

# FINAL TRANSCRIPT

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## CA - Q1 2011 CA. Earnings Conference Call

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## CORPORATE PARTICIPANTS

**Kelsey Doherty**

CA. - SVP of IR

**Bill McCracken**

CA. - Chairman, CEO

**Nancy Cooper**

CA. - CFO, EVP

**George Fischer**

CA. - EVP, Group Executive - Worldwide Sales and Operations

**David Dobson**

CA. - EVP, Group Executive - Customer Solutions Group

## CONFERENCE CALL PARTICIPANTS

**Todd Raker**

Deutsche Bank - Analyst

**Michael Turits**

Raymond James - Analyst

**Greg Moskowitz**

Cowen and Company - Analyst

**Kirk Materne**

Rafferty Capital Markets - Analyst

**John DiFucci**

JPMorgan - Analyst

**Matt Hedberg**

RBC Capital Markets - Analyst

**Phil Winslow**

Credit Suisse - Analyst

**Katherine Egbert**

Jefferies & Co. - Analyst

**Gonzalo Cavenaghi**

Goldman Sachs - Analyst

**Israel Hernandez**

Barclays Capital - Analyst

## PRESENTATION

**Operator**

Good day, everyone, and welcome to the CA Technologies' first quarter 2011 earnings conference call. Today's call is being recorded. At this time, I would like to turn the call over to Kelsey Doherty, Senior Vice President of Investor Relations. Please go ahead, ma'am.

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**Kelsey Doherty** - CA. - *SVP of IR*

Thank you and good afternoon, everyone. Welcome to CA Technologies' first quarter fiscal 2011 earnings call. Joining me today are Bill McCracken, our Chief Executive Officer, and Nancy Cooper, our Chief Financial Officer. Also on the call and available to answer question are David Dobson, our new Executive Vice President and Group Executive Customer Solutions Group, and George Fischer, Executive Vice President and Group Executive, Worldwide Sales and Operations. Bill will open the call with an overview of the quarter. Then, Nancy will review our first quarter results and update full-year guidance. Bill will return with a discussion of his operational priorities, and we will then take your questions.

As a reminder, this conference call is being broadcast on Wednesday, July 21, 2010, over the telephone and the Internet. The information shared in this call is effective as of today's date and will not be updated. All content is the property of CA Technologies and is protected by US and international copyright law and may not be reproduced or transcribed in any way without the express written consent of CA Technologies. We consider your continued participation in this call as consent to our recording.

During this call, non-GAAP financial measures will be discussed. Please note as we told you on the last earnings call, all non-GAAP operating measures will be reported excluding shared-based compensation expense on an ongoing basis. Prior period non-GAAP metrics also reflect this change for comparative purposes. Reconciliations to the most directly comparable GAAP financial metrics are included in the earnings release which was filed on Form 8-K earlier today as well as in our supplemental earnings materials, all of which were available on our website at [Investor.CA.com](http://Investor.CA.com).

Today's discussion will include forward-looking statements subject to risks and uncertainties, and actual results could differ materially from these forward-looking statements. Please refer to our SEC filings for a detailed discussion of potential risks. So with that, let me turn the call over to Bill.

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**Bill McCracken** - CA. - *Chairman, CEO*

Thanks, Kelsey, and good afternoon, everyone. Thank you for joining us. June 30 marked the end of my first full quarter as CEO of CA Technologies. And I am pleased that we met our revenue, operating margin, earnings per share, and cash flow plan for the quarter. During the quarter, we focused on execution to unlock value, accelerate growth, and establish our Company as the industry leader in IT management, and security for virtualization and cloud. We also continued to invest in our core strengths in managing and securing mainframe and distributed environments. We are making progress, and we believe we will meet our updated financial expectations for the full year. During the first quarter, we realigned our organization to make our business more even more customer-centric and focused, brought in new senior talent to complement our management team, divested non-strategic IT governance products from the portfolio, started the process of rebranding the Company, began realizing value from our newly acquired technologies, and announced more than 20 new products to more than 5,000 customers and attendees at our successful user conference, CA World.

From a financial perspective, revenue grew 3% in constant currency, which is right where we thought we would be. Operating margins were down as expected. This was the result of expenses related to CA World and acquisitions closed last fiscal year. Non-GAAP EPS was down 1% in constant currency, and finally, cash flow was in line with our expectations, although down for the quarter. This was primarily the result of a decrease in upfront, single installment payments. We achieved these results even though our renewal portfolio was approximately half of what it was last year. Renewal yields were in the low 90% range. These results, combined with continued growth in the current portion of the revenue backlog on a constant currency basis, are why we are confident in our full-year outlook. However, we also realize there is more we can do, especially when we look at new product sales performance during the quarter.

We saw growth in the dollar value of stand-alone sales of new products, meaning sales not attached to a renewal. Year-over-year, stand-alone sales were up more than 30% and contributed to the more than 50% cost of currency growth in our software fees and other revenue line. This quarter, stand-alone deals improved upfront revenue and underscored the value of our product portfolio. However, improvements in stand-alone sales were not enough to offset the negative impact the lighter inventory

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renewals had on our ability to drive new product sales. Quarters with lighter renewal inventories generally result in lower new product sales as renewals are an important opportunity to sell new products. As a result, new product sales, excluding mainframe capacity, were down mid-teens, year-over-year. At the same time, stand-alone sales, which typically feature shorter contract lengths, in combination with a lighter renewable portfolio, contributed to a significant decrease in average contract duration. During the quarter, our average contract length was 2.9 years, the lowest it has been in more than 12 quarters and down from 4.2 in the prior year period. This change in duration is reflective of customer preferences, but is also influenced by our renewal portfolio causing duration to fluctuate quarter to quarter. Adjusting for the change in average duration, first quarter new product sales excluding capacity were up high single digits on an annualized revenue basis and helped drive growth in our current revenue backlog.

While we are encouraged by the underlying fundamentals of the business this quarter, we are focused on ways to improve free-standing sales, help customers in new and emerging growth markets, and become an even more strategic partner to our customers. We believe that by focusing on these key areas, we will further improve execution and accelerate new product sales. With that, let me turn the call over to Nancy to talk further about our results and our updated outlook. Nancy?

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**Nancy Cooper** - CA. - CFO, EVP

Thank you, Bill. To start with, please note that all growth rates are year-over-year unless otherwise indicated. Now to the quarter. As Bill said, we saw constant currency growth in our total revenue backlog, and even more encouraging in the current portion of this backlog, despite a decline in new product sales. Let me explain. Total new product sales tell only a part of the story this quarter. To fully understand the impact of new product sales on backlog and future revenues, we also look at the contract duration of the new product sales in each period. Adjusting for this difference in duration, on an annualized revenue basis, new product sales excluding capacity were up high single digits. This explains why our current revenue backlog grew during the quarter.

Current revenue backlog is an important leading indicator of future revenue, and a reason we are confident in our full-year revenue expectations. Total revenue backlog at the end of the quarter was \$7.7 billion, up 2% in constant currency and flat as reported. The current portion of backlog grew 4% on a constant currency and 2% on an as-reported basis. Current revenue backlog growth was driven by new distributed software sales of service assurance where we believe we have the most complete and compelling stack in the industry.

NetQoS grew new sales by more than 40% in the quarter. We also saw growth in project and portfolio management where customers believe our solutions are best in class. This was offset by declines in virtualization and service automation and identity and access management. We announced availability of five new virtualization management products at the end of the first quarter, which have yet to contribute to our results. And we are in the process of rebuilding our pipeline in identity and access management, which delivered sequential quarters of record performance in the back half of fiscal 2010. Sales of new mainframe products, as well as capacity, were down year-over-year. Mainframe sales correlate to the underlying renewal portfolio, which, as you know, was lighter this quarter. We anticipate that mainframe new product sales and capacity will accelerate in the back half of the year, driven by a more robust portfolio of renewals.

Total revenue for the quarter was \$1.09 billion and grew 3% in constant currency and 5% as reported. This include a favorable foreign exchange impact of approximately \$15 million. We did see a slight sequential decline in total revenue from the fourth quarter, which is attributable to currency. 2% of our revenue growth in constant currency was from products, primarily acquisitions and 1% from services. Subscription and maintenance revenue was \$961 million, up 1% in constant currency, and 2% as reported. Revenue from software fees and other was \$52 million, up 51% in constant currency and 58% as reported. This reflects contributions from NetQoS and CA Wiley. Revenue from professional services was \$78 million, up 11% in both constant currency and as reported. This quarter, we focused on completing services projects. However, we did see a deceleration in new services engagements, which was a function of the underlying business.



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Now, I would like to turn to the remainder of the income statement, starting with our non-GAAP results. Operating expenses were \$724 million, up 8% on a constant currency basis and 10% as reported. This included costs associated with CA World and from acquisitions that closed in fiscal year 2010. These incremental expenses are reflected in almost every expense line item. Operating income before interest and taxes was \$367 million, down 6% on a constant currency basis and 5% as reported. For the quarter, our non-GAAP operating margin was 34%, a decrease of 3 percentage points reflecting previously discussed investments in CA World and accusation dilution. Non-GAAP earnings per share from continuing operations was \$0.45, down 1% in constant currency and flat as reported. Our non-GAAP tax rate for the quarter was 33.5%.

Turning to GAAP results, GAAP operating margin was 30%, compared to 31% in the first quarter of last year. GAAP operating income from continuing operations was \$324 million, down 8% in constant currency and flat as reported. While earnings per diluted common share from continuing operations was \$0.43, up 7% in constant currency and 16% as reported. Our effective GAAP tax rate for the first quarter was 28.3%.

Cash flow from operations in the quarter was \$117 million, compared to \$262 million in the first quarter of fiscal 2010. First quarter cash flow from operations was affected by a year-over-year decrease in single installment payments, which were \$90 million in the first quarter of fiscal 2011 compared to \$164 million in the prior year period. In addition, cash flow was affected by the year-over-year increase in expenses. Cash flow varies quarter to quarter, and we remain comfortable with our full-year 2011 expectations. Total billing backlog of \$4.5 billion was up 7% in constant currency and 4% as reported. DSOs were up, but we are confident they will return to normal.

Looking at our balance sheet, CA ended the quarter with approximately \$2.5 billion in cash and cash equivalents and \$1.6 billion of total debt, bringing our net cash position to approximately \$918 million. Between the middle of May when our newly authorized \$500 million repurchase program was announced and June 30, we purchased approximately two million shares of stock for a total of \$40 million. Between July first and July 20, we repurchased an additional one million shares for \$20 million. This leaves approximately \$440 million in remaining approval on the new program, and we continue to be in the market.

With that, I would like to reaffirm guidance for revenue, operating margin, and cash flow, and increase our GAAP and non-GAAP earnings per share outlook for fiscal year 2011. We continue to provide guidance for growth rates on a constant currency basis, which we believe best illustrates the operational performance of the Company. With the exception of earnings per share, changes in the dollar amount of the ranges reflect currency fluctuation only as we have not changed our expectations regarding growth rates from guidance given in May. In addition, guidance presented this afternoon includes approximately \$0.06 of dilution in earnings per share from the acquisitions closed during fiscal year 2010. As a reminder, it has been our practice to provide guidance based on June 30, exchange rates, which include a partial hedge of operating income.

Guidance is as follows. Total revenue growth is expected to be in the range of 3% to 5% in constant currency. At June 30 exchange rates, this translates to reported revenue of \$4.4 billion to \$4.5 billion. The range on non-GAAP operating margin is expected to be 34% to 35%, which is flat to up 1 percentage points from fiscal year 2010. We expect our GAAP and non-GAAP tax rate to range between 33% and 34% in this fiscal year, flat to 1 point improvement over fiscal year 2010. Growth in non-GAAP diluted earnings per share from continuing operations is expected to be in the range of 7% to 14% in constant currency. This reflects a 2 point or \$0.03 increase to the top end of the range provided in May. At June 30 exchange rates, this translates to reported non-GAAP diluted earnings per share from continuing operations of \$1.82 to \$1.94. Growth in GAAP diluted earnings per share from continuing operations is expected to be in the range of 5% to 13% in constant currency. This reflects a 2 point, or \$0.03, increase to the top end of the range provided in May. At June 30 exchange rates, this translates to reported GAAP diluted earnings per share from continuing operations of \$1.51 to \$1.63. And cash flow from operations is expected to grow at 2% to 7% in constant currency. At June 30 exchange rates, this translates to reported cash flow from operations of \$1.38 billion to \$1.45 billion. This includes approximately \$50 million in restructuring cash payments where the expense was incurred in the fourth quarter of last year. These payments will reduce cash flow by 3% and is one of the reasons why our non-GAAP earnings per share and cash flow from operations growth differ in fiscal 2011.



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For the full year, we expect approximately 510 million actual shares outstanding and a weighted average diluted share count of approximately 511 million shares. This does not include the effect of any future stock repurchases. Guidance does not include the effect of any future material acquisitions.

Before I turn the call back to Bill, I would like to provide additional color on the remainder of the year and the second quarter. As we have said, our full-year renewal portfolio is approximately 10% lighter as compared to the inventory of renewals in fiscal year 2010. It is also weighted toward the back half of the year. Specific to the second quarter, our inventory of renewals is approximately 0.75 of last year. Due to the correlation between renewals and cash, we would expect cash flow to be stronger in the second half of this year. We understand that currencies continue to fluctuate, so I will provide some additional color on CA Technologies' currency exposure.

We hedge approximately 80% of our forecasted cash flows for six currencies. The euro being the largest component. This results in a partial hedge of approximately one third of our operating income. Therefore, as a rule of thumb, a \$0.03 decrease in the euro affects our revenue by \$12 million and our EPS by approximately \$0.01 for the remainder of the fiscal year. Using June 30 exchange rates, our quarterly revenue is negatively impacted by about \$30 million when compared to original guidance. With that, I will turn the call over to Bill to conclude. Bill?

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**Bill McCracken** - CA. - *Chairman, CEO*

Thank you, Nancy. I have spent a lot of time talking to customers over the past three months, and as a result, I am even more confident in our long-term direction. At CA World, I saw first-hand the reaction of our customers to the direction we are taking the Company and the products that are backing up that strategy. With our strategy clearly defined, we now have one focus -- execution. Operationally, our priorities are -- increasing the number of freestanding sales with new products and getting them in the hands of our customers. Responding to customer demand in growth geographies and growth accounts and continuing to align the organization to be more responsive to customer needs and emerging trends. Specifically, we will grow freestanding sales with new products by -- driving sales for the new products we introduced at CA World in May, adding new sales leadership and new quota-bearing salespeople, and developing and delivering new services offerings.

Second, we see demand outside our current markets and are building our global emerging markets business. Our approach includes a channel and partner strategy. We recognize that these markets will purchase and consume technology differently than our traditional customer base. This is why we purchased Nimsoft with more than 300 MSP partners and continue to invest in our software as a service capabilities. While these initiatives will take a few quarters to show meaningful growth, we expect most of the heavy lifting and investment, which is already built into our plan, to be complete this year and results to start to show in fiscal year 2012.

Third, we are continuing to realign the organization beyond our strategy, creating a new customer solutions group or CSG, led by David Dobson and designed to move CA Technologies from a product-centric approach to one driven by needs of customers. We are now focused on market position and improving share through leveraging our portfolio and expertise. This year is about execution. You will see immediate impact in some areas, and in others, it will take some time. But it is about realizing our potential, unlocking our value, and growing CA Technologies. We know clearly what we have to do. And we are doing it. So with that, I will turn it back to Kelsey, and we look forward to your questions.

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**Kelsey Doherty** - CA. - *SVP of IR*

Thank you, Bill. As the operator is polling for questions, I would like to inform you that CA Technologies is presenting at the 12, Annual Pacific Crest Technology Leadership Forum, on August 9 in Vail, Colorado, the Oppenheimer Annual Technology, Media, and Telecommunications Conference on August 11, in Boston, the 2010 Citi Global Technology Conference on September seventh in New York City, and the Deutsche Bank 2010 Technology Conference on September 14, in San Francisco. In addition, we will be hosting virtualization events with Deutsche Bank on August 12, in Boston and in New York City. Please contact CA

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Technologies' Investor Relations if you are interested in attending. In the interest of time, please limit yourself to two questions. Operator, please open the call for questions.

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## QUESTIONS AND ANSWERS

### Operator

Thank you. (Operator Instructions) We will go to our first question from Todd Raker with Deutsche Bank.

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### Todd Raker - Deutsche Bank - Analyst

Hello. Just diving into the new products, and you highlighted virtualization, identity management and authentication as being down. Clearly, there was an impact in terms of contract length. But two questions for you. One, you talked about rebuilding the pipeline in identity management. Can you give us a little bit more insight in terms of what happened there in the dynamic? And then as you look at some of the emerging opportunities around virtualization and automation, where do you think you stand in terms of market share? Is the market just not really kicked in here? Or is it that you don't have production-ready products into the market yet -- and the road maps there, but the products aren't there yet? Thanks.

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### Bill McCracken - CA. - Chairman, CEO

Thanks, Todd. I am going to have George answer most of that question.

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### George Fischer - CA. - EVP, Group Executive - Worldwide Sales and Operations

Sure. Hi, Todd. We're coming off two very strong quarters with IAM across the globe. We had great results for IAM. We continue to see great competitive wins, and we announced quite a few products and vision at CA World. So we are getting good growth on that. We don't think that's an issue, and that's just a continuing process.

In addition, across the pipeline, the new virtualization products that we announced at CA World are growing, and as you know, virtualization management continues to be in high demand. On the mainframe side, too, you see with -- as our renewal portfolio gets very much stronger in the second half of the year, we continue to see a growth in the pipeline for the mainframe products, also. And we announced a series of new products at CA World there, and as you know, coming soon is the new [z] platform. So there is some excitement around pipeline there also. So we're confident on the security piece because as you also know, there's a consistent demand for security and service assurance for anyone that's moving to the Cloud.

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### Bill McCracken - CA. - Chairman, CEO

Todd, you really hit it on the second part of what you said. We announced those five new products at CA World. That was the back end of the quarter so the GA really in most cases rolled into this quarter. We'll see that build over the next quarters. We'll see some this quarter. But over the third and fourth quarters of this year, we should see that kick in.

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### Kelsey Doherty - CA. - SVP of IR

Do you have another question?



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**Todd Raker** - Deutsche Bank - Analyst

Yes. Just on the stock buyback front, Nancy. Is there anything that prevents you from accelerating from your current pace -- whether it be cash sitting overseas versus the US? Or clearly, you're buying more back, but is there anything that prevents you from accelerating the rate at which you're buying back?

**Nancy Cooper** - CA. - CFO, EVP

No. We have 46% of our cash in the US, and you can see with \$2.5 billion of cash, we have lots of liquidity.

**Todd Raker** - Deutsche Bank - Analyst

Okay. Thanks.

**Nancy Cooper** - CA. - CFO, EVP

Thank you.

**Operator**

We'll go to our next question from Michael Turits with Raymond James.

**Michael Turits** - Raymond James - Analyst

Hello. Obviously, this question of the renewal portfolio is important both because it shows up in how much bookings, but now you've been stressing that it pulls in a lot of additional new product sales. Are we -- is this the trough -- is this the low point in that portfolio? Both, let's say, over the last couple of years, and then over the next year or two?

**Nancy Cooper** - CA. - CFO, EVP

Sure, Michael. It is the lowest quarter we've had in the last 12 quarters. I did indicate on the call that second quarter will be 75% of last year. But then our renewal portfolio grows in the second half of the year by over double digits. So what we have got here is a low first half and a much better second half.

**Michael Turits** - Raymond James - Analyst

Okay. And then, another question. Subscription revenues were up just 1% constant currency. They were up 2% constant currency last quarter, and they had been up around 4% in prior quarters. So it seems as if subscription revenue is decelerating. At the same time, you have had a big pickup in software fees. Is this something systematic? In other words, are you shifting the type of sales from subscription to licensed software fees in a deliberate way?

**Nancy Cooper** - CA. - CFO, EVP

So what you have here -- it is a reflection of the lower renewal inventory. And we mentioned that when you annualize the revenue on new software sales, it's single digit. You can see it showing up in the current portion of our revenue backlog, which grew 4% constant currency. And so what you're seeing the impact of second half of last year from EMEA slowing through subscription. But looking forward, you look at the current portion of the revenue backlog, and that's up 4%.



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**Bill McCracken** - CA. - *Chairman, CEO*

And Michael, I think the other thing too, is that with on the new product sales, some of that comes in as perpetual as well, too. That has an effect on it, also.

**Kelsey Doherty** - CA. - *SVP of IR*

Great. Next question, please.

**Operator**

Thank you. That will come from Greg Moskowitz with Cowen.

**Greg Moskowitz** - *Cowen and Company - Analyst*

Thank you, and good afternoon. First question is for either Bill or George. Somewhat recently, you brought on new management in Europe, and I believe last quarter you saw the strongest level of new software sales in Europe in two years. Keeping in mind the renewal portfolio and seasonality in Q1, how did Europe perform over the last three months relative to your expectations? And secondly, how are you thinking about Europe over the remainder of fiscal 2011?

**Bill McCracken** - CA. - *Chairman, CEO*

George, why don't you take part of that.

**George Fischer** - CA. - *EVP, Group Executive - Worldwide Sales and Operations*

Sure. Hello, how you doing? As you said, EMEA's portfolio, like the broader portfolio, is lighter the first half. But we had very good results in terms of stand-alone. So as we talked about last time, we made some important changes to management and to sales over there and, in fact as planned, we have been adding sales people -- country managers in UK, France, and Germany. Where we have made those changes, and they have jelled up, we're getting really good progress both on execution and everything that we're talking about builds metrics around stand-alone sales, customer sat, et cetera. We still have a ways to go on that, and we're very confident that it's achieving plan. Despite the challenging economy, we have got great opportunity to grow across EMEA.

**Bill McCracken** - CA. - *Chairman, CEO*

So Greg, I think what George said -- the things he's done are moving forward well, but we do have mixed results coming out of Europe. I think it's been generally talked about with other folks as well, too.

**Greg Moskowitz** - *Cowen and Company - Analyst*

Okay. And then just secondly, how were Nimsoft bookings this past quarter? And can you talk specifically about Nimsoft On Demand? And what you're seeing with MSPs?

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**Bill McCracken** - CA. - *Chairman, CEO*

George?

**George Fischer** - CA. - *EVP, Group Executive - Worldwide Sales and Operations*

Sure. Very solid double-digit growth. They added close to 40 new MSPs, so great acceptance. The product is being well received across the markets. And we continue to see great customer satisfaction and adoption at all sorts of new customers where we typically didn't work with. So customer logo growth and great satisfaction. So that product is beating plan, and we think that's going to continue aggressively.

**Kelsey Doherty** - CA. - *SVP of IR*

Great. Next question, please.

**Operator**

Our next question will come from Kirk Materne with Rafferty Capital Markets.

**Kirk Materne** - *Rafferty Capital Markets - Analyst*

Thank you very much. George, earlier you mentioned that the pipeline for mainframe deals seems to be inching up a little bit, and IBM is obviously launching their next [zSeries], or announcing later this week. Could you just talk a little bit more about what's causing the pipeline to creep up? Is it people taking up [MIPs] in terms of existing contracts that you already have? Is it -- you all believe you are going to take some share? I'm just trying to get a sense on what some of the dynamics are around that? If it's just generally more capacity going in? Or it's something you all might be doing on your own?

**George Fischer** - CA. - *EVP, Group Executive - Worldwide Sales and Operations*

Sure. Hello, Kirk. Well, it's a series of things. One is, as always, we are very comfortable when IBM announces major changes to the platform and creates some excitement in the marketplace. You're seeing that. We don't normally tie that -- those capacity changes because obviously, we have multiyear contracts, et cetera. But it does create some focus, and the price performance level of what IBM is delivering is very, very good.

In terms of pipeline, there's two types of pipeline for us. As Nancy mentioned, the renewal portfolio will continue to expand the inventory through the next few quarters so that drives both capacity and new product. And then at CA World, we announced a series of products. One called Chorus, where it's a whole new way to manage mainframe tool sets. Getting good customer reception. So the number of tools we have available -- the bigger in the platform. And then in addition, we are doing some very specific software replacements and software rationalization. Our services organization has created a software rationalization practice, and we're doing some pretty good size replacements there, taking advantage of vendor consolidation. I think it's across the board, and we're very hopeful that as the renewal portfolio expands, it's going to look very good over the next few quarters.

**Kirk Materne** - *Rafferty Capital Markets - Analyst*

And just one follow-up. Can you all just talk a little bit -- there's been commentary from other companies recently just on the federal procurement cycle getting tighter? Could you just talk about your -- your outlook heading into September? I'm not sure what your expectations were generally, if their fiscal year ends. Could you just talk about maybe your view on that? And how that meshes in with your guidance for the September quarter?

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**George Fischer** - CA. - *EVP, Group Executive - Worldwide Sales and Operations*

Sure, Kirk, I'll take that. I have got -- first of all, we have a global public sector business. So it's not just the US public sector, which is obviously the largest. We have got good response around the world on the public sector business. As you know, those sales cycles can be fairly long, but we're quite used to that and have the appropriate teams for that. We just got probably the largest NetQoS order with a defense agency this quarter that was ever booked. So there is a high demand in the public sector for network management and various infrastructure, and they're catching on to a lot of big projects around virtualization. So it's right in our sweet spot. We expect the next two quarters for public sector to continue to be robust. And, as you know, we have a dedicated public sector organization for both state and local and federal. So we know the ins and outs, and we also have a fairly strong relationship set with the integrators, too. So we're tending also to get into larger projects. Though it's difficult to manage those long sales cycles, it's very good business for us.

**Kelsey Doherty** - CA. - *SVP of IR*

Great. Thanks. Next question, please.

**Operator**

We'll now hear from John DiFucci with JPMorgan.

**Kelsey Doherty** - CA. - *SVP of IR*

John, are you on mute?

**John DiFucci** - *JPMorgan - Analyst*

Hello, can you hear me?

**Kelsey Doherty** - CA. - *SVP of IR*

Yes.

**Bill McCracken** - CA. - *Chairman, CEO*

Yes, we can now.

**John DiFucci** - *JPMorgan - Analyst*

Sorry about that. Bill, you said -- it was mentioned in the press release, and I think implied in your prepared remarks that you are going to continue to make changes at the Company's operations to improve execution and accelerate the sale of new products. Wondering if you could expand a little bit on what are some of the things -- or at least, what are the areas that you expect to make changes in.



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**Bill McCracken** - CA. - *Chairman, CEO*

Yes, I sure can, John. I am going to use this -- I will make some comments here. But I am going to use this as the opportunity to introduce David to all of you a little bit as well, too. Because I think he can add some additional comments around that. It breaks into a couple of pieces. You heard George talking about the continuing changes he's making in the management structure and the sales organization as it related to EMEA and other geographies. He mentioned before, I think, last quarter as well, too, we increase our investments in the -- what we call our growth geographies by about 20%, 25% this year. We are seeing strength coming from those as a result of that, but that continues and there will be additional appointments that George will make in that area. And then, the reorganization that we did that was significant for us to align us with the market is what I would like David to talk a little bit about because we brought David in to run that, and he brings significant experience in the software industry to do that. So David, if you would?

**David Dobson** - CA. - *EVP, Group Executive - Customer Solutions Group*

That's great. Thanks, Bill. Hello, John. I look forward to having discussions with you on a go-forward basis when I can probably get into a little bit more detail of the business as I am finishing up my eighth day. But let me tell you that the formation of the Customer Solutions Group is really another example of how we're aligning our organization to be able to execute the strategy that we've called. So a little bit of a background -- CA has traditionally been organized around product groups, or product silos. The fundamental change is really quite simple. We have taken the opportunity to align my group and my team around selected customer markets and segments. So to give you a quick overview of what they are -- we are organized around our mainframe customers, our security business, our large enterprise data center segments and customers. And very importantly, and Bill commented on this in his remarks -- we have formed a team -- a new team to focus on these growth markets and customers that we have typically not focused on. So that's a wonderful opportunity for us to extend the capabilities and technologies we have to a new set of customers. So my team has end-to-end accountability for our business in those selected customer segments. And clearly, I'm working very closely with Ajei Gopal who returns now our technology and development team. And then, intersecting with George's sales and go-to-market team to be able to deliver on the market requirements my team's sensing and be able to do that with very heavy focus on execution.

So in the short-term, my team has a focus on the execution of our growth strategies that we have called in our strategy to improve our ability to develop and deliver solutions to the market more quickly. Clearly, I am going to be spending a lot of time, and have been, on looking at our share and our participation in these selected markets. Considering how we improve that, as well as tapping into this new growth markets opportunity. So, I'm delighted to be part of this team and look forward to executing on this strategy.

**Bill McCracken** - CA. - *Chairman, CEO*

And John, I would make maybe one wrap comment that with respect to that, too. Is what it gives me, which I particularly like -- it gives me now two senior executives -- both accountable for the total business as I am. One looking at it from a customer solution point of view. The other looking at it from a geography and a delivery point of view. So it think it just brings us together in a better way with the entire marketplace.

**John DiFucci** - *JPMorgan - Analyst*

Okay, but just a quick follow-up to that, Bill. You just went through a restructuring to -- where you let some people go. And will there be -- this sound like, actually, new or reallocated spending. I just wanted to understand, is the net spend going to change in a positive way? Or, is net spending going to go up, or down, or stay the same?

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**Bill McCracken** - CA. - *Chairman, CEO*

Good question. Nancy, why don't you hit on the spend side?

**Nancy Cooper** - CA. - *CFO, EVP*

The spending is not going up, which is why we could reconfirm guidance. What you're hearing here is making sure the way we run the business is with increasing focus to deliver the results we have committed to in the guidance.

**Kelsey Doherty** - CA. - *SVP of IR*

Great. Next question, please.

**Operator**

We'll now go to Matt Hedberg with RBC Capital Markets.

**Matt Hedberg** - *RBC Capital Markets - Analyst*

Thank you. Nancy, in your prepared remarks you talked about new product sales excluding capacity and adjusting for the change in average duration up in the high single digits, I believe. Could you drill into that a little bit more? And I guess I'm wondering on the linearity of that. Can you talk about -- did that accelerate throughout the quarter? And how is that trending into the July month already here? Thanks.

**Nancy Cooper** - CA. - *CFO, EVP*

Sure. So, Matt, I think what you are asking me -- duration went from 4.2 years to 2.9 years in the quarter, which is a 30% difference. Which is what we use to annualize it and came up with revenue growth in high single digits. That duration change tends to fluctuate every quarter, and it is a function of two things. The customers whose renewal contracts are scheduled and the number of freestanding sales, which tend to have slightly shorter duration. So both of those were what will fluctuate during the quarter and drove this down to 2.9. What I think you can see is that high single digits translated into a 4% constant currency revenue growth in the current portion of our revenue backlog. So we're encouraged that freestanding sales, which grew 30%, contributed to that growth.

**Matt Hedberg** - *RBC Capital Markets - Analyst*

Okay. Thanks. And then on the mainframe side, you instituted a price increase July first. And obviously, the mainframe 2.0 initiative is still fairly early. Can you give us some updated assumptions on feedback from customers there? And then, on the price increase -- again, it's early. But a couple comments on there would be helpful. Thanks.

**George Fischer** - CA. - *EVP, Group Executive - Worldwide Sales and Operations*

Sure, Matt, I'll take the first side of that. The excitement around some of the new announcements both from us and IBM are really around there is some excitement about that platform. So we continue to see people investing and using that to exploit the technology. And for that reason, we are very bullish about where it is going to go over the next two quarters. Primarily for us, it's very straightforward without any speculation at all as our renewal portfolio expands out. We have many opportunities to sell there. But the mainframe 2.0 initiative has been successful for us in the fact that we have been able to visit and interact

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with the majority of our users. And as part of that, we get to refresh the features and make the products easier to use, et cetera. So when we make those contacts, we also get an opportunity to build pipeline for new opportunity. And that's been great. And that's part of the reasons we have been able to have the pricing we have. Because our customers, frankly, are getting good value in the products.

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**Kelsey Doherty** - CA. - SVP of IR

Great. Next question, please.

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**Operator**

The next question will come from Phil Winslow with Credit Suisse.

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**Phil Winslow** - Credit Suisse - Analyst

Hello. Most of my questions have been answered, but I just wanted to get your perspective on what you're seeing for pricing on the mainframe. The past -- multiple quarters -- you've talked about relative stabilization. Has that continued? And just from a vertical standpoint, obviously, financial services, government health care often big mainframe users. Do you see any changes in any of those three? Thanks.

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**Nancy Cooper** - CA. - CFO, EVP

Sure, Phil. So let me first answer your question about how price increases impact us. We have multiyear contracts, and when each one of those contracts comes up for renewal, we will negotiate in that 5% increase. So you will see it's a phased approach over three years. Now, I will turn to it George for your second part of your question.

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**George Fischer** - CA. - EVP, Group Executive - Worldwide Sales and Operations

Yes, I have not seen any major changes in the distribution of verticals who are using the technology. And the typical large users that have always been able to -- whether government or some of the large outsourcers that use technology very effectively. So I see those trends continuing. And again, there's some excitement about IBM's investment in the [z] platform, and we're anxious to see how that drives activity. That's not always directly correlated quarter by quarter, but we see some enthusiasm for that. And we will be picking that up through quarters three and four.

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**Phil Winslow** - Credit Suisse - Analyst

Great. Thanks.

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**Kelsey Doherty** - CA. - SVP of IR

Thanks, Phil.

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**Operator**

We'll now go to Katherine Egbert with Jefferies.

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**Katherine Egbert** - *Jefferies & Co. - Analyst*

Hello. Good afternoon. The new product sales were up high single digits. How much of that was from the companies you acquired in fiscal 2010?

**Nancy Cooper** - *CA. - CFO, EVP*

We're encouraged by the -- our acquisitions. I mentioned earlier that 2% of our growth product was primarily driven off the acquisitions. So that was good, and service assurance had growth in the high 20% on this annualized revenue basis. So we feel it was growing plus it was also very complimentary to our other products, and now we feel we have one of the best [peaks] in the marketplace on service assurance.

**Katherine Egbert** - *Jefferies & Co. - Analyst*

Okay. And then, I think I heard you say you are going to hire sales people this year and new sales leadership. How many people are you going to hire? And where are you going to hire them?

**George Fischer** - *CA. - EVP, Group Executive - Worldwide Sales and Operations*

Yes. Just to be clear on that -- this is the plan that we discussed all along. So it's not outside of the expense envelope that Nancy discussed earlier in the call. We have an opportunity to pick up a lot of competitive hires. So we have had a good hiring run in North America. And as I mentioned earlier in the call, we've added some very good key leadership in EMEA, and also are adding folks over there. In addition as part of the plan, we have added some channel and alternate [route] leadership that is allowing us to recruit and enable some partners to exploit the strategy that Bill outlined on the alternate market side. Selective, but CA is a good place to work right now, and we've had an opportunity to hire talent away from our competition, and we are going to continue to do that.

**Kelsey Doherty** - *CA. - SVP of IR*

Great. Next question, please.

**Operator**

We will now go to Derek Bingham with Goldman Sachs.

**Gonzalo Cavenaghi** - *Goldman Sachs - Analyst*

Good afternoon. It's Gonzalo Cavenaghi on behalf of Derek Bingham. My first question is on the global public sector referenced earlier. How much does that contribute to CA, and are you seeing any difference between government purchasing behavior in the US versus Europe?

**Bill McCracken** - *CA. - Chairman, CEO*

George, do you want to speak to that?

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**George Fischer** - CA. - EVP, Group Executive - Worldwide Sales and Operations

I guess what we can say about government purchasing behavior -- it's consistent and expansive regardless of some of the economies. In our market, specifically, we have traditionally sold to very large mainframe users. We are seeing mainframe usage because of those applications. But also as governments upgrade their networks, and they also harness the Cloud and other network-reliant applications, they're investing heavily into network management, virtualization, and of course, security is a big issue in the public sector. We're seeing very much an interest for the technology that's in our sweet spot, and it's growing well. One of the advantages we have, we have had a coverage model to address the public sector for some time. We have folks that are very well versed in how to call on a government -- how to manage the process and how to work also with integrators globally. But I would say certainly that the United States continues to be a great opportunity for us.

**Bill McCracken** - CA. - Chairman, CEO

George hit on a good point. Let me just expand it slightly, too. That is that with the new technology platforms that are rolling out which we are leading the way on with virtualization and the Cloud implementations. From the government point of view, they're driving as businesses are to try to do more with less, and that technology that we're providing now is the pathway for them to get that done. So I think that helps us, and it sends the revenue our way as we implement this strategy.

**Gonzalo Cavenaghi** - Goldman Sachs - Analyst

Okay, great. And just follow-up on that -- to clarify. Have you not seen any change in government spending now versus six months ago?

**Bill McCracken** - CA. - Chairman, CEO

George?

**George Fischer** - CA. - EVP, Group Executive - Worldwide Sales and Operations

Yes. I would say that with the exception -- like I said, we got one of our largest orders ever in NetQoS in the first quarter. I don't see anything that is widely different. And that is probably because of the defense and civilian agencies that we work on. We have been involved more in EU and EMEA activities than we ever had before. I would not attribute anything that we are seeing to spend trends. Ours is just coverage model, focus, and the products are much more salient to what these governments are looking for.

**Kelsey Doherty** - CA. - SVP of IR

Great. Next question, please.

**Operator**

(Operator Instructions) We will now go to Israel Hernandez with Barclays Capital.

**Israel Hernandez** - Barclays Capital - Analyst

Good afternoon, everyone. With respect to your push into virtualization management, you have had a number of product announcements over the last few months. Can you just speak to how you feel the opportunity is going to progress over the



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course of the next 12 to 24 months? And do you think this is going to be a slow grind here? Or do you think there is an opportunity here to immediately move the needle in terms of new bookings? And specifically, what is the edge here that CA brings to the table relative to -- primarily VMware is obviously doing a lot of good things here on the management side. Thank you.

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**Bill McCracken** - CA. - *Chairman, CEO*

You really almost answered the question in your last comment. What VMware sells and does -- we manage. That is the demand that I think they have seen. That they're pushing into the marketplace. That is what we announced. It was five new products to go at that marketplace, and that's what we have said we are going to do when we have talked to you in the past as well to is that -- our strategy -- we are not going into a [hyper-visor] area. We are going into virtualization management. So we're sitting on top of what they're doing, and I think you have seen the demand that is generated as a result of that coming off of what they have said. So as we enter this market, as we've been in the market with our products from the past as we moved them into the virtual and the Cloud areas, but now with these new introductory products that gives them the tools to manage those things. We're riding on that growth in the market. George, can you comment further?

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**George Fischer** - CA. - *EVP, Group Executive - Worldwide Sales and Operations*

Yes. At CA World, we had the opportunity to roll out the five new products, and we hit the ground running with our service assurance. We have been doing a lot of virtualization monitoring. We have had for some time the capability to view VM instances. So we are very pleased that obviously we have a heterogeneous position for all this stuff, but the quarter that VMware had -- that's what we're seeing. We're seeing that companies who are adopting virtualization of infrastructure, and now they are moving to applications. And it's a combination of both Cloud and in-house applications. In addition, we have acquired 3tera, and we have several blue chip companies that are adopting that to manage both public and private Cloud. So we're seeing this virtualization item just continue to be top of mind. It's what people are buying right now, and it's right in the sweet spot for us as a management Company.

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**Kelsey Doherty** - CA. - *SVP of IR*

Great. Israel, do you have any follow up.

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**Israel Hernandez** - *Barclays Capital - Analyst*

No. Thank you very much.

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**Kelsey Doherty** - CA. - *SVP of IR*

Great. Thank you. We will turn it over to Bill to finish.

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**Bill McCracken** - CA. - *Chairman, CEO*

Great. Listen, thanks to all of you. I really appreciate the time you have taken with us this afternoon. As we've said, we have been making a lot of changes here. We're focused clearly on execution. We're absolutely satisfied, and the feedback from our customers say we're on the right strategy. We've done a lot. As we have said to you when we were going through this, we have more things we're doing, and we are going to do those. We know how to do them, and we will get those done. So we look forward to talking to you in another quarter. Thanks to all of you.

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**Operator**

Ladies and gentlemen, that does conclude today's conference call and we do thank you for your participation today.

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