FINAL TRANSCRIPT

Thomson StreetEvents℠

LWSN - Q4 2008 Lawson Software, Inc. Earnings Conference Call

Event Date/Time: Jul. 10. 2008 / 4:30PM ET

CORPORATE PARTICIPANTS

Barbara Doyle
Lawson Software - VP IR

Harry Debes
Lawson Software - President, CEO

Rob Schriesheim
Lawson Software - EVP, CFO

CONFERENCE CALL PARTICIPANTS

Alan Cooke
Merrill Lynch - Analyst

Nanden Umlauty
Deutsche Bank - Analyst

Steve Koenig
KeyBanc Capital - Analyst

Donovan Gow
American Technology Research - Analyst

Richard Williams
Cross Research - Analyst

Peter Goldmacher
Cowen and Company - Analyst

Mark Schappel
Benchmark - Analyst

PRESENTATION

Operator

Welcome and thank you for standing by. (OPERATOR INSTRUCTIONS). Today's conference is being recorded. If you have any objections you may disconnect at this time. Now I would like to turn the meeting over your host, Ms. Barbara Doyle.

Barbara Doyle - *Lawson Software - VP IR*

Good afternoon to everyone on the call. Welcome to Lawson Software's fiscal 2008 fourth quarter conference call covering the quarter ended May 31, 2008. With me on today's call are Harry Debes, Lawson's President and CEO; Rob Schriesheim, Executive Vice President and CFO; and Stefan Schulz, Senior Vice President of Finance.

Today we will discuss results for our fourth fiscal quarter and for our fiscal year and provide our financial guidance. Then we will open up the call to your questions as the operator described.

I would like to point you to some investors slides that we have prepared that show the trend of the financial progress we have made at Lawson's since 2005. You may find these slides informative, and Rob will refer to them in his remarks. You can find these slides on our Investor website at www.lawson.com/investor.

The slides depict annual results on a non-GAAP basis, which most of you measure, and a reconciliation to U.S. GAAP is included. We have provided a Company estimate of what fiscal 2005 and 2006 would have looked like had Lawson and Intentia been in combined for the full year.

Now let me review our Safe Harbor statement. We would like to remind you that this call will include forward-looking statements, which are subject to risks and uncertainties. These forward-looking statements contain statements of intent, belief, current expectations of Lawson Software and its management. Such forward-looking statements are not guarantees of futures results, and they involve risks and uncertainties that may cause actual results to differ materially from the potential results discussed in our forward-looking statements.

Our SEC filings contain further information about risk factors that could cause actual results to differ from management's expectations. We do not obligate ourselves to update forward-looking statements for circumstances or events that occur in future.

I would also like to remind you that in addition to reporting financial results in accordance with generally accepted accounting principles, Lawson Software reports non-GAAP financial results. A discussion of our use of non-GAAP results, as well as a reconciliation of our non-GAAP results to GAAP, is included in detail in our press release.

With that, let me turn the call over to Harry Debes.

Harry Debes - *Lawson Software - President, CEO*

Good afternoon everyone. I will begin by discussing our fourth quarter revenues and by giving my perspective on progress in fiscal 2008. Rob will then cover highlights of our financial performance, focusing more on the bottom half of the income statement, our cash flows and also guidance. I will then close with some comments on our opportunities in fiscal 2009 and beyond. And then we will open up the call to some questions. So let's begin.

In Q4 I am pleased to report that we had growth in all revenue lines, and the total revenue grew by 9% compared to last year. As far as license contracting and revenue is concerned, last year's Q4 was a very strong quarter, but we knew that we could exceed it, and we did. In the fourth quarter of 2008 we signed more than $51 million of software contracts, the highest quarter for software contracting in the Company's history. You may recall that the previous highest quarter was last year's Q4 when we signed $42 million.

Much of the license revenue from Q4 '08's contracting activity was deferred, and as a result our deferred license revenue balance has grown by 50% year-over-year and now stands at $54.6 million. This deferral has nothing to do with risk associated with the contracts themselves, as the software license fees for many of these deals has already been paid by the customers. The reason for the deferral is that there are specific criteria under U.S. GAAP for recognizing license revenue. And a few of these rules are outlined in our 10-K.

The bottom line is that our customers, new and existing, are buying and paying for more Lawson Software than ever before. For us moving this backlog from the balance sheet into the P&L is now simply a matter of timing, and we should be able to recognize the majority of these deals over the coming year.

Here's the good news. The greater our backlog, the more predictable our future license revenue becomes.

For the full year our license contracting increased 21%. And it was all organic growth, which came about through increased focus and improved sales force productivity. One metric that everyone has been following is our M3 business in the Americas. While in FY '08 we signed $15 million of software in this market, compared to $4 million when we started in FY '06.

Globally we won deals against much larger competitors that we could not have successfully engaged in two years ago. And we built a strong and efficient organization with a deep focus on our targeted verticals. In fiscal 2008 64% of our software sales were in our targeted verticals, and that is up from 40% in fiscal 2007.

The key takeaway here is that despite the economy and despite the competition, we are continuing to grow our software bookings, our license revenues and signed backlog of future license revenue.

Here are some key sales statistics for Q4 that provide perhaps some further insight into the year-over-year license revenue performance. First, you'll recall the Q4 results last year were boosted by about $11 million of Lawson's System Foundation deals. We sold 445 such deals in Q4 '07. In Q4 '08 we sold 162 LSF deals. Fewer because over the course of two years we have now sold LSF to about 70% of the S3 customer base. But as you can see from the results, we more than made up the drop in LSF sales by selling more of our standard application products. Our average selling price per deal in Q4 '08, excluding LSF, was $103,000, and that remained relatively flat year-over-year.

Nearly 30% of our Q4 '08 contracting was with new customers. We added 38 new name accounting in the quarter with an average selling price of $391,000. This is up slightly compared to the average selling price of $388,000 for new deals over the trailing twelve-month period.

Finally, we closed four deals greater than $1 million compared to two deals a year ago, and we signed eight deals between $500,000 and $1 million compared to seven last year.

Now let's move on to maintenance, which is 40% of our total revenue. For the fourth quarter non-GAAP maintenance grew by nearly $11 million year-over-year. That is a 13% increase. That was driven by strong renewals and new software contracts. As a result of moving to our December 31 and May 31 annual renewal cycle for our international and Americas customers, more than 65% of our total maintenance revenue for FY '09 has already been collected. This now allows us to focus on better ways to support our customers during year, rather than continually handling renewals each month.

It was difficult for some people to understand the benefit of this change when we introduced it two years ago, but these results are proof that this was the right decision.

Now I will move on to discuss our consulting services business. Consulting is a significant and extremely important business for Lawson, not only because it represents 45% of our total revenue, but because delivering implementation services directly from Lawson helps to differentiate us from our competition.

We grew our non-GAAP services revenue by 8% in Q4 and also by 8% for the full year. However, as we discussed last quarter we are de-emphasizing services revenue growth in favor of a greater focus on improving the margins from this business. Our objective is to consistently achieve a 20% plus gross margin, and we're making steady progress towards that goal. For example, in Q4 '08 we achieved services margin of 18.4% compared to 11% in the same quarter last year.

So while we have already made real progress, I know that there is still more opportunity for improvement. And here are two specific examples of services margin opportunities. First, in FY '07 we delivered 20,000 billable hours from our Manila facility, and then in FY '08 we delivered 127,000 billable hours. And then in FY '09 we expect to deliver within 230,000 billable hours, or 15% of all hours for Manila. That has already helped and it will continue to improve margins.

The second example in FY '07 we had 7% of our total hours delivered as free work to solve old outstanding customer issues. And then in FY '08 we had just under 5% of our hours as free work. And now in FY '09 we expect to deliver less than 4% of our hours as free work. And that will likewise improve our margins. So I'm just giving you two examples, but opportunities like this for more improvement exists, and we will continue [to hard] to realize those.

Now in addition to delivering on our revenue and earnings guidance, our Company also delivered on our mission, which is to make our customers stronger. We did that by providing customers a richer set of solutions to streamline their business processes, and provided them with a platform for growth. We launched 38 new or enhanced products during the year, with a specific focus on meeting the changing needs of our strategic industries. Here are a few examples.

In FY '08 we released our new Lawson Global Talent Management solution. And that is completely built in our Landmark Application Designer. We released a new Lawson Contract Management solution aimed at the healthcare market, also built with Landmark. We released Trace Engine for the food industry. We released a new version of e-Sales for the wholesale distribution industry. And we delivered our new version of services automation for the services industry.

Furthermore, we acquired VasTech, which added important functionality to our strategic Human Capital Management solution, specifically staff scheduling, which also addresses the unique needs of the healthcare industry. Then we acquired a division of Freeborders, which added product lifecycle capacity -- or capabilities to our fashion solution.

In addition, we provided customers with new technology innovations like Lawson Smart Office, which delivers a consistent user experience and productivity capabilities across all Lawson products. And Process Flow Integrator, which delivers consistent process choreography and integration, once again across all Lawson products.

And then to deliver a superior ownership experience for our customers, we launched Total Care, a series of application management services offerings. And to date we have signed 98 such Total Care deals. Finally, we released QuickStep preconfigured solutions for the food, fashion, healthcare, distribution, government and EAM plant maintenance markets. All designed to reduce the time and effort it takes to implement Lawson solutions, and thereby reduce our customer's total cost of ownership.

These deliverables are not simple updates. They are industry-leading innovations for our customers. And they are investments which will pay off handsomely in the future.

I'm pleased to say that our 400 development resources in Manila made a very significant contribution to our new offerings. Manila now develops and supports 40% of our products.

In summary, I believe we have made significant strides in all areas of our business. We are proud of our revenue and earnings growth in 2008, and of the consistency with which we have delivered on our commitments. We performed well in what has been a turbulent economic environment in the U.S., and we have grown our business substantially in Europe. With very few exceptions, we did everything we said we would do. And I would like the 4,200 professionals -- I would like to thank the 4,200 professionals at Lawson who worked so hard over the past year to make our business a success.

Now I would like to turn the call over to Rob.

Rob Schriesheim - *Lawson Software - EVP, CFO*

Good afternoon everyone. Let me just add a few comments to the press release and follow-on to some of Harry's comments. I will also provide our financial guidance for Q1 and fiscal '09.

Over the last eight quarters we have demonstrated a sound commitment to profitable growth. We have executed this commitment with a dual focus on strategic investments in people, products, customers and infrastructure, while delivering higher margins to the implementation of multiple transformational initiatives. And we have totally transformed the Company along three axes, strategically, operationally, and financially.

Strategically we have, as Harry has said, honed our vertical focus, as proven by our recent wins in the marketplace, with our organic growth rates. Operationally, our offshore hours are ramping up at an increasingly productive Lawson Manila, while our shared service centers and financial process improvements have enhanced our visibility and allowed us to eliminate the material weakness, as you will note, in our 10-K filing.

And financially our margins are improving and our balance sheet remains rock solid. By any measure we have shown improvements in our business while building a strong, sustainable model for growth.

Now let's turn to some financial highlights for Q4 and fiscal '08. Q4 was a very good quarter, with strong software contracting. Non-GAAP EPS of $0.10 was right in line with our guidance range. And total revenues of $233.4 million slightly exceeded the top end of our guidance.

Q4 non-GAAP operating margin was 11.5%, up from 9.9% last year. This was the highest operating margin in eight quarters, since the combination with Intentia in April of 2006. To put Q4 in another perspective, our starting point was a 3% margin in the first quarter post merger, with contracting that was less than half the level of our current fourth quarter. We believe we are on a good trajectory toward a key financial milestone of 15% operating margin within our business framework of building a growth platform with incrementally higher profits.

Revenue growth was the primary reason for the year-over-year increase in operating margin in Q4 and FY '08 in total. Our various offshore actions also resulted in a reduction of approximately $20 million of cost in FY '08, and a runrate reduction in excess of that when we achieve full productivity.

Q4 non-GAAP gross margin of 55% also increased nearly 400 basis points year-over-year. The biggest driver behind this improvement was services, where margin increased from 11% to 18.4% year-over-year. We have made considerable improvement in our services margins, and we anticipate that we can make further improvements in services margins in FY '09. Total operating expenses and other income came in as planned.

Our Q4 non-GAAP effective tax rate was 38%, down from 42% a year ago. Our average non-GAAP effective tax rate for the full year was 39%, down from 47% in 2007. The improvement in the effective tax rate added $0.05 to EPS for the full year, and is a result of a more efficient global structure.

Our Q4 fully diluted share count was 176.5 million shares, a 6% decrease in shares outstanding from the prior year, due to our share repurchase program. We used $106 million of cash to repurchase shares during fiscal 2008, and $160 million to repurchase 10% of our shares outstanding since inception of the program in November of 2006. We also announced today that the Board has authorized a $200 million increase to our buyback plan, giving us $240 million total authorized and available for buybacks.

We anticipate that we will repurchase shares at our discretion when market conditions permit through transactions structured through investment banking institutions, open market purchases, privately negotiated transactions, and/or other mechanisms similar to what we have done previously.

A few points on cash and cash flow. Our cash flow from operations in Q4 increased to $128 million versus $115 million a year ago, driven by maintenance renewals and collections. For the full year our cash flow from operations was $82 million and free cash flow was $59 million for the year. Both right in line with our guidance earlier in the year.

Our cash and cash equivalents balance at the end of May of '08 stood at $489 million. This was only $72 million lower than the May 2007 balance of $560 million, despite our share repurchases of $106 million, about $20 million of acquisitions, and $18 million of decline in fair value of our auction rate securities portfolio.

That brings me to one final note on our auction rate securities, as explained in our press release. Included in our May 2008 cash balance of $489 million was $45 million of investments in illiquid auction rate securities with a par value of $64 million. During FY '08 we have been proactive and transparent in disclosing the decline in fair value of these securities, which have been impacted by the overall global credit market conditions. In total, we took $18 million of impairment charges on these securities recorded as nonoperating losses and others expenses.

Subsequent to May 31 we sold all of our investments in auction rate securities for $45 million of cash. Lawson has no other exposure to auction rate securities. This sale concludes this matter in its entirety, while providing access to another $45 million in liquidity.

Overall we are very pleased with our results for the 12-month period. We are a stronger Company today on any measure that you want to consider. One area in which we did have to adjust our plans was the timing of when we would achieve a 15% operating margin. While we believe the most important thing is to deliver a consistent positive trend line, 15% is nevertheless an important milestone for us. All that being said, we have a dual focus of delivering higher margins while investing for growth, which necessarily requires us to strike a balance. We believe this model provides a sustainable approach to value creation.

As Harry has discussed, our revenues were well in line with our expectations. I will add that we showed year-over-year growth in every line of business, in every quarter in fiscal 2008. Also, we improved non-GAAP operating margin on a full year basis from 7% to 10%. We increased margins while investing in R&D, services, sales, marketing, G&A processes and our facilities in Manila and [Vasance], Switzerland, that have enabled us to grow our business globally.

We are delivering increased profitability through true organic revenue growth, prudent management of all costs, and strategic investments in capacity that provide business efficiencies and enable future growth.

Before I get into guidance, I would like to comment on the slides that Barbara mentioned at the beginning of the call that you can find on our Investor website. I believe they provide good visual context for investors on the progress we have made in revenue growth, operating margin and EPS. These slides show a similar trend, consistent, progressive improvement over the last four years.

Our FY '09 guidance continues the trend. On page 5 of the slides deck in terms of revenues you will see our trend of revenue growth at a 7% CAGR between fiscal '05 and '09. You can also see how the investment in our salesforce in FY '07 began to pay off in FY '08 with a 12% revenue growth in fiscal year '08, which included a 25% year-over-year revenue growth in license fees.

Non-GAAP operating margin, as shown on slide 6, improved from an estimated 3% in FY '05 to 10% in FY '08. That is a real improvement driven by a combination of organic revenue growth and productivity enhancements resulting from our investment programs.

On the last slide, page 7, non-GAAP EPS shows a four-year CAGR greater than 70%, from $0.05 per share in estimated FY '05 to our FY '09 guidance midpoint of $0.45. Not only did our organic revenue growth and improved operating margins help drive EPS, but so did our global tax structure, which we put in place at the end of FY '07.

By any measure we have delivered strong performance at this point in affecting this combination. And we have delivered financial improvements with consistency, following a highly complex business combination and navigating unprecedented events in the credit markets that have affected businesses globally.

Now for guidance. Consistent with prior years we expect to experience a seasonally weak Q1 and a seasonally strong Q4. Our revenues, margins and earnings will follow that same pattern. For Q1 of fiscal '09 we anticipate total revenues will be between $195 million and $200 million. We estimate GAAP EPS in the range of $0.02 to $0.04 per fully diluted share. Non-GAAP EPS is expected to be $0.06 to $0.07, compared with $0.07 in Q1 '08.

This guidance reflects substantially lower other income due to the lower yields on our cash balances in the current interest rate environment. We forecast that net other income will be less than $1 million per quarter in fiscal '09. Year-over-year this impacts EPS by more than $0.01 per share for Q1.

Our estimate of Q1 non-GAAP EPS excludes $8 million of pre-tax expenses related to the amortization of acquisition-related intangibles, amortization of purchase maintenance contracts, stock-based compensation charges, and purchase accounting adjustments for acquired deferred revenue balances.

For fiscal 2009 we anticipate total revenues between $920 million and $925 million. We estimate GAAP EPS in the range of $0.28 to $0.32 per fully diluted share. Non-GAAP EPS is anticipated to be in the range of $0.43 to $0.47.

Lower interest yields will reduce other income by $8 million compared to FY '08, which is $0.03 negative impact to EPS year-over-year. We highlight this decline in other income as we do not believe all analysts have modeled it consistently, and that it could be adding approximately $0.03 to the current consensus EPS for FY '09.

We estimate a fiscal '09 non-GAAP effective tax rate of 36 to 39% for modeling purposes. Our estimate of full year fiscal '09 non-GAAP EPS excludes $36 million of pre-tax expenses related to the amortization of acquisition-related intangibles, amortization of purchase maintenance contracts, stock-based compensation charges, and purchase accounting adjustments for acquired deferred revenue balances.

We also anticipate cash flow from operations will exceed $100 million in fiscal '09. We plan to continue to make investments in our global infrastructure and back office systems and processes in fiscal '09, requiring capital expenditures and investments of approximately $30 million, up from about $23 million in fiscal '08.

Our long-term goal of 17% to 19% operating margin and the near-term milestone of reaching 15% remain very much intact. We have shown solid progress toward these goals, and we expect we can continue to make progress in fiscal '09. We have diversified streams of revenue, of which more than 25% is already backlog. We have a diverse geographic business profile, with 50% of our revenues in the Americas and 50% outside the Americas. We have ample pipeline and opportunity in our targeted customer segments. And our investments in global productivity are beginning to pay off, giving us great confidence in our business.

With that, let me turn the call back over to Harry for some closing comments.

Harry Debes - *Lawson Software - President, CEO*

Rob did mention it in the middle of his comments, but it is worthwhile reminding everyone of Lawson's financial strategy. Our plan is not to grow purely through acquisition. Our plan is not to focus exclusively on revenue growth with hopes that profits will materialize in the future. Our plan is not to cut expenses and minimize investments to achieve purely short-term earnings. Rather our plan is to make the necessary investments which allow us to build a business and a brand that can deliver steady growth in revenue and in earnings over a sustained period. I think the decisions we have taken and our results show that we are already delivering on that strategy.

And now as we focus on FY '09 and beyond, I feel more confident about Lawson's prospects than ever before, primarily because only I and a few other people know the challenges that we faced and overcome during the last two years. Today I can tell you that we are in a much, much stronger position.

There is no longer any doubt about whether the Lawson Intentia combination will succeed. Today the business is a truly combined and financially sound Company. Our product portfolio is richer than ever before, and we are receiving unprecedented recognition from industry analysts for our vision and our execution.

Customers want legitimate choices. And in our target markets, regardless of customer size, we have a better value proposition than SAP, Oracle or Microsoft. And by our actions we have earned the support and respect of our 4,000 customers.

And finally, the most significant investments in our integration, our infrastructure, our offshoring have already been made. And while we still have six months of IT and back office investment to complete in FY '09 and beyond, we will realize a significant return from these initiatives.

The bottom line is that despite a complex combination, despite significant investments, despite competition from much larger rivals, and despite turbulent economic times, we have shown continued and sustained progress. Moving from this point to true world-class financial performance will be a new and different challenge, but with our progress over the last eight quarters and with the assets and resources now at our disposal, I have every confidence that we can successfully continue on that journey.

Operator, that concludes our comments and we're ready to take some questions.

QUESTIONS AND ANSWERS

Operator

(OPERATOR INSTRUCTIONS). Alan Cooke.

Alan Cooke - *Merrill Lynch - Analyst*

You mentioned that the timing of your 15% operating margin goal has been pushed out, because you're investing further in the business. Can you explain or give some more details on what you're investing in specifically?

Harry Debes - *Lawson Software - President, CEO*

I think Rob mentioned it. We're continuing to invest in Manila. We are investing in IT infrastructure, our back office systems, specifically. Those would be our primary investments. And although much of those have been made historically, there's a little bit of work left to do, and I mentioned it in my closing comments. I think we have about six to nine months worth of investments left in those areas before we feel like we are really finished.

Alan Cooke - *Merrill Lynch - Analyst*

Then in terms of your timing for reaching your mid-term goal of 15%, and then your longer-term goal of 17 to 19%, can you give some more details about that?

Rob Schriesheim - *Lawson Software - EVP, CFO*

I think in terms of the longer-term goal we have always been comfortable with a three-year timeframe as far as meeting the 17 to 19% operating margin. As far as the 15% operating margin, it gets a little bit difficult to predict exactly what quarter you are going to hit a particular operating margin, since the operating margins are greatly impacted by things like revenue recognition associated with software accounting and the like.

We clearly think that our operating margin for FY '09 will be significantly higher than what it was for FY '08, which was 10%, which is about a 300 basis point improvement over FY '07.

But in terms of giving you a specific quarter when we might hit 15%, or be above 15%, or be below 15%, we purposely didn't do that, although we did give quite a bit of color on revenues, EPS, other income, cash and capital expenditures.

Harry Debes - *Lawson Software - President, CEO*

I would just add that it is within our grasp.

Alan Cooke - *Merrill Lynch - Analyst*

Thank you.

Harry Debes - *Lawson Software - President, CEO*

We're not asking you to wait two or three years. It is within our grasp. You could do the math here, but we signed a lot of software in Q4. We didn't recognize all of it. We did have the expenses of the selling effort. If we had been able to recognize that in the same quarter, we would have been very darn close to that number. So it is within our grasp.

Alan Cooke - *Merrill Lynch - Analyst*

Then in terms of revenue mix that is behind your guidance for both Q1 and FY '09, can you give us some details on what percentage you expect to get from licenses versus maintenance versus professional services?

Rob Schriesheim - *Lawson Software - EVP, CFO*

I guess, I don't want to get into giving quarter by quarter line item guidance, because we do -- our crystal ball just isn't that (multiple speakers).

Alan Cooke - *Merrill Lynch - Analyst*

Sure. How about through FY '09?

Rob Schriesheim - *Lawson Software - EVP, CFO*

I guess for FY '09 it is certainly a fair question. I will give you that. We gave you guidance for the full year of about $920 million to $925 million for FY '09, which is about 8% growth. As near as I can tell, the analyst average for services is in the range of about 3 to 4%. And I think we're comfortable with that, FY '09 over FY '08.

And for maintenance we grew 13% FY '08 over FY '07. And certainly we won't be at that type of growth rate for FY '09. I looked at analyst averages and I think it is in the high single digits, and we're certainly comfortable with that.

As far as license revenue, again, we grew 25% FY '09 over FY '08. The market rate of growth is about 7%. I think we can do well above the 7%. I believe analysts averages, of the dozen analysts that follow us, show a revenue growth rate of about 13 to 14% on license revenues year-over-year. I would say we're comfortable with that.

I think if you look at it, the revenue mix probably works out to roughly 15% license, 40% maintenance, and 45% services.

Operator

[Nanden Umlauty], Deutsche Bank.

Nanden Umlauty - *Deutsche Bank - Analyst*

Nanden Umlauty, I work with Tom Ernst at Deutsche Bank. A couple of questions on the deal sizes, vis-a-vis the size of the deals. In the context of the macroenvironment are you seeing any kind of delays related to getting these deals signed, because the dynamics of the deal sizes, obviously the deal sizes have grown, but have they -- but the number of deals haven't grown. Are you --?

Harry Debes - *Lawson Software - President, CEO*

Actually the number of deals has grown. It has changed. Remember, last year we did -- if you just take quarter by quarter, last year we did 445 RSF deals. This year in the same quarter we did 162. But we made that up with traditional software applications rather than the LSF initiative, which was a one or two-year initiative and it has pretty much run its course.

Then the big question was, when we closed off last year, well, have you emptied the pipeline? Have you drained all of the opportunities? While LSF has started to dwindle because we have now penetrated that market -- 70% of our customers have acquired it, we have made -- more than made that up with other products.

But to answer your question about macroeconomic environment, which I have been getting every quarter for a year now, and my answer has been the same -- is we're not seeing a slowdown in buying patterns or behavior. We're not selling to banks. We're not selling to homebuilders. The organizations that are buying our solutions are doing so as a long-term investment to make themselves more efficient, to save money, and to get a return.

So the buying cycles are what they are. They take from anywhere from six to 12 months, sometimes 18 months. But all of the news and all the Squawk Box news hasn't been affecting our customer buying cycles.

Nanden Umlauty - *Deutsche Bank - Analyst*

Then a relative question. The size of the deals, the average selling price went up $86,000. Is that an indication of more modules being sold?

Harry Debes - *Lawson Software - President, CEO*

I think we have been saying all along that with greater focus on our vertical targets, customer size doesn't matter. And we have been saying that for almost two years. As you're going to see us selling larger deals to larger organizations as we move up the food chain. And that is what we have been doing. The average selling price for new deals in the fourth quarter moved up marginally. I think it was from 388 to 390 something (multiple speakers). So that is really not a big change, a $3,000 or $4,000 change. And the average selling price of all transactions moved from $102,000 to $103,000, so again that is not a big change.

I wouldn't read too much into that, by the way. I think what you've got to do is look at long-term trends. And we do look at long-term trends. And long-term trends had been the same to slightly up, but nothing significantly up.

Barbara Doyle - *Lawson Software - VP IR*

Those numbers that Harry referred to, the $103,000 versus (inaudible), that differs from what is on our press release because that excludes the category of LSF sales, which had a very big impact, because of a very much lower selling price in average applications. That $103,000 average selling price for Q4 excludes LSF.

Operator

Steve Koenig, KeyBanc Capital.

Steve Koenig - *KeyBanc Capital - Analyst*

Just wondering if you can help us understand a little bit on the licenses that were deferred. This quarter can you give us any sense of either how big the biggest ones were or how concentrated those are in particular deals?

What has to be done to go live on those deals? You said there was really no risk, but what has to be done to get those deals delivered and recognized?

Harry Debes - *Lawson Software - President, CEO*

I think what you're not asking, but what some other people on the call may be asking is why is this happening in the first place? It is happening because -- there many reasons, but there are three major reasons. The first one is that we tend to deliver probably more services with our software than our competitors do. I think some of our competitors, in the case of Microsoft delivers no services, in the case of SAP and Oracle deliver a lot less services.

It is a strategy of our us to in fact be intimately involved with our customer, not just to sell them software. We don't think of ourselves as a software publisher. We think of ourselves as a solutions company, and that involves services. So we have made a conscious decision to be intimately involved with our customers to implement and deliver that software.

The people who make the accounting rules in their wisdom have decided that when you do that then you can't recognize the software. I don't agree with the ruling, but it doesn't matter whether I agree with it or not. Those are the rules and we have to abide by them.

If the services are fixed-price, if there are milestones attached with the projects, if there are enhancements that we do to the product, those all capture the software and then the software gets recognized as a percentage of completion or attached to the particular milestone dates. That is what the consequence are.

We have situations where customers have already paid us the full amount of the software license. And so that is why I said there is no risk to the recognition effort. It is a just a question of now completing the project, the services engagement. Does that help you understand?

Steve Koenig - *KeyBanc Capital - Analyst*

It does. It does. But can you help us understand in the deals that were deferred this quarter, have concentrated are those? Are the largest 20%, 80% of the deferred? How big are those deals getting?

Harry Debes - *Lawson Software - President, CEO*

Some of them are more than $1 million and some of them are a couple of hundred thousand dollars. They are a real range. It depends on the specific customer. I will give you an example. This really happens. A customer has had a very, very bad experience, maybe more than once with a former vendor. Perhaps the project kept going on and on and on and the price tag kept rising, rising, rising. And suddenly the organization says, -- and the project was unsuccessful. So they come to us and say, look, we learnt from our experience. We're not going to engage in an open ended agreement ever again, because has just burnt us too bad. And our Board is adamant that says we must have a fixed-price agreement with a certain timetable, and perhaps even penalty clauses for late delivery.

So we add the appropriate contingencies in it. And you know -- but as we've got confidence in what we're doing, we take those kind of arrangements. That kind of a deal gets automatically captured.

I think if you look at it from a customer's perspective, you can certainly understand why it is important to them to feel like their software vendor is a partner in this transaction with them, and why they're asking for those kind of engagements. And we will accept those kind of engagements. We don't think that they are high-risk. But it does have an impact on software revenue recognition.

Now the other question. Were there any megadeals in Q4 associated with this, no. If there were, we would have called those out to you.

Rob Schriesheim - *Lawson Software - EVP, CFO*

The other thing I would add that Harry has pointed out on several occasions, is that we are growing our deferred revenue balance of our licensees on our balance sheet significantly at the same time that we're also showing very high growth rates in our recognized license revenues.

So even though we showed 25% year-over-year recognized license revenue growth, we grew our deferred revenue balances on our balance sheet from $35 million at the end of Q4 '07 to $54 million at the end of Q4 '08.

And really if you look at a software company, particularly an application software company, where this revenue recognition phenomenon is more prevalent than any other type of software company because of the implementation issues associated with it, the biggest indicator of underlying health is your deferred revenue balance. Certainly one of the biggest indicators. So we've got this revenue already in the bank, so to speak. It is a matter of when it flows off the balance sheet. But is a very good indicator -- a leading indicator of the health of the business.

Harry Debes - *Lawson Software - President, CEO*

All SaaS companies work in this way. Their revenue is all deferred, and it is recognized on a monthly basis over the life of the arrangement. So it is similar to that in some ways.

Operator

Donovan Gow, American Technology Research.

Donovan Gow - *American Technology Research - Analyst*

Nice job on the quarter. Software contracting looked very strong to me. I was wondering if you could talk a little bit about what is driving that growth. Is that sales just performance as the salesforce has ramped? Are you getting into more deals? Are you seeing increased win rates? What is driving that strength there?

Harry Debes - *Lawson Software - President, CEO*

I think it is all the things that you have mentioned. I think first of all, Rob mentioned in his comments that in 2007 we made a big investment in our sales organization. We hired a lot of people and we got rid of some dead wood. We changed some sales leadership. And that -- it takes a little while for the salesforces to really get their feet on the ground, to develop their pipeline, and to start to work the opportunities. I think that you are seeing -- what you are seeing in 2008 for us is the results of that investment is starting to pay off.

I always knew that the market opportunity was there. It was an exercise for us of executing, going out and get it. We had to have a strong story. I think we have a great story. We had to have greater focus, focusing in the verticals in the areas where we really know that our opposition is weak, and we have a great story, great reference, great solution. And we have clearly focused on it.

I mentioned that it is significant that 64, 65% of our software in FY '08 actually came from our targeted verticals. A couple of years ago only 40% came from those targeted verticals. I think is focused. It is disciplined. It is better leadership. Eduardo joined us about almost -- well, nine months ago. I think he has had a big impact. He has taken a lot of pressure off me, that's for sure. I work with him cooperatively, but I think he and the rest of the sales leaders have done a great job. We made some other changes to our sales leadership in September in line with when Eduardo joined. I recognize the guys in Europe who have been a spectacular job for us in the last year. Frank Cohen, the head of European sales has done a wonderful job.

And you know, also our story is becoming a better story. And customers -- frankly customers want choices. How awful would this world be if there were only one or two choices for people in terms of the software industry. They would be held hostage. Some of them have felt like that. They have been held hostage.

So I think the world is actually cheering for Lawson's Software. And I don't think I am overstating that.

Donovan Gow - *American Technology Research - Analyst*

On the M3 growth, you saw very strong growth in fiscal '08. How should we be thinking about not going forward? Was a lot of that just untapped opportunity or do you see similar types of growth rates looking at fiscal '09?

Harry Debes - *Lawson Software - President, CEO*

We're just scratching the service with M3. M3, especially in the Americas, could triple over X number of years. I'm not going to give you a one, two, three-year horizon, but I know that the potential exists because when I was at A.G. Edwards, we had 150 salespeople selling effectively a similar product into the Americas market and driving three or four times as much license revenue every quarter.

I would tell you that the M3 product is a stronger product than A.G. Edwards' product. It is more rich. It is more mature. It is technically stronger. It has got a much better user interface. There's a lot of things that we have as an advantage over both SAP and Oracle. Especially again, as we're not trying to be everything to everyone. We are really zeroing in on target markets where we think we have a competitive advantage. So there is still a lot of growth potential for us there.

Donovan Gow - *American Technology Research - Analyst*

Great. Nice job guys.

Operator

Richard Williams, Cross Research.

Richard Williams - *Cross Research - Analyst*

I just wondered if you could give us a little more color on the different geographies from the perspective of selling conditions?

Harry Debes - *Lawson Software - President, CEO*

Okay. So Europe was a strong -- well, actually it has been strong all year, frankly. I think, with the exception of possibly Q1 of last year where it was a little slow getting started, but then Q2, 3, 4 very strong. And the momentum has continued, and we feel very good about that.

Americas, we got off to a slow start last year in Q1 as well. We did make some changes in the sales leadership at the EVP level and also in some of our business unit areas. And with the changes in the sales leadership and the new initiatives and the new energy that that brought in Q2 we started to really pick up momentum.

I would say that we really haven't seen the kind of slowdown that everybody keeps talking about in the U.S., even though, who knows it could still come. It might still happen. If it happens -- if there is a U.S. wide slowdown in spending, I am sure it will impact us, but honestly we haven't seen it just yet.

In Asia we have been growing. We would like to grow faster there quite frankly. We think that there is still lots of untapped potential. But we have been making progress. We would just like to go a little faster if we could.

Richard Williams - *Cross Research - Analyst*

Also, if you could give us a little bit more in terms of the manufacturing segments?

Harry Debes - *Lawson Software - President, CEO*

For manufacturing there are a couple of -- again, we don't do generic manufacturing. What do we focus on? We focus on fashion. We focus on food. We focus on wholesale distributors. And if you are talking about a generic manufacture, that is not where we -- we don't go there.

Again, if you think about it, we're transforming the business from somebody who used a shotgun to someone who is using a rifle to look after our potential opportunities. We go into market in a vertical way because we have built our solutions to meet needs of certain targeted industries.

So I can speak to you about the fashion industry, which is growing -- the manufacturing of fashion and the retailing of fashion -- which continues to grow. That there is a lot of Asia content in that. And so that was probably our strongest market for Asia. Food is big for us as well. Wholesale distribution is big for us. So those are the markets that we have really made inroads. That is, frankly, where we are concentrating our marketing and development sales efforts.

Operator

Peter Goldmacher, Cowen and Company.

Peter Goldmacher - *Cowen and Company - Analyst*

At your last analyst day you had a presentation on progress, selling licenses through indirect channels, as well as trying to build up a better stable of implementation partners. Can you give us an update on that? And if you can correlate any margin improvement next year, that would be really helpful.

Harry Debes - *Lawson Software - President, CEO*

They have in fact -- that has actually paid off handsomely for us. It has gone up significantly, but albeit from a fairly small number. Last year in FY '07 it was a very small number. And I don't have the exact number at my fingertips in terms -- I think we can get that, and perhaps later I can give you the data. But it did -- I do know for a fact that it grew significantly, I just can't put my finger on the percentage. Quite possibly double -- in that range. But, again, I will tell you it was from a small number.

It was also a year of -- an earlier year of growth. These initiatives took place about a year, year and a half ago. These resellers take a while, just like in AE, to ramp up, to get trained, to develop their pipeline, develop their skill sets, and then to translate potential prospects into customers. But nevertheless in places like the Middle East, in Eastern Europe, in parts of Asia, in Latin America, in all of those regions we had several wins of new accounts in the last year.

Operator

Mark Schappel, Benchmark.

Mark Schappel - *Benchmark - Analyst*

Harry, could you start off by telling me how many sales account executives you ended the fiscal year with?

Harry Debes - *Lawson Software - President, CEO*

Yes, the number on the 31st of May was 206; however, that number went up significantly in the last two weeks of the year. For most of the year we had about 194, 195. So actually we ran for 95% of the year with a headcount in sales slightly lower than what we started with on the 1st of June last year, which was a little disappointing. We are committed to make that up. And while we're not planning to increase headcount by 30 or 40%, you should expect to see us increase our sales resources by about 20%.

This is one of those -- by about 10% I should say. This is one of those trade-off decisions. Right? If we decided -- and you can easily convince me, and I could easily convince you that we should have 300 salespeople. Well, that would mean I would have to increase our sales headcount by 50% over the next 12 months, which I think in the next year would impact -- pay huge dividends.

However, that would mean I would have to answer that 15% question again. And I don't feel like answering that every 12 months. So we're growing slower so we can get past that, and just prove a point. And then we'll go back to making the right kind of long-term investments. So we're going to grow by about probably 10, maybe 15% year-over-year, knowing full well that those new sales heads probably aren't going to be that productive in the first year.

Mark Schappel - *Benchmark - Analyst*

Rob, could you give us an update on where the Company stands with respect to duplicate staffing in Manila?

Rob Schriesheim - *Lawson Software - EVP, CFO*

We are still -- you are revisiting the issue that we talked about last year where we indicated that we would incur a certain level of duplicative staffing for fiscal year '08. It did certainly cost us some money during fiscal year '08. And we still are incurring a level of duplicative staffing in fiscal year '09, just as a matter of course. We haven't talked about the amount of duplicative staffing.

I think the bigger issue for us in FY '09, as Harry has indicated, is we have gone from having something like 340 people to 750 people in Manila. And FY '09 is really not about a focus on increasing the number of people, as much as it is increasing the productivity of the people that we have there. So duplicative staffing in FY '09 rears its head in the form of until we get the people more productive, you've got more people onshore, for example, than you would if the people offshore were more productive.

I can't give you a specific number because we really do manage this. It is difficult to manage on a quarter-to-quarter basis. It is part of an ongoing process. We have been reasonably successful at going from having nothing offshore to having a pretty sizable amount of our hours delivered -- 10% of our hours now delivered offshore.

Barbara Doyle - *Lawson Software - VP IR*

And maybe another way to look at this is, we have saved in our total costs and expenses this year we approximate about $20 million from the productivity and the team in Manila. On a runrate basis we think that can be substantially higher.

Rob Schriesheim - *Lawson Software - EVP, CFO*

We already know that on a runrate basis the $20 million that we saved in FY '08 on a runrate basis in excess of $30 million. I think that there is, again, significantly more opportunely for us. And that was confirmed in both the comments that Harry made and that I made as far as increasing the margins in the services business where our objective is well in excess of 20% gross margins. That is clearly going to come by increasing the productivity in the offshoring capacity that we have.

Operator

There are no further questions.

Harry Debes - *Lawson Software - President, CEO*

All right. Thank you for joining our call today. We feel good about the quarter. We feel good about the year we have had. We're very excited about the year that is ahead of us. We think we have put a lot of the right investments in place. We still have a little left to go. As we have pointed out, there is still a bit of investing left, but I would tell you that is not another 12 or 18 months of investing. We probably have six or nine months of long-term investments to make. And we believe that those investments and the other things that we have done now enable us to go forward much more aggressively and build on the base that we have established.

So thank you for your participation today. We will speak to you at the end of next quarter.

Operator

This concludes today's call. Thank you for participating in the agenda today. You may disconnect at this time. And have a lovely evening.