

# FINAL TRANSCRIPT

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## **DLX - Q4 2008 Deluxe Corporation Earnings Conference Call**

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**Lee Schram**

*Deluxe Corporation - CEO*

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## CONFERENCE CALL PARTICIPANTS

**Charles Strauzer**

*CJS Securities - Analyst*

**John Kraft**

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## PRESENTATION

**Operator**

Good day ladies and gentlemen, and welcome to the fourth quarter 2008 Deluxe Corporation earnings conference call. I will be your coordinator for today. At this time all participants are in a listen-only mode. We will conduct a question and answer session towards the end of this conference. (Operator Instructions) I would now like to turn the presentation over to your host for today, Mr. Terry Peterson, Vice President of Investor Relations and Chief Accounting Officer. You may proceed, sir.

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**Terry Peterson** - *Deluxe Corporation - VP, IR, CAO*

Thank you, welcome to Deluxe Corporation's 2008 fourth quarter earnings call. I'm Terry Peterson, Deluxe's Vice President of Investor Relations and Chief Accounting Officer; Joining me on the call today are Lee Schram, Deluxe's Chief Executive Officer; and Rick Greene, Deluxe's Chief Financial Officer. Lee, Rick, and I will talk questions from analysts after the prepared comments. At this time the operator will instruct you how to ask a question. In accordance with Regulation FD this call is open to all interested parties. A replay of the call will be available via telephone in Deluxe's website. I will provide instructions for accessing the replay at the conclusion of our teleconference. Before I begin, let me make this brief cautionary statement.

Comments made today regarding financial estimates and projections and any other statements addressing management's intentions and expectations regarding the Company's future performance, are forward-looking statements as defined in the Private Securities Litigation Reform Act of 1995. As such, these comments are subject to risks and uncertainties, which could cause actual results to differ materially from those projected. Additional information about various factors that could cause

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actual results to differ from those projected are contained in the news release that we issued this morning, and on the Company's Form 10-K for the year ended December 31, 2007, as updated in the Company's Form 10-Q for the quarter ended September 30, 2008. In addition, the financial and statistical information that will be reviewed during this call is addressed in greater detail in today's press release which is posted in the Investor Relations section of our website, [www.deluxe.com](http://www.deluxe.com) and was furnished to the SEC on the Form 8-K filed this morning. In particular, any non-GAAP financial measures are reconciled to the comparable GAAP financial measures in the press release. Now, I'll turn the call over to Lee Schram, Deluxe's CEO.

**Lee Schram** - *Deluxe Corporation - CEO*

Thank you, Terry, and good morning, everyone. Given the very difficult economic environment, clearly we had a challenging quarter, but given our strong spending controls, disciplined approach to deploying capital, and focus on operating cash flows, we were able to meet our adjusted earnings per share outlook and significantly expand our cost-reduction program. In this tough economy, revenue was slightly more negatively impacted than anticipated in holiday cards and other discretionary products, such of imaging, apparel, and retail packaging products. It was also impacted by lower check volumes mid-quarter from a couple of large financial institutions that were recently acquired. Even with these revenue shortfalls, we were able to control spending and fully offset the earnings per share impact of the revenue shortfall, excluding the impact of restructuring and impairment charges.

With the challenging economy in financial crisis, we continue to focus on basic blocking and tackling in our core check businesses by continuing to extend contracts and further stabilizing margins. We also had our best quarter ever on new non-check revenue. In response to an even further weakening economy, we also challenged ourselves to more aggressively reduce cost and expenses, and now have expanded our previous \$250 million cost-reduction initiative to \$300 million. At the same time we continue to invest in our future with progress in many revenue initiatives, including e-commerce where we continue to see growth in site visitors. We also growth in loyalty, retention, fraud and security and new business services including payroll services, logo design, web services and business networking. We are prudently managing our Company. Closely monitoring the small business and financial institution markets, and focusing on strong free cash flow generation while offering a very attractive dividend as we continue to transform Deluxe and steadfastly execute on our turn-around plan. In a few minutes I will discuss more details around our recent progress ad next steps, but first Rick will cover our financial performance.

**Rick Greene** - *Deluxe Corporation - CFO*

Thanks, Lee. Earlier today we reported diluted earnings per share for the fourth quarter of \$0.55, which included a loss from discontinued operation of \$0.05, following our decision to sell the non-strategic low-margin Russell and Miller retail packaging and signage business. Excluding restructuring and impairment charges, we reported earnings per share from continuing operations of \$0.68.

As Lee indicated, revenue was below our outlook due to an even greater downturn in the economy than expected. However, we were able to fully offset the impact of lower revenue with spending controls and cost reductions, primarily in SG&A expense. Revenue from continuing operations for the quarter came in at \$364.9 million, with continued softness, primarily in small business services, where we continued to see declines in our seasonal and more discretionary products, including holiday cards. During the quarter, we reclassified \$3 million of revenue from the Russell and Miller business to discontinued operations.

Excluding the impact of restructuring charge, operating margins for the quarter were in line with our expectations, with favorability coming from our personal check businesses, offset by a small shortfall in SBS. Operating cash flow for the year totaled \$198.5 million, which was at the upper end of our previous outlook. Cash flow benefited from a delay to 2009 of approximately \$10 million in contract acquisition payments. In the fourth quarter of 2007, we reported diluted earnings per share of \$0.77. The 2007 period benefited from higher revenue and lower restructuring and asset charges, partially offset by higher performance-based compensation in 2007, and additional cost savings in the 2008 period.

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Companywide, revenue was down 11% from 2007. The year-over-year decline was due to continued weakness the economy, primarily in SBS, as well as lower volume in our personal check businesses and lower revenue per order in financial services. Gross margin for the quarter was 62.6% of revenue, down 1.3 points from 2007. The restructuring-related charges reduced gross margin by 0.7 points in the quarter. Lower revenue per order in financial services also impacted our gross margin. Selling, general, and administrative expense decreased \$23.5 million in the quarter, and was 45.1% of revenue, compared to 45.9% in the same period last year. Benefits from continued execution of our cost-reduction initiatives, and lower performance-based compensation contributed to the improvement.

Within continuing operations, restructuring-related costs, and asset impairments for the current period were \$6.5 million or \$0.08 per share. The restructuring costs include severance benefits related to new cost-reduction initiatives in our fulfillment, sales, and marketing organizations, and transition costs for the planned closure of six printing facilities. An asset impairment charge of \$0.3 million relates to a trade name in small business services. Operating income in the quarter was \$60.4 million, compared to \$71.1 million last year. Results from discontinued operations include a pre-tax impairment charge of \$3.4 million, or \$0.04 per share, related to writing down the net assets of the Russell and Miller business to their estimated fair value.

Next, let's cover a few highlights in each of our three business segments. In small business services, revenue of \$218.7 million was down 11.5% versus 2007. Revenue in this segment was unfavorably impacted by continued economic softness in the quarter, particularly in our discretionary products such as holiday cards, apparel and other promotional products. Continued declines in checks and forms and a lower Canadian exchange rate, which alone accounted for a \$3.8 million reduction. These declines were partially offset by contributions from the Hostopia acquisition, and organic growth in fraud protection services.

Operating income in this segment was \$27.1 million or 12.4% of revenue, compared to \$37.8 million in 2007. The quarter's results include \$3.7 million of restructuring costs and an asset-impairment charge which reduced operating margin by 1.7 points. In financial services, revenue was \$102.3 million, down 9.4% versus the fourth quarter last year. The decline was due to a 7.2% reduction in check order volume, as well as lower revenue per order, given the competitive pricing environment which more than offset a recent price increase.

Financial services operating income was \$20.6 million for the quarter, or 20.1% of revenue, up from \$18.7 million in 2007. The quarter's results include \$1.1 million of restructuring costs, which reduced operating margin by 1.1 points. Excluding the restructuring costs, operating margin was up 4.5 points versus 2007.

Finally, Direct Checks revenue totaled \$43.9 million, down 11.7% on a year-over-year basis, due to continuing declines in check writing and a weak economy that is negatively impacting our ability to sell additional products. These reductions were partially offset by higher revenue per order from recent price increases. Operating income in the segment was \$12.7 million for the quarter, or 28.9% of revenue. Restructuring costs of \$1.7 million in the quarter reduced operating margin by 3.9 points. Excluding the restructuring costs, operating margin was up 3.2 points versus 2007.

Turning to the balance sheet and cash flow statement, total debt at the end of the quarter was \$853 million, compared to \$844 million at the end of 2007. Cash provided by operating activities for the year was \$198.5 million. The decrease from last year was due to a higher 2007-related incentive compensation payment earlier this year, and lower earnings, partially offset by lower income tax payments and progress with our working capital initiatives. Capital expenditures for the year were \$32 million, and depreciation and amortization expense was \$64 million.

Now turning our focus to 2009. We expect the challenging economic conditions that have persisted in 2008 will continue to present headwinds throughout the year. As such, consolidated revenue is expected to range from \$1.3 billion to \$1.4 billion on a full-year basis. In addition, we expect earnings per share, excluding \$0.04 of restructuring-related costs, to range from \$1.95 to \$2.35.

There are several key factors that contribute to our full year 2009 outlook. Given our expectation of a weak economic outlook throughout 2009, we expect small business services revenues to decline in the mid-single to low double digits, as decline in

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core business products will be partially offset by benefits from our e-commerce investments, and strong double-digit growth in our business services offerings. In financial services, an acceleration of check order declines to approximately 6 to 7%, given the turmoil in the financial services industry, and increases in other forms of electronic payments, which we expect will be partially offset by continued contributions from non-check revenue streams. Double-digit revenue declines in direct checks given check usage declines and the weak economy, which is negatively impacting our ability to sell additional products, focused execution on our cost-reduction initiatives, partially offset by increases in material and delivery costs, as well as higher performance-based compensation, and significantly increases in employee and retiree medical costs, and an effective tax rate of approximately 35%.

We expect to continue to generate strong operating cash flows, ranging between 175 million and \$200 million for the year. Lower earnings will essentially be offset by continued progress on working capital initiatives, and lower performance-based incentive compensation payments in 2009. We expect contract acquisition payments to be approximately \$20 million, up from the 2008 level due to a shift of approximately \$10 million of payments from the fourth quarter. Capital expenditures are expected to be approximately \$40 million as we plan to expand our use of digital printing technology, further automate our flat check delivery packaging process, and make other investments in manufacturing productivity, as well as key revenue growth initiatives. Depreciation and amortization expense is expected to be \$70 million, including \$19 million of acquisition-related amortization.

For the first quarter of 2009, we expect revenue to range from \$335 million to \$350 million. Diluted earnings per share are expected to range from \$0.38 to \$0.46, excluding restructuring-related costs of \$0.03. In comparison to 2008, the factors affecting our full-year outlook are similar to those affecting the first quarter. In addition, the 2009 quarter will have one less business day, which accounts for nearly \$6 million of revenue.

Finally, let me finish this financial overview with a few comments regarding our capital structure, and uses of cash in 2009. We enter the year on a solid foundation with robust cash flows, a strong balance sheet, and reasonable access to capital. We remain well above the 3 to 1 EBIT to interest coverage ratio on our existing credit facilities, and expect to remain in compliance for the balance of their terms. With no long-term debt maturities until 2012, we are focused on a disciplined approach to capital deployment that balances the need to continue investing in initiatives to drive top-line growth, including tuck-in acquisitions, and further debt reduction. Although we have periodically repurchased shares in the recent past, our focus will now shift to further reducing our debt. We also expect to maintain our current dividend level.

In summary, we believe that we are well positioned to not only weather the volatile capital markets, but more importantly also have the capability to take advantage of selective opportunities to deploy cash to effectively drive long-term value. Now I'll turn the call back to Lee.

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**Lee Schram** - *Deluxe Corporation - CEO*

Thank you, Rick. I'll continue by comments with an update on what we are focused on overall, and then highlight progress in each of our three segments. I will also include throughout a perspective on what we hope to accomplish in 2009, and wrap up with an update on our cost-reduction initiatives.

Especially now during these challenging economic and liquidity crisis times, we understand that it is critical for us to be able to stabilize core checks and business products while overtime demonstrating an ability to drive sustainable revenue growth. We have broadened our risk-management framework, instituted even more disciplined spending controls, and are focused on the strength of our balance sheet. To sharpen our focus and align key leaders and capabilities, we are targeting five key areas for 2009.

First financial institutions and our core check capabilities, plus growth outside checks and helping FIs expand core deposits. Second direct to the consumer and optimizing cash flow. Third, small business core business products sold through enhanced e-commerce capabilities, and an improved segmented customer focus. Fourth, higher growth business services including logo

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design, payroll, business networking, web hosting and other web services. And fifth, cost-reductions and simplification, where we expect to continue the solid work already underway as part of our expanded \$300 million cost-reduction initiative.

As we enter 2009, although we know it will be more challenging to grow revenue in this economy, we believe our portfolio is becoming better positioned to deliver sustainable future revenue growth opportunities, as the broader economy recovers. It starts with stabilizing the rate of decline in our core check businesses, then adding existing organic initiatives, such as enhanced e-commerce, loyalty, retention, and fraud and security offers. It includes growing business services, such as payroll services, logo design, web, hosting, and business networking services. We will continue to access potential tuck-in acquisitions that complement our large customer bases. With a focus on business services and new products and services aimed at helping financial institutions grow their core deposits.

As we indicated in early September, 2008, in a more normal economy, we believe this would position us for a roughly flat top line in 2009, and 5 to 9% earnings per share growth. However, given the weakened economy, and still looming financial crisis right now, we believe it is prudent for our 2009 revenue outlook to range from a decline of approximately 10 -- 10 to 5% with diluted earnings per share in a range of a decline of roughly 20 to 5%.

More specifically, the upper end of our outlook assuming the current economic trends do not improve throughout the year, and that we benefit only a modest amount from our revenue initiatives. On the lower end, we have assumed that there is a considerable deterioration in the economy throughout the year. We are not happy with this revenue range. But given the difficulties predicting trends in this weak economy, we believe it is prudent to plan this way. Because of this, in the fourth quarter, we were even more aggressive in working to reduce our cost structure. We thought it would be important to bridge our thinking from early September 2008 to today. So here is some additional color.

Our goal, even in this very tough economy, was to build a 2009 outlook targeted at a 5% earnings per share improvement over 2008, excluding restructuring and impairment charges. If we take 2008's results, excluding restructuring and impairment charges, and reduce operating margin for the volume-related revenue decline impact of approximately \$65 million, higher incentive compensation of approximately \$20 million, higher employee and retiree medical expenses of \$12 million, higher material and delivery cost of \$12 million, and then factor in margin improvement from an incremental \$90 million in cost and expense reductions, and approximately \$8 million in savings from a 2009 wage freeze, this would roughly equate to flat earnings per share at the top end of our outlook range.

Excluding the \$12 million increase in employee and retiree medical expenses, driven by the significant unfavorable asset losses and discount rate movement from September 2008 to year end, would have enabled us to achieve the 5% earnings per share growth outlook goal. We are relentlessly eliminating unnecessary cost and building a significantly more robust infrastructure and improved processes, so when the economy improves, we have solidified the Company, and will be well positioned for success. Now shifting to our segments.

In small business services, as expected, economic softness continued to impact our business. Shortfalls to our fourth quarter outlook were primarily in holiday greeting cards, but also in imaging, apparel, and retail packaging products. These are the more discretionary type products that small business owners ramped down or did not purchase. Positively, we saw growth in payroll services, a continued ramp in our EZShield check protection service and in logo design services. Both in e-commerce visitor traffic where we continued to add content, capability and coverage. Significant growth in business networking members from Partner Up, where we now have nearly tripled membership since our acquisition. And solid growth in web services from our Hostopia acquisition, where they, again, grew at a double-digit rate year-over-year.

We also added Web Domains through a small tuck-in purchase of a customer list at a distressed price, which will be included in Hostopia. We also have our very low margin non-strategic Russell and Miller retail packaging and signage business up for sale. And now have included this roughly \$15 million revenue business in discontinued operations.

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In 2009, given the state of the economy, where we know small businesses are being impacted with fewer starting up, more struggling to get funding, and more eliminating or delaying spending, we are not forecasting an improvement in the current weakened economy for the full year. In core business products, our focus is on acquiring new customers, and increasing our share of wallet through enhanced e-commerce capabilities, and improved small business segment focus.

In 2008, we were able to introduce a new e-commerce platform, improve its functionality and get approximately 50% of our products and services into one system. In 2009, by early in the second quarter, we will further refine the platform, link it directly to an enhanced Deluxe.com, improve usability, and have approximately 90% of our products and services in one system, and start retiring multiple legacy platforms. These moves will allow us to better cross-sell, simplify ordering for our customers, and better position our brand.

In new business services, we are pleased with the continued revenue integration of our logo design, web hosting, and business networking services acquisitions. In 2009, we expect strong double-digit growth. We also believe there are opportunities to add more business services on the Hostopia unified technology platform.

In financial services, we continued again this quarter to proactively extend several check contracts, and have all large contracts extended through 2009. Completing these extensions helps lock in more predictable annuity-based check revenue streams, and allows us to focus on winning several competitive national accounts, including one, which has already started their RFP process. Again, this quarter, we continued to see strong overall new acquisition rates, especially in the credit union space, and our retention rates also remain strong, in excess of 90%. We continue to simplify our processes and take complexity out of the business, while reducing our cost and expense structure.

The banking crisis did have some impact on our business, as we did see softness in check orders from two of our larger financial institutions, who were recently acquired, likely due to the lack of new demand deposit account holders and current ones leaving. In all likelihood once there was clarity and confidence around the acquisitions, check volumes from both of these customers improved towards the end of the quarter. As initially indicated on our third quarter call, we did see some improvement in the fourth quarter in check orders from community banks and credit unions. It has been reported that more consumers may be shifting their deposits here, and this fits well with our strategy, as we have been able to increase check business in these markets.

In addition to our strong core check revenue, we made progress again in the fourth quarter in advancing new non-check revenue growth opportunities. We grew revenues sequentially over the prior quarter, and over last year in our non-check loyalty retention and fraud and monitoring protection solutions. Although we continue to see momentum building in these new non-check revenue initiatives, we also see decisions by financial institutions taking longer with more approvals, and a focus on spending less.

In 2009, we expect check order declines to accelerate to around 6 to 7%. Some of this is due to turmoil in the financial services industry, and some is due to increases in electronic payments. We expect to maintain our high retention rates and acquire new check customers. We also expect some revenue contribution from non-check offers aimed at helping financial institutions grow core deposits. Our expectation is that these new initiatives could add a couple of percentage points of incremental revenue in the financial services segment this year, and they are accretive to operating income. Finally, we will continue the simplification work with the goal of taking complexity out of the business and reducing our cost structure.

In Direct Checks, our revenue was basically in line with our expectations, and we had another solid operating margin in the quarter, coming in at 33%, excluding restructuring-related items. We continue to look for opportunities to provide accessories in other non-check products and services to our consumers. In 2009, we expect double-digit declines in revenue driven by consumer usage reductions in a continued weak economy. We expect to reduce our manufacturing cost and lower SG&A in this segment, and keep our profitability profile within 1 to 2 points of a 30% operating margin level while generating strong cash flow.

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In addition to these actions in each of our segments, here is an update on our cost and expense-reduction initiatives. The plan has now been increased to target a \$300 million reduction through 2010, where \$90 million of net savings are expected to be realized in 2009 on top of \$155 million already -- already realized from 2006, 2007, and 2008. We expect to realize the remaining \$55 million in savings in 2010. Approximately 40% of the \$300 million reductions impacts go to market sales and marketing and support, 30% impacts fulfillment, and 30% impacts shared services infrastructure.

Overall, we had another solid quarter, delivering slightly more than expected in the fourth quarter, excluding the additional restructuring charges. For 2009, reductions again will not necessarily be linear through the quarters. Be aware the savings will flow the first half, especially in the first quarter for three primary seasons. First, as we highlighted on our last call as well, we will have some duplicative cost as we transition four fulfillment centers. Second, we will have some additional upfront cost as we continue to reposition our channel and sales support structures. And third, we have some higher costs for an updated Deluxe.com, and Shop Deluxe e-commerce release scheduled for early in the second quarter.

Here are some highlights of the key cost reduction activities for the fourth quarter and focus areas for 2009. These are in addition to the ongoing savings that are occurring each quarter from previously implemented actions. In our go to market sales and marketing, we continued to realign sales and marketing back end operations. Refine our channel management structure and improve our call center productivity. In 2009, we will continue to realign sales and marketing back-end operations through process centralization, simplifying business processes, platform and tool consolidation, and leveraging e-commerce capabilities. We will close our thoroughfare call center in the first quarter. We also are revamping our marketing services media customer touch points, as we improve the mix of paper catalog, online, and search engine optimization.

For fulfillment, we had a strong quarter with lean productivity improvements and direct-spend reductions. In 2009, we will close five additional fulfillment sites. Three of which are targeted to close the end of the first quarter, and the remaining two late in 2009. In addition, we recently closed one small fulfillment site. Further, we expect to completely automate our flat check package processing by the end of 2009. Introduce more digital printing, continue our lean product -- product standardization, spoilage reduction, and direct and indirect spend reduction initiatives. Plus advance our work on realigning to a common manufacturing platform. We also plan to initiate more strategic supplier sourcing arrangements, and enhance value-stream mapping, improvements and efficiencies.

Finally, for shared services infrastructure, we continue to make good progress in information technology, driven by data center cost reductions, and other system utilization, networking, and voice communication efficiencies, as well as in finance, human resources, and real estate. For 2009, we expect to continue to reduce cost in all areas, as opportunities exist to centralize, streamline, standardize, and improve efficiencies. More specifically, we are reducing outsourcing and contractor spend for information technology. Shifting to a more regional, self-service human resources structure. And continuing to reduce our real estate footprint with planned elimination of another 13% of our square footage.

As we exit 2008 on the heels of a very challenging economy, we have made tremendous progress in transforming Deluxe, but we still have a lot of work and opportunities ahead of us in 2009. We are not expecting the economic climate to improve, but we are expecting stability in our core check businesses, continued strong progress on our cost-reduction initiatives, and more meaningful revenue contributions from e-commerce, and our new business services, and non-check financial institution revenue offers. Right now, we believe Deluxe has demonstrated its value as a disciplined and stable Company in these challenging economic times; and that we have made positive strategic moves to reposition the Company for sustainable longer-term growth, while currently generating strong cash flows and a very attractive dividend.

Before I open the call up for questions, I would like to take this opportunity to thank all the Deluxe employees for their hard work and dedication in what was clearly a challenging 2008. Thank you Deluxers. Now operator, Rick, Terry, and I will address questions.

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## QUESTIONS AND ANSWERS

### Operator

(Operator Instructions) And your first question comes from the line of Charles Strauzer from CJS Securities.

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**Charles Strauzer** - *CJS Securities - Analyst*

Good morning.

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**Lee Schram** - *Deluxe Corporation - CEO*

Hi, Charlie.

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**Charles Strauzer** - *CJS Securities - Analyst*

A couple quick questions. Actually, just one question in two parts. If you could give me a little bit more granularity, first of all on CapEx, I believe you are calling for a 25% increase in CapEx year-over-year in your guidance, a little bit more granularity on what that spend will entail? And the secondly, Lee, maybe you can give us a little bit more on the puts and takes in the industry -- the bank industry, given that Goldman and Morgan become banks, you've got a lot of moving pieces with acquisitions and disposable banks into other banks, kind of where you see, kind of the year shaking out with potential new RFPs there?

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**Lee Schram** - *Deluxe Corporation - CEO*

Yes, let me start, Charlie with the CapEx. We are planning to spend more clearly, from the 32 million to \$40 million. And I think the way to think about it, as Rick said in his prepared comments, really the focus on is with all of the initiatives that we have got going now to get an improved cost structure, yes, but also improved processes, we just decided it is best right now for us to get a lot of those initiatives out of the way now and actually accelerate them, and that's the work that we did in the fourth quarter. So with that, Charlie, comes a little bit more in CapEx spending, and again, I know it's not all what you see out there, but we believe this is a really prudent move for us to get after this now, and get some of the things in our manufacturing with our flat packaging done at a faster pace, a little bit more of a shift to digital printing that we think is going to help us in the long term, and then also we made some moves to get a little more ambitious about getting our -- our Deluxe.com and our Shop Deluxe, e-commerce moving at even a brisker pace. So when you add all those up those are really the core things. And then we're investing organically. We want to keep investing smartly in this -- in this tough economy, and that's kind of the net of the additional spend.

On the banking, this is very interesting what is happening out there right now. What we're trying to do first and foremost is lock in those big national deals. We're really proud of the fact we have got a great sales team out there that has been able to do that, already for the 2009 period. And then another one of our focus areas has been to really make sure that we are balanced and getting a lot more of our new business in the community bank space as well, in the credit union space, so we have been able to do that, and that's really our focus, as we move forward, is getting that balance between the nationals and the communities and the credit unions, and that's what we're going to continue to do in 2009.

I think if you think about really what is happening out there, is it's becoming hard -- harder to predict and -- what is going to happen, as more noise around the bank concerns in the general population, so what we're trying to do is just make sure we're balanced with the nationals, and balanced as best we can in the community and in the credit union space. And that's what our focus is right now.

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**Charles Strauzer** - *CJS Securities - Analyst*

Great. Thanks so much, Lee.

**Operator**

Your next question comes from the line of John Kraft from DA. You may proceed.

**John Kraft** - *D.A. Davidson - Analyst*

Good morning, fellows.

**Lee Schram** - *Deluxe Corporation - CEO*

Hi, John.

**John Kraft** - *D.A. Davidson - Analyst*

I just wanted to follow-up on the last question a little bit first. The -- you mentioned that there, several larger contracts coming up for bid. If you were to win those, would those be a 2009 contract starts?

**Lee Schram** - *Deluxe Corporation - CEO*

Some of them would, John, and some of them would be, probably be later in the year to the beginning of next year. And also just to comment, there's probably right now three or four of them that we think are out there, and none of those are included in the guidance that we put out.

**John Kraft** - *D.A. Davidson - Analyst*

And would you also say none of those are yours, then?

**Lee Schram** - *Deluxe Corporation - CEO*

None of those are ours.

**John Kraft** - *D.A. Davidson - Analyst*

Okay. And then, Lee, back to the beginning of your prepared remarks, you mentioned something that I was a little confused by. You said that -- that it was the best quarter ever for new non-check revenue. Can you clarify that?

**Lee Schram** - *Deluxe Corporation - CEO*

If you think about some of the initiatives, John, that we have been talk about in the FS segment around trying to bring, loyalty, retention, fraud and security-type offers to our financial institution clients, we have basically had the best quarter that we have ever had in revenue in that space.

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**John Kraft** - D.A. Davidson - Analyst

Okay. That's what I thought. And then you also said that you expect check volumes to be down 6 to 7% in 2009 due to the turmoil. Is that what you see for Deluxe or is that what you see for the industry? And then is that what you see from now on?

**Lee Schram** - Deluxe Corporation - CEO

John, this is a great question. And, what -- let me try to be very careful and be -- in terms of the way I kind of answer this. And careful, being very methodical here. We cannot tell right now if the Fed study that was done in late 2007, was completed from '03 to '06, and it said there was basically a 4.1% decline in checks being written, and we have used 4 to 5%. We can't tell whether that's still 4 to 5% at this point in time. What we're seeing for our guidance that we put out is we are assuming our check orders are going to decline 6 to 7%. And we think it is prudent right now, and based on what we saw in the fourth quarter, just what is going on in the economy, what is going on in the banking turmoil, and then what -- obviously we know will be a continued commitment towards consumers moving toward electronic payments. We just felt the prudent thing to do was to plan it for that 6 to 7% from our perspective.

**John Kraft** - D.A. Davidson - Analyst

Okay. That's fair. Because from your perspective those client losses from M&A obviously are impacting the volumes in '09. The -- the last question, I just wanted to talk broadly about margin target -- segmented margin targets, we have had -- it looks like on the check side in both direct and regular, these are the high owes levels we have seen forever, or in a long time. You said the target for direct would be pushing 30%. What about for financial institutions?

**Lee Schram** - Deluxe Corporation - CEO

Yes, I think, John, remember that the -- to think about the timing. When you think about the Q3 or the Q4 performance in both financial services and Direct Checks, most of the reductions that you get from a run rate benefit, and then the new ones that we -- we get out at the end of the year. We had the biggest quarter of cost takeout in Q4. So that obviously helps the financial performance. So I think the way to think about it for 2009 as I said in my prepared comments is plus or minus 1 to 2 points of 30% in Direct Checks, and, I would use mid -- the mid-double digits or -- for FS, and I would use the low double digits to maybe low teens for the small business services segment. I think that's pretty consistent with what we have -- what we have communicated historically.

**John Kraft** - D.A. Davidson - Analyst

Okay. That's helpful. Thanks, guys. Certainly some encouraging signs out there, I would say.

**Lee Schram** - Deluxe Corporation - CEO

Thank you, John.

**Operator**

And your next question comes from the line of James Clement from Sidoti. You may proceed.

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**James Clement** - Sidoti & Co. - Analyst

Good morning, gentlemen. Lee, my question is about the integration of e-commerce in some of your other businesses. I mean, can you take us through, what you have been able to accomplish in the back half of 2008, and what you want to accomplish in 2009 in terms of integrating whether it's -- Direct Checks, that web platform, the Shop Deluxe platform, as well as the -- the logo and networking -- the web services businesses that you have acquired. Can you walk us through a little bit more, sort of where you see those businesses going kind of in the next year or so, and the kind of work that you feel you need to do?

**Lee Schram** - Deluxe Corporation - CEO

I think the important thing, is Jamie is first of all what we inherited when we acquired NEBS several years ago. We had disparate systems and tools, just based on the philosophy NEBS management team had in running their various brands. What we've been working really hard at is bringing all those together and really getting all those. We believe that, as I said in my prepared comments again, that by the beginning of the second quarter, early in the second quarter, we will have 90% of all products and services on to one system, and then getting rid of all of those platforms and that -- the legacy platforms, and then, really, continuing to build upon that strong linkage to Deluxe.com. And we want to be able to have a seamless order entry and cross-selling for our call center sales force, and be able to bring that into a much simpler and a much clearer and a much cleaner overall e-commerce platform.

And then we see, again, as I said in my prepared comments the wonderful opportunity to continue to have the interface into, Hostopia, as I said earlier, but also to be able to leverage more products and services, really, more service in the case of Hostopia, on that unified technology platform. So it is bringing all of this together more and more, and the exciting news from our end is this is becoming more and more -- it's closer to being a reality for us. I mean there has been a lot of hard work that has gone in between the segments and our CIO function, but we're starting to get close, as you can hear now in my comments, to where we think we're going to have a lot more robust systems and tools. And just helps our customers, helps all of our call center associates and so on and so forth.

**James Clement** - Sidoti & Co. - Analyst

Just to follow-up, Lee, you just mentioned timing there. Are we sort of to understand that, by the end of 2009, significant progress will have been met so that the -- that what you want to have out there in terms of the storefront to your small business customers will be close to the way you want it? I mean is that the right time frame? Like a couple of quarters to a year? How should we think about that?

**Lee Schram** - Deluxe Corporation - CEO

I don't think you are ever done in this day and age with this. You use the word as we exit 2009, yes, I think we're going to have a much more robust, and kind of where -- where we want it to be, but always continuing to make improvements. We want to be able to stay ahead of what is out there, and what will be in the industry, but I think you're going to see a significantly stronger overall platform.

**James Clement** - Sidoti & Co. - Analyst

That is very fair. Thank you. And just one follow-up question, one thing that it was a little -- just a little bit curious about was I think you -- you mentioned in the prepared remarks that in FS, your average revenue per order was down. What sort of confused me about that a little bit was you did have a price increase during the quarter, but all of that together -- I was surprised by the magnitude that your -- your segment profit margin was up year-over-year. Was that all cost savings? What else might have been going on there?

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**Lee Schram** - *Deluxe Corporation - CEO*

Yes, I think you heard it right, Rick's comments, clearly the challenge is that this continues to be a very price-competitive market, and, some of it I think -- and obviously it is the competitive landscape, but also it is where the banks are at this point, and pushing the competitors and ourselves, in terms of where they see the value of checks in terms of the -- their model. But where did the big benefit come from? It clearly came from the fact that we have annualized benefit coming through from all of the cost reductions plus our strongest quarter of the year in terms of cost takeout. And that's just again, the timing of what happened, and that's why I made comments this year. It is not linear every quarter, but our best quarter was in Q4 of '08.

**James Clement** - *Sidoti & Co. - Analyst*

Okay. Great. Thank you very much for your time.

**Operator**

Your next question comes from the line of [Adam Stillman] from PPM America. You may proceed.

**Adam Stillman** - *PPM America - Analyst*

Thanks a lot. I just had a couple of quick housekeeping, I just missed it. For the full-year outlook, you said something about depreciation, and then you said including \$20 million of acquisition. Could you just repeat that please?

**Rick Greene** - *Deluxe Corporation - CFO*

Yes, for the outlook for 2009 in my comments I said the depreciation and amortization expense would be approximately \$70 million including \$19 million of acquisition-related amortization in that number.

**Adam Stillman** - *PPM America - Analyst*

Contract acquisition or -- you mean -- acquired companies?

**Rick Greene** - *Deluxe Corporation - CFO*

Acquired companies.

**Adam Stillman** - *PPM America - Analyst*

Acquired companies. Thank you. And did you say what the tax rate was?

**Rick Greene** - *Deluxe Corporation - CFO*

For the full year, approximately a 35% tax rate.

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**Adam Stillman** - PPM America - Analyst

Okay. Thank you. And then the second one is just to talk a little bit about -- I mean, it looks like in this quarter it was kind of an 11% decline. It looks like on the low end you are calling for that in Q1, and at the low end that's what you are calling for 2009. How much visibility to do you have into -- I mean into first quarter for instance? And then how do you -- how conservative do you think that kind of 11% decline is when you look out over the full year?

**Lee Schram** - Deluxe Corporation - CEO

I'm sorry what -- the last word?

**Adam Stillman** - PPM America - Analyst

How conservative.

**Lee Schram** - Deluxe Corporation - CEO

Oh, how conservative. Well, here's again, the way I would position, we try to put this out in our prepared comments. When we look at the top end of the 1.4 which we put out, that assumes that we are not going to get any improvement in the, what we see in the economy as we kind of exit 2008. What we then said is look, it's becoming harder to predict this. It's becoming harder for everybody. So what we said is that on the low end at the \$1.3 billion, that -- that that would say that over the course of the year that we would have continued deterioration in the business, and so the frames that we put out is, yes, we believe we have clearer visibility earlier in the year in the first quarter obviously, and closer to where we are today, but over time, that becomes harder to tell. No one has a clear picture of where the economy is going. So that's kind of the way we did our framework and our thinking. We think it is the prudent way to do it, and what we really like about our strategy is, we have got more and more after our cost structure. We've got more and more after improving our processes. Putting better metrics around them. And what we believe is we also are continuing the investments that we want to make organically, and then continuing to try to drive the acquisitions that we have done to get them to be a stronger foothold in our Company. And what we like about that is we believe that as we do that, if the economy does cooperate better than what we have predicted, that's going to help our operating income tremendously, and so that's the prudence of what we have done, and we just think it's the right way to do it, and we have got everybody rallied around that in terms of the way we're running the Company today.

**Adam Stillman** - PPM America - Analyst

All right. One more jut on capital allocation. I heard you loud and clear, and you guys have been good soldiers putting outlooks out there in light of what is low visibility for almost everybody. It is not rocket science to get to your -- you have a cash flow number, you have CapEx and you have the dividend which you basically said you plan on keeping, can you commit to a debt-reduction number? Or conversely do you have an acquisition number you are looking to spend this year?

**Rick Greene** - Deluxe Corporation - CFO

I think with the pieces of information that we have put out there around our operating cash flow guidance, and you mentioned CapEx and dividends, you have enough data there to be able to estimate what the debt reduction would be for the year.

**Lee Schram** - Deluxe Corporation - CEO

And I also mention, Adam, tuck-in acquisitions, so all we're trying to project is the same thing I just went through, a very balanced approach to being prudent now in the marketplace, given the -- the liquidity issues that are out there in the outside world, and

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then just being balanced with making sure we are doing the things organically, and through tuck-in acquisitions as it makes sense for us to continue to advance the ball here at Deluxe.

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**Adam Stillman** - PPM America - Analyst

Just to be clear here, to the extent -- are you saying you are going to pay down debt in the absence of any acquisitions? I mean, you are saying acquisitions, that would reduce the amount of debt you pay down, right?

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**Lee Schram** - Deluxe Corporation - CEO

If we did acquisitions, it would reduce the amount of debt you we pay down, yes. And we do not have a specific number of acquisitions or debt that we're giving here today.

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**Adam Stillman** - PPM America - Analyst

All right. Thank you very much.

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**Operator**

Your next question comes from the line of Todd Morgan from Oppenheimer and Company. You may proceed.

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**Todd Morgan** - Oppenheimer and Company - Analyst

Good morning.

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**Lee Schram** - Deluxe Corporation - CEO

Hi, Todd.

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**Todd Morgan** - Oppenheimer and Company - Analyst

Hi. You've talked about this a little bit but I was hoping you might be able to parse it again for us. Check order volume you said was down about 7% in the fourth quarter, and sort of a similar-type range is what you expect for the year. If I look at your past financial statements you've talked about order volume being down around 4.5% excluding acquisitions. I don't know if that's a comparison, if that sort of check trends would sort of foot both of those numbers, assuming that's the case it obviously spiked up in the fourth quarter. Can you give us a sense of how much of that would have been tied to the bank mergers, how much is the general economy, is there any way to delineate that and how much is -- any change in what you think is a secular shift going on there?

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**Lee Schram** - Deluxe Corporation - CEO

I can't, Todd, to be honest with you. It's just -- it's too short of period of time right now, and I mentioned we saw some of the banks that were acquired go down mid-quarter, but then they came back up, and so, what -- and we're not far enough into the new year here to see how predictive, the turmoil in the banking industry, and what other banks are going to play into that right now, and how deep it is going to go, how broad it is going to go, and then, again, we know electronic payments are moving over time and becoming more prevalent, and then the weakened economy, so our view is, look, we aren't going to -- we cannot

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figure out exactly what that historic 4 to 5% is right now, so we're just being prudent in the way we plan we believe in saying our view right now, best we can tell, is that 6 to 7% check order decline. Best we can do for you.

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**Todd Morgan** - *Oppenheimer and Company - Analyst*

Okay. Do you have any sense of what your sort of market share trend is in check printing at this point?

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**Lee Schram** - *Deluxe Corporation - CEO*

No, I don't, other than the fact that I have made comments around we have been retaining at record levels, and we have been winning deals as well in the -- clearly in the community, and in the credit union space, so I'll let you figure out market share from there.

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**Todd Morgan** - *Oppenheimer and Company - Analyst*

All right. Well, good, and then, I guess, lastly, 2009 -- I mean I think -- I appreciate you guys framing the sort of revenue stories as you have here. To the extent that that isn't the way the world turns, can you talk about what sort of contingency plans may exist or other things you could do on the cost front? Are there other things above and beyond the cost plans that you have for this year that might be available if needed?

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**Lee Schram** - *Deluxe Corporation - CEO*

Here is the way I would think about it. We put guidance out that we believe that we can make within the ranges that we have on the revenue, and the ranges that we have on earnings per share. And we tried giving our best -- and a lot of people are going away from it right now, but we believe we can make the guidance that we got out there, and we believe with what we have shown in the fourth quarter, is we went back to hard work and got more identified in terms of cost reductions, and I think the way to think about Deluxe is we're going to continue to do that and continue to operate that way, and if we see something that -- I think what you are alluding to if it gets even worse than the low end on the revenue, what would we do? We would continue to get after this as best as we can, and stay on top of it as early and we can, and hopefully be able to protect the low end of that \$1.95 that we put out there for earnings per share. And I think that's the way this management team has operated in the past. And I think you are going to continue to see us robustly staying after this as we move forward.

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**Todd Morgan** - *Oppenheimer and Company - Analyst*

Okay. Thanks, good luck.

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**Lee Schram** - *Deluxe Corporation - CEO*

Thank you.

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**Operator**

Your next question comes from the line of [Robert Korlic] from IH Capital. You may proceed.

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**Robert Korlic** - *IH Capital - Analyst*

Yes, good morning.

**Lee Schram** - *Deluxe Corporation - CEO*

Good morning, Robert.

**Robert Korlic** - *IH Capital - Analyst*

I just wanted to understand, it looks -- just looking through our numbers, assuming no acquisitions, it looks like you pay off your bank debt by the end of the year?

**Lee Schram** - *Deluxe Corporation - CEO*

There -- are you talking about the credit revolver?

**Robert Korlic** - *IH Capital - Analyst*

Yes.

**Lee Schram** - *Deluxe Corporation - CEO*

Yes.

**Robert Korlic** - *IH Capital - Analyst*

And where -- where is your bank debt now?

**Rick Greene** - *Deluxe Corporation - CFO*

In terms of the credit facilities?

**Robert Korlic** - *IH Capital - Analyst*

Yes, in terms of how much is outstanding?

**Rick Greene** - *Deluxe Corporation - CFO*

Approximately 80 million to \$85 million right now.

**Robert Korlic** - *IH Capital - Analyst*

80 to 85. Okay. So that's -- yes, that's what I figured. 85 would be the low end of your operating cash flow number.

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**Lee Schram** - *Deluxe Corporation - CEO*

Let -- the total debt at the end of the year, Robert was \$855 million.

**Robert Korlic** - *IH Capital - Analyst*

Right.

**Lee Schram** - *Deluxe Corporation - CEO*

Of that amount, 775 is in the 2012, 14s, and 15s.

**Robert Korlic** - *IH Capital - Analyst*

Correct.

**Lee Schram** - *Deluxe Corporation - CEO*

The balance of that is what Rick was alluding to in the credit facility.

**Robert Korlic** - *IH Capital - Analyst*

Right.

**Lee Schram** - *Deluxe Corporation - CEO*

I just wanted to make sure that we were clear.

**Robert Korlic** - *IH Capital - Analyst*

Yes, that what I was thinking about. And how are you thinking about further debt reduction? Would you consider buying back bonds at some point?

**Rick Greene** - *Deluxe Corporation - CFO*

Yes, I mean in recent year our debt reduction was focused primarily on paying down our credit facilities, but we also have the stability to consider opportunistic purchases of long-term maturities, either through open market purchases or private transactions and that's something that we have disclosed in our SEC filings.

**Robert Korlic** - *IH Capital - Analyst*

Very good. Thank you.

**Lee Schram** - *Deluxe Corporation - CEO*

You are welcome, Robert.

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**Operator**

And your next question comes from the line of Mike Hamilton from RBC. You may proceed.

**Mike Hamilton** - RBC - Analyst

This isn't as big a factor as perhaps in past years, but as we look out into fourth quarter next year with some of the discretionary items that typically have built in holiday cards, apparel, et cetera, obviously there is a lot more pressure there and some of these businesses may actually be eroding at an industry macro level. How are you thinking about those areas as part of the longer-term business model?

**Lee Schram** - Deluxe Corporation - CEO

As to whether or not, Mike, we stay in them or?

**Mike Hamilton** - RBC - Analyst

No. No. More what kind of growth is really available? Feel free if you want to touch on -- I assume at this juncture you aren't going anywhere on business that maybe they are for divestiture, but are areas like holiday cards moving toward a longer-term secular decline?

**Lee Schram** - Deluxe Corporation - CEO

I think that we want to be -- we absolutely believe there's growth in what we call the imaging and the -- and the apparel, and the -- and the -- those surrounding more discretionary type retail packaging-type product type of things. Do we believe that -- the way of -- Mike, to look at the holiday greeting card area, it is not a big growing market. It has never been a big-growing market, but because we have had such little volumes, primarily, it's not a big part of the Deluxe business. We have had an opportunity to gain wallet share in that space. And that's been the opportunity more than it's a big growth market for holiday greeting cards. That's a small growth market, but we have the ability to grab share. The challenge that we have had is, again, more -- we just sold less holiday greeting cards in the quarter, and by the way it wasn't just Deluxe. I think you're going to find that people in those segments that are out there, are going to tell you the same story. We've seen some of the releases on that as well. But no, we want to continue to be in the market. We think it is a good opportunity for us and we'll continue to play in the imaging and apparel, and retail packages, and, the holiday card space.

**Mike Hamilton** - RBC - Analyst

Yes. Thanks for the help.

**Lee Schram** - Deluxe Corporation - CEO

Thanks, Mike.

**Operator**

And we have no further questions in queue. I would now like to turn it over to Mr. Lee Schram for closing marks.

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**Lee Schram** - *Deluxe Corporation - CEO*

Thank you everybody for your participation and your questions today. And clearly we're going to get back to work here, and we look forward to providing another positive progress report on our next earnings call.

**Terry Peterson** - *Deluxe Corporation - VP, IR, CAO*

Just a reminder, a replay of this call will be available until February 2, by dialing 888-286-8010, when instructed provide the access code 82005908. The accompanying slides are archived in the investor relations section of Deluxe's website at [www.Deluxe.com](http://www.Deluxe.com). Again, thank you for joining us and have a good afternoon.

**Operator**

Thank you for your participation. You may now disconnect, and have a wonderful day.

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