

FINAL TRANSCRIPT

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TLEO - Q2 2010 Taleo Corporation Earnings Call Q&A Session

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Michael Gregoire

Taleo Corp. - Chairman and CEO

Katy Murray

Taleo Corp. - Executive Vice President and CFO

CONFERENCE CALL PARTICIPANTS

Jovan Matthew

Deutsche Bank - Analyst

Jen Swanson

Morgan Stanley - Analyst

Dave Hasker

JPMorgan - Analyst

Stephanie Withers

Goldman Sachs - Analyst

Brendan Barnicle

Pacific Crest Securities - Analyst

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Feltl and Company - Analyst

Sasa Zorovic

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Michael Nemeroff

Wedbush Morgan Securities - Analyst

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PRESENTATION

Mike Magaro - *Taleo Corp. - Senior Director of Investor Relations*

Thank you, and welcome, everyone to Taleo's second quarter 2010 earnings conference call. This is Mike Magaro, Senior Director of Investor Relations for Taleo

With me on the call today are Mike Gregoire, Taleo's Chairman and Chief Executive Officer, and Katy Murray, Taleo's Chief Financial Officer.

Before we begin, let me remind you that the Company will be discussing GAAP and non-GAAP results to supplement understanding of the Company's financials. A schedule that provides GAAP to non-GAAP reconciliations is available in the press release issued today and also in the Investor section of Taleo's website.

Also as a reminder for everyone, today's discussion contains forward-looking statements, and Taleo's actual results could differ materially [audio gap - lost connection] 10-Q as filed with the SEC on May 7, 2010 which is available through the Investor Relations section of our website at taleo.com or through the SEC's website at sec.gov.



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With that, I will now turn the call over to Mike.

Michael Gregoire - *Taleo Corp. - Chairman and CEO*

Thank you, Mike. Good afternoon.

The second quarter was another record for Taleo. We achieved record application revenue of \$47.9 million and record total revenue of \$56.3 million. Our signed application and services business this quarter grew 24% over Q2 2009. The small and medium-sized business sector saw 55% quarterly growth in new customers. Total RFPs increased 50% year-over-year as well.

Our largest single transaction during the quarter was a multi-million dollar up-sell of performance management to one of the world's largest professional services firms. We are extremely well positioned to meet the need we're seeing from our customers worldwide to deliver better talent management that directly powers their growth and initiatives. I'd like to thank all of our customers, partners and employees for a strong first half of 2010.

And now, I'd like to open it up for Q&A. So, operator, if you could open up the line, that'd be fantastic.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions)

Your first question comes from the line of Thomas Ernst with Deutsche Bank.

Jovan Matthew - *Deutsche Bank - Analyst*

Hi. This is actually [Jovan] on behalf of Tom. Thanks for taking my question. Great quarter, guys.

I think the key takeaway from this quarter, I guess, is what gives you the confidence of macro improvement? What are you hearing in Europe? What are you seeing in recruiting performance management that gives you the confidence to increase investments in 2010?

Michael Gregoire - *Taleo Corp. - Chairman and CEO*

Sure. Actually there's a lot of things that we've triangulated on to give us that kind of confidence.

You know, first and foremost, I had 16 companies reporting today. So, I appreciate everyone taking the time to listen to our call.

But, every single CEO is looking for growth, and if you're looking for growth, it's going to have a dramatic effect on talent and talent management. So, from a macro effect, I think that everyone who runs a company has understood that having the right people in your company has a direct correlation to your ability to grow.

Secondly is our RFP and our pipeline has shown that that growth is absolutely there. And then, all of you can see it in the growth in deferred from the bookings business we had both in Q1 and Q2, and big deals are back. I know SAP reported last night. They reported a number of big deals. Some of our competitors have reported big deals. So, there's an awful lot of business out there with respect to applications as everyone searches for ways to grow and be more efficient.

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With respect to Europe, the second part of your question, Europe is definitely spotty. There are transactions that can be won there, but it is spotty. And you do have to spend more time in the sales cycle helping some of these European businesses feel confident that they have the money to spend, first of all, and you're spending a little bit more time walking them through both the advantages and the cost savings of a talent management system.

Jovan Matthew - *Deutsche Bank - Analyst*

Okay. My next question is when you talk about 20% bookings growth, is that a 2011 number? And given that, do you see applications growing faster than services?

Michael Gregoire - *Taleo Corp. - Chairman and CEO*

Application is obviously growing faster than services. It's always been our business.

The first answer to your question, that's the run rate into 2011.

Jovan Matthew - *Deutsche Bank - Analyst*

Got it. Thanks.

Michael Gregoire - *Taleo Corp. - Chairman and CEO*

Operator, do the next question, please.

Operator

Your next question comes from the line of Adam Holt with Morgan Stanley.

Jen Swanson - *Morgan Stanley - Analyst*

Hi. This is actually Jen Swanson calling in for Adam.

So, we've had two quarters with two multi-million dollar performance management deals close, which is fantastic. Is that how we should think about the potential in performance management? I mean, those are some really big deals that you're closing there. Should we expect to see more of these big deals going forward?

Michael Gregoire - *Taleo Corp. - Chairman and CEO*

Yeah, our pipeline supports that, and we'd like to see more of it, obviously. I'd like to see 10 or 11 per quarter, but we're going to work towards as many as we possibly can.

But, our sweet spot is definitely at the high end of the market. We've got the proven track record in the high end of the market. The performance management system is built on the same platform as recruiting. And as you know, we have 48 of the Fortune 100 in recruiting, and we're driving 40 million plus transactions a day with the highest levels of security.

So, having the ability to scale, and the proven ability to scale, and then layering the application on top of that, I think puts us in a great position to sell at that high a level.

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The other thing that I think is really interesting is we're seeing more customers want the whole idea of recruiting, performance management and compensation on one platform where you can drive analytics and intelligence out of all of those platforms.

And big companies like to do business with one provider that gives them the seamless integration across the board. They really do understand that it's more than just a feature function argument. It's an architectural and future partnership, and we've proven that we can handle those kinds of partnerships by our supporting customers that size over the long haul.

Jen Swanson - *Morgan Stanley - Analyst*

And I just like to follow up on that a little bit. So, we had a big multi-million dollar deal last quarter. We had another one signed this quarter. It sounds like the momentum in the business is really picking up given the level of investment that's going on right now.

When should we think about those investments starting to yield some fruit? And how should we think about it in terms of -- you beat this quarter by about \$500,000. You're raising the guidance by \$1 million, which is directionally great to see, but it does seem a little conservative given the momentum that you're clearly seeing right now. So, how should we reconcile those two items?

Michael Gregoire - *Taleo Corp. - Chairman and CEO*

Well, I think we've always had a track record of providing the best guidance we can and making sure that we can achieve that guidance. So, I don't think there's any reconciliation required.

Maybe, Katy, you might want to add to that?

Katy Murray - *Taleo Corp. - Executive Vice President and CFO*

Yeah, so Jen, I think obviously the fourth quarter has a pretty big uptick given where we set application revenue guidance for the year.

And I want to remind everybody, so back in Q1, we actually signed two large multi-million dollar PM transactions, and one of them specifically regarding Bank of America. We knew that was going to be a little bit later on the deferred side and a little bit later on the revenue side. And that will be coming in, in the fourth quarter, and that will be built out into the ongoing revenue into 2011.

So, I think what you're seeing coming into the fourth quarter is really the opportunity to have all of these deals come through. We're obviously optimistic and looking very -- looking forward to on the third quarter and the opportunity, as Mike said, on the pipeline deal opportunities, and that's really where you're seeing the fourth quarter benefit from that type of activity and momentum, and that'll be going into 2011.

Jen Swanson - *Morgan Stanley - Analyst*

Okay. So, just to -- to just close it out. So, we should think about the multi-million dollar deals that -- B of A started showing up on the balance sheet this quarter, but the real meat of those in terms of revenue should really start rolling in Q4 and '11?

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Katy Murray - Taleo Corp. - Executive Vice President and CFO

And they will because the first two at the beginning of the year, B of A will start coming in, in the fourth quarter, the other deal started coming in this quarter. And then again, the large transaction that we just signed, we'll have the opportunity to hit the fourth quarter as well.

So, really, the fourth quarter again is the culmination. And we always see that in our business that current quarter bookings have some impact on the current quarter, but really just the strong impact is as it continues to build up through the year.

2011 will have a consistent revenue growth and momentum. All deals will be in at that time that we've signed this year.

Jen Swanson - Morgan Stanley - Analyst

Great. Thank you.

Operator

Your next question comes from the line of John DiFucci with JPMorgan.

Dave Hasker - JPMorgan - Analyst

Hi, guys. This is [Dave Hasker], and thanks for taking the question. John's just -- so sorry he couldn't be here.

Guys, as you're looking to invest in the business this year, you've talked about how you think about revenue and the bottom line with EPS. But, how are you thinking about the cash flow this year? I mean, could we potentially see the cash flow decline this year as you invest in the business?

Katy Murray - Taleo Corp. - Executive Vice President and CFO

So, we talked a little bit about this on the second quarter call as well. Cash flow for the first half of the year was strong. I think the second-half momentum will be better than the first half.

Cash flow from operations in 2009 was over \$50 million. And again, we've invested. You can see the increase in our headcount. You can see the increase in expansion around R&D investment. So, it may be slightly down from where it was in 2009. But, really the offset on that is look where the billings and the booking growth have come out of this second half.

And we exited the second quarter with almost 20% billings growth on the application revenue line, not including services. So, I think that you can see that these investments that we're making this year, while possibly a bit of a drag on cash flow a bit coming off of last year, are really setting us up for a strong 2011.

Dave Hasker - JPMorgan - Analyst

And if I could just ask a couple more follow ups.

Katy, you mentioned some commentary on how you think gross margins will trend. It sounds like you have a little more visibility now as you've got the services revenue recognition change a bit behind you. Can you just review that?

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Katy Murray - Taleo Corp. - Executive Vice President and CFO

Absolutely. So, the application margins last quarter did take a bit of a decline. As we talked about last quarter, we had some duplicate expenses related to the build out of our new data center in Chicago. I'm pleased to say that that is up and running and was on time, ahead of schedule, and their costs were a one-time quarterly issue, and there's no longer any drag going into the third quarter on that.

Application margins should return back to the historical average of around 78%. And then, as I've always talked about on the long-term operating model, really looking to get the increased efficiency with this new data center going into 2011 and in 2012 where we can start seeing application margins get back to some of the historical highs getting closer to the 79%, even maybe 80%. That's longer-term model, but in the near term, you're going to see a return to roughly around 78%.

Consulting margins right now are benefiting. As everybody knows, we adopted the new accounting standard at the beginning of the year. Consulting margins were high this last quarter at 22.6%. And you're going to continue to see consulting margins in this range, possibly a bit higher, going into this next quarter as we continue to not only get the benefit of the waterfall with amortized revenue coming in, but we're also starting to see a increase in services revenue that's being delivered in the current quarter.

And as a result we delivered Taleo 10 at the beginning of the year. There's a number of implementations, conversions and all of that activity is building up through this year. And so, consulting revenue and consulting margins will take the benefit. And I think you're going to continue to see that as we go into 2011.

Dave Hasker - JPMorgan - Analyst

Sure. And then just lastly, going back to the -- what you were saying before, playing to the strong 20% billings growth. And I know you guys only talk about this once a year, but can you just maybe give sort of qualitative color on trends you're seeing on the revenue backlog, the off-balance sheet portion?

Katy Murray - Taleo Corp. - Executive Vice President and CFO

We can't give out the exact backlog numbers. You were right, we do give that out at the beginning of the year.

But, what I can say is we saw backlog growth in 2009 coming into this year. And 2009 was a challenging year, so when you're looking at now that we're exiting the second quarter at a 20% billings growth just on the application revenue line, I feel very confident that going into 2011 we're going to see the increase year-over-year gain substantially into the mid-teens and starting to get back to our historical norms, high-teens, and into 2011 back into the 20s.

Dave Hasker - JPMorgan - Analyst

Great. Thanks very much.

Operator

Your next question comes from the line of Stephanie Withers with Goldman Sachs.

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Stephanie Withers - Goldman Sachs - Analyst

Hey, guys. So, you have talked a lot about stepping up --or, I guess, in the prepared remarks -- stepping up investment for growth in the second half of this year.

So, a couple questions. First, where should we expect that investment to go? Will it be directed more toward enterprise, small business or equally distributed to both?

And secondly, should we think of this as just a tactical move to address what's a really hot market right now or should we think about it more as a change in philosophy and how you're thinking about the trade off between growth and profitability?

Michael Gregoire - Taleo Corp. - Chairman and CEO

First, with respect to which business, it's across the board. Both on TB and the enterprise, we'll continue to get more sales headcount and quota-carrying reps.

With respect to whether it's philosophical or tactical, it's kind of both. Seeing the market move as quickly as it has, it's made us take a look at the market and just understand that the best thing for us to do to add the most amount of value (inaudible - background noise) is to take advantage of it, especially now that we have multiple (inaudible).

We have 4,700 customers now. And for us, a lot of the growth is going to be in the customer base over time. So, rethinking how we go to market and the velocity in which we go to market has definitely changed. But, the impetus of that change is seeing the pipeline grow.

I've always said that the most expensive way to hire pipeline -- to build pipeline is to hire quota-carrying reps. You want to be able to time getting the reps onboard as the market moves and be agile. We've never been a company that looks upon hiring a bunch of sales reps one quarter then firing them another quarter. And that just didn't make a whole lot of sense to us. We like to build up our pipeline and build on our business with reps that understand our products and the commitments to customers. And that all shows up in our customer satisfaction rating. It also shows up in our technology footprint.

Katy Murray - Taleo Corp. - Executive Vice President and CFO

And Stephanie, to your question on the operating model end -- and I want to address this from a long-term perspective. Last year we exited on average for 2009 at 13.2%. We obviously showed that we can margin the company. We had a fourth quarter at 16.2%.

The Company is committed to balancing the operating leverage in the model with the opportunity for investment. But, I think, again, when you start looking at our balance sheet and you're looking at the deferred revenue growth sequentially coming out of Q1 and Q2, and the momentum that we're seeing in the market, the right opportunity right now is to make the investments in the business. And you're going to continue to see operating margin expansion as we continue to grow.

Deferred revenue, generating into sales, cash flow, and I think you're going to see the growth in those metrics over the next couple of years.

Stephanie Withers - Goldman Sachs - Analyst

That makes a ton of sense.

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And then, just one more. It looks like the SMB business continues to be really strong. Is that a balance between recruiting and performance and talent management? Are you seeing growth in both there?

And I think one of your competitors may be pulling back a little bit. Are you getting any benefits from that?

Michael Gregoire - *Taleo Corp. - Chairman and CEO*

Obviously, when a competitor exits the market, you definitely get benefit. So, we are getting a little bit of benefit from it. But, more importantly, that's just a -- to your point before -- a philosophy in strategy. If you have had a strategy that's been very successful in recruiting, we're going to do the same thing in performance management.

We went after the very high end of the market in recruiting, and then we started TBE to go after the low end of the market, which really compresses the market. Nobody can be cheaper and more efficient than us at the low end of the market. Nobody can be more effective and have a better platform than us at the high end of the market. And then, we just put the squeeze on and force the competition in the market to a place where we have a little bit more control. We can play with pricing, we can play with packaging, we can play with some of the marketing, and that's worked very well for us in recruiting. We're continuing to do the same thing with respect to performance management.

In recruiting, people abandoned the high end of the market, and that was -- they abandoned the high end of the market, and that pushed them into a situation where the only place that they could really hunt was in the 5,000 to 10,000 to 15,000 employee market, which is unbelievably difficult.

They have the same appetite and complexity of the 50,000 person company, yet they have the budget of a 2,000 to 3,000 person company. And oftentimes they have the sophistication of those types of companies. So, those are the hardest -- that's the hardest market to be -- to margin in.

And what we found is going from this top-bottom approach, both in performance management and recruiting -- and the broader talent management industry is a philosophy of ours, and we think it works very well.

Stephanie Withers - *Goldman Sachs - Analyst*

All right. Thank you very much.

Operator

Your next question comes from the line of Brendan Barnicle with Pacific Crest Securities.

Brendan Barnicle - *Pacific Crest Securities - Analyst*

Thanks, guys. I was just trying to clarify maybe a little on how this is rolling out this year. Looks like Q3's a little lower than where I can sense as Q4's is going higher.

Is it right to think about this in terms of the way we all were modeling the roll up from these big deals? They're just getting -- the recognition of revenue is just really being pushed out to the fourth quarter, which is maybe a little later than what had been modeled, but that's what's sort of driving that on the growth side?



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Katy Murray - Taleo Corp. - Executive Vice President and CFO

Yes, Brendan, I think going out of Q2, and I think I was pretty open about it, the big deals that came in, in Q1, we knew that they would come in and benefit the second half, but predicting the timing was a bit difficult at that time coming out of the first quarter.

I called it out in the prepared remarks that the deferred revenue growth in Q2 did see the benefit of those deals coming out of Q1. So, I think what we're seeing is better visibility around these transactions. The transactions from Q2 will be benefiting the fourth quarter.

And again, while there is a bit of hockey stick and a bit of an uptick in the fourth quarter, I feel very good about where the fourth quarter is and very good about raising the application revenue guidance.

Michael Gregoire - Taleo Corp. - Chairman and CEO

The other thing to help out with that too, Brendan, is, number one, is this is the PM buying season, Q3, Q4. So, you get a little bit of seasonality with respect to Q3, Q4 with that particular product, now that that particular product's having a significant impact to our bookings. Well, we have to take that into account.

And then, Taleo 10, we have a number of referenceable customers in Taleo 10 now, and people want to get the Taleo 10. And that is helping in the marketplace, especially with net new customers. When they see Taleo 10, the user interface, the whole concept of talent intelligence being able to pull analytics from both the performance management system, the compensation system and the recruiting system to give you a full business picture, that's helping accelerate net new sales with net new customers.

So, all of these things together put us in a situation where the gestation period for some of those deals will take us up into the Q4 timeframe. And it's hard to predict that when you're sitting in our shoes looking at a quarter, at 90 days, when is something going to transact, and when will we be able to recognize revenue.

Is that helpful?

Brendan Barnicle - Pacific Crest Securities - Analyst

Yes, that's helpful.

And then, looking at the bookings -- you're talking about exiting this year at 20% bookings. Last year, I think, bookings in Q4 were still down year-over-year. And you, I think, averaged the year at about 4%, and now we're seeing revenue that's growing at about 16%. And I know we've got some puts and takes in there from acquisitions and EITF and whatever, but as we look at this 20 -- exiting at 20% bookings, I mean, that should imply some pretty significant acceleration in revenue growth next year based on what the bookings have done.

Am I interpreting that right?

Michael Gregoire - Taleo Corp. - Chairman and CEO

You are interpreting that correctly.

The other thing you should take into account is my commentary on what we're doing with sales headcount. The sales headcount we're adding today is clearly for 2011, 2012. We're taking a much broader approach to this business, and we definitely want to

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be the dominate force with respect to talent management. And we are putting ourselves in the situation where 2011, 2012 continue to be that kind of growth that we currently see right now.

Brendan Barnicle - *Pacific Crest Securities - Analyst*

Great. And then, Katy, just two quick housekeeping things. With the Chicago data center open now, CapEx drops down to \$2 million a quarter or so, drops pretty dramatically from what it was the last two quarters. Is that right?

Katy Murray - *Taleo Corp. - Executive Vice President and CFO*

Yes, it does. It's going to go back to the historical norms of roughly \$1.5 million to \$2 million. It'll be back -- and again, if we have an opportunity to do something from an internal infrastructure, maybe it'll be right at \$2 million. But, you should expect it to be between \$1.5 million and \$2 million ongoing now.

Brendan Barnicle - *Pacific Crest Securities - Analyst*

And then, did you give us a -- in the prepared comments, I might have missed -- a year-end target for shares outstanding?

Katy Murray - *Taleo Corp. - Executive Vice President and CFO*

I did. Our shares outstanding for the end of the year, basically it'll be 43 million fully diluted for the year.

Brendan Barnicle - *Pacific Crest Securities - Analyst*

Great. Thanks, guys.

Katy Murray - *Taleo Corp. - Executive Vice President and CFO*

Thanks, Brendan.

Operator

Your next question comes from the line of Scott Berg with Feltl and Company.

Scott Berg - *Feltl and Company - Analyst*

Hi, guys. Excellent quarter. Very nice to see.

Katy Murray - *Taleo Corp. - Executive Vice President and CFO*

Thank you, Scott.

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Scott Berg - *Feltl and Company - Analyst*

Yes, two quick questions. First of all, with the return of some stand-alone consulting contracts, it appears that all aspects of the business appear to be very strong right now because to me, that was kind of the last leg to drop that we hadn't seen yet in the first quarter.

But, are there any areas in the business right now that you would still -- that you still feel need some improvements or should our view on the business be that you are hitting on all cylinders?

Michael Gregoire - *Taleo Corp. - Chairman and CEO*

I think, I would say we're hitting on all cylinders. The slowest business to pick up after the 2009 downturn is the training business -- people paying for training. And we're starting to see a little bit of that pick up. But, while everything else is at -- doing very, very well, that seems to be the slowest of multiple well-run businesses.

Scott Berg - *Feltl and Company - Analyst*

Okay.

And I guess my last question at the moment is on the M&A front. You're still sitting with a -- quite a large pile of cash obviously. How does the M&A landscape look, and does it change with Katy's departure here over the next three months because I know that's an area that she was, obviously, very involved with?

Michael Gregoire - *Taleo Corp. - Chairman and CEO*

The landscape has not dramatically changed. I think a lot of vendors that we look at needed to come out of a tough 2009. That was not a -- that was a great buyer's market. It was not a great seller's market.

And I think what they've learned in 2009 is that they got rational to what the value for the companies are really worth. But, at that point, buyers like us, we were probably not as rational as we wanted to be. And I think we're getting to equilibrium where we're going to be able to transact because buyers and sellers are both getting more mature and thoughtful about what valuations should look like. So, I think the environment's definitely improved.

With respect to Katy leaving, it doesn't slow us down or have any impact at all on our ability to transact. We've got a very big and sophisticated deal team. We've bought five companies here. We've got a very strong financial organization. We have the ability to run the kind of models. And all of our transactions are driven from the business, not from the finance team.

Scott Berg - *Feltl and Company - Analyst*

Very good. Thank you.

Operator

Your next question comes from the line of Sasa Zorovic with Janney.

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Sasa Zorovic - *Janney Montgomery Scott - Analyst*

Thank you. So, my question would be specifically regarding the growth versus investment balance that you've been very careful in your expression even today just giving balance and guidance in the past.

Now, why is it now specifically that you're looking to shift a little bit your position in the balance? So, what is it specific about it now that you're looking to shift rather than previously you haven't done it?

Michael Gregoire - *Taleo Corp. - Chairman and CEO*

That's a great question, Sasa.

I still think we're very balanced. It's all about risk management. Spending shareholder dollars on sales and marketing with no return, that doesn't make anybody feel good.

Taking a look at our pipeline growth and our marketing programs and our products and how they're being received in the market and understanding that that pipeline and the market is there, and then pairing that up with the ability to transact, I think that's just the rational way of running a business.

And we're in the situation right now where we've got the pipeline and the momentum, and we need to spend some money on sales professionals to be able to transact.

So, I don't see our philosophy changing. I still think it's important for our company to operate in a constrained environment because I think it forces better decision making. We have a commitment to shareholders to continue to show the leverage of the model. We just may not accelerate that leverage as much as we could.

But, we're making that decision. We know for a fact that we can operate that at a higher operating margin if we want to. We're choosing to go for a little bit more growth, but we're still going to keep a very keen eye on operating margin and cash flows. I think that's just a responsible way of running the business.

Katy Murray - *Taleo Corp. - Executive Vice President and CFO*

And then, Sasa, specifically the investments that we're making -- and we talked about it before -- these are revenue-generating and revenue-accelerating investments. These are not back office. This is specifically around those things that can give momentum around revenue.

So, you're going to see that, whether it's in the R&D line and continued acceleration around products and functionality or in the marketing line and the sales line. You're not going to see it in the general operating line, like G&A.

Sasa Zorovic - *Janney Montgomery Scott - Analyst*

And then, also following up on that, is this something that you're making a decision about regarding this balance for the next couple of quarters or also this is something that maybe is going to be a case tilting more towards growth for the next couple of years or so as you've been talking about positioning for this growth in 2011, 2012?

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Michael Gregoire - *Taleo Corp. - Chairman and CEO*

You've hit it absolutely right on. This is about positioning ourselves to continue to grow in 2011, 2012. And as long as our pipeline continues to increase, and our sales capacity and sales productivity continue to increase, we're going to add professionals and the support infrastructure to make that happen.

The other thing we shouldn't lose sight of here, it's not just about adding sales professionals, but making those sales professionals more productive. That's not something that I'm willing to give up on, either. I think that over time and as we get better understanding of talent management and how this market evolves, I think our sales productivity definitely needs to increase.

We've seen that happen in the past. As we took on more market share with recruiting, our win ratio went up. Part of that had to do with less competition. We will eventually see that again when it comes to performance management and compensation and analytics and onboarding. Those types of products, as we're selling them back into the customer base, I would expect the selling of that to be more efficient than net new client purchases.

Sasa Zorovic - *Janney Montgomery Scott - Analyst*

Thanks. And then, my last question would be in terms of these new deals that you're seeing and adding the sales people for. Is this that you're seeing multi-million dollars coming into the pipeline and so there's a funnel or are you also seeing them go faster through the funnel, so that the sales cycle's getting shorter?

Michael Gregoire - *Taleo Corp. - Chairman and CEO*

No -- Sasa, this is Mike. I wouldn't say the sales cycle is getting any shorter. I think that the velocity of deals coming into the pipeline have increased.

When you're selling a lot of multi-million dollar deals, it's that process just is not built to act any faster than what we typically see.

Sasa Zorovic - *Janney Montgomery Scott - Analyst*

Great. Thank you very much.

Operator

Your next question comes from the line of Michael Nemeroff with Wedbush.

Michael Nemeroff - *Wedbush Morgan Securities - Analyst*

Hey, guys. Thanks for taking my questions.

Just building on the some of the earlier ones, I don't know if you mentioned this in your prepared remarks, but what percent of the bookings in the quarter were recruiting versus performance? And where do you expect that to go maybe over the next couple of quarters? I think, Mike, you had mentioned that performance gets a little bit more popular in the back half of the year.

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Katy Murray - Taleo Corp. - Executive Vice President and CFO

Hi, Michael. We did not break out the percentage of recruiting versus PM in the bookings number. What I'll tell you, though, is I think you can see -- and part of that comes from a number of up-sells. They're closing multi-million dollar deals around PM, so they are gaining momentum. They are becoming more substantial in the overall bookings and in the revenue number.

At this point in time, that's not something we're going to be breaking out because, again, customers are coming in. They're buying multi-product. It's not just PM, it's also compensation with that. But, it has been very, very pleasing from what we're seeing on the momentum around PM and the percentage that it is driving in bookings.

And I would say the other piece of that is we are seeing an increase in the bookings percentage around the up-sell back into the existing install base. It's something we've been focused on, and that has been accelerating as well. And PM and compensation have definitely been driving that.

Michael Nemeroff - Wedbush Morgan Securities - Analyst

Mike, could you give us a sense of what the attach rates have been on the Worldwide Comp product and just give us a status update on that?

Michael Gregoire - Taleo Corp. - Chairman and CEO

Sure. We been selling somewhere between six to 10 deals per quarter. So, if you take a look at last quarter, we did 18 deals. I think two to three of those were combined. So, it's still selling well standalone. And we're pretty happy with how that product is evolving and fitting into the marketplace as well as fitting into the sales force. I think the sales force is definitely getting comfortable selling and marketing that product, and the pipeline is starting to build for it.

Michael Nemeroff - Wedbush Morgan Securities - Analyst

And then, just one last one if I may on the acquisition front. You guys -- you raised a little bit of money, and you've got a healthy balance sheet. Is that still something that you're interested in, and if it is, what kinds of things are you looking for and sizes? Thanks.

Michael Gregoire - Taleo Corp. - Chairman and CEO

Yes. We haven't changed our philosophy in years with respect to acquisitions, and it's always worth repeating, and I always repeat it to our own deal team. We like complete overlap products where we like the customer base, and we just do a discounted cash flow on that customer base and move them over onto the Taleo products. We like those kinds of deals, and any deal that fit that market, regardless of size, we would be definitely interested in.

You know this market as well as anybody, Michael. There's just not a lot of big companies left on the recruiting side that would really take up a lot of our cash.

The second thing we like is deals like Worldwide Comp where there's some unique type of IP where we view the business decision and -- really based on time to market and complexity is, should we build it ourselves or we'd be better off to buy it and integrate it. And we like those types of transactions.

Once again, not a lot of transactions fit the profile that are really large just staying within our core. With respect to staying in our core, we are definitely a software company. We're not a services company. We would move outside our core if we thought

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that talent management wasn't such a wide open space. But, we think talent management still has multiple years of growth. And for us to reinforce our core we think is the best way to add shareholder value through acquisitions.

Michael Nemeroff - *Wedbush Morgan Securities - Analyst*

Thanks for taking my questions.

Operator

Your next question comes from the line of Mark Marcon with R.W. Baird.

Mark Marcon - *R.W. Baird - Analyst*

Thanks for taking my question.

I was wondering if you could talk a little bit about what you're seeing in terms of pricing, both in terms of performance management as well as talent acquisition, particularly now with the RFPs ticking up? It seems like pricing should be getting a little bit better.

Michael Gregoire - *Taleo Corp. - Chairman and CEO*

Yes, pricing has definitely been pretty stable, I think, all through 2009. And this is the difference between mature companies and not. Publicly-traded companies, I think, behave a lot better when it comes to pricing. And I think there's mutual respect among the competitors that nobody wants to be giving their product away or selling their IP in their future and not getting value for it.

So, I think the market is really moving towards the public company competitors. The public company competitors are rational when it comes to pricing. Everybody will pick one deal or two a quarter where they just want to go and really own that piece of business because strategically it works for them or they think if they own that customer they can sell multiple products. But, across the board, I would say that pricing is relatively stable.

Mark Marcon - *R.W. Baird - Analyst*

Right. And, Mike, can you talk a little bit about -- a little more about your vision on business intelligence? You've got a couple of releases coming out. What's going to be incremental to the current suite?

Michael Gregoire - *Taleo Corp. - Chairman and CEO*

Well, first of all, the product itself -- the ability to go across multiple databases and pull intelligence with respect to how you treat your talent is unique only to Taleo. We're the only company in the world that has the ability to do that.

Coupled with that, we have so much data with respect to how talent is being managed on a global basis. There's so much intelligence traffic in the Taleo platform with 48 of the Fortune 100, some of the most respected companies in the world. We can create heuristics and trends for how talent is being managed -- how many succession plans are under management, what is the average performance rating for a particular job set -- and help our customers, through the Knowledge Exchange, understand that data.

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And this is something that's been a long-term vision for us, is to get all of the human capital management strategic data in one place and be able to run true strategic analytics. And it's just now where we're starting to get a number of performance management customers and compensation customers, both in the TBE as well as in the TE market, that we can brush up against that vision.

And I think we have multiple years of being able to push up against this. We have 4,700 customers, and of those 4,700 customers, as you well know, a small fraction of them own multiple products. And for us to be able to dive into that customer base, as well as keep the accelerator on net new, augment that with some smart inorganic growth, I think puts Taleo in a very, very exciting position to be a large meaningful technology company that's solely focused on strategic talent management.

Mark Marcon - *R.W. Baird - Analyst*

That actually sounds like the "holy grail" that a lot of HR directors are looking for.

Michael Gregoire - *Taleo Corp. - Chairman and CEO*

Well, and that's the -- it's one of the things that you have to have the right level of vision and the right level of humbleness when you're talking to some of these HR directors. They know what they want, and they have a very articulate way of trying to get it. But, they've been burned so many times of being promised to get the data warehouse that never shows up. They've been promised so many times to get a strategic HR management system, and what they do is that they get the leftovers after the CFO buys their financial system.

This is a frustrated user base that's looking for a true partner, and I think if we just spend the time listening to them and understanding them, and then use all of the assets that we have -- we have a great R&D center. We spent \$37 million on R&D. We have the ability to build these products, and listening to these customers, I think, gives us a leg up on what is really required to go run modern companies.

Mark Marcon - *R.W. Baird - Analyst*

That's great. And then, just as a follow on to that, can you talk a little bit about the performance management, the big wins that you've gotten because it's all sounding like some of them are clients that have already been using you for recruiting and do have the intention of tying everything in together? In the cases where you've gotten the performance management -- particularly the professional services company you just signed, is that one where there was a system that was displaced or how would you describe that?

Michael Gregoire - *Taleo Corp. - Chairman and CEO*

Every performance management we win, especially at the high end, is a competitive win. It all RFPd. We're going against all the usual suspects, including homegrown systems.

And what they're looking for is a number of different things. If I was to force rank them, number one is they're looking for scale and security. These large companies are not going to partner with a company that does not have the ability to tangibly demonstrate that they can handle the scale and security. This is employee data, this is the bread and butter for their business, and if they don't feel comfortable with it, they're just not going to do it.

Number two is they buy into the edition of the integrated suite. It's very seamless for them to understand that there is transactional HR systems, things that take care of health as well as benefit information, and that's separate from the real strategic-types of



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information that they want to have. There's, "What's going on with my pipeline of employees coming into the company, and what am I doing with those employees from both a performance, succession planning, compensation or career development?"

That's all the strategic stuff, and they want to be able to look at that holistically and be able to look at that and slice it and dice it any way they want to. "Where are we getting good recruits from? Who stays in the company the longest? Who are the people that get the highest ranking in the company? How long did they stay? What countries do a better job of hiring than others? Which managers do a better job of keeping talent than others?" They want to be able to understand all those types of things.

And when we're selling our product, we're selling -- not a vision of that, we're actually showing them that this is how it's done. And when they see that, I think that's what really attracts them to a unified talent management vision.

Mark Marcon - *R.W. Baird - Analyst*

Great. And I think it makes all the sense in the world to ramp up the sales process there.

When we think about the incremental margins going forward, should we think about potentially the back half of this year as kind of a model in terms of how the incremental margins should role out?

Katy Murray - *Taleo Corp. - Executive Vice President and CFO*

Hi, Mark. I think -- right. I think as you're looking at this year, obviously in the prepared remarks, we're committed to delivering an operating margin for the year over 13%. I mentioned earlier, we came out of last year at 13.2%. We're sure that we can leverage this business.

So, as you're looking at the margins coming out for the rest of this year, I think that is a fair way of thinking about it going into 2011. Obviously, with some of the seasonality we always see in some of the quarters, like Q1 -- it's typically a tougher quarter with all the resets.

But, next year we'll continue to show leverage and build off of the momentum coming out of this year. And again, we're committed to the long-term operating model. We're not losing sight that this company can get past the 15% mark, leverage up into the high-teens. But, we're going to take the opportunity to balance the investments as we can if we can see the opportunity for growth on the deferred revenue and the billings side.

Mark Marcon - *R.W. Baird - Analyst*

It does sound like maybe the incremental margins that we're looking at for this year are something which apply to next year, overall, as you continue to ramp up sales and marketing and R&D --.

Katy Murray - *Taleo Corp. - Executive Vice President and CFO*

-- I think that's fair. I think that's fair when you're looking at about 100 to 150 basis points and the like going into next year.

Mark Marcon - *R.W. Baird - Analyst*

Great. Thank you.



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Operator

And, ladies and gentlemen, we have reached the allotted time for our questions today.

I would like to turn the call back to management for closing remarks.

Michael Gregoire - Taleo Corp. - Chairman and CEO

Great. Well, thank you.

In closing, in the quarter we added 225 customers to the largest installed base in the talent management industry, comprised of nearly 4,700 customers in 48 of the Fortune 100.

More and more businesses see the powerful link between talent and growth and are embracing Taleo's unique offering of solutions, service and ecosystem.

We are pleased to be in the position to provide them with talent intelligence to give them more insight into their top talent that drives the growth.

Again, thank you and all of our customers and partners and employees for a great quarter. And thanks for joining our call today.

Operator

Thank you. Ladies and gentlemen, this will conclude today's conference call. You may now disconnect.

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