's growth strategy centers around three main goals, which we list on slide 19. We are focused on increasing our industry coverage, which will enable ATA to add new test titles in new and existing industries to better serve test candidates. We delivered a total of 6.9 million billable tests during fiscal 2011. This database of test takers is naturally a resource from which ATA can draw for future growth.

For example, if an individual wishes to take a securities exam, another option may be to also take a banking or futures exam to further advance their individual career path. In many ways, our Company is focused on helping to provide options and access to fair and valid assessment exams to China's diverse student base and growing workforce.

We expect to continue our proactive sales and marketing efforts, via campus recruiting and also marketing to specific sectors of candidates. We plan to continue expanding our geographic base, which is already far and beyond the largest network of testing centers in China, while increasing our number of test titles, which at the end of fiscal 2011 was over 400 different titles.

We believe these strategic goals will allow ATA to grow in shareholder value, while also serving the greater good. Again, in terms of social responsibility, ATA is committed to increasing public awareness of the advantages of education and eventually obtaining an official license or certification for stable and fulfilling employment.

As we continue to closely monitor economic activity throughout China, we still feel very confident that our business will continue to grow at a healthy rate in the long term. ATA intends to leverage its state-of-the art technologies in this high-growth market of delivering large-scale testing. We have a proven track record. Our large-scale tests are simultaneous, consistent, secure, and cost-effective, and this is why our clients stay with us for many, many years.

On that note, let me outline our annual guidance for fiscal 2012, shown on slide 20. We expect revenues to be between RMB395 million and RMB415 million, which in USD is approximately US\$60.3 million to US\$63.4 million.

We think that our Company will continue to expand its gross and net margins as we increase scale, and are projecting net income of between RMB40 million and RMB45 million, or approximately US\$6.1 million to US\$6.9 million.

We are basing this guidance on our own internal growth projections. We are optimistic about the outlook of the China computer-based testing market because of growing demand, improving brand recognition, and increasing awareness among both our corporate and government clients – and our test takers.

While still early in the year, we are confident that ATA will continue to see accelerating growth from our testing services business, while achieving improved levels of profitability from HR Select and TOEIC.

We also expect to begin realizing benefits from the investments made during FY2011 in designing and implementing new, large-scale tests, such as the nationwide security guard certification exam. Our Company is continuing to generate excess cash flow and is well positioned to continue healthy, organic growth.

With that, operator, let us open it up for any questions, please.

Mark Marostica, Piper Jaffray:

Thank you, and congratulations on the quarter and the great year. The first question has to do with your budget for this year. I wonder if you could give us a little bit more detail about how you build up your budget for this year, the top exams you expect as part of that budget, and how we should see the revenue play out on a quarterly basis. I appreciate, Benson, you giving us some color on the relative strength of the quarter, but any more detail there as well would be helpful.

Benson Tsang:

Sure, Mark. Let me start with the revenue figure. As stated in the guidance, we expect the revenue growth in the range of 30% to 36%. The way we will build up the budget, for those of you who have the slide with you, which is slide 14, I will try to give you some more color on the growth expectation.

Under our services for the traditional type of business we expect 15% to 20%; for HR Select we expect to continue to have strong growth, we expect about 50%; and for TOEIC we also expect about 50% growth; and for the remaining services, mainly the test preparation and other revenue, we expect 15% to 20% growth as well.

For the test-based education service, I just want to highlight this is actually mainly related to the Microsoft partnership. The Company has discussed with Microsoft and decided to discontinue this business. So, this year we generated about RMB25 million, and for fiscal year 2012 we expect this revenue figure to drop significantly. We expect it will be probably in the range of RMB3 million to RMB5 million.

And then, in terms of the revenue breakdown by quarter, we expect for the 1 half we can probably achieve 1/3 of our guidance, so it should be in the range of RMB130 million to RMB140 million, and the remaining 2/3 will be in the 2 Half.

For the 1 half, we expect 1Q probably in the range of RMB64 million to RMB68 million, versus last year's RMB85 million. And let me try to elaborate this a little bit. Last year RMB85 million 1Q actually included the banking exam, which is about RMB24 million, and for the 1Q 2012 we will not have the banking exams. And during the year, banking exam is in the process to apply for governmental approval, to make the qualification exam become a requirement rather than an encouragement basis. As a result, the banking association expects it will take a couple of quarters to go through the approval process, and currently the banking association only plans to have a one-time exam, which will happen in the 3Q of the fiscal year.

So, if you take away the RMB24 million of the 1Q 2011, comparing apples to apples it should be actually only about RMB61 million, compared to the 1Q 2012 fiscal number I just gave, this RMB64 million to RMB68 million.

So in terms of the bottom line, we predict the net income for the 1 half will probably breakeven, or in a loss position of about US\$100,000, versus 1 half 2011 about US\$90 thousand loss. And we expect the fiscal 2 half 2012 will be very solid, we expect probably the remaining 2/3 of the revenue will generate positive net income for both quarters.

Hopefully that gives you enough color of our budget in our fiscal year 2012, Mark.

Mark Marostica:

I was going to say, as a lot of analysts, Benson, I will speak for the crew of analysts it is never enough, right? Let me dive into the 1 half: could you give us a sense of 1Q versus 2Q on the profitability side? You gave us a sense of revenue of 1Q, and I curious if you could make any comments as to how profitability looks like in 1Q.

Benson Tsang:

1Q will probably be in a loss position, probably in the range of US\$100,000. So we expect 2Q probably in the range of breakeven.

Mark Marostica:

Got it.

Benson Tsang:

I just want to add one more comment on our 1Q: out of the RMB64 million to RMB68 million of net revenue, already in our pocket is RMB58 million. So, we feel pretty comfortable about our 1Q figure.

Mark Marostica:

OK. I will ask one more question, and I will turn it over, so I do not use up the whole queue, and that is relative to your full-year guidance of revenue. How much of that is already contracted, or backlog, if you will, very visible revenue? Thank you.

Benson Tsang:

Based on our estimate, probably in the range of 55% on a full-year basis.

Mark Marostica:

OK. Thanks, Benson. I will turn it over.

Ella Ji, Oppenheimer:

Thank you. Good evening, Kevin, Walter, and Benson. Congratulations on very strong results. I just wanted to follow up with the prior question. Benson provided guidance for HR Select and TOEIC rose both above 50% revenue growth.

I am just wondering, did you factor in maybe new accounts that you hope to get in the next year, or are those growths purely from the existing accounts?

Benson Tsang:

It will be both.

Ella Ji:

And could you share some color in terms of how many new accounts you expect to get for both tests?

Benson Tsang:

For the HR Select revenue, we expect 60% to 70% will be from existing clients, and 30% to 40% will be from new clients.

Ella Ji:

OK. Thank you. And also, I am just wondering if your guidance has included any potential revenue from the Security Guard or Internet Cafe?

Benson Tsang:

Yes. Included in our revenue, we included about RMB50 million to RMB55 million from our Security Guard program.

Ella Ji:

And which quarter is that in?

Benson Tsang:

We expect the revenue will come and start in the 3Q and also in the 4Q.

Ella Ji:

In the 3Q and 4Q. OK. How about Internet Cafe?

Benson Tsang:

Internet Cafe, we signed a contract with the Ministry of Culture, and we are doing the preparation work. We expect to start testing services in the end of the 2Q or early 3Q. But as I shared in previous quarters, we do not expect the contribution will be significant, but the true meaning to us is the continuous relationship with the Ministry of Culture, which we can build other cooperation opportunities.

In terms of the revenue contribution in my budget, we expect to have about RMB1 million to RMB2 million from this test title.

Ella Ji:

Got it. And switching gears to the margin, so your next year's guidance suggests about 10.8% of net income margin. I am just wondering what would be the long-term margin level that you think ATA can achieve, as you continue growing the business, just a rough end of the margin level, that would be helpful.

Benson Tsang:

Sure, Ella. As I shared with you before, ATA has a very unique business model, it is very scalable, and we have proved this scalability in our 3QFY2011.

As we go forward, as we scale our business, more revenue coming in and we can control our fixed cost, we expect the net margin will continue to improve. And I have to be honest with you. At the moment, we do not know the limits. We are quite confident that on an annual basis we will continue to see improvement not only on the gross margin, we expect a better improvement on our net margin.

Ella Ji:

OK, great. And lastly, regarding your use of cash, in addition to the dividend, could you also elaborate what type of CAPEX or gross spending you plan for the next year?

Benson Tsang:

In our current budget we have a CAPEX of about US\$1 million. And as usual, the CAPEX we have is mainly buying more servers, maintenance CAPEX, and also buying some new computers.

We do not have any major CAPEX plan at the moment, but as we move down towards the end of the year or towards the middle of the year, if we do have any new business plan, we will definitely share with the street.

Ella Ji:

Great. Those were all my questions. Thank you.

Operator:

Thank you, ladies and gentlemen. There are no further questions from the floor. I will now pass the call over to Mr. Kevin Ma for closing comments. Mr. Ma, please begin.

Kevin Ma:

Thanks again to all of you for joining us today. We look forward to speaking with you again after we report our 1Q financial results. As always, we welcome any visitors to our offices in Beijing. Thank you.

Operator:

Thank you, ladies and gentlemen. Thank you for your participation in ATA's conference. There will be a webcast replay within an hour. Please visit ir.ata.net.cn. You may disconnect now. Goodbye.

"This document is a transcript produced by MZ. MZ uses its best efforts to guarantee the quality (current, accurate and complete) of the transcript. However, it is not responsible for possible flaws, as outputs depend on the quality of the audio and on the clarity of speech of participants. Therefore, MZ is not responsible or liable, contingent or otherwise, for any injury or damages, arising in connection with the use, access, security, maintenance, distribution or transmission of this transcript. This document is a simple transcript and does not reflect any investment opinion of MZ. The entire content of this document is sole and total responsibility of the company hosting this event, which was transcribed by MZ. Please, refer to the company's investor relations (and/or institutional) website for further specific and important terms and conditions related to the usage of this transcript."