Axway
2012 Annual Results Presentation

Paris, February 20, 2013

Introduction

Christophe FABRE
Chief Executive Officer

Good day, everyone. Welcome to our presentation of Axway's annual results. The presentation will last about 40 minutes. It will be followed by a questions and answers session. With me are Patrick Donovan, our chief financial officer, and Patrick Gouffran, our company secretary and investor relations manager.

Patrick Donovan and I will conduct this presentation together. He is American and based in Phœnix with me. I will handle the French parts and he the English part. The slides are in English, but we can of course give you all the details. A French translation is available on our website.

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Three parts, starting with our 2012 review; then Patrick Donovan will cover accounts and finances, and I'll finish up proceedings with the third part on strategy.

2012 Review

Christophe FABRE
Chief Executive Officer

Let's begin with our 2012 results, broken down by region of operations. We've adopted a new presentation separating France from the rest of Europe. France is very important, and needs to be looked at in detail. We had a bit of a tough year in France in 2012, especially as our client base was exposed to the financial markets, which posed some difficulties for us. The Americas region – mainly the United States – posted organic growth of 4%, in line with industry trends, while the rest of Europe declined by 1.6% and Asia grew by 10%. We completed our acquisition of Vordel at the end of 2012. These numbers include two months of Vordel's operations. Vordel posted year-on-year growth of 40% in 2012, compared to 2011.

Revenue by sector of operations: our licensing revenue fell by 15%. The first three quarters were very disappointing, with €71.4 million in total revenue. Maintenance, which constitutes a software company's core business, grew by 11.4% year-over-year and saw steady improvement in the average conversion rate of high-value-added contracts per sales proposition. Maintenance cancelation rates were very low, below 10%, which is also very good by industry standards. Lastly, services suffered from a lack of license sales, leading to a shortage of projects, to the extent that we finished the year with negative growth of 1.8%.

We typically post our strongest results in the fourth quarter. We often point this out, but not everyone bears it in mind. However, the fourth quarter is the key quarter for software companies. This is when the nine to twelve months of work pay off. We had a very good fourth quarter, with some variations by country.

The United States grew by 25% in the fourth quarter following comprehensive efforts. We are intensifying the roll-out of our operations. France posted 10% growth, which is a good figure. It's a recovery, but does the fourth quarter point to an underlying trend? No. We benefited from a licensess being unfrozen. Has the situation in France turned the corner? I don't think so. The rest of Europe experienced negative growth of 8.3% during the fourth quarter of 2012. This €1 million difference actually corresponds to a [potential] big contract that we may or may not get, so it doesn't mean much. Asia continued to grow slightly.

In the end, total organic growth reached 10%. The United States continued its positive trajectory, while France experienced a recovery.

Sources of revenue: licensing grew by 14% during the fourth quarter, which accounted for €34 million out of the €71 million [licensing revenue] for the year. In other words, we obtained practically half of our licenses in the fourth quarter, which is typical for a crisis year. The fourth quarter is always strong; it was particularly important in 2012.

Maintenance put up a good performance with nearly 10% growth. Services also improved slightly by 2.6%, but remains a difficult sector. Growth in services will stay tepid as long as our license projects haven't gotten fully under way.

On the macro-economic front, we've often tended to point out that the Unites States market was the same size as France whenever the dollar behaved in a similar fashion to the euro. Since 2012, it seems that the United States has become our principal market, even when taking an unfavorable dollar exchange rate into account, with France accounting for 34% and the rest of Europe 25% of our business.

Operations: recurring maintenance contracts grew by a strong 44%, which is typical for software companies. Licenses grew by 32% and services by 24%.

Some prime examples: Dignity Health is a major contract in the United States, which we were anticipating throughout the year. It's an 8-figure deal worth over $10 million, including licenses, services and maintenance for a 3-year period. Dignity uses Axway's platform to digitize and manage all of their data flows within their ecosystem. It's a really good deal.

We clinched another great deal with a well-known Japanese carmaker, whose name begins with an "H", for a file flow management platform. It's one of the year's highlights in a competitive market. Our business continues to target large companies and their ecosystems.

Swedish customs continue to purchase from Axway. Tullverket is a platform extension. We are continuing to expand our operations with new and extended contracts.

La Banque Postale depends on us and continues to roll out Axway products and services to manage their data flows.

Let's turn now to licenses, which fell by a hefty 15%, and look at some annual metrics. We closed around 2,500 deals over the year, which is 10% less than last year. Our business is often split into three tiers. People begin at level two, or licensing contracts between €50k and €250k. Mass and special contracts go over €250k, [which is] tier-1. Tier-3 is made up of contract extensions below €50k, such as the repurchase of a protocol or a small software package to link a subsidiary.

Our priority is tier-1, because it drives everything. Our biggest gains come from our biggest clients. Tier-1 typically has relatively few clients, with 2% of the total; but it accounts for over a third of our revenue. Its value dropped sharply in 2012.

Total channel sales were steady at around 15%. The opening of accounts mainly includes new customers, which is a bit misleading, because our new business should also include sales of new products to existing customers. In any case, the opening of pure accounts represented 12%, which is a good figure.

Total aggregates are a bit meaningless. It's better to look at average levels per tier. Tier-2 was steady at around €100k. The average price of tier-1 – large contracts and big projects – was stable at around €550k. Tier-3 was also stable. This shows that prices are not falling drastically. Our prices did not come under pressure. Instead, we didn't have enough opportunities.

A vertical analysis is required to properly complete our review. We made some very good breakthroughs, in the healthcare sector with 26% growth and in the public sector with 15% growth, measured by sales value. In contrast, we had some difficulty in the banking sector, which fell by 30%, although it still accounts for 30% of our business.

In summary, we understand where our problems lie: in France, with tier-1 business and with the banks. Much of it is due to the economic environment.

We acquired slightly more staff in 2012. Our staff levels have been fairly stable over the last five years, with an increase of about 10% for a company that has grown tremendously, which points to gains in productivity.

We record our costs of sales in a different manner to most other publishers, which requires an explanation. Gross margin is 68%. We deduct two elements from revenue - costs of product revenue. This is the difference compared to other publishers. Our costs of product revenue are our support teams and embedded products, to which we add our service costs. Our operational costs are recorded in another line. This therefore gives us a 68% gross margin, when other publishers record an 80% gross margin.In fact, their gross margin levels are more or less the same as ours.

Service revenue came to €54.7 million, against €51.1 million in service costs, resulting in a pretty ordinary margin. Here too, it must be noted that the €51.1 million in service costs contains an investment in cloud capacity. We haven't yet created a separate business unit for cloud-based services. In 2012, we invested in developing a cloud infrastructure that is up to standard. Cloud revenue is coming in slowly. We recorded this revenue under subscriptions.

Expenses by type: our sales and marketing expenses were stable at around 28%. R&D expenses fell slightly to 14.5%, against 15.7% in 2010, with 20% of R&D still going to innovation and 80% to regular maintenance. This 20% is what we need in order to innovate over the long term and [improve our] products and services. We continue to have and to maintain our capacity for innovation. We don’t have large annual investments, but we are making continuous efforts. Our G&A expenses were stable at around 9%.

Lastly, our operating margin fell slightly compared to last year, to 15.6%. However, this was due to negative organic growth of 1.6%. Overall, we showed once again, as in 2009, that we are capable of keeping costs down and generating good margins in years of crisis, without compromising our future business prospects.

Accounts and finances

Patrick DONOVAN
Chief Financial Officer

As Christophe mentioned earlier, our revenue for 2012 was EUR224 million. Our profit from operating activities was EUR35 million, which was quite stable compared with 2011 and if you restate 2011 at constant currency between 2011 and 2012, our operating result would have been EUR15.7 million for 2011 versus EUR15.6 million for 2012. This is quite stable and it shows that we were able to control costs for 2012 to protect the margin.

For 2012, we had the full-year effect of our stock option and free share plans issued in late 2011 and 2012. We also had a small increase in our amortization to the acquisition of Vordel and our other income and expense represents acquisition charges in 2012 versus mostly spin-off costs for 2011. For 2012, our net result was EUR24.7 million versus EUR21.5 million for 2012, representing a 15% increase year over year. Our basic earnings per share for 2012 was EUR1.22 per share versus EUR1.2 for the prior year.

On our balance sheet, we have EUR377 million of total assets versus EUR304 million for 2011. Our increases in 2012 mainly relate to the goodwill and intangible assets picked up in the Vordel acquisition as well as an increase in our trade receivables for a strong Quarter 4 (Q4) business, which left a lot of the sales in our receivables balance. Our cash - Treasury - at the end of 2012 is EUR35 million.

In our liabilities, we picked up EUR40 million of bank debt and our bank credit line used to finance the Vordel acquisition. There is not really much change to our equity section except for what is coming from the profit for the year. It is right to point out that 2011 was the year of our spin-off and we had a lot of activity and equity relating to our spin-off in that year.

As regards our cash flow, we generated EUR11.7 million of cash for the year and we can see the impact of the loan and investment activity on the Vordel acquisition. With our trade receivables increasing at year end, our *besoin en fonds de roulement* (BFR) - working capital - was EUR-10.8 million for the year.

Our bank covenants are solid and we have the ability to use the rest of bank credit lines within our current bank covenants. We had no change in our shareholder structure, which is quite stable. We had EUR20.3 million in shares outstanding at the end of the year.

Strategy

Christophe FABRE
Chief Financial Officer

Thank you, Patrick. In terms of position and strategy, it is good to look back at the project and see if we are still on track and what we need to do to deliver. The aim is to achieve USD500 million as soon as possible and here we are talking about 2015, although taking the economy into account, it might be 2016. However, the key point is that if you have looked at the numbers, you will have seen that 2010, 2011 and 2012 in terms of licenses have been a bit flat and that is what we have to change, and we have worked on that a lot.

We had a turning point from 2003-2005. We created Synchrony, which gave us the first version of our software platform. The computing industry changed drastically between 2010 and 2012. In a way, it's time for Axway to adapt in order to get back to growth, without changing our core business.

The macro-economic horizon isn't all that cheerful. The Eurozone is expected to decline by 0.1% in 2013. France is more or less at this level. The United States is growing at 2% and emerging markets at single digits. To reach our objectives, we need to achieve 10% organic growth year after year on cruising speed. This means that we have to outperform the market.

Regarding IT spending proper, Gartner is looking at 4.2% for next year. We're already closer than what happened in 2012.

In terms of middleware, which is our software sector, Gartner anticipates average growth of 7.5% in a segment worth $27 billion in total. This offers us a market space.

Our services typically cover data exchanges and data flows, traditionally between a company's staff, clients and service partners. In 2012, we initiated change with Vordel, which will allow us to take into account the trend towards mobile data flows. Information systems are increasingly being accessed via mobile devices; this is bringing about a technological revolution.

More and more software is being accessed via the cloud. Information therefore needs to circulate between the internal information system and the external part. We're also asked from time to time to put platforms and software in the cloud; in other words, to put our own infrastructure in the cloud. This process is currently fully underway.

There is a technological revolution happening, to which we are trying to respond with Vordel: the rise of APIs [application programming interface]. What is an API? Seventy percent of Twitter interactions go through APIs, from machine to machine. These APIs are like a kind of socket one can plug into to retrieve certain types of data. For example, a bank can use a socket to retrieve an account balance. These sockets obviously need to be extremely secure in order to control who can plug into them and what and how much information they can access. These APIs make it possible to outsource previously in-house services, in a completely B2B context.

Blackhawk Network is a typical example of a Vordel customer. They are the people who make prepaid gift cards, for instance with €50 preloaded or €50 to spend on iTunes or the Apple store. Blackhawk Network is one of the industry leaders in the United States, managing one billion cards per year. Managing these cards requires being connected. Transactions on iTunes or the Apple Store have to pass through an API. Some sites reconnect to other sites via APIs. Mobile applications use APIs to retrieve information from their partners' information systems. It's a revolution.

A mobile phone is not very complicated. Mobile applications are very simple. However, thousands of mobile phones can be accessing an information system at a given moment. For example, a bank's API server has mechanisms in place to prevent normal back-office systems from collapsing under the weight of these extra data flows. These API servers keep data in memory. They are also capable of providing access to millions of mobile phones at the same time.

The main thing to remember is that APIs are a real revolution at the frontier of the company in managing the rise of mobile phones and the cloud. Before, applications were accessed via a PC interface. Now, this is no longer the case. Every chief information officer is saying that the first goal is to make applications accessible from a mobile phone or tablet. An API server is needed to manage the load and make it secure. It's the trend.

What's more, it doesn't only involve mobile phones. A car is also a mobile device. When you use the emergency system or the new [driver] assistance systems, your car behaves like a mobile device. The methods of consuming information made available by APIs are increasing exponentially.

These data flows benefit Axway, because our core business revolves around managing them. Since this acquisition, we are the only company capable of offering a service managing all of these data flows in a single platform. Management is the key element. Whatever format the information is provided in, chief information officers and business lines want to work with a partner offering a comprehensive platform. It doesn't matter if information is consumed on a mobile phone, the cloud or a traditional laptop: they want a partner that provides all of the information to manage these data flows at the frontier of the company. It's huge, and it's really where we are headed as a company.

One has to see the other side of the coin: there's the defensive aspect of managing security, but there's also an offensive aspect. The Axway platform makes innovation possible; it offers the capacity to make any information available, whatever its format or volume, for any consumer at any time, on the cloud or from mobile devices. With Axway, it's possible to design these data flows, or in other words, to define and connect them. It's also possible to control and analyze them, and ultimately reduce costs and improve services.

Yesterday, we announced the new version of this suite, which will include Vordel's components. The latest version of our software platform is called Axway 5 Suite. It really is the first platform to allow all data flows to be managed together. It includes Vordel and Axway components. It manages them better than before, and it manages some new ones as well. Vordel enables us to branch out into mobile and cloud computing. This platform-5 includes other innovations, which are the fruit of two or three years of R&D investment. The entire suite is available in API. We have better analytics. We have new dashboards that can monitor data flows so that CIOs can access their business metrics on their mobile devices. We have a new generation of File Transfer and lots of new features.

This strengthens our market position. In the middleware sector, you have the general software companies – Oracle, IBM, and SAP – that offer middleware to everyone. Then you have the specialists like Informatica, Software AG, TIBCO, GXS and Axway. Each of these specialists focuses on an area it's better at than the others, such as data integration in the case of Informatica, process management for Software AG, real-time for TIBCO, traditional B2B for GXS and data flow management for Axway. We also have competitors that are "niche players". Apart from Seeburger, Ipswitch, Liaison, Opentext and Metastorm, there are also API vendors such as Layer 7, Apigee and Mashery. In this competitive environment, we are still the only ones to have all the data flows in one single platform. The niche players do not have the whole platform and the big players don't specialize in platform software. We always try to have a distinct advantage in order to give large companies that little bit extra. We operate in a different segment than the other specialists.

All of this allows us to confirm our goal of reaching $500 million. We are capable of protecting our margins in a difficult environment. Last year, we adapted our vision by formalizing our strategy of “governing the flow of data”. By integrating cloud and mobile computing, we are really putting ourselves in a position to benefit from the new economic drivers. Today, the problems of CIO lie in connecting mobile devices and managing the cloud. We weren’t really in this market before – now we are.

Other than our new Axway 5 Suite product, which will service our fleet, and the acquisition of Vordel, we’ve worked hard to reinforce our management structures with individuals who have already worked in the tier of $500 million or more.

Guidance: the climate for 2013 is uncertain. The outlook for France, Europe and the FSI is not very encouraging, yet a large part of our business is concentrated in those markets. An IDC survey conducted on IT managers in France concluded that there was an 82% chance that spending would grow in 2013, but I tend to think there is an 85% chance that spending will fall. This has an important effect on guidance: France certainly did record an excellent Q4 2012, but there’s no guarantee that 2013 will be a very easy year.

We are continuing our transformation. We are integrating Vordel and continuing to invest in the cloud so that we can take advantage of it at any given moment. We are also able to make new acquisitions to complete our suite or develop distribution networks. I hope this transformation will bear fruits fairly quickly, but it could take some time. All of this leads us to be cautious in our guidance: we should be able to achieve a slight increase in development, with slightly positive growth, while maintaining our margin levels.

The first steps are encouraging. The Q1 PIPE is good; very good, even. Nonetheless, 50% of licenses were made in Q4. We will therefore remain cautious on that aspect this year.

I am now ready to take your questions.

Société Générale

After your performance in 2012, what kind of maintenance growth rates are you expecting in 2013? Is there still any upside in terms of contract upgrades? What impact will the negative license sales growth in 2012 have on the growth rate in 2013?

What was Vordel’s contribution to revenue in 2012? What are your forecasts for 2013?

Finally, your ASP [average selling price] is stable. Is that not a sign that your cross-selling strategy is difficult to implement and that you are struggling to sell several products to one client at the same time?

Christophe FABRE

We recorded very good maintenance growth in 2012, driven by very low cancellation rates and an increase in the average rate of new contracts. We should have a strong rate in 2013, but lower than in 2012. We really recorded a very good improvement in the average conversion rate.

Vordel grew by 40% in 2012 compared to 2011, whether as part or outside of Axway. We expect good growth in that aspect in 2013.

We therefore have two very positive elements, maintenance and Vordel, but we haven’t forgotten that we have nine months to build a sales pack. If the European climate stays depressed, it could impact the numbers.

Société Générale

My question related to Vordel’s precise contribution to your revenue in 2012, as well as your expectations for 2013.

Christophe FABRE

We integrated two months of Vordel's operations. It slightly reduced growth, with a few extra tenths of a percentage point on our margin. Vordel did not impact Q4. It was the rest of Axway that generated organic growth.

I haven't looked at the numbers for ASP. I don't know if it would rise if we were to cross-sell. We want more tier-1 business. I don't think we have an ASP problem. We will focus on closing more tier-1 deals.

Kepler

Could you quantify the synergies in revenue and expected costs with Vordel in 2013 and 2014?

Have you observed a new aggressiveness on the part of your competitors, especially IBM or niche players?

Christophe FABRE

Our first problem is to get back to growth. We've got a good handle on our margins. With Vordel, we need to take advantage of this emerging sector to sell more API servers and close deals across the globe. These are direct synergies with API servers and platforms. We're really looking to grow. The impact on margins will be limited.

Regarding competition, we haven't seen an offensive from IBM on MFT [managed file transfer] or B2B, and they're not in a position to move into API servers. They're oriented towards SOA governance with Data Power instead.

There isn't much competition in API servers yet. There are very few players. The main ones are Layer 7, Mashery and Apigee. There's enough space in the market for us to not really be in competition. We think that having integrated Vordel into our Axway 5 platform will give us an advantage. Providing APIs is all very well, but the back-office needs to be connected for the service to be provided automatically. That's the basic problem. We have the advantage of being an old hand at integration. We've also got something to say about Open API – APIs that are open to partner communities. In view of the strength of our R&D, we hope to deliver more than the others.

CIC Securities

Have you seen a change in the way you sell your products? Do you have more SaaS?

Christophe FABRE

When we talk about the cloud, we're selling tools to exchange cloud data on premise or between clouds; or customers ask us to sell them solutions in the cloud. It doesn't usually begin with the cloud, but with customers wanting to manage their data flows. Our business model has not changed. We're still into value sales. We're not active in the cloud itself. If there's a gold rush, we sell the shovels. We're not gold prospectors.

We'll need more indirect sales to reach $500 million, even if 15% is already good. However, we'll need to use system integrators more. Vordel gives us an opportunity to connect the dots. Many large customers are asking themselves how they can make the most of APIs. System integrators such as Sopra might be interested in working with us to offer value and take a position on the market. We're working on it.

Unidentified participant

How do you see the bank-finance client segment? 2012 was a fairly complicated year. Do you expect a turning point, a stabilization or more negative growth in 2013?

Christophe FABRE

It all depends on the region in question. FSI PIPEs in the United States are looking good for 2013, with some nice tier-1 contracts that include API servers. Our PIPEs don't look great in France. We don't see new FSI opportunities in Europe. I don't know if that will change in 2013. Instead, we see opportunities in the government sector in the United States, in healthcare and in supply chains, which are B2B consumers.

Sycomore

You've already been asked a question on Vordel, but the information must be confidential, since you didn't answer it. What is Vordel's annual revenue?

Christophe FABRE

That information is publicly available. Vordel made €8.5 million in revenues in 2011 and €11.9 million in 2012.

Société Générale

What is the difference between a cloud integration broker and an API server? ESB [enterprise service bus] vendors can connect a cloud application or an information system in the cloud to the customer's back-office on premise. Does a customer have to choose one or the other solution?

Additionally, I'd like to understand your mobile product offering, which is already well served by SAP, Sybase, Software AG and IBM in particular. What sets you apart?

Lastly, could you advise the contribution of cloud-based services to your annual revenue in 2012, and your expectations for 2013?

Christophe FABRE

Forrester just released an excellent report on the difference between API and SOA. Basically, API is at the edge of the company. It aims to connect something that needs to be controlled. In contrast, an SOA platform is internal. There's no identity check. There's no authorization, no identity management. An API server can offer identity management because there has to be an authorization. It's also possible to limit the number of calls a partner [application can make], for example per hour. That's really the difference between A2A [application to application] and B2B.

Moreover, one has to be able to respond to the growth of mobile computing, which requires REST [representational state transfer] architectures, which are the opposite extreme of ESB architectures. There's no state management. The server doesn't keep track of what happened before. SOA architectures are absolutely not made to manage B2B, which is where API servers come in.

One has pretty much everything with an API server and ESB, but why should one go back to an ESB after an API and before a mainframe? One may as well integrate directly. In general, one has to spend at least €500k for the smallest project with TIBCO and Software AG, and the customers end up telling themselves that it's useless, since Vordel and some good Axway [data] connectors offer the same thing for much cheaper.

The mobility aspect goes back to the old story between applications and middleware. SAP has an end-to-end application. There's not much need to put anything in the middle, except that most clients have their own mobile applications. We're not saying that we're going to branch out into all mobile solutions, but as soon as a customer wants to have their own solution, they'll install architecture with an API server to manage their security and volumes. So it's not an offering to counter service applications. I even think that service applications will have to integrate an API server to make them open.

Lastly, cloud-based revenue in 2012 was in line with our expectations, at around €5 million. Cloud-based revenue is growing little by little. It's generally a matter of multi-year contracts.

Unidentified participant

Are other external growth outlooks possible in 2013?

Christophe FABRE

Yes. Nothing has been put forward yet, but we are working to either strengthen our products and services, or to bolster our distribution networks. We don't have anything to announce over the short-term.

Unidentified participant

What tax rate can we expect?

Patrick DONOVAN

In 2012, we were able to release another EUR4.4 million of tax losses that we have put a valuation amount on in the US. As we continue to have profitable operations in the US, we are able to release this valuation amount and we were therefore able to recover EUR4 million this year, which reduces our effective tax rate.

From the floor

What about 2013?

Patrick DONOVAN

For 2013, we have a total of EUR45 million available, with the reserve against it not activated, and EUR38 million of that is in the US. Therefore our ability to forecast profitability in the US allows to release the amount.

Christophe FABRE

In conclusion, please note that as far as the mobile sector is concerned, we are a middleware specialist. We are not targeting the overall mobile market, which is much bigger than us. We have a good solution for data flow management.

Thank you very much.

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