iSOFT H1 FY10 Presentation Transcript

Sydney – Tuesday, 16 February 2010 – iSOFT Group Limited (ASX: ISF) – Australia's largest listed health information technology company released the transcript of the H1 FY10 presentation held at the company's Sydney offices at 10:30AM AEDT today.

Gary Cohen, Executive Chairman & CEO

This morning I release our results for the first half FY 2010.

H1 Key Themes

Our Revenue was $237m and EBITDA of $40.8m. This result should be viewed in the light of a significant currency translation effect on revenue and earnings when compared to H1 of FY09. You may recall that over half of our revenue is in UK pounds and a further quarter is in euros.

The substantial drop (up to 40% in GBP, and up to 28% in Euro) in these two currencies vis-a-vis the Australian dollar has meant that we have reported a lower revenue and earnings when these amounts are translated back to Australian dollars.

Whilst most of these operations are naturally hedged (except our Indian operation where we fix the Indian rupee to the British pound using forward contracts) there is a lower amount of overhead recovery of our corporate costs resulting in a lower margin over the previous corresponding period. The presentation provides a good degree of transparency as to the effect of currency translation on our results.

Notwithstanding the currency and some margin erosion from the phasing of National Programme milestone revenues in the first half compared to Full Year 2009, each of the main business segments performed according, or ahead, of their budgets in their local currency. The exception to this was the ANZ, and Asian, Middle East and African segments, which represented 17% of total revenue.

Our Core business – excluding the National Programme contract, generates 80% of our revenue. We have seen significant growth in our core business. In particular, the UKI business (excluding the National Programme) grew 11% year-on-year.

The Non-National Programme backlog – or accumulated orders where we haven't booked revenue – has grown by 48% compared to the previous corresponding period. This is based on the growth that we are experiencing in most of our markets, building on the confidence of our customers in iSOFT and our solutions, and gaining more market share from the competition.

We also have sought to bring greater visibility to our revenue under the National Programme contract. In December we signed a new agreement with CSC. And although we will see some drop in revenue from the National Programme contract, with CSC compared to the previous corresponding period we are confident of offsetting this with more profitable opportunities to sell product to CSC as well as direct to the NHS Trusts.

Based on what I've just told you, our guidance for the full year is that we expect this year to have overall revenue growth of between 6 – 10% on a constant currency basis, an EBITDA margin of 21- 23%, and this to be split between the two periods by 1/3 versus 2/3.

Although the Global Financial Crisis has affected growth in government expenditure in some of our markets – particularly in ANZ and the Asia Middle East and Africa segments – we are seeing very encouraging signs of changes to that position.

In Australia, where Health Reform is very much on the Federal Government Agenda and the Health Reform Commission has advocated the adoption of electronic health records, we have seen the early signs of the Government preparing the foundations for e-health with the legislation for patient unique identifiers.

In Europe, China and Latin America we expect our market share to continue to grow as health IT spending outperforms the general market.

However, the major growth driver is the US$34 billion stimulus investment in Healthcare IT. This will lead to the reshaping and the transformation of the US Healthcare IT market, as well as most likley lead to the rest of the world playing catch up.

I will explain later why iSOFT is able to benefit from this major government spending initiative and how we can leverage from the significant investment we have made in Lorenzo and the associated solutions.

H1 Key Financials

Our revenue of $237 million was 1% down on the previous corresponding period when compared on a constant currency basis. EBITDA of $40.8 million was 27% down on a year ago on constant currency basis, whilst Underlying Net Profit After tax (which is NPAT with tax-affected amortisation intangibles on acquisition added back) was only down 9%.

Leaving aside currency impact, the recognition of a milestone under the National programme in H1 distorts the comparison and the phasing of the revenue and earnings between the H1 and H2 period.

Backlog

What is especially worth noting is the growth in overall backlog year-on-year – and over $176 million increase in backlog growth (a 48% increase) from our core business (excluding the National Programme contract). This highlights that we are making significant headway of growing our base business rather than just relying on one major contract.

Operations

Turning to our operations, the UKI segment (excluding National Programme) saw significant revenue growth (11% year on year) with a number of new major sales to Hospital Trusts – including Sheffield, Wandsworth and East Cheshire NHS Hospital Trust. iSOFT Business Solutions saw the number of new contracts nearly double.

In the National Programme we had a number of new go-lives for LRC release 1 – where 7 NHS Trusts have now implemented this solution for a part in part of their hospitals. Bury NHS Trust was the first to implement LRC Release 1.9 (an integrated administration and clinical solution) - and this was in a primary care Trust. We are on track with Morecombe Bay to implement LRC 1.9 in a Hospital setting by end of Q1.

In Continental Europe we have seen growth, with 21 new customers – resulting in an increased market share – particularly in Germany. In Latin America we have won good size contracts with hospitals in Dominican Republic and Peru, and being awarded a new State programme in Mexico.

Operations continued

Across the organisation we have achieved success with our deliveries. In Australia we saw a substantial number of go-lives for our Hospital web Pas solution at both Healthscope and St John of God Hospitals across Australia. All of these go lives underpin the growth our recurring maintenance streams – which is currently about 40% of our revenues.

This year we established the iSOFT Academy which has facilitated the knowledge transfer process covering over 50% of our new solutions. We have reshaped the way we have managed some of our product development – moving to agile development to achieve greater efficiencies.

In the half, we have invested in people and resources in the Product management and the CMO organisations – building on our expertise in these areas and the innovation of new products. We have launched a number of new solutions during the half. Some of these are based on the Lorenzo IP – such as Health Studio, Health Intelligence, Vantage Point and Lorenzo Primary Care.

iSOFT Solutions

Health Studio is a development toolkit that enables a healthcare organisation model to develop work flow processes over their existing IT solutions. Health Intelligence enables the management of clinical and financial data across a health care organisation. These two solutions are significant innovations in their own right and we expect that they will provide substantial revenue growth either as standalone solutions or as part of a broader solution offering. Vantage Point is our new user interface that enables the aggregation and presentation of information that the user wants using the latest technologies.

We released other products too. iSOFT Aged Care which is designed as a new generation solution for Aged and Community Care facilities. We see the aged care and community area an important growth market as the push to treat chronic illness and the push to lower the overall costs of care mean that more care is being done in home and the community.

We also have increased our portfolio with new solutions we acquired including Viaduct – an integration engine and the AIMS solution designed to manage adverse medical events in the hospital.

The CMO organisation has also started to look at ways we can leverage our solution and clinical presence in the life sciences area. This group focuses on working with CRO's (clinical research organisations) and pharma companies to enable bringing drugs to the market faster as well as helping with the management of the clinical trial process.

Marketing

Another area in which we have invested is the iSOFT brand and associated marketing efforts. We have a new WebSIte (to be launched in March 2010). We are making significant use of Social media and have our own iSOFT channel on You Tube. Also we created Ideaworks for Healthcare which was successfully attended by over 200 leading Healthcare IT personnel in the UK in October and is now being followed by many on the iDeaworks for Healthcare web site and on twitter.

UKI and National Programme

As there are a number of uncertainties and potential opportunities regarding the National Programme, and we have decided to provide you with some information that will help you more fully understand the issues.

UKI-NPfIT Revenue Split

First, the UKI segment today represents about 55% of our total revenue. Excluding the National Programme the UK revenue was $82m up from $74m on the pcp (constant currency). The National Programme revenue represented 37.5% of UK Revenue and has become less significant to group revenues than during the pcp.

UKI-NPfIT Contracts

The National Programme is a £12 billion programme to modernise the NHS through a major IT programme. iSOFT with its Lorenzo solution was awarded three of the five regions. This contract, all now with CSC, was executed in 2004 and covers the period to 2016. iSOFT was responsible for developing and maintaining its solutions whilst CSC was responsible for installing and servicing the NHS trusts and managing the delivery over a data centre.

In June 2007, prior to the acquisition of iSOFT plc, CSC and iSOFT agreed on a new risk sharing model. CSC agreed to be responsible for the development of the solutions and iSOFT agreed to make 750 personnel available to CSC for a period up until April 2010. CSC would accept the risk under its contract with the NHS and iSOFT was to be paid a fixed fee together with milestone payments tied to software releases.

In March 2008 a further agreement was entered into with CSC whereby CSC agreed to second additional personnel from iSOFT on a cost-plus basis. Today an additional 600 personnel are working for CSC on this basis.

In December 2009 a new agreement was entered into to extend the agreements until 2012 and to simplify the rates and the basis of the cost sharing under the June 07 and the March 08 agreements. The milestone arrangements remained untouched.

UKI-NPfIT Table

As you can see from the table we are forecasting that total revenue from the National Programme Contract with CSC, as it currently stands will deliver $90m of revenue for FY10 compared to $106m for the pcp.

NPfIT Market Update

Now let's turn to look at the current changes that are being mooted in the UK. First, the NHS has commenced negotiations with CSC and iSOFT to reshape the deliverables under the programme. Whilst there is currently a lot of speculation about the extent of that reshaping – there is currently no agreement in place. Although we expect that this will be concluded in the coming weeks. However, we feel relatively confident that despite some of the rumours to the contrary, much of the clinical functionality of Lorenzo for hospitals will still be required.

In the Southern Region, which was originally allocated to Fujitsu with a Cerner solution, this region has now been opened up to competition as the Trusts will be funded directly by the National Programme. The NHS has advised that solutions that are to be procured must comply with all the standards that the NHS has previously set out for operating across the Spine. iSoft has over 50% of NHS Hospital Trusts with its solutions in the South.

In the London and Southern Regions seven major hospital Trusts (iSOFT 7) have elected to opt out of the Cerner solution and to remain with iSOFT and seek an upgrade path from iSOFT.

What are the risks and opportunities?

The table sets out our view here. Simply put as we own the IP to Lorenzo we can use the solution in the UK I outside the contracted solution to CSC to sell directly to NHS Trusts (or via a partner). Further, if the programme gets re-scoped additional modules can be supplied by us for additional revenue. Moreover the opportunities outside the UK are becoming very significant and we have now the ability to use much of the developed product today to sell into these markets.

It is this area of major growth where I would like to spend some time talking to you. I will do that after our Finance Director, Martin Deda takes us through the financials in some detail.

Martin Deda, Group Finance Director

Martin: Thank you Gary

Ladies and Gentlemen the following slides give details of our financial results. As the exchange rates of the groups main currencies have varied materially to the prior corresponding period, we show H1 09 in both the reported exchange rates and at constant rates to H1 10.

Financial Highlights

The currency translation impact of $34m on Revenue and $12m on EBITDA can be seen on this slide. Underlying NPAT did not have the flow through effect of the lower margin due to National Programme phasing as this was compensated for by material lower financing costs through the repayment of the OCP Loan in H2 09 and lower LIBOR in the current period.

Cash at the end of the period was much higher than in the corresponding prior period, due to significant receipts from CSC and effects of the refinancing of the bank facility.

Operating Cash Flow was negative as per H1 last year and we expect this to be significantly positive in H2 as was the trend in FY 09. Days sales outstanding improved over the period, based on the continuing focus on collections within the group.

Revenue Mix

Adjusting for the phasing effect of the National Programme revenues, Licence revenue was flat at constant currency. Implementation revenues grew through more project work. Maintenance and support revenues, which represent the recurring revenue base, also grew.

Segment Results

As can be seen from the 4D, Group costs increased period to period. This was primarily due increased spend in Marketing to drive growth, increased Management, Administration and Facilities costs reflecting the requirements of managing a global business and increased business development costs due to the effect of now having to expense acquisition costs per the accounting standards. Had Group costs been at FY09 levels, the Continental Europe and LA EBITDA would have been approximately $13m and the margin 19% which reflects the underlying strong performance of this segment. The margin impact in ANZ is due primarily to the lower revenue and increased cost base to be able to deliver to the expected Federal Healthcare reform agenda.

Research and Development

At constant currency we increased our R&D spend by $15.8m compared to H1 09. $7.7m of this increase was capitalized and represents the investment in new releases of existing products as well as the development of new solutions including Health Studio, Vantage Point, Health Intelligence and Lorenzo Primary Care as described by Gary earlier in the presentation. Of the $41.6m R&D spend that was expensed, approximately $5m was for Research and the remainder was expenses related to the CSC contract as well as to project and maintenance and support revenues across the business segments

Cash Flow Analysis

As indicated to the market, operating cash flow in H1 10 at $12.1m negative trended as per H1 09. Investment Cash flow has $11.5m higher than in the same period last year at constant currency, and this negative free cash flow was funded through the bank facility and proceeds from the issue of shares. We expect operating Cash flow in H2 to be significantly positive as per the trend in H2 09.

Balance Sheet (statement of Financial Position)

Borrowings have reduced materially from December 2008, predominately through the repayment of the OCP Debt and repayment of Contract funding. The refinancing of the Facility and extension of the term has reduced the level of current borrowings. The significant reduction in the value of intangible assets is due to the translation effect of the exchange rate movements as the intangible assets are carried in GBP, Euro and AUD.

Refinanced debt facility

We refinanced our existing facility effective on 30 December 2009. We had significant take-up and had to scale back the syndicate as the funds offered were higher than our requirement. The syndicate has become more international with KfW, a German Bank, Banco Santander a Spanish Bank and Bank of Ireland joining better reflecting our geographic coverage. Clydesdale/Yorkshire (wholly owned by NAB) joined Westpac as the Australian contingent.

The main changes to the terms are the extension of the term to 30 June 2013 and the removal of GBP25m cancellations in the Revolving facility.

The facility remains in GBP to provide a natural hedge to our cash flows used to service the Debt.

I now pass you back to Gary

Gary Cohen

The Global Health IT Market

The global Health IT market for software and services is about US$30 billion p.a. of which US comprises a 50% market share. Whilst we see some solid growth from our core markets, particularly UKI, Continental Europe, China and Latin America – we see that some markets will take longer before the opportunities are realised. In our opinion it is likely that Australia will follow the lead of others in this area.

US: Changing Dynamics

On the other hand the US have allocated an additional $34 Billion to Healthcare IT over the next two to three years. This will see US Healthcare accounting for 66% of global demand and also increase growth by nearly 100% each year for the next two years.

The ARRA (stimulus package) will put $34 billion into the areas of interoperability and driving clinical quality improvements. Further the shape of the market is changing. There is a shift from fee for service to fee for performance. There is a need for information sharing across the healthcare providers. There will be greater pressure on the system if universal coverage is afforded (Health Reform Bill). What is particularly interesting is that many existing US vendors do not have open systems, are based on dated technology and a number of them will struggle to meet the requirements of this new model.

This is why we see the US as a significant growth opportunity.

iSOFT US Platform

We have already a market entry position with our Bridge Forward acquisition. Further we have strengthened the office with additional personnel, new recruits and transfers from our UK office. We have rebranded the US company.

iSOFT Solutions

Moreover our solutions have been designed in an environment where exchange of information and sharing of data across health networks is fundamental. This is the world of socialised health care found in many of our markets. This is where the US is moving towards.

We have some particularly valuable solutions that are “US ready” in this regard - particularly Viaduct, Health Intelligence and Health Studio. We will release over the next few months our “Health Information Exchange” solution. We will be announcing this and previewing this at the US HIMSS show in Atlanta in March ’10. Further, Lorenzo clinical will once adapted to the US market meet the “meaningful use” criteria required for Electronic Health Records and Clinical systems.

Whilst not wanting to overstate the US opportunity we do see that this will start a major additional growth phase of our business over the next couple of years.

Outlook

If you restate our FY 2009 results in constant currency you see that our Revenue would have been $470m and EBITDA would be $113m.

We are providing guidance that based on the same exchange rates the growth in revenue will be around $500 - $520m (6%- 10%).

We expect EBITDA margins to be 21% -23% , which takes into account an expected one off charge of $7m to be used to rationalise some of the operations and facilitate our US market entry

We expect H2 operating cash to be substantially positive and to trend similar to 2009.

We also expect to pay a full year dividend.

Thank you

End of release

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About iSOFT Group

iSOFT Group Limited (ASX: ISF) is the largest health information technology company listed on the Australian Securities Exchange, and among the world's biggest providers of advanced application solutions in modern healthcare economies.

iSOFT works with healthcare professionals to design and build software applications that answer all of the difficult questions posed by today's healthcare delivery challenges. Our solutions act as a catalyst for change, supporting free exchange of critical information across diverse care settings and participating organisations.

Today, more than 13,000 provider organisations in about 40 countries use iSOFT's solutions to manage patient information and drive improvements in their core processes. The group's sustainable development is delivered through careful planning, in-depth analysis of the market, and anticipation of our clients' evolving requirements. Our business is driven by the collective talent, experience and commitment of more than 4,700 specialists, including more than 2,700 technology and development professionals.

A global network of iSOFT subsidiaries, supported by an extensive partner network, provides substantial experience of national healthcare markets. As a result, we offer our clients comprehensive knowledge of local market requirements in terms of culture, language, working practices, regulation and organizational structure.

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