
MANAGEMENT DISCUSSION SECTION

Operator: Good day and welcome to the Harris Interactive First Quarter 2010 Earnings Conference Call. Today's conference is being recorded. At this time, I'd like to turn the conference over to Mr. Michael Burns, Vice President of Investor Relations and External Reporting. Please go ahead.

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

Thank you. Good afternoon and thank you for joining us to discuss Harris Interactive's first quarter fiscal 2010 financial results. With me today are Ms. Kimberly Till, our President and Chief Executive Officer; and Mr. Robert Cox, our Executive Vice President and Chief Financial Officer.

The format for today's call will include formal remarks by both Kimberly and Bob on the state of the business and our first quarter performance. After the formal remarks, Kimberly and Bob 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 provisions under the Private Securities Litigation Reform Act of 1995. These statements include 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 operations. 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 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'll also be discussing non-GAAP financial measures, including adjusted EBITDA and adjusted EBITDA with the add-back of 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 will now 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 and welcome also to our employees who are listening in.

On today's call, I'd like to cover two main areas. First, I'll provide a brief overview of our Q1 fiscal year '10 performance, and then after Bob delivers his remarks on our financial results, I'll update you on the progress we've made to date on our key strategic initiatives.

So, first, turning to our Q1 results. Our first quarter financial performance showed continued trends which I believe clearly demonstrate the positive impact of the proactive decisions we made during fiscal 2009 to realign our cost structure with our revenues. Specifically, we achieved operating income in our U.S. operations of 0.8 million in the first quarter making this the second consecutive quarter in which our U.S. operations have achieved an operating income.

We also generated adjusted EDITDA with the add-back of restructuring and other charges of 2.1 million or 5.3% of revenue as compared with 0.7 million or 1.4% of revenue for the same prior-year period.

And we saw significant improvement in our selling, general and administrative expenses, as a percentage of revenue. They went – we had 39% for last year's first quarter and it went to 33% for this quarter.

As you know, our first quarter has historically been our lowest quarter from a revenue standpoint. We experienced a 23% decline in our consolidated revenues for this year's first quarter compared to the same period a year ago. But to put this in context, it's important to note that we did not begin to see the impact of the global recession on our performance until the second quarter of fiscal 2009. So it is difficult to compare last year's first quarter to the first quarter of this year. Despite this decline, I am pleased with our efforts to rebuild our revenue base and we will continue to focus heavily on this area.

Before I turn the call over to Bob, I want to talk about two recent leadership changes we've made which I believe will have a positive impact on our revenues and profitability.

Art Coles has joined us as the Head of our Health Care business. If Art's name sounds familiar to you this is because he led our practice for Harris earlier in the decade and was responsible for growing it into our single largest industry group at the time. While our health care practice has been impacted by challenges within the industry in recent years, I'm confident in Art's ability to rebuild our health care practice very quickly.

Robert Salvoni, our Managing Director for Europe will now also lead our Asia-Pacific business. Robert has done an excellent job in leading our European business over the past five months and I'm delighted that he will now take on the Asia-Pacific responsibility. He has a strong track record in growing technology-based service businesses and is a motivational leader with strong client relationship development skills. He will be focused on capitalizing on the growth opportunities that exist in our Asia-Pacific business, while growing profitability in that region.

As I look ahead at the remainder of the fiscal year, I am confident that we are on track to deliver on the key strategic initiatives and financial goals that we've set out to accomplish in fiscal year 2010. I will provide a progress update on several of our initiatives after Bob provides us with a more detailed look at the financial performance for the first quarter. Bob?

Robert J. Cox, Executive Vice President, Chief Financial Officer and Treasurer

Thank you, Kimberly, and good afternoon, everyone. I'd like take you through our financial highlights for the first quarter of fiscal 2010.

On a consolidated basis, our revenues were 38.9 million, a decrease of 11.3 million or 23% when compared to last year's first quarter revenue. As Kimberly noted, we did not begin to see the impact of the global recession on our performance until the second quarter of fiscal 2009. So last year's first quarter cannot be directly compared to the first quarter of this year.

Foreign currency fluctuations also negatively impacted us in the quarter by 1.4 million and accounted for 13% of our overall revenue decline. By country, as compared with last year's first quarter; in the U.S., revenue was down 25%; in the U.K., revenue was down 17% in local currency and 29% on a U.S. dollar basis; Canadian revenues fell 16% in local currency and 19% in U.S. dollars; revenue in France was up 35% in local currency and 30% in U.S. dollars; in Germany, revenue was down 19% in local currency and 22% in U.S. dollars; in Asia, revenue was down 15% in U.S. dollars, with de minimis impact from foreign currency translation.

Our bookings for the quarter were 32.7 million, down 25% from 43.5 million in the same period last year. We ended the quarter with secured revenue, formally referred to as backlog of 42.5 million, which was 29.3% lower than the 60.1 million we had at the end of the first quarter of fiscal 2009.

Similar to our revenues, the comparability of bookings and secured revenue were impacted by the timing of the impact of the global recession on our business. For the quarter, foreign exchange rate fluctuations accounted for approximately 14% of the decline in bookings and 22% of the decline in secured revenue.

Our selling, general and administrative expenses decreased by 6.6 million during the quarter when compared with last year's first quarter. SG&A was 33.3% of first quarter revenues compared with 39% of revenues for last year's first quarter. Selling, general and administrative expense was principally impacted by the following: A 3.5 million decrease in payroll related expense driven by head count reductions taken throughout 2009; a \$0.6 million decrease in stock based compensation expense driven by the forfeiture of stock options and restricted stock upon the departure of several senior executives in fiscal 2009; \$0.5 million decrease in travel expense driven by our continued focus on controlling these costs; and a \$0.3 million decrease in office rent driven by space reductions taken during fiscal 2009. These trends in SG&A clearly demonstrate the continuing benefits of the cost reductions we made during the second and third quarters of fiscal 2009.

Our operating loss for the quarter was 0.4 million compared to a \$3.2 million loss for the first quarter of last year. Included in this year's Q1 loss was 0.1 million in restructuring and other charges compared with 0.6 million for the same period last year. Our net loss for the quarter was 0.6 million or \$0.01 per fully diluted share compared with a net loss of 2.3 million or \$0.04 per fully diluted share for the same period last year.

Non-GAAP adjusted EBITDA with restructuring and other charges added back was 2.1 million compared with 0.7 million for the last quarter – last year's first quarter. At September 30, we had cash and marketable securities of 14.4 million and 20.8 million in outstanding debt.

We continue to believe that we have sufficient liquidity to meet our current operating needs as well as to service our – as well as our debt service requirements, and expect to be in compliance with all of our debt covenants, including minimum revenue, total indebtedness to EBITDA, and interest-to-EBITDA coverage ratios throughout the remainder of 2010.

Given the continued uncertainty of the macroeconomic conditions, we do not believe that it is prudent to provide guidance on our results for the remainder of fiscal 2010 at this time. I'll now turn the call back to over to Kimberly for an update on strategy. Kimberly.

Kimberly Till, President and Chief Executive Officer

Thanks, Bob. As I mentioned on our last call, we are making substantial progress on each of the four key elements of our strategy. Let me share some of the key initiatives we are pursuing this year to implement our strategy.

So the first element is to deliver superior expertise in client service. We are developing deeper and more differentiated levels of expertise, such as the creation of a Corporate Reputation Practice, which leverages our Reputation Quotient proprietary product. And we are also profiling our panel to identify environmentally friendly panelists whose views can be explored for deeper insight into this growing market segment.

We are also developing larger, more strategic account relationships, which we think will strengthen our revenue base over time. The second main element of the strategy is leveraging technology internally for efficiencies and externally for product innovation. We are making significant improvements in our workflow processes and systems, including implementing a next generation global panel management system. These efforts should yield attractive cost savings for us.

We are significantly revising our website to create an integrated portal for the general public, our panelists, employees and clients. We expect marketing and panelist management benefits from this effort. We are also increasing our presence on social media sites to raise awareness of our brand and our product offerings. For example, you can now follow us on Twitter at twitter.com/HarrisPoll.

In addition to leveraging technology for internal operational efficiencies, we are also using technology to create a strong pipeline of products and methodologies. For example, we are well along the way in developing a mobile platform for surveying, which can be combined with Internet data collection to reach larger audiences of respondents.

Third element is creating a seamless global infrastructure and expanding in key geographic markets. We are creating a global account program targeting some of the largest purchasers of market research, and coordinating business development worldwide, which should drive incremental revenue.

As I mentioned earlier, we've put Robert Salvoni to manage Asia Pacific. And he will lead our expansion efforts there with a particular focus on China, which is one of the fastest growing market research markets. We've also strengthened and expanded our global partner network. We recently added Global Research Institute in South Korea as a partner. And we are holding client development meetings with them in November to target some of the largest potential clients based in South Korea.

The fourth and final element is product and solutions innovation. In addition to developing a robust pipeline of new products and methodologies, we are also forming strategic relationships with other companies to develop new offerings. We just signed a collaboration agreement with Ideas To Go. They are a leading innovation process consulting firm that specializes in early-stage ideation and concept development using their proprietary panel of creative consumers.

Together with them, we will bring a new dimension of research creativity and rigor to the product development lifecycle process. This will enable our clients to go from a blank sheet of paper to a fully strong pipeline of prioritized ideas.

These are just a few examples of the initiatives we have underway in fiscal year 2010. We have a comprehensive plan in place to drive the four key elements of our strategy and to achieve our financial goals for the year. I'm pleased with the progress we have made thus far and excited about the initiatives we have underway.

So, Mike, why don't I turn the call back over to you?

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

Thank you, Kimberly. Operator, you may now open the queue for questions.

QUESTION AND ANSWER SECTION

Operator : Thank you. [Operator Instructions]. We'll take our first question from Steven Kohl with Mangrove Capital.

<Q – Steven Kohl>: Good afternoon. And first off, Kimberly congratulations on – about your one-year anniversary at the company. I wanted to ask a couple of quick questions. Recognizing we're still in the early innings of the turnaround of the company, I was hoping you could give us a little bit of insight on where the company can return to in terms of sustainable revenue and EBITDA levels.

And I know that you guys, in the near-term have not felt comfortable with the macroeconomic environment to really disclose too much in terms of guidance, albeit there is some of that in the lending agreement, I am not sure how relevant it is, but it gives us some minimum levels, but could you give us an idea on when we might expect to return to kind of the levels that we saw of EBITDA, profitability on margins or absolute levels?

You know even in '08, I think, we did a little over 14 million in EBITDA; and fiscal '07, over 20 million and we had our EBITDA margins approaching 10%, and I commend you on some of the initiatives. I guess I'm just curious, we're in the mid-five's now, obviously, on EBITDA margins. We have the comfort of – when will we have the comfort to be able to see the predictability in this business and then getting back to those levels of profitability.

<A – Kimberly Till>: Yeah. Thank you for the anniversary. Congratulations, it's been a great year. I think we've accomplished a lot. Bob, do you want to address the kind of future [inaudible]?

<A – Robert Cox>: Yeah, sure. Steven, I think that one of the reasons that we're not all together comfortable talking about the way and is indeed because of the microeconomic situation out there, and the fact that some of our large customers are still in the midst of budget crunches as it relates to their marketing research budgets. So, largely speaking until we see the return of those budgets, which we think we've seen a moderate amount of stabilization, they don't seem to be declining at the same rate they might have been previously.

We also haven't necessarily seen the return, so it will be hard to give you a time on those. That said, we are striving everyday here is about rebuilding revenue, and frankly, making sure that that revenue is profitable revenue. And hopefully, you've seen from our last two quarters, with over two million in adjusted EBITDA, in both of those quarters that we are on the right track, but that's about as far as I think we could go on, on giving any more color.

<Q – Steven Kohl>: Let me ask you one follow-up, if I could. I know last quarter you've talked about reinvesting in the business. I think you used the number six million or something is coming to mind. Where are we in terms of spending that money and how will that be determined relative to, to what you see? I know usually the summer quarter is a better quarter, what we expect to see that your spending will also ramp up, or we're not comfortable yet to really ramp the spending of some of those commitments yet?

<A – Robert Cox>: Well, it's a good question, and I'd say, if you put in perspective, we probably invested less than 10% of that amount back into the business thus far. And certainly again as I mentioned, we are very focused on the cost side as it relates to adding – certainly as to adding fixed cost. And so when we see the return of the revenues and when we see our revenue base building, at that point we will begin to add more of those costs. So hopefully that answers your question.

<Q – Steven Kohl>: Very good, I'll pop out and let somebody else ask. Thank you.

<A – Robert Cox>: Thank you very much.

Operator: [Operator Instructions]. At this point there are no questions in the queue, [Operator Instructions]. And we do have a question. We'll go ahead and take our next question from [inaudible].

<Q>: Thanks for the call and congratulations on the quarterly results. I was curious with reference to the prior questioner's enquiry and to echo what he said, could care less about when anything's going to happen, but I'm curious in terms of the essential fundamentals of the industry and your particular business, has there been any impairment from a big picture view, and if there hasn't, one would reasonably assume that if there is an economic return to normality that we would be able to get to those levels of profitability that we saw a couple of years ago. So again, don't really care when it happens, but just curious structurally if the business – if there is reason to believe that the business could return to prior revenue levels and profitability levels without having any discussion whatsoever about when that would happen?

<A – Robert Cox>: So [inaudible], I think the answer to that is, yes. As we've seen companies tighten up on the budget side, they're certainly concerned about what they're getting for their budget dollars that's clear. But I don't know that we've seen any structural changes to the way we do business that would lead us to believe that we couldn't get back to historic EBITDA levels as the market returns. In fact, we talked about leveraging technology. That's certainly one way we could become even more efficient as an organization. So, we are confident that when the market returns that we'll be able to build up that EBITDA line, and frankly, that EBITDA line as a percentage of revenue.

<Q>: Just as a follow-up, are you guys expecting normal seasonality into this fourth quarter – or I am sorry, December quarter?

<A – Robert Cox>: I think, normal is maybe a difficult thing to say, but we are expecting to see the benefits of seasonality that – the summer as we have said is always the slowest quarter in market research. We don't think this year was any different.

<Q>: Okay, thank you very much.

Operator: And we'll take our next question from [inaudible].

<Q>: Can you hear me?

<A – Robert Cox>: Yes, [inaudible].

<Q>: This is [inaudible]. Just a balance sheet and cash flow question; what was your cash flow from operations during the quarter? And also, what was your CapEx?

<A – Robert Cox>: Well, let me dig that one up here quick [inaudible]. So, easy one first, CapEx was \$60,000, and our cash flow from operations was about a negative 2.9 million.

<Q>: 2.9 million, okay. And I'm assuming that your debt pay-down was consistent with your covenants of 1.7 million?

<A – Robert Cox>: It was.

<Q>: Great, thank you.

<A – Robert Cox>: I am sorry [inaudible], hold on.

<Q>: Yes.

<A – Robert Cox>: I'm sorry. The cash used in operations number was negative 1.5 million.

<Q>: Negative 1.5 million. Okay.

<A – Robert Cox>: And CapEx was correct at about \$60,000.

<Q>: Great, thank you very much.

<A – Robert Cox>: Thank you.

Operator: And there are no further questions at this time. I'd like to turn the conference back over to Michael Burns for any closing comments.

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

Okay. Well, thank very much to everyone for joining us today. We look forward to speaking with you again in January when we announce our second quarter fiscal 2010 results.

Operator: This does conclude today's conference call. We thank you for your participation.

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