
MANAGEMENT DISCUSSION SECTION

Operator: Good day, ladies and gentlemen and welcome to the Third Quarter 2009 Harris Interactive Earnings Conference Call. My name is Melanie and I'll be your coordinator today. At this time, all participants are in listen-only mode. We will conduct a question-and-answer session at the end of this conference. [Operator Instructions].

As a note today's call is being recorded. I would like to turn the call over to, Mr. Mike Burns, Vice President, Investor Relations and External Reporting. Please proceed, sir.

Michael T. Burns, Vice President, Investor Relations and External Reporting

Thank you, good afternoon and thank you for joining us to discuss Harris Interactive third quarter 2009 financial results. With me today are Ms Kimberly Till, President and Chief Executive Officer and Ms. Deborah Rieger-Paganis, Interim Chief Financial Officer.

The format for today's call will include formal remarks by both Kimberly and Deb on the state of the business, and our third quarter performance. After the formal remarks Kimberly and Deb will be available for questions.

A webcast replay of this entire call will be accessible via the Investor Relations section of our corporate website later this evening and will be archived there for at least 30 days. However, no telephone replay of this call will be provided. We will post the transcript of this call as soon as practicable after the call.

We would like to take this opportunity to remind you that certain statements made during this conference call are forward-looking statements for purposes of the Safe Harbor provision under the Private Securities Litigation Reform Act of 1995. These statements includes beliefs, predictions and expectations related to the company's future financial performance, other business and operating metrics, as well as statements regarding the company's future plans and operation.

They involve a number of risks, known and unknown, that could cause actual results, performance or achievements of the company to be materially different from the expectations discussed on this call.

Factors that could cause the company's results to materially differ from the forward-looking statements made today and which are incorporated by reference herein, are more fully described in today's press release as well as the company's SEC filings, particularly including the Risk Factors section.

You are urged to consider these factors carefully in evaluating such forward-looking statements and are cautioned not to place undue reliance on them. The forward-looking statements are only made as of the date of this presentation and the company undertakes no obligation to publicly update them to reflect subsequent events or circumstances.

We also will be discussing non-GAAP financial measures, including adjusted EBITDA and adjusted EBITDA with the add-back of the restructuring and other charges. These items are reconciled to GAAP financial measures in today's press release, and are posted on the company's website.

I would now like to turn the call over to Harris Interactive's President and Chief Executive Officer, Kimberly Till. Kimberly?

Kimberly Till, President and Chief Executive Officer

Thank you, Mike. Good afternoon everyone and thank you for joining us. As you can tell, I have a little bit of a sore throat. So, please bear with me, as I make my remarks. I would like to focus on three things on today's call. First, I will provide brief highlights on the third quarter results and Deb will go into greater detail in her remarks. Second, I will review the significant accomplishments we made during the third quarter, and then third, I will update you on progress we have made on our key strategic initiatives.

We are beginning to reshape Harris Interactive for what, I believe, is a very bright future, and I am excited to bringing you up to date on what has been happening behind the scenes, since we last spoke. So let's begin with some brief financial highlights.

First, it is important to know that we announced earlier today, we have strengthened our financial position by completing the amendment to our credit agreement, which I am especially pleased about, that we were able to do this in very challenging credit environment. The revised terms of the credit agreement provide us with important financial stability and flexibility, as we continue implementing our strategic plan.

With regard to our third quarter revenue, we experienced a 30% decline over the prior year, which we believe was predominantly impacted by the global economic downturn.

This decline in revenue also caused a decline in adjusted EBITDA, with the add-back of restructuring and other charges, which was down as compared with the same period a year ago, but was still positive for the quarter.

I want to be very clear and assure you that returning Harris to revenue growth and profitability remains our top priority.

I would now like to focus on our accomplishments during the third quarter. As I mentioned last fall, we plan to augment our existing talent here at Harris with key hires from both within the market research industry, as well as from other industries. These new hires will bring a fresh approach to delivering insightful and impactful expertise to our clients.

March was a very busy month in executing on our talent strategy. First, we added Stefan Schmelcher, as President of Global Loyalty Solutions across U.S., Canada, Europe and Asia. Stefan brings more than 15 years experience to Harris, and will be primarily responsible for developing and implementing the strategy and plans to significantly grow our global loyalty practice, by emphasizing our new ways of research based insight generation, that provide our clients with practical and actionable advice on how to rely on their go-to-market strategy against their stakeholders expectations.

Also in March, we boosted our technology leadership with the addition of Enzo Micali as Global Executive Vice President of Technology and Operations. Enzo joined Harris with over 20 years of experience, and was most recently at TNS, where he led IT and Operations for North America custom research business as the CIO and EVP of Operations.

I was also excited by our hiring in April of Richard Scionti, as Global Chief Technology Officer. Richard will have responsibility for global technology innovation, including process automation and solutions development.

He will also lead our global efforts in leveraging Social Media. Arun also has joined us, and will be responsible for technology architecture, a key role as we use technology to innovate the market research space. He has held similar positions at GNS and 1-800-FLOWERS.

I am very pleased with the caliber of people we have recruited for our technology and innovation team. They will be responsible for streamlining and automating our workflows, processes and infrastructure, which will provide cost savings, quicker turnaround time, and higher quality deliverables.

This team will collaborate with George Terhanian, our President of Global Solutions, to develop innovative solutions and methodologies for reaching and retaining attractive respondents and for meeting other research needs of our clients and prospects.

We believe that this will have a positive impact on both our revenues and profits.

To round out our global hires, we also brought on board Marc Levin in March as Senior Vice President and General Counsel. An experienced legal talent with industry expertise, Marc is responsible for our worldwide legal affairs. He will also support our business development, strategic planning and new business initiatives, while working closely with our Board of Directors to develop and maintain best practices in corporate governance.

We have also just added Robert Salvoni as MD of Europe. Robert brings both large company and entrepreneurial management experience to his new role. He was the Senior Executive at British Telecom where he undertook a number of general management, sales directorship and CEO roles within the Group. Most recently, he was the Managing Director of IRIS Accountancy Practice Solutions where he delivered significant growth following a management buyout. His proven ability to drive revenue growth and profitability will be an asset to our European businesses.

We also have a strong pipeline of additional candidates for a few key roles. I believe we are building a management team with the industry knowledge, functional expertise and drive to make significant progress on our strategic and financial objectives in the coming months.

With my prior comments about returning the Company to profitability in mind, I would like to review with you the steps we recently took to help align expenses with revenue. Given the macro economic environment, we anticipated there would be an impact on our revenue. We were very proactive and made some difficult and necessary choices during the past six months to help ensure the long-term financial health of the business.

We took certain cost-reduction actions during the second quarter and additional actions during the third quarter, which taken together we expect to yield approximately \$21 million in annualized savings.

While Deb will provide more details on this quarter's restructuring charges, as well as further information on the amended credit facility, in short, we expect that these measures, reducing our annualized expense base and strengthening our financial position, will help us stabilize and streamline the Harris Interactive business model going forward.

Before I turn the call over to Deb, I wanted to say that I am very proud of our team and the tremendous talent we have within the Harris organization. The ability of our team to deliver deep insights to our clients will enable Harris to become a leading provider in the market research industry.

I'll now turn the call over to Deb to provide a more detailed look at the financial performance for the third quarter, and then after Deb's remarks I'll review our progress against our strategic plan.

Deborah Rieger-Paganis, Interim Chief Financial Officer

Thank you, Kimberly. Good afternoon, everyone. I'd like to take you through the financial highlights for the third quarter. On a consolidated basis, our revenues were \$39.9 million, a decrease of \$17.4 million or 30.4% when compared to last year's third quarter. The revenue decline impacted nearly all of our geographic regions and was due in large parts to macroeconomic factors. Foreign currency fluctuations also negatively impacted us by \$4.4 million. This accounted for 25.2% of our decline.

In the U.S., our revenue was down 33% for the quarter. In the U.K., our revenue actually grew by 2% on a local currency basis but was negatively impacted by the foreign exchange conversion resulting in revenues declining by 27% on a U.S. dollar basis.

Revenue in Germany was down 17% local currency and 25% in U.S. dollars. And Canadian revenues fell 25% local currency and 40% after the impact of foreign currency translation.

On a more positive note, our two bright spots are Asia and France. In France, revenues grew 24% on the local currency basis, and 9% on the U.S. dollar basis, compared with the same period last year. This was primarily driven by the growth in the healthcare and consumer industries.

In Asia, our growth of 81% or 76% on a U.S. dollar basis was primarily attributable to new opportunities in the pharmaceutical, telecommunications and hotel industries.

Our bookings for the quarter were \$37.9 million, down 38% from \$61.3 million in the same prior year period. We ended the quarter with a sales backlog of \$56 million, 27% lower than the \$76.9 million we had at the end of the third quarter fiscal 2008.

Similar to our revenues, bookings and backlogs were impacted by macroeconomic factors and foreign exchange rate fluctuation. Foreign exchange rate fluctuations accounted for approximately 6% of each of these declines.

Our selling, general and administrative expenses decreased by more \$5 million during the quarter from prior year levels. However, SG&A was 1.4% higher as a percentage of revenue than last year. Certain of our costs are fixed and they negatively impact our operating expenses as a percentage of revenue, when revenues decline.

As Kimberly noted, we made significant cost reductions in the quarter, but will not realize the full benefit of these reductions until next quarter.

Payroll related expenses in SG&A, were down by \$3.4 million which was driven primarily by the head count reductions taken throughout the year.

Stock based compensation expense has decreased approximately \$700,000 due to the departure of several senior executives from the prior management team.

Travel expense is also down \$600,000 as a result of our continued focus on controlling these costs. And our office rent expense has decreased approximately \$500,000 from space reductions taken during fiscal 2008 and 2009.

At this point, I wanted to highlight some changes that we made in our financial statements presentation relating to SG&A.

Our income statements to the third quarter and current year to-date reflect two changes in presentation that we elected to make.

Firstly, in prior periods, the costs associated with professional staff time that were not directly billable to a client project were reclassified to SG&A. These costs are now included in cost of services, as we believe that this presentation best reflects the true cost of our professional staff. We've reclassified prior period to reflect this change in presentation.

Secondly, we've also elected to include expenses from our selling and marketing efforts in SG&A rather than report a sales and marketing expense line.

As we have streamlined our selling process to place greater emphasis on involving professional staff in our selling efforts, we no longer believe that separately presenting expenses associated with our selling efforts provide meaningful information for investors.

We've reclassified our prior period to reflect this change in presentation.

Our operating loss for the quarter was \$7.3 million, compared to \$1.9 million loss for the third quarter last year. Much of this loss is attributable to the \$5.3 million of charges taken in the quarter relating to our restructuring of the business. We incurred \$3.4 million for severance and other termination benefits related to our U.S. and U.K. reductions in force and senior executive departures.

In March, we reduced our workforce in the U.S. by 92 people, and announced plans to reduce our U.K. workforce by up to 30 people in May.

We incurred \$1.1 million in consulting fees for services rendered in connection with performance improvement initiatives, banks negotiations and in providing interim CFO services. We have other charges of \$900,000 which included \$400,000 related to a note receivable whose flexibility became doubtful during the quarter and \$300,000 in legal fees related to our bank negotiation.

As Kimberly stated we anticipated that these actions will result annualized savings of nearly \$21 million. We encouraged by the positive impact of the cost reduction actions we have implemented to date. However, we'll continue to proactively monitor our costs on an ongoing basis to ensure expenses remain aligned with current revenue expectations.

Our net loss for the quarter was \$6.7 million or \$0.12 per fully diluted share compared with a net loss of \$2.1 million or \$0.04 per diluted share for the same prior year period.

Non-GAAP adjusted EBITDA, which is defined in EBITDA plus stock-based compensation was negative \$4.8 million compared with a positive \$1.6 million for the same period last year.

Non-GAAP adjusted EBITDA with restructuring others charges added back was positive \$500,000 compared with a positive \$3.5 million for the same period last year.

At March 31st, we had cash and marketable securities of \$16.9 million. And our debt was \$24.2 million. We continue to believe that we have sufficient liquidity to meet our current operating needs as well as our debt-to-service requirements.

As Kimberly mentioned earlier, we now have completed the amendment to our credit facility. Some key points of the amendment include prior covenant defaults have been permanently waived and we are again in compliance with the terms of our amended credit agreement. The amendment also includes both the addition and modification of certain definitions, terms, financial covenants and reporting requirements.

The company's credit facilities under the amended credit agreement now consist of its previously existing term loans, which mature September 21, 2012 and a revolving line of credit, which matures July 15, 2010.

A maximum amount of \$5 million is available under the revolving line, and borrowings are subject to certain conditions. The principal amount outstanding under the term loan \$24.2 million at March 31, 2009 and the payment terms of the term loans remain unchanged.

As a result of the amendment, the non-current portion of long-term debt outstanding at March 31st has been reclassified to non-current liabilities.

Given the continued uncertainty, as a result of the macroeconomic conditions for the remainder of fiscal 2009, we do not believe that it's prudent to provide guidance on our full year results.

I'd now like to turn the call back over to Kimberly for an update on strategy. Kimberly?

Kimberly Till, President and Chief Executive Officer

Thank you, Deb. We are continuing to move forward on our four strategic areas of focus. First, we expect to deliver superior client insight and service through the creation of client teams with specialized expertise.

We are leveraging industry and solutions experts to deliver higher levels of expertise to our clients, for example Stefan Schmelcher will play a key role in developing and implementing the strategy impacted surrounding Harris's Loyalty Management Solutions. We are also developing capabilities in areas like brand and communication, and new product development. And we are establishing within Harris an internal center for innovation dedicated to creating the next generation of products and services in a systematic manner.

The second area of focus, which I feel strongly about, is leveraging technology; I believe increasing our use of innovative technology has the potential to substantially impact the future of our business, as well as the products we deliver to our clients.

Working directly with me now to help drive a new technology vision for Harris are Enzo Micali, Richard Scionti and Arun Padmanabhan.

Technology will help us further automate our business and reduce cost, while increasing our efficiency and quality. We also expect to leverage technology to innovate our business, reach hard to find respondents, as well as create new revenue streams.

Finally, our new technology team expects to develop our global technology infrastructure to streamline our worldwide business.

Our third area of focus is creating and growing a seamless global company. We have begun looking at opportunities to strengthen our international presence. I have reached out to our international partner network and plan to strengthen how we partner with them. We are also looking at geographic markets with attractive size and growth, such as China and Japan and we will develop plans for expanding there in the future.

Fourth and final, is the development of new products. We will do this with both internally and through strategic relationships. For example, we just signed a partnership with Clarabridge to launch Harris Interactive Text Analytics. It's a new solution that integrates Clarabridge's text mining capabilities, with our advanced analytics to enable clients to gather insights into customer loyalty and competitive performance.

This is just one example of the types of value-added partnerships we are looking at building going forward. It is through these types of relationships that I believe we can expand our revenue opportunities and deliver incremental insights to our clients.

In closing, I feel very positive about the decisive steps that we've undertaken on the finances of the company. I'm also very pleased with the quality of the people we have been able to retain at the company and recruit from other organizations.

Also, we are making good progress on all aspects of our strategic plan. I fully realize the impact that the economy will continue to have on the market research business in the coming months. We will continue to manage the company in a very proactive manner with the goal of creating a financially strong and strategically well-positioned company for the future.

With that I'll turn it back over to Mike and the operator for questions.

Michael T. Burns, Vice President, Investor Relations and External Reporting

Thank you, Kimberly. We can now open the queue for questions.

QUESTION AND ANSWER SECTION

Operator: Yes sir. [Operator Instructions].

Michael T. Burns, Vice President, Investor Relations and External Reporting

If there are -- are there no questions in the queue?

Operator: Standby. And no sir, I found no questions at this time. I'll turn the call back over to management for any closing remarks.

Michael T. Burns, Vice President, Investor Relations and External Reporting

Thank you very much to everyone for joining us today. We look forward to speaking with you again in August, when we announce our fourth quarter and fiscal year end results.

Operator: Ladies and gentlemen, thank you for your participation in today's conference. That does conclude the presentation. You may disconnect, have a wonderful day.

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