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CA - Q3 2012 CA, INC. EARNINGS CONFERENCE CALL

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OVERVIEW:

CA reported 3Q12 total revenue of \$1.3b, GAAP operating income from continuing operations of \$413m, and GAAP diluted EPS from continuing operations of \$0.54. Expects FY12 reported revenue to be \$4.8b and reported GAAP diluted EPS to be \$1.86-1.90.



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Gregg Moskowitz *Cowen - Analyst*

Aaron Schwartz *Jefferies - Analyst*

John DiFucci *JPMorgan - Analyst*

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Scott Zeller *Needham & Company - Analyst*

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PRESENTATION

Operator

Good day, ladies and gentlemen, and welcome to CA Technologies' third-quarter, 2012 earnings conference call. At this time all participants are in a listen-only mode. Later we will conduct a question-and-answer session and instructions will be given at that time. As a reminder, this conference call may be recorded. I would now like to turn the conference over to Miss Kelsey Doherty. Ma'am, you may begin.

Kelsey Doherty - CA Inc - SVP IR

Thank you and welcome to CA Technologies' third-quarter, fiscal 2012 earnings call. Joining me today are Bill McCracken, our Chief Executive Officer; and Rich Beckert, our Chief Financial Officer. As a reminder, this conference call is being broadcast on Tuesday, January 24, 2012, 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. Reconciliations to the most directly-comparable, GAAP financial measures 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 are available on our website at CA.com/Invest. 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.



Bill McCracken - CA Inc - Chief Executive Officer

Thanks, Kelsey. And good afternoon to everyone. Thank you for joining us. I hope you have had a chance to review our press releases announcing our third-quarter, fiscal 2012 earnings and our enhanced capital allocation program.

I'll start this afternoon with a brief overview of our third-quarter performance. I'll then talk to you about our capital allocation strategy, which we first discussed with you at Investor Day in July, and then indicated in October that we would provide you an update this quarter. I will conclude with the review of our progress-driving sales growth and margin expansion, which will then provide details on the quarter and guidance for the remainder of fiscal 2012. We will then take your questions.

In the third quarter, we saw growth in revenue and EPS and operating margin expansion, even after adjusting for a single license payment we received. As noted in our release, the unsolicited early single payment from a software company relates to a license agreement we entered into in connection with a litigation settlement we first announced in February 2009.

This payment was not included in annual guidance provided by the Company in October, because we expected it in fiscal years 2013 and 2014. Headlines from the quarter, which reflect year-over-year growth rates, include revenue growth of 10% in constant currency and as reported. The license payment added about 3 points to this growth.

Non-GAAP operating margin was 38%, including approximately 2 points from the license payment. Non-GAAP earnings per share growth was 28% in constant currency. The license payment added 10% to this growth.

Cash flow from operations, including the license payment, declined 19% in constant currency and 20%, as reported. As we have anticipated, cash flow for fiscal 2012 is weighted towards the fourth quarter, and this afternoon we confirmed our cash flow guidance for the year. Our current revenue backlog grew 2% in constant currency and 1%, as reported.

While we had a good quarter on many measures and continued to make solid progress against our long-term goals, we know we are not done. We remain focused on executing our strategy and driving further operational improvements, including new product sales, execution in EMEA, greater sales productivity and continued work on our expense structure.

Now let me go to our enhanced capital allocation program starting with some background. As you recall, in July we said, as part of our long-term guidance, that we expected to return 40% to 50% of our free cash flow to shareholders in the form of share repurchases and dividends. As I mentioned in October, Management and the Board were continuing to evaluate ways to optimize our balance sheet while maintaining the financial flexibility we need to build our business and continue to improve our competitive positioning.

We believe our enhanced capital allocation program announced this afternoon puts us on a path to achieving a balanced approach to return more cash to shareholders while still enabling us to invest in our future. It is a logical extension of the strategic and operational priorities we outlined at Investor Day.

Fundamentally, the dividend increase and share repurchase authorization underscore the Board's and Management's confidence in the Company's long-term business outlook and our ability to generate significant free cash flow on a consistent basis.

It is our consistent free cash flow, driven by our current and projected operating performance, that allows us to fund this ongoing return of capital, and at the same time continue to invest in our future to further improve our strategic market position and deliver superior mainframe enterprise and cloud solutions and services to our customers.

Today we are focused on three priorities to build long-term value for CA Technologies' customers, employees and shareholders. First, to continue to execute our strategy and improve our operating performance. Second, to provide for a greater return of cash to shareholders through increased dividends and share repurchases. And third, to effectively use the balance sheet to return additional cash in the near term through an accelerated buyback.

In summary, we are targeting to return to shareholders approximately \$2.5 billion through fiscal year 2014, or about 80% of our expected cumulative free cash flow over that period.

Key elements of the program include, one, an increase in the dividend from an annualized rate of \$0.20 per share to \$1 per share. That is a yield of approximately 4.5% based on yesterday's closing market price, and currently puts our dividend yield at the top of comparable technology companies. The Board and Management view returning cash to shareholders through dividends as an important component of our overall approach to enhancing shareholder value.

Two, a new \$1.5 billion share repurchase authorization through fiscal 2014, including an accelerated repurchase of approximately \$500 million under an agreement to be executed in the fourth quarter of fiscal 2012. Including the accelerated share repurchase and shares we've purchased year-to-date, we expect we will have spent approximately \$1 billion to buy back shares during fiscal year 2012.

The \$1.5 billion authorization replaces the approximately \$230 million remaining under our current authorization. We are confident we have the balance sheet capacity to get this done, and the program is expected to be funded by available US cash.

Three, our strategic plan anticipates that we will continue our investment in the business consistent with that of previous years, or approximately \$1 billion annually. This includes acquisition activity in the range of \$300 million to \$500 million per year on average through fiscal 2014, and the approximately \$600 million we invest on average each year in organic research and development.

So let me answer the critical question of how we intend to continue to improve execution against our strategic plan. As was highlighted in this afternoon's Capital Allocation Release, we remain comfortable with the long-term targets for the period ending March 31, 2015, that we'd provided at Investor Day in July. This includes an acceleration to mid single digit constant currency organic revenue growth and an expansion of our non-GAAP operating margin by 100 basis points a year.

Our expectation is that over time much of this operating margin expansion will come from improvements in execution and in our Enterprise Solutions segment, driven by accelerating product sales and greater efficiency in our sales force. We intend to continue to drive more growth and more profit from each dollar we invest, and we will continue to systematically improve productivity and efficiency in our organization. In our second-quarter earnings call, we outlined three immediate growth initiatives. Expanding product penetration in new accounts and gross geographies, continuing to improve our results in EMEA and driving consistent performance out of our acquisitions.

In terms of product penetration, this past quarter we focused on three main areas. First, we continued our market segmentation initiative, which, as a first step, includes the rebalancing of our sales force to align what has been a highly concentrated coverage model to new opportunities in approximately 1000, large, new enterprise accounts and approximately 7000 accounts in the mid-market. Focusing these groups on sales of new products to new customers, our market segmentation effort is designed to drive product penetration in new accounts and accelerate performance of our acquisitions.

Second, we told you we expect to add an incremental 300 new, quarter-carrying sales reps globally by year-end. One-third of these resources will be new to CA Technologies, while two-thirds reflect a reallocation of existing internal resources. All of this will be accomplished under our current expense profile. At this point we are approximately halfway through this process and expect to be completed by the end of the fourth quarter.

Finally, we have continued to make significant investments in growth geographies. These are long-term investments in markets that are key to accelerating new product sales and our ongoing success in the years to come. This quarter we had excellent results in Latin America, where we added more than 30 new enterprise customers to the region and expanded our footprint in more than 60 current customers.

In Asia-Pacific, we added more than 30 new logos to the region, including 15 for Nimsoft. Growth and new product sales more than doubled in China and grew more than 40% in Korea. Next in EMEA, we believe the team we have in place is introducing the right discipline and incentive structure to keep both our renewals process and new business pipeline on track.

Our plan is focused on improving sales execution and productivity, driving marketing and brand awareness and developing our people. While we do not want to get ahead of ourselves, we were pleased to see modest revenue growth in EMEA this quarter and wins with Volkswagen, SAP, Daimler and Credit Agricole.

Lastly with respect to acquisitions, we believe our strategy to aggressively capitalize on the evolution of virtualization management, cloud-computing implementation and fast delivery of IT is working. We continue to focus on driving results from investments we have made both through organic development and in companies such as Nimsoft, 3Tera AppLogic, ITKO and Arcot. Results achieved during the quarter give us confidence that our strategy to reach new customers and the mid-market is the right one.

This quarter, Nimsoft added a record 100 new logos; and in December, we received notification that Net1 Systems formally selected Nimsoft to be their platform of choice for their future business services for their XOC-managed operations center, one of the largest in Japan. We closed a significant transaction with IGT, which selected AppLogic to continue innovating how casino games, systems and experiences are delivered with the IGT cloud.

ITKO delivered a record quarter, closed five deals over \$1 million, and saw their average transaction size significantly increase. Customers like DirecTV and So Cal Edison report return on their investment in ITKO in terms of weeks, and continue to expand their usage and licenses. Finally, Arcot is protecting approximately 150 million identities worldwide. During the 2011 holiday shopping season, we averaged 1 million transactions per day for e-commerce authentication on our SAS platform.

In conclusion, the strategic initiatives and priorities we continue to pursue, in combination with our enhanced capital allocation program, reflect the ongoing commitment of the CA Technologies' Board, Management and employees to deliver outstanding solutions and services to our customers and attractive, sustainable returns to CA shareholders. Now I will turn the call over to Rich for a closer look at the third quarter.

Rich Beckert - CA Inc - SVP and CFO

Thank you, Bill. Turning to our third quarter results, please note that our growth rates are year-over-year, unless otherwise indicated, and all results are from continuing operations. As Bill mentioned, this quarter's results include the single license payment from a software company. This payment came in earlier than we had anticipated and was not included in the fiscal year 2012 guidance we provided in October.

The single license payment contributed the following to the quarter. Revenue of \$39 million reported in our Mainframe Solutions segment and in the software fees and other line on the P&L. GAAP and non-GAAP operating income of \$36 million. GAAP and non-GAAP earnings per share of \$0.05 and cash flow of \$39 million. Total revenue for the quarter was \$1.3 billion and grew 10% in constant currency and as reported. 8 points of this growth was organic, while 2 points of this growth came from acquisitions.

This quarter we saw a \$20 million increase in perpetual sales associated with Enterprise Solution products, including \$10 million of products that were newly eligible for up-front recognition during the quarter. From the segment perspective, Mainframe Solution revenue was \$682 million, up 9% in constant currency and as reported.

The single license payment contributed 6 points of growth in constant currency and as reported to Mainframe Solutions. Our Enterprise Solutions revenue was \$478 million, up 11% in constant currency and 12%, as reported. Services revenue was \$103 million, up 16% in constant currency and 17%, as reported. Underlying our results for the quarter, total new capacity and new product sales were up below single digits.

In Mainframe Solutions, new product sales for the quarter grew both with and without single license payment. Capacity sales were down more than 20%. Quarter-to-quarter capacity will fluctuate, driven by the nature of the customers in our underlying renewable portfolio. Year-to-date we are encouraged by the capacity trends which are up and believe that IBM Mainframe is bringing increased attention to the platform, and over time should serve as a slow, steady tailwind to CA Technologies.



Enterprise Solutions' new product sales were down approximately 5%. We saw growth in virtualization and automation and identity and access management. This was offset by service portfolio management and service assurance. Underneath these service assurance results, we saw growth in application performance management that was offset by infrastructure monitoring.

Finally, new service engagements were down slightly year-over-year. Our renewal yield was just below 90%. We closed one transaction, a merger that negatively skewed the results during the quarter. Excluding this transaction, the renewal yield would have been in the mid-90s.

We continue to expect the 2012 renewal portfolio to be down approximately 15% year-over-year. For modeling purposes, please note that fourth-quarter, 2012 renewals face a difficult, year-over-year comparison. This is due to a more-than-\$500 million, system-integrator license agreement that was signed last year in our fiscal fourth quarter.

Looking at revenue backlog, current revenue backlog was \$3.6 billion, up 2% in constant currency and 1%, as reported. Total revenue backlog was \$8.1 billion, up 2% in constant currency and as reported. From a non-GAAP perspective, non-GAAP operating income, before interest and tax, was \$475 million, up 21% in constant currency and 23%, as reported.

For the quarter, our non-GAAP operating margin was 38%. Operating margins for Mainframe Solutions was 59%. Operating margins for Enterprise Solutions was 12%. This includes 4 points of continued investment in this segment. Finally, operating margin for services was 11%. Non-GAAP, diluted earnings per share was \$0.65, up 28% in constant currency and 30%, as reported, including a year-over-year, \$0.01 tailwind from currency.

This quarter, EPS benefited from previously-mentioned license payment, operational improvements and our stock repurchase program. Our effective non-GAAP tax rate for the third quarter of 2012 was 31.5%. Cash flow from operations in the quarter was \$396 million, down 19% in constant currency and 20%, as reported.

Single installment payments were \$107 million in the third quarter, compared to \$152 million in the previous period. Total billings backlog of \$5 billion was up 7% in constant currency and 6%, as reported. DSOs were essentially flat year-over-year.

Moving to third-quarter, GAAP results. Third-quarter, operating margin before interest and taxes was 33%. GAAP operating income was \$413 million, up 22% in constant currency, and 24%, as reported. And GAAP diluted earnings per share was \$0.54, up 39% in constant currency, and 42%, as reported. Our effective GAAP tax rate for the third quarter was 34.9%.

Now moving to the balance sheet. We ended the quarter with approximately \$1.1 billion in net cash. Between October 1 and December 31, we'd purchased approximately 9.6 million shares of stock for a total of approximately \$200 million.

Now let me turn to fiscal 2012 guidance. As has been our practice, guidance is based on December 31 exchange rates. This includes a partial hedge of operating income, and updates our expectations for share count.

Guidance is the following. Total revenue growth is now expected to be 6% in constant currency, at the high end of our previous range of 5% to 6%. This translates to reported revenue of \$4.8 billion.

Non-GAAP diluted earnings per share growth and constant currency is now expected to be in the range of 11% to 13%, an increase from our previous range of 7% to 10%. This translates to reported non-GAAP diluted earnings per share of \$2.21 to \$2.25. GAAP diluted earnings per share growth in constant currency is now expected to be in the range of 11% to 13%, an increase from our previous range of 6% to 9%. This translates to reported GAAP diluted earnings per share of \$1.86 to \$1.90.

We continue to expect that cash flow from operations will grow at 3% to 5% in constant currency. This translates to reported cash flow from operations of \$1.44 billion to \$1.47 billion. Underlying this guidance, we expect our GAAP and non-GAAP tax rate to be 31% to 32% in this fiscal year.



At the end of the year, we expect approximately 463 million shares outstanding and a weighted average diluted share count of approximately 486 million shares. This share count reflects the \$500 million ASR under an agreement we expect to execute in the Company's fourth quarter. We expect our non-GAAP operating margin to be a strong 34% for fiscal year 2012. And now I will turn the call back over to Bill.

Bill McCracken - CA Inc - Chief Executive Officer

Thanks, Rich. I'd like to conclude by saying that our third quarter performance and positive operating momentum reinforce our belief that we have the right strategic plan in place. As I have said, we remain focused on execution and feel strongly that the initiatives we continue to pursue allow us to invest in our Company's future and at the same time reward our shareholders. And with that, Kelsey, let me turn it back to you.

Kelsey Doherty - CA Inc - SVP IR

Thank you, Bill. As the operator is polling for questions I'd like to remind you, on Tuesday, February 7, the Goldman Sachs Technology Conference in San Francisco on Wednesday, February 15; the Morgan Stanley 2012 Technology Media and Telecom Conference in San Francisco on Tuesday, February 28; and the Raymond James Institutional Investor Conference in Orlando, Florida, on Monday, March 5.

In the interest of time, we ask you to please limit yourself to two questions. Operator, please open the call for questions.

QUESTIONS AND ANSWERS

Operator

Thank you. (Operator instructions) Our first question comes from Shaul Eyal from Oppenheimer & Company.

Shaul Eyal - Oppenheimer & Co. - Analyst

Good quarter, congratulations.

Bill McCracken - CA Inc - Chief Executive Officer

Thank you.

Shaul Eyal - Oppenheimer & Co. - Analyst

Two quick questions on mind. Rich, can you guys provide us with a slightly more quantitative data on Europe? I know, Bill, you indicated some modest growth, but maybe a little bit of more color on that, that will be helpful. Thank you.

Rich Beckert - CA Inc - SVP and CFO

Sure. So this quarter what we saw coming out of Europe for the first time, two things, one, we saw them hold their forecast, which was great. And then by the end of the quarter, it actually grew. So there's some positive momentum. We are not getting ahead of ourselves, but in the right direction.



More important than that, though, we saw them able to sell outside of the renewal cycle, which, as you know, is low this year, and especially in Europe, but for all of CA, allowing them to have their best, up-front revenue since we have been starting this program on the distributed side. It has allowed them to grow their revenue year-over-year, and it demonstrated their ability to sell outside the renewal cycle. Does that help?

Shaul Eyal - *Oppenheimer & Co. - Analyst*

Yes, absolutely. Another question. On the cash flow, a little bit on the weaker side as it relates to consensus numbers. Is it just a matter of collections? Is it timing? Is it just being back-end loaded?

Rich Beckert - *CA Inc - SVP and CFO*

Right. Great question. It's preliminary timing. We are very confident with our full-year guidance. If you look at it on a year-to-date, CFFO is only down \$14 million or 2%. Billings year-to-date is actually up \$177 million or 6%. Customer collections is up \$117 million or 4%, and billings backlog is up 11%. So we can see a clear road map to how we are going to get to our 3% to 5% guidance.

Kelsey Doherty - *CA Inc - SVP IR*

Great. Thanks, Shaul, next question, please.

Operator

Our next question comes from Gregg Moskowitz from Cowen.

Gregg Moskowitz - *Cowen - Analyst*

Thanks and good afternoon, everyone. Congratulations on the capital allocation plan. It's a pretty impressive commitment, to say the least. I just had a clarification and then a follow-up.

So, Rich, it seems as though, as you said, 80% of your free cash flow through fiscal 2014 is expected to go to buy back some dividends and an additional \$600 million to \$800 million in M&A. I believe, if I'm not mistaken, that would be roughly equal to or perhaps a bit above the \$3 billion or so in future cash flow generation over this period. So first of all, I just wanted to see if that was correct.

Rich Beckert - *CA Inc - SVP and CFO*

No, we said our acquisitions would be in the \$300 million to \$500 million range over time.

Gregg Moskowitz - *Cowen - Analyst*

And I'm sorry, Rich, the \$300 million to \$500 million, is that per annum or is that between now and 2014?

Rich Beckert - *CA Inc - SVP and CFO*

That would be an average over that time frame, so in any one year, we could do \$300 million to \$500 million, so averaging into that.

Gregg Moskowitz - Cowen - Analyst

Right. And that was essentially just more or less doubling that in terms of starting with \$600 million in M&A. So my question is in terms of the future cash flow generation between now and fiscal 2014, is essentially all of it coming down to buy back dividends in M&A or is there another piece that I'm missing here?

Rich Beckert - CA Inc - SVP and CFO

No, that's -- we are looking at buybacks, the \$1 dividend, and our M&A. And we think through our continued operations and efficiency, we will be able to easily do that. We have source and uses for that cash outside of the Americas, and we are confident that we can do all of our capital allocation with US dollars.

Gregg Moskowitz - Cowen - Analyst

Okay. Great. And then just in terms of my follow-up, Rich, so a multipart question, if I could. How much cash, if you don't mind sharing with us -- how much cash is currently onshore at CA? Secondly, if you could complete this plan, how much will remain onshore by the end of fiscal 2014, according to your projections. And then third, does this plan contemplate any issuance of debt, or no?

Rich Beckert - CA Inc - SVP and CFO

I'll answer two of those three for you. I will tell you that we are at 36% of our free cash flow -- or our cash is here in the US. And we don't plan on having to issue any kind of debt in order to do this capital allocation plan, but I don't plan on doing a forecast by GO, going out over time.

Gregg Moskowitz - Cowen - Analyst

Great, Rich, thanks very much.

Rich Beckert - CA Inc - SVP and CFO

You're welcome.

Kelsey Doherty - CA Inc - SVP IR

Next question, please.

Operator

Thank you. Our next question comes from Aaron Schwartz from Jefferies.

Aaron Schwartz - Jefferies - Analyst

Good afternoon. You talked a little bit about some of the -- or actually even showed some numbers in terms of the up-front license fees in the quarter. Is there any change in terms of what you're bundling in with ELAs? And I don't know if that's related to your focus on new customer growth, but I would think that those would tend to be maybe one product sales versus bundled sales. I was wondering if you could walk through that dynamic?



Rich Beckert - CA Inc - SVP and CFO

That's a great question. What we are really seeing in the up-front revenue, we had announced some new products. It's actually refreshed products out at CA World. We also had our products -- because right now where we are in the renewal cycle, as I talked about earlier, in Europe -- when the distributed products that is sold outside of renewal without mainframe, they qualify for up-front revenue. And so you see a little higher percentage of that happening because of the lower weighting, if you will, of transactions happening outside of the renewal. Remember we also have ITKO. One of our new acquisitions had a very strong quarter. That's all up-front revenue, so we were pretty happy with that.

Aaron Schwartz - Jefferies - Analyst

Okay. Thank you. That's helpful. And then maybe a follow-on question to what Gregg had asked. But obviously you laid out quite a bit of capital commitment here in terms of the cash allocation. Is there any way you can prioritize the M&A side versus what you're committing to shareholders? And then on that front, does this at all -- your intention to go from 40% to 50% now up to 80% of free cash flow to shareholder. Does that change your view on hiring, on retention, anything operationally that you would have to do differently?

Rich Beckert - CA Inc - SVP and CFO

No, the only thing that you will see, and we were already anticipating doing this as part of this capital allocation, is you'll see us leverage our overseas operations more, so some globalization will occur. Where we actually do our M&A acquisitions, some of those will actually happen outside of North America, so some of that cash will be non-US cash. So it is right in line with where we want it to go.

Aaron Schwartz - Jefferies - Analyst

And last question for me if I could, is there any intention to repatriate some of the overseas cash and pay the tax on that?

Rich Beckert - CA Inc - SVP and CFO

No.

Aaron Schwartz - Jefferies - Analyst

Okay. Terrific. Thank you.

Operator

Thank you. Our next question comes from John DiFucci from JPMorgan.

John DiFucci - JPMorgan - Analyst

Thanks. My congrats to you, not just from me, but from the Market. It really likes what you're doing and doing the right thing with the capital structure here. I'll let others ask questions on that. I also know, Rich and Bill and team, that you're totally focused on the business operations. And I don't necessarily see this as a signal, and you're talking about how you're going to continue to grow and that's good to hear.

And you can do both by returning cash and growing here. But when I look at the results for this quarter, which look decent, but when I adjust for the \$39 million single license payment foreign exchange, and if I adjust for the EDS revenue in the quarter, or the large service provider in the

quarter, and I realize that's real revenue, but at the same time it's not -- as far as a run rate, it's about the same business run rate as it was prior to the renewal. When I make those adjustments, I come up with revenue growth of about 2% on an organic constant currency basis, and bookings. And I realize, Rich, you really shouldn't be looking at it, and you drove this home and we understand you can't look at it, the bookings, just because of timing, but the bookings would have declined. So I guess looking at the 2% growth -- (multiple speakers)

Rich Beckert - CA Inc - SVP and CFO

Can I just, John, jump in for a second? It's about 2% for the system integrator. About 3% for that single license. So to your point, you could argue 5 points. That'll be 3% that's organic and 2% that's acquisitive.

John DiFucci - JPMorgan - Analyst

Yes, but it's actually 3.4%, and it's 2.2%; and when you round them all up, they all add up to about 8%. It's like 7.7%.

Rich Beckert - CA Inc - SVP and CFO

But I'm telling you it's 8.2%, but keep going.

John DiFucci - JPMorgan - Analyst

Okay. So if it's 8.2 -- I guess, my question is, this 2% to 3%, is this what we should be expecting or should we be expecting more than this as far as the -- we understand you're going to be buying some companies and some exciting technologies. But so far, that's still in progress. Should we be seeing more of this, and how are we going to see it? Are we going to see even maybe perhaps more product out of CA that's not just through acquisition? Are there changes being made, as Peter has come on board, as far as more organic product development even or something along those lines?

Bill McCracken - CA Inc - Chief Executive Officer

John, there's a couple of things that we've mentioned here, as we look forward. The acquisitions we have been making over the last two years, many of them now have moved into the organic area, and as we have added additional capability to those, those are supporting our organic growth as we go forward, and that will continue into next year.

When you look at the segmentation that we talked about in the last quarter with the 300 additional sales reps we were moving out, and we are moving into the segmentation area, that growth, new products and new accounts, will add to the organic growth as we go forward. And I think one of the, probably, key points that's worth looking at in the quarter is that, you may recall a year ago, when Nimsoft was reporting, we talked about 20 or 30 new accounts. We had over 200 new logos in the quarter.

And so with Nimsoft and with Latin America coming on very strong, now starting to get growth in the Asia countries and a return a bit from EMEA, we are starting to see the organic growth coming out of what we had previously done from the new products and acquisitions as well as from new segmentation pieces. So as we look forward on the base business, we see organic growth being the way we move next year.

John DiFucci - JPMorgan - Analyst

Okay. Thanks, Bill. And if I could just a follow-up from Aaron's question for Rich. Rich, we saw a sequential decline in subscription revenue this quarter, which is odd to see given your model. This was more than offset by a big jump in the software fees and others, even if you back out the single license payment. So if you could just explain what's going on there?



Rich Beckert - CA Inc - SVP and CFO

Right, so what you did see, and it was reflected in my discussion on Europe as an example, if you were to combine the subscription bookings and the SFO bookings, you'd see we are up single digit, John. And really, outside of the renewal, when we are doing a lot of our distributed transactions are going to be taken as SFO, which then does put pressure on the revenue backlog and the subscription line.

Kelsey Doherty - CA Inc - SVP IR

Great. Thanks. Next question, please.

Operator

Thank you. Our next question comes from Walter Pritchard from Citigroup.

Walter Pritchard - Citigroup - Analyst

Thanks. Just a question on the bookings, and I know not a focus here in the quarter, necessarily, but you have had about 11 out of 15 quarters on an annualized basis over the last three years or so, four years, have declining bookings. I'm trying to get a sense of when we should start to see the bookings turn around. It seems like you can't grow revenue forever without annualized bookings growing, and it seems like you'd see that here shortly. So I wanted to get a sense of how far we need to look out to see bookings growth resume.

Rich Beckert - CA Inc - SVP and CFO

Right. So if you recall just for clarity, this fourth quarter we will have a very difficult compare with the \$500 million transaction we did last year. So we will be down for the year 15%. Next year is the end of our trough for the renewal cycle and we start a very strong 2014 and 2015 thereafter. So to the degree that the renewals have -- and they do weigh heavily on the total bookings, because they tend to be longer in duration -- it will put pressure on that.

To a degree, we continue to sell outside of the renewal cycle, which allows us to grow footprints, products like Nimsoft, which, back to John's question, by this time next year we will generate about a point of growth, we really start to have other engines that are starting to kick in. ITKO will have another strong year. Again, that's outside of the renewal cycle. So I think you're right, it will continue to be on the lower side. And in May, we will give you guys more guidance on FY13.

Walter Pritchard - Citigroup - Analyst

Just a couple specifics on the capital allocation. You talked about \$1 dividend. Can you talk about the path to get there? I assume that's not \$1 for next year. Is that \$1 exiting 2014, or any color on that? And then, also a share count around with the ASR next quarter? I think the share count will come down.

Rich Beckert - CA Inc - SVP and CFO

So that starts this quarter, so on February 14, I believe, if you're a holder, then you'll get \$0.25 per share.

Walter Pritchard - Citigroup - Analyst

Got it.

Rich Beckert - CA Inc - SVP and CFO

And for modeling purposes for everyone on the line, as we said on the call, you should assume 486 million shares on average to do your model for EPS.

Walter Pritchard - Citigroup - Analyst

Okay. Great. Thanks a lot.

Operator

Thank you. Our next question comes from Kirk Materne from Evercore Partners.

Kirk Materne - Evercore Partners - Analyst

Thanks very much. A couple of clarifications, Rich, first, going forward can you give us any idea of just what your assumption is or what the historical split has been on operating cash flow between US and international, just so I can get a sense of what you're saying. You guys have said you can pay for all this with your US cash flow. I'm just trying to get a sense of how that's broken out. I know you've given us what the balance sheet split is. I'm trying to get a sense on historically what it's been, if you don't want to give us any forward-looking number.

Rich Beckert - CA Inc - SVP and CFO

It's roughly a 40/60 split. It depends on the particular time of year and depends on the size of certain transactions that might come in that might move it a little bit. Even though we have already accumulated through year-to-date \$550 million worth of shares, we are still at 36% of our US to non-US at 64%. So it's pretty healthy, and we feel confident that we can continue in that range going forward.

Kirk Materne - Evercore Partners - Analyst

Sorry. It's 40% US. 40% comes in the US and 60% is international in your operating cash flow?

Rich Beckert - CA Inc - SVP and CFO

And right now it's 36%.

Kirk Materne - Evercore Partners - Analyst

Okay.

Rich Beckert - CA Inc - SVP and CFO

I'm talking about the cash on the balance sheet, to be very clear.



Kirk Materne - *Evercore Partners - Analyst*

Okay. But I'm just trying to get a sense on when you guys are planning this out. You obviously had to make an assumption on what the US international cash flow was going to look like. And I know you don't want to get into guidance, but just historically, when you bring in \$1 of cash historically, I guess how is that broken out? Is it 60%, 70% US, and 40% -- I'm just trying to get a sense on it, so I can do the math to make sure the numbers and what you've committed to make sense.

Rich Beckert - *CA Inc - SVP and CFO*

It's approximately 60% in the US free cash flow. It will depend by quarter, but it's approximately 60%.

Kirk Materne - *Evercore Partners - Analyst*

Okay. That's helpful. Thanks. And then just lastly, you guys have obviously recommitted to growing operating margins by 100 basis points per year. Does that also take into account any kind of M&A you'd be doing? So if you do go through the \$300 million to \$500 million you're talking about M&A, would that be inclusive of that or would that potentially have to be adjusted depending on the deal?

Rich Beckert - *CA Inc - SVP and CFO*

Any more tuck-ins would be included in there. Any of size would not be included in there.

Kirk Materne - *Evercore Partners - Analyst*

Okay. Can you give me an idea what you're thinking about size? Over 100 million? 200 million?

Rich Beckert - *CA Inc - SVP and CFO*

It will depend on the year, I think, going forward. So as we do make those, we will make corrections. We will make sure that we let everyone know what that guidance change is.

Operator

Thank you. Our next question comes from Michael Turits from Raymond James.

Michael Turits - *Raymond James - Analyst*

Two sets of questions. First is a clarification of Kirk's question about the margin expansion. So if you do the \$300 million to \$500 million in a given year, should we anticipate you get a point of margin expansion or you get less?

Rich Beckert - *CA Inc - SVP and CFO*

As I said, it will depend on what the acquisition is, Mike. And it will depend on the size of it, when it happens in the year. So right now, the guidance that we are giving is currently without any impact. In other words, if we do an acquisition and it impacts us, then we will have to modify it, so it's as if there's no impact to that. We will let you know if it changes.

Bill McCracken - CA Inc - Chief Executive Officer

What you should expect is that we are driving operations cost and expense to improve 100 basis points on margin every year. If there's a transaction that comes into it that would change in any way, we will tell you that, but the operational improvements we make on cost and expense are at the rate that we have told you in the past and in our guidance.

Michael Turits - Raymond James - Analyst

Okay. So I'll assume the base line assumption for a point of margin expansion is zero or close to zero in acquisitions. And then -- (multiple speakers)

Bill McCracken - CA Inc - Chief Executive Officer

Acquisitions, correct.

Michael Turits - Raymond James - Analyst

And then follow-up, obviously it was a solid quarter in a lot of ways, but two things that jumped out at me. One is that the growth rate for the current, one-year revenue backlog, that growth rate decelerated again. I think it went down about 2 points, 2%, and that's been going down for a little while. And then the other thing that jumped out that was of some concern to me was that, again, in Enterprise, you had a decline in new product sales.

So what is really going on in terms of the fundamentals of selling Enterprise, new Enterprise software licenses? Is it getting to be overall a tougher thing to do and do those numbers reflect that? And when can those start reversing?

Rich Beckert - CA Inc - SVP and CFO

Okay. So the first part of your question on the revenue backlog, it did slow down, although it did grow sequentially 1%. And there's a waiting on the lower renewal portfolio and the higher number deals that are done outside the renewal cycle would drive that. And therefore, you move more of your products to the perpetual license that's accounted for in the SFO line.

From a new sales standpoint, I think the way we would tell you is we were pleased with our virtualization and automation, identity and access management. Service assurance was mixed where we had good growth in application performance management, and that was offset a bit by infrastructure monitoring. And we had a decline in service portfolio management. So it was mixed, but in general we had some very good bright spots. We had very good Mainframe new license sales as well, excluding even that single license payment.

Michael Turits - Raymond James - Analyst

Okay.

Bill McCracken - CA Inc - Chief Executive Officer

What you do see is that the SFO line does go up, as Rich explained, and that has a lot to do with what we talked about last quarter with respect to market segmentation we are going and selling new products and new accounts. And a lot of those flow in on the upfronts. And as an example, ITKO last quarter had \$1 million. This quarter, \$20 million. So we are seeing significant growth in the upfronts with respect to the new products and new accounts.



Kelsey Doherty - CA Inc - SVP IR

Great. Next question, please.

Operator

Thank you. Our next question comes from Mark Moerdler from Sanford Bernstein.

Mark Moerdler - Sanford Bernstein - Analyst

Very nice number, guys. Couple questions on it. First are, what are the levers for the margin expansion of the 100 basis points annually? Are these savings spread across R&D, sales and marketing, in G&A, or is it from one of the specific areas? And then the second is, you lowered guidance last quarter and now you're moving into the high end of the range. What's changed to give you more confidence?

Rich Beckert - CA Inc - SVP and CFO

Okay. So I'll answer the second one first. The single license payment added a little under a point of revenue growth, which allowed us to move ourselves up to the high end of guidance. That will probably be a strong 6, just so people understand where that sits. We thought, though, it was prudent to keep it within the top end of the range due to the macro environment. We don't want to get ahead of ourselves, as Bill had said earlier.

On your first part of the question, most of the improvements we will see next year, we continue to make improvements on G&A. It will all be predominantly in the Enterprise Solutions segment, as we talked about back in July, and you see us continuing to demonstrate efficiencies that we are able to work through the business in all elements. So sales will become more efficient.

We talked about the 300 people that, by Q1, we will have moved out of overlay positions into quota carrying, so that drives your sales E to R. Our development E to R, we think is actually set fairly well, so we are not looking to do much to the sales unit. We would always continue to make improvements to the G&A line. The G&A line, of course, will benefit all segments. Does that help?

Mark Moerdler - Sanford Bernstein - Analyst

That helps. Thank you.

Kelsey Doherty - CA Inc - SVP IR

Great, next question, please.

Operator

Thank you. Our next question comes from Matt Hedberg from RBC Capital Markets.

Matthew Hedberg - RBC Capital Markets - Analyst

Thanks, guys, and congratulations on the quarter as well. Most of my questions have been asked at this point, but you guys made a point about indicating that within Europe you've seen a nice improvement in interquarter sales beyond the renewal period, which has been something you



guys have been working on for a while here. Could you address that beyond Europe? In North America, APAC, and give us a sense for maybe how some of these newer SAS products are helping in some of those [GOs] as well?

Bill McCracken - CA Inc - Chief Executive Officer

We are seeing that now happening, we had talked about it before happening in North America. And I think as we work on the growth geographies, as we've talked before, Latin America for this quarter was a very significant expansion. In fact, they were up around 60% year-over-year, and a lot of that comes out of those selling outside of the ELA cycle. Same thing was true in Asia as well too.

So that has been a focus of ours, and it is a big piece of what we have been talking about here with all of these questions as to the revenue flow that we get out of the new products and new accounts and the up-front license as it is booked from that perspective. So that is a big part of what our strategy was and how it fills in from a revenue point of view on a quarter-to-quarter basis.

Matthew Hedberg - RBC Capital Markets - Analyst

And then one last question. You guys are making some nice progress on your quota-bearing sales rep hiring here. I'm wondering how has attrition been, and in terms of productivity, what more can we expect from productivity as we enter your fiscal fourth quarter? Thanks.

Bill McCracken - CA Inc - Chief Executive Officer

We have not seen any significant change in the attrition at all. And as we said, about 100 of the 300 will come from outside. That was the plan, as we talked about last quarter. We've got about 150 of those folks in place and we will finish that this quarter, but we haven't seen a significant change with respect to attrition in any of our geographies.

Rich Beckert - CA Inc - SVP and CFO

On your question on sales productivity, we continue, as we had said back in July, that over the next few years we will be taking a point or two out of that total sales-to-revenue ratio.

Kelsey Doherty - CA Inc - SVP IR

Great. Next question, please.

Operator

Thank you. Our next question comes from Philip Winslow from Credit Suisse.

Philip Winslow - Credit Suisse - Analyst

Hi, guys. Most of my questions have been answered, but just wanted to go back to the new product sales commentary from earlier. You guys talked about how Enterprise Solutions' new product sales were down approximately 5%. Now that's better than last quarter when they were down 20%, but just that line in particular, you guys put a lot of focus in terms of incremental growth from here. And even excluding renewals, when do you think we are going to start to see that turn around and what's really going to be the driver for that? Thanks.



Bill McCracken - CA Inc - Chief Executive Officer

The key thing on that is, when you look back two years ago, one of the things we talked about when we bought Nimsoft was that we bought two things. We bought technology, but we bought a delivery channel and primarily the MSBs. New products and new accounts mid-market is growing rapidly. In fact, Nimsoft is up 70% the last two years in this growth piece. That is where the market seems to be gone as well too.

In fact, I think you've seen it in the industry, the IM piece is actually cutting back a little bit in its historical way that it flowed. And what we are finding is that we are bringing the Nimsoft piece up as the PNCV on the other piece goes down, and that is, for us, been one of the strength pieces as of the way it's balanced it versus the way the rest of the market for some of our competitors have worked.

The second thing is, and probably very importantly, the acquisition of ITKO adds significantly to that. And as we mentioned, that was a major growth, not only in the revenue shift this quarter, but also in the transaction size, because it's about triple the size it was a quarter ago. Does that help?

Kelsey Doherty - CA Inc - SVP IR

I think we have lost him, unfortunately. I think we need to move to the next question, please.

Operator

Our next question comes from Scott Zeller from Needham & Company.

Scott Zeller - Needham & Company - Analyst

Hi. Thank you. First question is around the sales changes. You mentioned in the prepared remarks, the 1000 high end accounts and then the 7000 below that. Is that, I'll call it, a reassignment or redrawing of accounts, is that complete, the reassignment?

Bill McCracken - CA Inc - Chief Executive Officer

The segmentation of the piece we talked about last quarter, we are halfway through on the total, which is 150 of the 300. As far as the segmentation is concerned, yes, that work is done, and the assignment of those folks to that is completed as well.

Scott Zeller - Needham & Company - Analyst

Okay. And then on the Enterprise Solutions group, the virtualization-related products, could you talk about bookings, trends and that group of products, please?

Rich Beckert - CA Inc - SVP and CFO

Sure. We were pretty pleased with the performance of the products in virtualization. I think what you'll see is we have two large transactions inside of that space that really have benefited us. And again, as we talked about ITKO earlier, it really had an outstanding quarter right on target with what we had anticipated internally for our acquisition case.

Scott Zeller - Needham & Company - Analyst

Okay. Thank you.

Kelsey Doherty - CA Inc - SVP IR

Great. This will be our last question.

Operator

Thank you. Our final question comes from Kevin Buttigieg from Collins Stewart.

Kevin Buttigieg - Collins Stewart - Analyst

Thank you. Just two quick questions on capital allocation. First of all, I was just wondering if could you talk a little about your philosophy between the return of shareholder funds in the form of dividends versus buybacks. Obviously you have been much more skewed towards buybacks historically, and this is a very significant increase in the dividend here today.

And then just secondly, I wanted to ask, I understand, Rich, what you're saying about there's no need to issue debt here, but my question would be why not? If you look a few years ago, CA had \$1 billion more in net cash and \$1 billion more in debt. So clearly there's the flexibility on the balance sheet, and it would give you more flexibility today, including the possibility of an even greater return of cash to shareholders, particularly when the cost of debt is so low. So just wondering if you're targeting a specific debt rating there or really what your thought process is on those two issues?

Rich Beckert - CA Inc - SVP and CFO

Sure. So the first piece, the increase today in the amounts really underscores our confidence in our ability to have a very strong long-term business outlook and our ability to generate cash over the long term, which is going to be given out via dividends. And we think by having the dividends, it really rewards our shareholders and the partnership we have with them over time.

On your second question on why we wouldn't leverage up the balance sheet, that tends to be more of a shorter term view. If we were to do something like that, it would really be more for a very large acquisition or something along those lines, which we do not plan on doing at this time. We do not see the advantage of taking on incremental debt and we are happy with the credit ratings that we currently have.

Bill McCracken - CA Inc - Chief Executive Officer

And on the dividend piece, I think it represents our confidence, both the Board and Management's confidence, in our operational performance going forward when we put it in the form of a dividend to reward our shareholders as well.

Kevin Buttigieg - Collins Stewart - Analyst

Thank you.

Kelsey Doherty - CA Inc - SVP IR

Thanks, Kevin.



Bill McCracken - CA Inc - Chief Executive Officer

So let me just wrap up. I guess I would make three points as we wrap up. First is, we are going to continue to press, as we have been, on executing the strategy and improving our operational performances. On the second point, as we have mentioned today, we want to return cash to our shareholders and reward them, because we believe we can both invest in our future as well as return cash to our shareholders.

And then finally, we want to make sure that we keep our balance sheet as an efficient balance sheet in the things we do going forward. So we were pleased with this quarter, and we believe that going forward we have an opportunity to both invest in the future and also return cash to our shareholders. Thanks for hooking up with us.

Operator

Ladies and gentlemen, thank you for participating in today's conference. This concludes our program for today. You may all disconnect and have a wonderful day.

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