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Corporate Participants

Sarah Bowman
Guy Dubois
David Arnott
Max Chuard

Presentation

Operator

Thanks for standing by, and welcome to the Temenos 2012 Financial Outlook conference call. At this time all participants are in a listen only mode. There will be a presentation, followed by a question and answer session, at which time if you wish to ask a question you will need to press star and one on your telephone keypad. I must advise you that this conference is being recorded today, Wednesday 14 March 2012.

I’d now like to hand the conference over to your speaker today, Ms Sarah Bowman. Please go ahead.

Sarah Bowman

Hello everyone. Thank you very much for joining the conference call today to discuss the 2012 financial outlook for Temenos.

As you’re aware, following the termination of our recent merger discussions, we’re no longer bound by the UK Takeover Code, so we’re therefore able to provide some forward looking statements for you.

On the call with me today are our CEO, Guy Dubois; CFO, David Arnott; and Max Chuard, Head of Corporate Finance and Investor Relations. You can download the slides for the results presentation from the Investor Relations section of our website. And as usual our prepared
remarks will be followed by some Q&A, and 48 hours from now you’ll be able to download a transcript of the entire call from our website.

Before I hand you over to the speakers I just want to note the legal disclaimer on slide three of the presentation: various factors may cause actual results to differ materially form company estimates, and indeed may cause company estimates to change. Therefore undue reliance should not be placed on the forward looking statements made during this call which reflect the company’s opinions only as of today.

I would now like to hand you over to Guy who will speak about the present market conditions and give our financial outlook.

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**Guy Dubois – CEO**

Thank you Sarah. This is Guy Dubois speaking. And thank you all for taking the time to join us today. As a matter of fact it is good to have you back again. And this time I have no chaperone with me, which is obviously a great thing.

Anyway I wanted to start my section on slide 6 by reminding everyone of the core banking market dynamics. Not only is our market large, growing and openly traded and fragmented, but it is also underpinned by strong structural drivers. The challenges banks face are global; they are more intense in some regions or segments, but they affect all banks. And these challenges are pushing down banks' return on equity, leaving them with a profitability gap. Bank customers are becoming more demanding and less loyal; they can easily compare prices; they have higher expectations than before; and if they don't get either the prices or the services they walk. Funding costs have increased: for instance the percentage of funding banks make available to each other has been falling for decades. Actually it means that banks need all the sources, especially deposits, and competition for deposits pushes up the cost. The banks have to offer a higher interest to secure your savings. As a result of the banking crisis governments want to make banks safer. The most effective way is to make them hold more capital as a buffer to absorb any future losses and write downs. The problem is that holding more capital pushes down the returns on capital overall. And lastly, because banking has been so profitable it has attracted more competition; and more competition has lowered overall profitability because it pushes down prices. So, banks’ return on equity has fallen from let’s say 16% pre-crisis to a normalised rate of about 10% post crisis.
If banks want to improve their return on equity there are only five ways; the beauty of this is always and any way provides investment in technology. So, first you can move into more profitable areas; but you need the ability to move faster than any other competitors, and it requires more technology to launch new products faster, for instance. The second way, well you can improve customer profitability by selling more to your customers; but this requires excellent customer system information, which in turn requires more systems, more good systems. Thirdly you like to manage your risk better and so lower the level of provisioning and so raises revenue for assets. But again, to manage risk better requires high quality real-time information systems. Fourthly, you can exploit economies of scale as you grow; but because banking is a data intensive business the greatest economies of scale will come from managing and processing information more efficiently through having better systems, again. Lastly, banks can cut costs; but the only way to reduce costs sustainably is automation.

So, banks will need to invest in technology to solve their problems; and that is why our market has grown and will grow strongly for the foreseeable future.

I would like to move on slide number seven, and I wanted to speak a bit about market conditions. Well, firstly, as I'm sure you can appreciate, we are not out of the woods yet. The banking market is still experiencing difficulties and it's still impacting our sales cycles. The problems are most acute in Europe; but we know that it is generally taking longer with most deals and particularly to close deals with larger banks. The (unclear) announced by the European Central Bank has eased funding pressure in Europe. But it is a bit of a short-term fix, and we still note a high level of uncertainty among our customers. And as a result banks are still more reluctant than normal to commit to large projects.

In 2011 emerging markets therefore merged better, and we expect the same in 2012, because buying decisions are predicted on growth, the decision cases are much easier to defend. Therefore the strong funnel built in being more consistent is turning into new signings.

In 2011 existing business was also more resilient, and we again expect that to be the case. The fact is that existing deals are smaller in value: they tend to be for products with a short implementation time; they tend to be not competitive. And we know the decision maker.

We always see pressure on pricing, but since the software element of an overall core banking project is smaller we have been able to defend pricing. All of these trends were substantiated by
the IBS league table results. The results show that the market was difficult; the volume of deals was down significantly, while the only region to grow let's say significantly was Asia.

So, in summary conditions remain difficult, but we do observe brighter spots, notably Asia and certain segments like wealth management.

On slide nine I wanted to elaborate on why Temenos is so well placed, both in general terms but also to cope with these difficult conditions. We have a market leading value proposition: our combination of functionally rich open, computerised and packaged software delivers the best return on investment. Our customers enjoy much higher profitability than banks running either legacy systems or systems from other third party vendors. We continue to grow our market lead; we did not jump up the league table of 2011 which measures volumes of deals; but we continue to generate significantly higher licensed revenues than any other player in the market – actually more than twice the level of the number two player. Sales to existing customers proved much more predictable in 2011. As part of our mid-term strategic plan we are targeting higher sales from existing customers to improve predictability, grow revenues and grow margin. We have the largest installed base of any vendor through acquisition and organic development; we now have a wider set of products to sell. So, therefore the opportunity is significant, and we are investing in account managers to develop this. In 2011 we grew like-for-like pricing; this came as a result of firstly price increases and lower discounts. This reflects our market leading value proposition.

Lastly, we are well exposed to fast growing markets; we are the clear market leader in most emerging markets; and we are investing strongly. In addition we are the market leader in private wealth management, which continues to show strong growth in fundamentals. Lastly, we believe our banking business intelligent tool will continue to deliver strong growth.

So, in summary we are well placed both to continue to cope with difficult conditions and also to benefit from any improvement of our markets.

On slide nine I wanted to reiterate our strategic priorities for the business over midterm. To expand our product leadership by continuing to out innovate our competition we deliver the best new applications built on our cutting edge seminal banking framework; to place relentless focus on sales to drive growth, in particular by taking up our licences from private wealth management and retail segments, but from our existing customers as well and from Asia and America. To increase a profitable knowledge led expert services group; no one knows our products like us, therefore it is essential that we continue to provide expert services to our partners and to our customers to ensure they extract maximum value from the software. To continue to strengthen
our partner ecosystem to have the business to scale services and sales. To continue to exploit growth opportunities through creative acquisitions. And lastly to deliver strong and sustained growth in revenues, profit and cash. Our intention is to accentuate our competitive advantages and improve execution to deliver significant growth.

On slide ten I have set out the outlook for 2012. For total revenue we expect growth of between minus 5% and plus 6%, giving an implied rate of 450 and 500 million. In addition in 2012 we set that the slight currency headwind such that for on a like-for-like basis the implied range would be 460 to 510 million. In terms of adjusted EBIT we expect to deliver better margins than in 2011. We give a range from 19% through to 22%; this reflects both a further change in the mix towards measurement which we would expect to be circa 45% at the low end of our range, and it reflects the annualised effect of restructuring carried out in Q4 2011. Lastly, we expect to convert 100% of adjusted EBITDA into adjusted operating cash.

So, in summary we give a fairly broad outlook range for revenues in 2012 to reflect the continued high level of uncertainty about the environment. Whatever the revenue in 2012 we are focused on delivering better margins. Our range runs from 19% to 22%. In the event of coming in at the high end we would release more investment and there would be more variable costs; at the low end of the range investments would be more staggered and there would be less variable pay.

I shall leave David to explain the 2012 (unclear) in more detail.

David Arnott - CFO

Thank you Guy. I really have added a couple more slides here to add a bit of flavour to the outlook that Guy has presented. And I'm starting this on slide 12.

Slide 12 builds a bridge between our 2011 adjusted costs and our 2012 adjusted costs. And you can see on the left-hand side $386 million was our total adjusted costs for 2011. And what I've done here is to split out what I've called variable costs, which are things like sales commissions, third party commissions, which flex with profit. There were no discretionary costs in 2011; discretionary costs being basically bonuses.

So, starting with the 2011 costs excluding variables you can see that from our restructuring plan undertaken in 2011 we've reduced the locked in cost base going in to 2012 by $25 million. And
this takes us to a locked in fixed cost base for 2012, which is the sum of those two, so $341 million.

Building back up from there to 390 million, which if you do the maths on the outlook slide you'll find is the implied adjusted cost at the top end of our outlook cost range, you have two buckets: the first of which is variable costs, and the second is purely discretionary costs. For 2012 discretionary costs can include variable costs that will crystallise if we deliver the year, and also a small level of investment, which we are holding back until we feel comfortable. In variable costs we have sales commissions and third party commissions. And the reason I've split these out like this is to allow you to do your own cost model. Very simply I would say discretionary cost is a balancing figure at the end of the year if we met our numbers; whereas variable cost tends to move semi-linearly with our revenue performance. So, for example if you take the bottom end of our cost outlook for 2012 you will find that it is something like 25, 30 million lower than the 390, which therefore removes all of the discretionary spend and around a third of the variable. So, hopefully laying it out like this will make you comfortable that we're able to protect the margin even at the low end of the revenue range through reducing our fixed cost base early in the year, and leaving ourselves with discretionary investment which we are holding back until we have revenue visibility. In fact if you look at the difference between the 390 and the implied low end cost base you will find that that is quite similar to a number that I'm going to show you on the next page.

So, if you turn now to slide 13 what I've shown here is on the left-hand side 2010 licence revenues and on the right-hand side 2011 licence revenues; and for each of these I've split the revenues into existing customers and new customers; and for new customers split into mature markets – primarily Europe and developing markets. The reason I've split them out like this is to pick up on the trend that Guy has been talking about just a little while ago in that behaviourally existing customers are non-competitive, they've proven the value proposition of buying T24, they tend to be shorter projects with shorter paybacks; and this business has been extremely resilient right through the last downturns, and we expect it to continue to be resilient.

Moving now to new customers, again developing markets, so that's primarily Asia, South America, Middle East and Africa, tend to behave more like existing customers inasmuch as demand is driven by the need to have a quick to market product in areas like private banking, or to meet the demands of a system that needs to expand rapidly to take on new customers. So, again, that behaves more like an existing customer. And the part which is most volatile is the new customers in Europe buying software for the first time – the numbers I've highlighted in red here.
So, for 2010 you can see that that was 22% of total licence revenue; and you can see in 2011 that part, which is by far the most challenging part and the bit that suffered in 2011, was down to 13%. And I think splitting it out like this will help understand that existing customers and developing markets for new customers tend to behave very strongly, and did so throughout 2011; and that therefore the part which is a challenge for us going into 2012 first of all has a quite easy comparative now, it was only 13%, and secondly that 13% is 13% of a licensed revenue number, which is only 35% of total – in other words the real at risk new business licensing is probably something like 5% of total revenues, given that maintenance and services have a high locked in component at this time of year. And you'll find if you do that maths on that that is very similar to the variable costs on the last slide. And that is why we believe we have protected profits for 2012.

To finish off on slide 14 I would just like to reiterate our mid-term financial goals; these remain unchanged after our fourth quarter results announcement. They are, in brief: a return to 10% to 15% annualised licence growth; restoring services to a double-digit margin whilst keeping to around 25% of total revenues, and therefore not diluting overall group margins; leveraging areas like services margin, G&A costs, possibly a little bit of R&D, whilst investing in sales and marketing to move towards a more industry standard model, and overall in that equation delivering 100 to 150 basis points average margin improvement; and finally converting 100% of that EBITDA generated from that margin improvement into cash from operations. And if you combine that revenue growth with the margin improvement and the cash conversion on top of that, and then you look at the efficient tax and financing structure, you'll be able to model that with this scenario we will generate significant free cashflow over the next few years.

So, that ends the formal part of the presentation. Operator, we'd now like to open up the call to questions please.
Questions and Answers

Operator

We now begin the question and answer session. If you wish to ask a question please press star and one on your telephone keypad and wait for your name to be announced. If you wish to cancel your request please press the hash key.

Your first question comes from the line of Chandra Sriraman of Bank of America. Please ask your question. Chandra Sriraman your line is now open; can you hear me?

Chandra Sriraman – Bank of America

Hi, good evening gentlemen. I have a couple of questions. If I were to back calculate your licence and your guidance here – I do realise, I appreciate that you don’t recommend it – but if I were to calculate, again worst case scenario of licence in decline of 15% or so, and given that your major market contribution is only 13% this assumes that other parts of the business also go down this year. And this is surprising given that your costs are also reasonably easy. So, can you give us what are the assumptions that go into this guidance?

And number two is if I were to look at your performance in 2009 I saw a massive margin leverage there; your margins jumped up by 700 plus basis points; whereas I don’t see that here. Can you give us some colour as to why that is happening? Are you trying to invest somewhere and to restrict this margin expansion?

Thanks

David Arnott - CFO

Okay, Chandra, this is David; let me take both of those. The first point, to be clear, within the total revenue outlook, whilst you can model maintenance pretty accurately what you can't see is the split between licence revenue and services revenue. Now, if you look back to 2011 we did absorb
the majority of the reduction in services coming from the attachment rate as we moved towards partners. So, whilst in the last few years coming up to 2011 we were signing on average 71% of attachment rate – so for 10 million of licensing we get 7.1 million of services – last year we saw a step reduction in that number to around 51% as the partners picked up the difference. That resulted in a decline in revenues in absolute terms. And we believe the steady state attachment rate could go down slightly from here, and that could therefore result in a further reduction of services. This is probably the last quarter of the services attachment rate decline that we need to make. The good way to model it is around 25% of total revenues: if you take services at 25% of revenues you should find that licensing will not decline by 15%. Again though, just to be very clear, we do not personally guide on the individual lines. You'll find at the bottom end the implied licensing with services at 25% is more like a minus 5%.

If you look back to 2009 – to take the second part of the question – 2009 was a little bit different in that it was shorter and sharper. We had an almost total absence of deals between October and December 2008; the world just froze post the Lehman's crisis. And those deals came back very, very quickly; within two quarters we'd signed all of those deals in 2009. And therefore because Q4 was seasonally very high, 2008 in total because not much got done was quite a low number. And by the time you add that on with a normal 2009 with its own strong Q4 you've really got quite significant licence revenue growth; but not much happened on the cost base. Now, what we're seeing this time is a much longer cycle. We didn't see the full Q4 normal seasonal peak that we normally do on new business; although we did see it on existing business. And we're not expecting the sales cycle to come back to a more steady nine to 12 months immediately.

Chandra Sriraman – Bank of America

Thank you.

Operator

Your next question comes from the line of Josep Bori of Exane. Please ask your question.

Josep Bori – Exane
Good afternoon. Thank you very much for taking my question; I have a couple if I may.

First one, to what extent does your current guidance reflect an impact in Q1, potentially first quarters, of the Misys initiations versus the macro environment? Could you give us some sense of the sort of split in this impact?

And second follow up question to this, how have the clients reacted to the open discussions with Misys? Have they postponed deals? Is that part of your concerns in terms of revenue of the top line as we go through this year?

**Guy Dubois – CEO**

This is Guy speaking. Thanks for the questions. Let's face it we entered into this process, the Misys process with our eyes wide open. We knew entering into this process would drive attention and energy. So, what I did is to create what I would call a Chinese wall. The first decision was to drag as less as possible any resources from Temenos into this process. As a matter of fact only Max Chuard, who is in charge of our corporate development and David were heavily involved. Andreas, the Chairman, Andreas Andreades and myself were involved too, let's say; but we were giving guidance and support; and we are obviously well supported by advisors. So, it was a team. So, the first decision was to contain as much as we could this overall process; and I believe we did and we did well.

As far as Q1 is concerned actually we do not give any guidance on a quarterly basis; and I do not want to share anything as far as Q1 is concerned. Anyway you know that all our quarters are quite heavily backend loaded. But there is nothing I can say more about Q1.

What were the clients' reactions? Actually we had many reactions from our customers and from our partners, but they were all very consistent, and they were very supportive. And the reaction one was: okay, guys, it makes sense for you to do these deals; but you are extending yourself into another area, and that's okay because you remain a very strong leader in core banking, with or without the deal – which means there were no real changes from our starting point. Actually the second point that they raised was: make sure you take care of us and do not start to be dragged into a lot of things which could have an impact on our relationship. So, we listened very loud and clear to the feedback of our customers to continue to be very focused on what we are
doing; which is to deliver the products on time and sell them the best possible way. So, that’s what happened in Q1 as far as this overall transaction process was concerned.

Josep Bori – Exane

Thank you very much. Just a quick follow up on the comment you made that obviously you don't want to give guidance on Q1; let me ask you differently. Can you give a sense of the seasonality profile of 2012? Obviously Q4 was pretty painful; should assume that kind of trough, and you should expect a gradual recovery? Or do you think things will still get worse before they get better? Thank you.

Guy Dubois – CEO

Thanks again, Josep, for the follow up question obviously. But I wouldn't like to express myself too much about Q1. As you know there is always a seasonality in our years, and there is no reason why we shouldn't have the same in 2012. So, we always have a second part of the year which is stronger than the first part of the year. That has been the case now for many years, and we don't see any reason why that would change.

Operator

Your next question comes from the line of Takis Spiliopoulos of Bank Vontobel. Please ask your question.

Takis Spiliopoulos – Bank Vontobel

Thanks. Just one; most have been answered. Talking about the sales side which you have been mentioning and discussing also with Q4 results; have you seen any further deterioration respective to that, or even an improvement, or just stabilisation? So, what is like out there in this one? Thanks.
Guy Dubois – CEO

Takis, thanks for the question. It's good to hear you. Frankly we talked like a month ago or something; I don’t want to comment because there is not enough data point for me to give you a real event information. Forgive me. Maybe we will wait to answer this question when we talk again at the Q1 results.

Takis Spiliopoulos – Bank Vontobel

Okay. Then a further one on your partner model: have you seen there any further improvements against if you look at the guidance of other big software companies who are rather confident going forward? Obviously they’re not just banking on banking software. But do you see any optimism on the side of your partners? If I look at their forecasts they don't look that doomsday.

Guy Dubois - CEO

As you know in 2011 we are pleased with the performance of our partner programme, since the volume of business brought by our customers grew quite significantly in 2011 compared to 2010. We did not give guidance short term on which kind of volume we do expect from our partners. But I believe we are happy with the programme so far; we continue to see a good relationship with our partners; we see multiple options for us to continue to strengthen the relationship with our partners and obviously we want to take advantage of it. But I would not give specific numbers relative to the volume of business supposed to be brought by our partners in 2012.

Takis Spiliopoulos – Bank Vontobel

And then the last one would be more on technology. I mean, you announced your goal to be ready on a componentised basis for the platform early December. Now three months, or almost three months into 2012 what were the initial reactions of your let’s say prospective tier one and tier two banks? Is this... have you got enough feedback that this is a feasible way going forward?

Guy Dubois - CEO
Yeah, it would by itself as you know a longer discussion about it. As you know we are embarking into a compentisation (sic) – I’m not sure this is the right word but I’m sure everybody understood what I just said – a compentisation of the actual product. It has actually been built on a different framework. In R12 we will announce, very soon actually during our TCF event which will take place in May in Barcelona, obviously a new improvement of the compentisation. You will see in particular improvement around the interaction framework and integration framework; which are two very key elements helping us to go towards the tier one, tier two business. So far we are pleased with R12; R12 is ready to get out and will be launched as scheduled during our event in May. So, stay tuned; we will launch it probably at that time.

Operator

Thank you. Your next question comes from the line of Mohammed Moawalla of Goldman Sachs. Please go ahead and ask your question.

Mohammed Moawalla – Goldman Sachs

Thank you. Guy, can you just comment on the state of the pipeline? Because I think about a month ago you were fairly optimistic. But since the sort of Misys discussions have ended how long will it take you to perhaps restore the pipeline and connect it to that? Can you perhaps just talk about the differences in sales cycles between the three different segments you gave for the licence revenue between the mature markets, developing markets and the existing customer business?

Guy Dubois - CEO

Hi, Mohammed, how are you doing? This is Guy speaking again. Thanks for your question. As you noticed when we talked like a month ago we talked about the pipeline, and in particular we said that our pipeline improved in Q4 against Q3. So, one of your questions was about the evolution in the size in the cycles. The first one was related to Misys; in other words have you suggested that the pipeline had been affected by Misys? Actually the answer is no. We continue
to be balancing and checking our pipeline on a regular basis. As I said already a month ago, the pipeline is a good pipeline. It hasn't been affected because actually as a competitor Misys is what I would call not one of our major competitors; we don't see Misys frequently when we compete; we see other, other actors obviously when we compete before Misys. So, it hasn't been affected at all actually.

The sales cycle could be, I believe, split into three categories. On the existing business the sales cycle is better understood, better managed. Why? Because we know the customer; we understand the sales cycle; we understand who is the decider; we understand what is installed and we know better what to do. That is why you notice in 2011 why the business was tougher for us we delivered and improved more revenue from our install base – or let's call it the existing base, to use the same terminology. And obviously this is one of our key focus areas for this year.

Now, what is different is in the emerging markets, let's say the fast growing or fast changing markets: we delivered a fairly good portion of business from this area last year, and we continue to be focused as much as possible this year.

Regarding the developed market, new business, a bit of the same. But obviously, as I said last time we talked, finding new projects in what I would call our well known customer base i.e. Europe in particular, has been tougher; sales cycles have deteriorated. And as I said to Takis, it is too early for me to tell you if I see further deterioration or not. So, I will refrain myself to say anything about it. And maybe when we have a few months in 2012 I will feel better to say if we have proof points telling me if we go one way or the other.

So, this is where we are at. Obviously, as I told you already I believe a few months ago, we changed quite substantially the overall way we merge our pipeline, we report our pipeline; we have now a full tool we have up and running which is bringing us by far more visibility and evidence of the evolution of all our deals. We are quite happy with this. And we expect to see that turning as a good productivity tool as well which will help us to better understand our business going forward.

Operator

Your next question comes from the line of Will Sheldon of UBS. Please ask your question.
Will Sheldon – UBS

Hi, thanks for taking my question. What sort of gross margin will the services business make this year, please?

David Arnott – CFO

Okay, first of all to clarify, we don't report gross margin; we report net margin. So, our service margin, and in fact if you look at the way we present our numbers, all of our four cost centres are fully loaded with their relative portion of overhead. So, I think it would be confusing to give gross margin.

On a net margin basis, which is the equivalent of a minus 12% last year... [Line interruption] Our services margin, as I've said, we report on a net basis. We've given a medium-term target of 10% to 15% margin for services; and we will trend towards this over the next three years.

In 2012 specifically on a net basis it is not yet clear to us that we will achieve breakeven. Most likely we will end up mid single digit loss making for this last year; but trending clearly towards our medium-term target margin of 10% to 15%.

Operator

Your last question comes from the line of Alex Tout of Arete. Please ask your question.

Alex Tout – Arete

Thanks. All questions already answered.

Operator

Thank you. Please continue.
Guy Dubois - CEO

This ends the presentation of today. Thank you for joining us and we will speak in a month's time. Thank you. Bye.