

ATA

TRANSCRIPT

ATA Inc.
August 5th, 2011
Q1 Fiscal Year 2012 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

Ella Ji

Oppenheimer

Mark Marostica

Piper Jaffray

Operator:

Welcome everyone to 1QFY12 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 now 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, you may begin.

Adam Prior:

Thank you and good morning, everyone. Thank you for joining us. Copies of the press release announcing the fiscal 1Q12 results are available at the IR Section of ATA'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 USD amounts in this conference call, relating to the Company's most recent financial results, are converted from RMB using an exchange rate of RMB6.4635:US\$1. All historical conversions are accurate as of the time reported, unless otherwise noted. The Company reports its financial results under US 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 agenda and overview of the Company on slide three.

The Company's President, Mr. Walter Wang, will open with an operational overview, beginning on slide four. The Company's CFO, Mr. Benson Tsang, will discuss the financials, and the Company's Chairman and CEO, Mr. Kevin Ma, will then provide closing remarks.

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

Walter Wang:

Thank you, Adam, and hello everyone. ATA continued to make progress in its operations throughout the quarter, as we saw growth in HR Select and TOEIC, achieved margin expansion, and reported a healthy profit. As Chairman Ma will discuss later, we have a strong financial position and are comfortable re-confirming our financial guidance for the 2012 fiscal year.

As we noted in our earnings call in June, the 1Q12 was affected by the rescheduling of the exam for the China Banking Association, or CBA. The exam is now expected to take place in our fiscal 3Q, or the period ending December 31st, 2011. Later in the call, Benson will discuss the impact of this rescheduling.

During the quarter, we delivered 1.8 million billable tests, approximately the same from the prior-year period despite the rescheduling of CBA. This is largely due to expansion in our HR Select and TOEIC services, along with general growth in other segments of our business.

Please turn to slide five, where we outline a few of our operating highlights. For those of you who have interest, we provide regular updates on these types of events on our website, and you can subscribe to them via RSS feed as well.

A recent example of our success occurred in June, where over the course of one weekend, ATA delivered approximately 788,000 qualification tests for the Securities Association of China, which is reported as revenue in the Company's 1Q and is a 20% increase from the Company's

March 2011 record of administering 655,000 exams in a single weekend. This is the highest total number of tests ATA has administered in any given weekend over the Company's history.

We are often asked how high this number can go. This is, of course, based on the demand from our clients. We are always continuing to expand our service offerings and testing capabilities, and we currently have a daily capacity of potentially delivering one million tests. We believe that demand is growing, and ATA is trying to stay ahead of it.

On slide six, this map illustrates our nationwide network of over 2,000 test centers that we have developed since our inception in 1999. These centers typically take 3 to 6 months to develop to ATA's standard, which includes preparing the necessary facilities and manpower. We are not aware of any comparable size network in China.

Overall, our operations continue to expand. 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 candidates. We delivered a total of 6.9 million billable tests during fiscal 2011. This database of test takers is a resource from which ATA can draw for future growth. We expect to continue our proactive sales and marketing efforts, via campus visits and also marketing to specific sectors of candidates.

With that, I would like to turn it over to Benson for a review of the financials.

Benson Tsang:

Thank you, Walter. We are pleased with our operating results for the quarter, where we improved all of our bottom line metrics, both in terms of margin percentage and incomes, and remain focused on cash generation and stable growth.

On slide eight, we show in USD that ATA once again exceeded the market's consensus estimates, which it has done for the past five quarters, in terms of net revenues, gross profit, net income, and diluted earnings per ADS. We continue to budget carefully, and while we do not focus on beating the estimates from the street, we are always vigilant as to what our covering analysts provide to all of you for reference.

On the next slide you will see a breakdown of the Company's financial results for the quarter. Gross profit for the 1Q12 increased 2.6% to RMB45 million, approximately US\$7 million, from RMB43.8 million in the same period last year. Gross margin increased to 58% in the 1Q12 from approximately 52% in the prior-year period, primarily due to a price increase for the Securities Exam and higher-margin test preparation revenue.

The Company reported income from operations in the 1Q12 of RMB14.2 million, approximately US\$2.2 million, compared to RMB11.2 million in the prior-year period. This increase was primarily due to lower operating expenses resulting from our efforts since the 4Q11 to improve productivity and cost efficiency.

The Company reported net income of RMB13 million, or US\$2 million, compared to net income of RMB9 million in the prior-year period. Basic and diluted earnings per ADS were RMB0.58 and RMB0.56 respectively, compared to earnings of RMB0.40 in the prior-year period.

On slide ten, we provide more detailed information about our revenues, both by year and by quarter. As Walter and I noted earlier, the quarter was somewhat affected by the rescheduling of the China Banking Association exam. Last year, we successfully administered 0.5 million exams amounting to about RMB24.5 million for the China Banking Association.

Despite this scheduling change, we greatly increased our volume on other billable tests. During the quarter, we delivered 1.8 million billable tests. If you exclude CBA exams from last year's total, that is an increase of about 40% compared to the prior-year period.

As the chart on the right illustrates, fiscal 3Q, which runs from October to December, is typically our strongest, while fiscal 4Q, which runs from January to March, is typically a weaker quarter. 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 and TOEIC, while still a relatively small portion of our revenue, will help to offset the inherent lumpiness of our business from quarter to quarter.

In the next slide we outline the quarter by our business segments. Our business can be broken down broadly into two areas, testing services and online test preparation. At about 86%, our core segment of testing services was once again a high percentage of our total revenue in the 1Q12. This includes specific types of exams ranging from professional certification exams in various industries, such as securities and futures, 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 for English language education. This is where we package our testing services together with comprehensive training content, and an online delivery platform. We charge these testing-related services generally on a per-head-delivered basis.

We often have questions about fluctuations in our pricing on a per test-taker basis and whether we are seeing any trends in that regard. Our pricing varies for each client, and like our test scheduling, it is difficult to identify trends from quarter to quarter. That being said, it is fair to note

that a number of the marketing initiatives and lower margin tests that we delivered over the past two years have slowly been supplemented by tests with more standard pricing. As a result we have, and are hopeful for, continued margin expansion.

We continue to be supported by strong free cash flow and a solid balance sheet, which we have highlighted on slide 12. Cash generated from operating activities in the 1Q12 was RMB18.2 million, about US\$2.8 million. As of June 30th, 2011, we had over US\$44 million in cash and no long-term debt. We also do not have any short-term borrowings.

We believe that 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.

Some of you may have seen the announcement of a special dividend we made in June. The total amount of cash distributed in the dividend was approximately USD\$9.8 million, paid on August 1st, 2011. The Company reported this figure as a dividend payable on our balance sheet ended June 30th, 2011, of approximately RMB63.6 million.

The amount per ADS delivered to our shareholders was about USD\$0.40. We feel that this dividend speaks to our Company's ability to produce free cash flow, thereby allowing us to return capital to our loyal shareholders.

Before I turn it over to Kevin for closing remarks and an outlook for the year, I would like to provide some projections for the 2Q of our current fiscal year. As we noted in the last call, we expect during the 1H12 that ATA will achieve about a third of our revenue guidance, which should be in the range of RMB130 million to RMB140 million.

We expect, based on existing exam schedules, 2Q revenues will be in the range of RMB57 million to RMB62 million. We also expect continued net margin expansion. The 2H12 will be strong, with approximately two-thirds of our guidance being achieved in the last two quarters.

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

Kevin Ma:

Thank you, Benson. As we noted in the last call, over the last two years, we feel that we have successfully built a foundation for growth. Our business is inherently scalable. We feel that we have an advantage in that ATA is so far ahead of any potential competitor in terms of history, capability, and perhaps most important, security.

Further, we are flexible and well capitalized. A quarterly fluctuation, such as the rescheduling of the CBA exam, does not affect our budgeting or operations in any way on an annual basis. While we understand that these changes from quarter to quarter make it difficult for investors to readjust their models, we feel it is a decided advantage for us.

We also expect to begin realizing benefits from the investments made during fiscal year 2011 in designing and implementing new, large-scale tests, such as the nationwide security guard certification exam. Our company is generating positive cash flow and is well positioned to continue healthy, organic growth.

On that note, we are re-confirming our annual guidance for fiscal 2012, shown on slide 15. We expect revenues to be between RMB395 million and RMB415 million. And net income of between RMB40 million and RMB45 million. We believe we can achieve the high end of the net income range.

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.

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

Ella Ji, Oppenheimer:

Thanks. Good morning and congratulations on a very strong quarter. Benson, I heard you said in terms of the 2Q revenue guidance, I heard you say the high end is RMB67 million, but it is RMB62 million on the press release. I just want to clarify on that.

Benson Tsang:

Ella, the range is RMB57 million to RMB62 million.

Ella Ji:

OK. Yes. And I noticed you are now comfortable with the high end of your net income guidance range, but given that you already achieved RMB13 million net income in the 1Q, I am just wondering, are you just being conservative or is there anything we should be aware in the remaining of the year that may, you know, pressure your net income?

Benson Tsang:

It is correct. Based on the current forecast, we expect in the 1H we will probably finish in the range of RMB13 million to RMB15 million net income. We also foresee for the 2H, 3Q and 4Q combined, as a minimum we will be able to achieve RMB30 million, combining the 3Q and 4Q.

What we do not see right now is a strong, good visibility of some of the new projects, in particular it is Security Guard program. As I shared in the past, we are following our time schedule; we wanted to start confirming commercial contracts with selected provinces or cities so we can start the examination in the 3Q.

So, unfortunately, at the moment we still do not have a very strong visibility of the timing of the exam that we will start delivering, but we are confident that for the Security Guard exam, we will be able to commence in the 3Q.

So, as we are doing the 2Q earning call probably in November, we will have a much better visibility to share to the street.

Ella Ji:

I see. So you are still expecting the Security Guard will start in the 3Q, but you just relatively speaking, have a low visibility in terms of how much revenue that will bring to you. Is it fair to say that?

Benson Tsang:

This is correct.

Ella Ji:

OK, great. The SAC test had a price increase this year again, I think it is the second this year already. So, do you think they will continue to raise prices each year? Meaning, is that going to be a recurring benefit for you?

Benson Tsang:

First of all, this year we managed to again another price increase as a direct result of SAC. They see the partnership with us, and we can actually make contributions to them to improve the SAC image and also increase the number of exam takers.

Going forward, our ability to raise the price will depend on the value we can bring to the table. So, we surely hope that we can continue to do so. It is a bit too early for me to say this will continue, but I strongly believe that ATA can continue to bring value not just to SAC. If we can demonstrate our value to other clients, we believe ATA will be in a strong position to raise the price.

Ella Ji:

OK. And then, moving on to the margins, you achieved a very impressive margin expansion in this quarter, in particular in the gross margin area. So, would you provide us some color in terms of margin outlook for the remainder of the year and also in the long term?

Benson Tsang:

OK. Yes, this quarter we achieved a very healthy gross margin increase. But allow me to remind the reasons for the increase. The first one is due to the price increase of SAC, it is a one-time hit of about RMB2.7 million, and this actually helped us the margin is about 3.5% in the 1Q.

The other reason for the improvement of the margin is a mix of revenue mix and also the efficiency we gained from the volume increase, on the number of tests we delivered to our clients.

Going forward, we strongly believe that the economies of scale on the number of tests we deliver to our clients will continue, and we expect the margin, as I communicated before, in the last earning call, we expect a minimum improvement on a quarter-on-quarter basis to be 1%, and we believe we can achieve a minimum improvement of 2%. So, on an annual basis, we believe the margin improvement will probably be in the range of 2 to 3%, due to the latest developments and what happened in the 1Q.

Ella Ji:

Great. And lastly, I am wondering if you can share some colors in terms of are there any other new tests in the pipeline that you are currently working on?

Benson Tsang:

Yes, Ella. We definitely have a few projects going on at the moment, but due to commercial reasons, we are not able to disclose the name. But I am happy to tell you we actually concluded a couple of new contracts, and those contracts will happen in the 3Q.

In fact, in our 3Q backlog we already included about RMB9 million of new contracts, but please bear with me, I cannot disclose the name of the client at the moment. But that RMB9 million is a confirmed backlog in my 3Q.

There are other customers we are following at the moment, and we are quite optimistic we will be able to close a few of them.

Ella Ji:

OK, great. Congratulations again, I will get back to the queue.

Mark Marostica, Piper Jaffray:

Yes, thank you for taking my question. I just want to start up with the question on HR Select: you have seen some nice traction this quarter and some nice growth in HR Select. Can you give us an update as to the revenue concentration you have in HR Select among customers?

Benson Tsang:

Sure. HR Select, right now in the 1Q, the majority of the revenues are coming from two sectors. The first sector is the banking sector, and the second sector is basically the IT-related sector, in particular from a major client, Huawei. We completed the contract from them in the 1Q totaling RMB2.5 million.

And for these clients, the banking clients and Huawei, we expect we will continue to get revenues from them in the remaining three quarters, but the size of the contracts may vary, depending on the demand and needs of our clients.

And overall, for HR Select we achieved over about 100% growth on a quarter-on-quarter basis comparing to last year, and on a full-year basis, we feel quite confident we can achieve the minimum 50% growth we communicated in last quarter.

Operator:

Now, I would like to pass it back to Kevin Ma, the Chairman. Please, begin.

Kevin Ma:

Thanks again to all of you for joining us. We look forward to speaking with you again after we report our 2Q financial results. As always, we welcome any visitors to our office in Beijing. Thank you.

Operator:

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 now disconnect. Good-bye.

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