

Keynote Systems
Second Quarter Fiscal 2007 Results Conference Call
Tuesday, May 1, 2007

I. Operator

- A. Good afternoon, everyone, and welcome to Keynote's conference call for the second quarter of fiscal year 2007, ending March 31, 2007. Today's call is being recorded.
- B. At this time, I would like to turn the call over to Kirsten Chapman for opening remarks and instructions.

II. Kirsten Chapman – *Lippert/Heilshorn & Associates – IR Contact*

- A. Thank you. Good afternoon, everyone, and welcome to Keynote's conference call for the fiscal 2007 second quarter ended March 31, 2007. I am here today with Umang Gupta, Chairman and Chief Executive Officer; and Drew Hamer, Chief Financial Officer. Umang and Drew will review our accomplishments for the quarter and then will be available to answer questions.
- B. Hopefully, by now, you have seen our press release that was distributed over Business Wire and the major wire services. For your convenience, the press release has also been posted on our website at www.keynote.com. The replay of this call will be available by telephone by dialing 800-642-1687 -- the pass code is # 4925751 -- or by webcast at the investor relations section of our website at www.keynote.com.
- C. I would like to remind you that statements made during the course of this call that are not purely historical are forward-looking statements regarding the Company or management's intentions, hopes, beliefs, expectations and strategies for the future. Because such statements deal with future events, they are subject to various risks and uncertainties, and actual results might differ materially from those projected in the forward-looking statements. Important factors that could cause actual results to differ materially from those in the forward-looking statements are discussed in today's press release and in the Company's annual and quarterly reports filed with the SEC.
- D. We have provided detailed guidance in our earnings release today, as we have in prior quarters. This guidance assumes no additional acquisitions or other significant or extraordinary transactions, other than those described in our earnings release. We will not comment on this guidance during the quarter, but may provide an update to this guidance in the event of material changes during the quarter.

- E. Before the company reviews the financials, I will review definitions for some metrics, which are not in accordance with generally accepted accounting principles, commonly known as GAAP.
1. The company defines non-GAAP net income or loss as net income or loss adjusted for provision for income taxes, less cash tax expense, stock-based compensation expense, and amortization of purchased intangibles. Non-GAAP net income per share equals non-GAAP net income divided by the weighted diluted share count as of that period end. Non-GAAP net loss per share equals non-GAAP net loss divided by the weighted basic share count as of that period end.
 2. Keynote SIGOS' revenue recognition policy under GAAP requires the amortization of most of Keynote SIGOS' software license revenues over a 12-month to 36-month period depending on the length of a contract. Therefore, Keynote's consolidated GAAP and non-GAAP earnings are likely to remain negative until quarterly GAAP revenues normalize with quarterly billings. Consequently, cash provided by operating activities, free cash flow and deferred revenue will be important metrics to measure Keynote's financial performance during that period.
 3. Free cash flow is defined as cash flow from operations less cash used for purchases of property, equipment, and software.
- F. Now, I would like to introduce Umang Gupta, Chairman and CEO of Keynote, who will review the company's quarterly highlights. Then Drew Hamer, Chief Financial Officer of Keynote, will provide the financial details for the second quarter and guidance for third quarter 2007. After which Umang will summarize the company's vision and open the call for questions. Please go ahead Umang.

Umang Gupta – Keynote Systems, Inc. – Chairman, CEO

G. Thanks Kirsten. Welcome, everyone, and thank you for joining us today.

1. Overall, our second quarter of fiscal 2007 was a great success. We delivered record total revenue of \$16.7 million, an increase of 31 percent as compared to last year. Revenue growth, combined with cost controls, resulted in another strong quarter of cash generation, and cash provided by operations was \$6.9 million, an all time high.
2. Mobile Test and Measurement once again had a stellar quarter, with Keynote SIGOS leading the charge. We acquired Keynote SIGOS a little more than one year ago, and I'd like to take a moment to discuss our accomplishments during that period. In the past quarter, our mobile business, most of which is attributable to Keynote SIGOS, delivered \$4.3 million in GAAP revenue and helped increase gross deferred revenues to \$26.1 million at the end of March 31, 2007. These are extraordinarily good numbers and they occurred earlier than we anticipated. We are very pleased with that financial performance. We are also pleased with the significant synergies we are beginning to see between the existing Keynote Mobile business and the acquired SIGOS business—particularly in the areas of technology exchange and customer acquisitions:
 - a) In terms of technology synergies,
 - (i) We have successfully integrated some of Keynote's Mobile Application Perspective content measurement components into the SIGOS SITE system, which is now undergoing testing at a major European mobile operator.
 - (ii) Keynote SIGOS' SIM multiplexer technology has become an integral component of the Mobile Perspective shared public infrastructure. Announced on March 27th, this network will be available by summer of this year in up to 20 locations globally. It will provide test and measurement access to mobile content developers and operators from more than 1,000 emulated handsets and dozens of real handsets, and it is capable of monitoring virtually all the major mobile networks of the world.
 - b) We have also begun to cross-sell products in our regions of strength.
 - (i) For example, we already have won two North American telecom customers for Keynote SIGOS, both of whom have begun to use SIGOS Global Roamer service. Our success was driven by the close cooperation between the Keynote SIGOS and US-based Keynote sales teams.
 - (ii) I am especially pleased to announce we recently signed a new agreement with Agilent whereby Agilent will become a preferred partner for the resale

and co-sale of the SITE System. As part of this new agreement, we are delighted to report Agilent will resell the SITE System in many parts of the world where we do not have direct sales capacity. In places where Keynote SIGOS already has direct sales relationships, such as Europe and North America, we will partner with Agilent on a co-sale basis as appropriate.

(iii) We whole-heartedly believe this is a win-win situation for both companies helping expand our possibilities for growth, especially beyond Europe and North America.

3. As thrilled as we are about our successes in the past year, this is just the beginning. We believe our shared infrastructure will deliver to mobile service providers, carriers and content developers a complete testing and monitoring service that is far superior and more cost effective than anything available from any of our competitors. We believe this infrastructure will lead to a significant increase in Keynote's customer base and provide seeding for bigger growth in years to come, especially among mobile content provider companies including the likes of MSN Mobile and AOL, both of whom are now customers of our Mobile Perspective Services.
4. As a point of reference, we believe in the past year Keynote SIGOS captured 40 percent market share of what OSS Observer estimates to be a \$50 million market for active testing and monitoring probes for mobile telecoms. We expect this market to grow approximately 25 percent per year. However, when combined with active testing and monitoring services for mobile content providers – we believe this market could grow even more significantly.

H. Internet Test and Measurement

1. While our Mobile products and services contributed a large part to our overall revenue growth, the majority of our revenue still comes from our Internet Test and Measurement products and services. Internet Subscriptions in the second quarter of fiscal 2007 grew quarter-over-quarter and year-over-year modestly, but more importantly, the replacement of single-page products with multi-page products continues at the steady pace we expected. In fact, we anticipate this replacement process could be finished within the next 24 months, at which point we no longer expect there to be an offsetting decline to the growth ramp of our transaction and broadband testing and monitoring revenue. It is important to note that our transaction and broadband revenues have demonstrated a historical compounded annual growth rate of 20 percent over the past five years.

2. Our load testing business did superbly and was a significant contributor to revenue in the quarter. Internet Test and Measurement key wins included Pitney Bowes, McKesson, Neiman Marcus, National Geographic, Shop Local and Zillow.
3. In the quarter, we also announced the availability of our Transaction Perspective High Frequency service – a strong product that delivers the true experience of the IE browser in a very cost-effective way to test Web 2.0 applications and content, notably Ajax and Flash. This product has already been met with great enthusiasm among our customers, and we believe will be a powerful and useful tool for our customers going forward - and should also contribute to a faster replacement cycle for our single-page products.

I. Customer Experience Test and Measurement

1. Our third business unit, CEM, is still progressing. Thanks to a stringent focus on containing costs, CEM continues to deliver efficiencies along with positive contribution margins, while we are implementing revenue growth programs that could start to bear fruit in the coming fiscal year.
2. One notable point was that Keynote Competitive Research reached one of its highest revenue quarters ever in the second quarter of 2007. Two examples of studies that were especially well received are as follows:
 - a) First, we conducted research that found AOL's marketing team was making significant improvements in AOL's image among search users. This was important information to our customer in light of intensive competition from Google, Yahoo!, MSN, and Ask.com.
 - b) Second, in a two phase contract, we first identified areas of improvement for Starwood Hotel's online marketing team, and then we determined if the steps implemented had successfully delivered improved results. Starwood was pleased to receive empirical evidence that it had in fact improved its marketing.
3. With that, I'd now like to turn the call over to Drew for a more detailed discussion of our financials.

III. Drew Hamer – Keynote Systems, Inc. – CFO, VP of Finance

- A. Thank you Umang.
- B. Ladies and Gentlemen, I am going to start by reviewing the financial details for the quarter.
 - 1. Our total revenue for the March quarter was \$16.7 million, compared to \$12.7 million in the same period last year and \$15.8 million last quarter. Total subscription services revenue was \$13.9 million or 83 percent of total revenue for the quarter. Subscription revenue posted a 40 percent increase compared to the same period last year and a 10 percent increase compared to last quarter, reflecting the previously mentioned success in our Mobile Test and Measurement products and greater demand for transaction and broadband test and measurement services. Professional services revenue of \$2.8 million, or 17 percent of total revenue for the quarter, remained flat compared to last year and declined 10 percent compared to last quarter.
 - 2. Our customer count was approximately 2,650 companies at both the end of March and December of last year – up from approximately 2,400 at March 31, 2006. We track the, the number of customers, excluding Keynote SIGOS, that purchased on an annualized basis at least \$100,000 or more of our services. In the second quarter it was 82 customers that represent 70 percent of total revenue, compared to 76 customers representing 70 percent of revenue and 85 customers representing 72 percent of revenue in the second quarter of 2006 and the first quarter of 2007, respectively.
 - 3. At the end of March 2007, we measured approximately 10,500 pages through our Internet Test and Measurement business. This compares to approximately 9,300 pages in the quarter a year ago and over 10,000 last quarter. For the second quarter 2007, overall average monthly revenue per page for the quarter was \$221, compared to \$234 and \$221 for the quarter a year ago and last quarter, respectively.
- C. Now, I'll review our expenses.
 - 1. Total expenses were \$18.0 million, including \$1.0 million in stock-based compensation expenses and a \$760,000 charge for amortization of intangible assets. Last quarter, total expenses were \$17.7 million, including \$920,000 of stock-based compensation expenses and a \$759,000 charge for amortization of intangible assets. In the second quarter 2006, total expenses were \$13.8 million, including \$908,000 of stock-based compensation expenses and a \$418,000 charge for amortization of intangible assets. The increases in year-over-year expenses are primarily due to the SIGOS acquisition.
- D. For the second quarter of fiscal year 2007, net income was \$30,000, or \$0.00 per diluted share, on a GAAP basis, which included the aforementioned charges as well as a \$193,000

income tax benefit. For the second quarter of fiscal year 2006, the net loss was \$154,000, or \$0.01 per diluted share, on a GAAP basis, which included the aforementioned charges and a tax provision of \$373,000.

- E. The non-GAAP net income for the quarter was \$1.4 million, or \$0.08 per diluted share, compared to non-GAAP net income of \$1.5 million, or \$0.08 per diluted share, for the same quarter a year ago.
- F. Now, moving to the balance sheet and our cash performance metrics,
 - 1. At March 31, 2007, our cash and short-term investments balance was \$93.2 million.
 - 2. For the quarter, cash provided by operating activities was \$6.9 million, compared to \$2.9 million for the same period last year.
 - 3. We invested \$1.4 million in property, equipment and software this quarter and \$1.1 million in the same quarter last year.
 - 4. Also, we generated free cash flow of \$5.5 million for the quarter, compared to \$1.9 million for the second quarter of 2006.
- G. As of March 31, 2007, accounts receivable net was \$6.0 million. DSOs were 32 days and 98 percent of accounts receivable were less than 90 days old.
- H. Total net deferred revenue at March 31, 2007 was \$19.5 million, up 33 percent compared to \$14.7 million at December 31, 2006 and up 174 percent from \$7.1 million at March 30, 2006.
- I. Ladies and Gentlemen, having reviewed the financial details for the quarter, I would like to provide some general guidance for the June 2007 quarter. The company consolidated Keynote SIGOS' financial reporting under U.S. GAAP rules starting April 3, 2006. U.S. GAAP required Keynote SIGOS' system license revenue to be ratably recognized over the initial duration of each customer contract, which ranges from 12 months to 36 months.
- J. As a result, Keynote will be able to recognize as revenues only a fraction of Keynote SIGOS' sales during 2007. Accordingly the acquisition will be dilutive to Keynote's U.S. GAAP net income although cash flow from operations is expected to be positive throughout.
- K. Management is providing the following guidance for the 2007 fiscal third quarter ending June 30, 2007:
 - 1. Total revenue is expected to be between \$16.7 million and \$17.2 million.
 - 2. Net earnings/loss per share is expected to be between a loss of (\$0.02) and earnings of \$0.02.
 - 3. Non-GAAP earnings per share are expected to be between \$0.05 and \$0.08.

4. Cash provided by operating activities is expected to be between \$3.5 million and \$4.0 million.
 5. Free cash flow is expected to be between \$2.0 million and \$2.5 million.
 6. When combined with our performance for the last six months, our third quarter projections for cash from operations lead us to believe fiscal 2007 will be a record year for cash from operations.
- L. The above guidance was based on the following assumptions:
1. Total stock-based compensation expense and amortization of intangible assets is expected to be approximately \$1.8 million.
 2. Interest income, net is expected to be approximately \$1.0 million, assuming no material changes in interest rates and currently planned use of cash.
 3. Cash paid for income taxes is expected to be approximately \$400,000, assuming no changes in required tax payments.
 4. Basic weighted average shares outstanding are expected to be approximately 17.3 million shares and diluted weighted average shares outstanding are expected to be approximately 18.0 million shares, assuming no additional issuances of equity or equity-related securities.
 5. Please note that for third quarter we have increased our purchases of property, equipment and software. We did this based upon scheduled tenant improvements related to a recently signed long-term tenant that will be occupying the fourth floor of our building. This brings our building occupancy to almost 90 percent when including the portion occupied by Keynote. We estimate that as a result of this investment and our new occupancy rate we will generate approximately \$800,000 in excess occupancy income in the full fiscal year of 2008.
- M. With that, I would like to return the call to Umang.

// Umang Gupta – Close

- A. Thank you Drew.
1. Keynote has been a leader and a pioneer in the internet industry and now is taking that spirit into the mobile industry and into the world of the new internet. The New Internet, sometimes also called Web 2.0, is all about mobile, broadband and programmable content and services. Thanks to our talented engineering staff, in the past year we delivered very cutting edge products in all three areas – products that we believe have been of great benefit to our customers and strengthened customer loyalty. Our product

innovation has also enabled us to put a premium price on our products. While the industry continues to get very competitive, we believe it is our ability to innovate and to build superior “software as a service” products that will enable us to expand our market share and grow revenues and profitability.

2. Of course in order to do that we must continue to invest in R&D and our sales and marketing platform. We have been doing so at a steady pace for the last year and have already started to see some results. We expect to continue that pace in the future.
3. We are excited about our opportunities and look forward to sharing our future successes with you.

B. Now, Drew and I would be more than happy to take any questions you have. Thank you.

IV. Operator Runs Q&A

V. Umang Gupta – Close

C. Thank you again for joining us today. As usual, we appreciate your support and look forward to discussing our company with you at various investor conferences we have scheduled in the upcoming months:

1. Both Drew and I will be presenting at the upcoming AeA Micro Cap Conference in Monterey California on May 7th.
2. Drew will also be presenting at the FBR Conference in New York City on May 30th and the Kaufman Brothers Conference in Boston on June 6th.
3. In addition, our investor relations firm Lippert/Heilshorn & Associates is arranging 1-on-1 investor meetings in late May and early June in these two cities. Please give them a call if you are interested in setting up a meeting.