Learning Tree International, Inc.
Fiscal 2006 Second Quarter Conference Call

Remarks by Mr. Nicholas Schacht, President and Chief Executive Officer

May 9, 2006

As a reminder, except for historical statements, the matters addressed in this conference call are forward-looking statements. Please do not put undue reliance on these forward-looking statements, since they are based on key assumptions about future risks and uncertainties. Although we believe that our assumptions are reasonable, inevitably some will prove to be incorrect. As a result, our actual future results can be expected to differ from those discussed in this call, and those differences may be material. We are not undertaking any obligation to update forward-looking statements.

To help you assess the major risks in our business, we have identified many, but not all, of them in Exhibit 99.1 to our Form 10K. Please read that exhibit carefully. Some of the factors discussed in Exhibit 99.1 that could affect us include risks associated with:

* The timely development, introduction, and customer acceptance of our courses;
* Competition;
* International operations, including currency fluctuations;
* Changing economic and market conditions;
* Technology development and new technology introduction;
* Efficient delivery and scheduling of our courses;
* Adverse weather conditions, strikes, acts of war or terrorism and other external events;
* Attracting and retaining qualified personnel.

I will begin today’s presentation by covering our performance in our second quarter and first six months of fiscal 2006, which ended March 31, 2006. I will then provide some forward-looking information about our forthcoming third quarter. After my presentation, we will open the floor for questions and discussion. LeMoyne Zacherl, our Chief Financial Officer, will join me in the Q&A section of this conference call.

For your convenience, we have posted the text of these prepared remarks in the Investor Relations section of our website. Go to: http://www.learningtree.com/investor.

Overall Results

Our revenues in the second quarter of fiscal 2006 were $34.3 million compared to revenues of $34.9 million for the same quarter last year. We recorded a loss from operations of $3.8 million in our second quarter compared to a loss from operations of $3.6 million for the same quarter of fiscal 2005. We reported a net loss for the second quarter of $1.9 million, or 11 cents per share, compared to a net loss of $0.9 million or 5 cents per share, for the same quarter last year. The disparity in net loss relates primarily to the substantial difference in the annual effective tax rate of 46% for fiscal 2006 compared to 67% for fiscal 2005, when permanent differences resulted in an unusually high tax rate because of that year's small pre-tax income. This year's 46% rate reflects a lesser effect of permanent differences in anticipation of somewhat improved annual pre-tax income.

For the six months ended March 31, 2006, our revenues were $74.1 million, compared to $74.6 million last year. During the first six months of fiscal 2006, we reported a loss from operations of $864,000 compared to a loss of $1.0 million for the same period in fiscal 2005. Net income was $345,000 compared to $26,000 for the same period last year. And net income per diluted share for the first six months of fiscal 2005 was $0.02 versus $0.00 in the same period of our prior year.

Although our results for our second quarter are in line with the guidance we provided in our last conference call, we are not satisfied with the performance of the company at the present time. We are taking steps to improve our profitability both in the short and long term through a combination of efforts to increase revenues and to reduce costs. We will describe some of these efforts in more detail in this call, and others in future conference calls.

Several common factors pertain to the financial discussion which follows. First, our management courses have a shorter average duration than our IT courses and, therefore, typically have a lower average revenue per event and cost per event than our IT courses. Management courses also use less computer equipment on average than our IT courses, and this further reduces their comparative cost per event. Additionally, courses held at customer locations are shorter, on average, than courses held in our own education centers. As a result, they typically have lower average revenue and lower cost per event. Finally, cost per event for courses held at customer locations is further reduced from those held in our own education centers because the cost of facilities is typically borne by the customer.

Second Quarter Revenue

During our second quarter of fiscal 2006, we trained 20,686 course participants, a 6% increase from the 19,471 participants we trained in the same quarter last year. In our second quarter of fiscal 2006, average revenue per attendee was 8% lower than in the same quarter of the prior fiscal year as a result of an unfavorable 4% effect of changes in foreign exchange rates and a decline in average revenue per attendee of 4% compared to the same quarter of the prior fiscal year. Excluding the effect of exchange rates, the decline in average revenue per attendee was primarily due to an increase in the number of courses held at customer locations and, to a lesser extent, an increase in the percentage of attendees at our management courses.

While we are pleased that the number of attendees at our courses continues to increase, we are now focusing on ways to increase revenue with similar effect. We are examining all aspects of our marketing processes, sales activities, and pricing to identify approaches to materially growing our revenues.

Second Quarter Operations
I will now discuss our operations in our second quarter of fiscal 2006 and how they compare with the same quarter last year.

Cost of Revenues. Cost of revenues increased to 53.3% of revenues in our second quarter of fiscal 2006 compared to 52.9% in our second quarter of fiscal 2005.

Changes in foreign exchange rates did not materially affect our gross profit percentage, since exchange rate changes decreased our cost of revenues by approximately the same percentage as they decreased our revenues in the quarter.

Excluding the effect of exchange rates, the cost of revenues as a percentage of revenues in our second quarter of fiscal 2006 compared to the same period in the prior year reflects a 5% decrease in our average revenue per event, largely offset by a 4% decrease in the average cost per event. The decrease in average revenue per event, excluding the effect of exchange rates, results principally from the decrease in average revenue per attendee discussed earlier, as well as a reduction of 1% in average attendees per event. The decrease in average cost per event compared to the prior period, excluding the effect of exchange rates, primarily results from a higher percentage of courses held at customer locations and, to a lesser extent, an increase in the percentage of management courses held during the quarter.

During our second quarter of fiscal 2006, we presented 1,749 events, a 7% increase from the 1,634 events conducted during the same period in fiscal 2005. This increase consisted entirely of additional events conducted at customer sites in the second quarter this year compared to the same period in the prior year.

We continue to be dissatisfied with our gross margin performance. We have taken steps to reduce facility-related expenses, the full impact of which will not be felt until future quarters. For example, in the second quarter of fiscal 2006, we signed a lease for a new education center in New York City and we will begin to see significantly reduced costs for that location in the fourth quarter of fiscal 2006. We are also considering changes at several other education centers, and we are carefully investigating every direct cost category to identify additional cost reductions we can make while maintaining the quality of our courses.

Course Development Expense. Beginning in the second quarter of fiscal 2006, we have significantly increased our spending on course development. We have identified a number of new IT and management course titles which, based on our research, we expect will bring additional attendees. We have accelerated our course development processes and are now producing more new titles more quickly than at any point in our recent history. In the second quarter of fiscal 2006, we introduced twelve new titles compared to an average of just over 4 new titles per quarter for the preceding four quarters. Our new titles included four management course titles and eight technology course titles. We also retired four course titles during the quarter. As a result, our library of instructor-led courses numbered 153 titles at the end of our second quarter of fiscal 2006 compared with 138 titles at the same point a year earlier.

Additionally, based on the strength of our customers' reception to our management curriculum, we believe that we have a significant opportunity to capture market share and continue growing our attendees at our management courses by offering customers a product that is better and different from anything available in the market today. Accordingly, we have initiated an intensive project to revise our management courses using proprietary, innovative instructional methods that we have developed internally, and which significantly advance the state of the art in instructor-led management training. Participant reaction to the first course title incorporating this new approach has been very positive, and we have now begun to rebuild a total of 15 management titles using this proprietary technique.

Our increased course development activity also requires an increased cash outlay. During the second quarter of fiscal 2006, course development expenses increased to 7.1% of revenues from 5.8% during the same quarter of the prior year. Course development expenses in our second quarter this year were $2.4 million, compared with $2.0 million in our second quarter last year.

Sales and Marketing Expense. Sales and marketing expense in our second quarter was 33.2% of revenues, compared with 32.8% for the same quarter in the prior year. Sales and marketing expense remained at $11.4 million, the same as during the second quarter of fiscal 2005. Our sales and marketing expenses in the current quarter included an increase in compensation expense for sales personnel compared to the same quarter in the prior year, offset by reductions in catalogs mailed during the quarter and the effect of changes in foreign exchange rates.

Our sales and marketing expense—and, in particular, our expenditure on course catalogs—is one of our largest expenditures. We have carefully adjusted the market segments to which we mail our catalogs, and are presently evaluating a number of additional ways to increase the efficiency of our marketing expenditures by spending less without materially affecting the response to that marketing. At the same time, we have been increasing our sales staff in certain operating units with appropriately trained and managed personnel, Based on our experience to date in those operating units, we believe that this strategy can contribute to revenue growth. Accordingly, we intend to continue expanding our sales staffing in order to implement this strategy in all operating units.

General and Administrative Expense. G&A expense in our second quarter decreased to 17.5% of revenues compared with 18.8% in the same quarter of our prior year. G&A expense in our second quarter was $6.0 million compared to $6.6 million in our second quarter last year. The decrease in our G&A expense primarily reflects some of the success of our efforts to reduce facility infrastructure costs as well as the effect of changes in foreign exchange rates, offset by $0.2 million in costs related to our adoption of FAS 123R.

Our second quarter results include expenses associated with stock option compensation in accordance with FAS 123R. Total FAS 123R expense for our second quarter was $0.3 million, the majority of which is recorded as general and administrative expense, as noted above. The remainder of our FAS 123R expense is apportioned among our other expense categories, based on where we record the labor costs for the individuals with whom the stock option compensation expense is associated. We do not expect the distribution of FAS 123R expense among expense categories to differ significantly from one quarter to the next. As we adopted FAS 123R effective October 1, 2005, we did not report stock option compensation expense in any quarter of fiscal 2005.

Results from Operations. As a result of these factors, we reported a loss from operations as a percentage of revenues of 11.1% compared to 10.4% in the same quarter of our prior year.

Other Income and Expense. In our second quarter of fiscal 2006, we recorded foreign exchange losses of $21,000 compared to losses of $40,000 in the same quarter of the prior year. In addition, in fiscal 2006 we had interest income of $836,000 compared to $596,000 in the same period of the prior year. The increase in interest income primarily reflects higher interest rates compared to those in the prior year.

Income Taxes. Our income tax provision in our second quarter of fiscal 2006 reflects a projected 46% annual effective tax rate, compared to the 67% annual effective tax rate we used in the second quarter of fiscal 2005. We have a number of sizeable permanent tax differences that result in a higher annual effective tax rate as pre-tax income decreases to low levels. Therefore, fiscal 2006 requires a lower effective tax rate than fiscal 2005 because of higher projected pre-tax income this year than in the prior year.

Net Income. In summary, our net loss for the second quarter of fiscal 2006 was 5.5% of revenues compared to 2.5% in our second quarter of fiscal 2005.

Liquidity and Capital Resources

During the six months ended March 31, 2006, the total of cash and available for sale securities decreased to $75.1 million from $75.3 million at September 30, 2005. This decrease primarily reflects the net effect of cash generated from operations of $4.9 million offset by fixed asset purchases of $2.7 million, the establishment of a long-term interest-bearing lease deposit of $1.5 million related to the lease for our new education center in New York, and the purchase of our Common Stock in the amount of $0.7 million. In the second quarter of fiscal 2006 we repurchased 60,927 shares of our common stock at an average price of $12.01. We may make additional purchases of our Common Stock through open-market transactions, but have no commitment to do so.

During the current quarter, we expect to make a significant cash outlay as we build out our new education center in New York. Those costs will be capitalized and depreciated over the anticipated ten-year life of that facility and, as we noted earlier, we expect to begin to see substantial savings in the fourth quarter of fiscal 2006.

Recent Trends
We are pleased to see continued increased demand for our management courses. We believe these results validate our previous statements about the market opportunity for training in project management, personal effectiveness and other key business skills. Accordingly, as we discussed earlier, our development plans for fiscal 2006 include a large number of new management course titles. In our second quarter of fiscal 2006 we offered 36 titles in our management curriculum, representing 24% of our overall library, compared to 30 titles, or 22%, in the second quarter of fiscal 2005. We currently plan to introduce approximately 10 more new management titles in the remaining two quarters of fiscal 2006. Also, as noted earlier, we are in the process of rebuilding 15 of our management titles to incorporate our new proprietary delivery and instructional methods which advance the state of the art in management training, with the ultimate intent of further increasing our competitiveness in the management training market.

As we have for the past 31 years, we continue to emphasize excellence in educating and training managers and IT professionals from government and commercial organizations around the world. We believe that quality is a significant differentiator in the eyes of our customers, and that Learning Tree's proven long-term record of exceptional performance is a reason for the tremendous loyalty of our customers. It is worth noting that all of our top 100 customers from 2000 remain Learning Tree customers today. We continue our emphasis on excellence by improving our core strengths: our expert instructors, proprietary content library, state-of-the-art classrooms, and worldwide course delivery systems.

Effect of Exchange Rates. Approximately half of our business annually is conducted in currencies other than US dollars and fluctuations in exchange rates will affect future revenues and expenses when translated into dollars. If the exchange rates of April 28, 2006 remain stable through the remainder of fiscal 2006, our revenues would be unfavorably affected by approximately 1% in both the third quarter and for our full fiscal year compared to the corresponding periods in fiscal 2005. Conversely, our expenses would be favorably affected by similar percentages in these periods.

Third Quarter 2006 Revenues
Our backlog at March 31, 2006 was $35.2 million, approximately 3% lower than it had been on April 1, 2005. This March 31, 2006 backlog included a 2% negative effect from changes in foreign exchange rates. Four weeks later, at April 28, 2006, our overall backlog was 1% higher than it had been on April 29, 2005. And, at April 28, 2006, the sum of our revenues for April courses plus our backlog for May and June courses was 5% lower than it had been at April 29, 2005. These April 28, 2006 backlogs each included no effect from changes in foreign exchange rates.

For many years we have provided these backlog metrics, which have significantly contributed to our forecasts of revenues for upcoming quarters. While historically the backlog metrics have been good indicators of long-term trends in our revenue performance, we have identified that in the past two years they have had relatively little value in short-term forecasts in the current environment. We discussed this recent tendency in our last conference call. We have studied this phenomenon further and have concluded that in recent periods, the effect of short-term changes in customer ordering, enrollment, and cancellation patterns on actual revenue attainment has eclipsed the predictive value of relative changes in backorder levels. Therefore, effective with our next earnings release we will discontinue our practice of providing this metric until such time as we believe it has again become meaningful.

In anticipation of discontinuing the release of overall backlog data, let me take a moment to explain our forecasting process. To forecast our revenues we continue to look at, but now place relatively little weight on, total current backlog in and of itself. Instead, we incorporate elements of this backlog information together with current enrollment and sales trends, customer cancellation trends, and our own processes for scheduling and postponing events. Each of these factors is evaluated by operating unit and by product line. From this process we derive the revenue and gross margin ranges that we provide in our guidance.

In our future conference calls and quarterly filings, we intend to continue to provide our best assessment of a range of predicted revenues for the successive quarter. We currently project that our revenues in the third quarter of fiscal 2006 will be between $38.8 million and $40.8 million, compared to $40.5 million in the same quarter of the prior year.

Third Quarter Gross Profit. We expect our gross profit percentage in the third quarter of fiscal 2006 to be between 49.5% and 51.0% compared to 49.4% in our third quarter of fiscal 2005. These projections do not incorporate the potential results of any future cost-saving actions we may take as a result of the efforts we discussed earlier; however we would expect minimal impact from those actions in the third quarter of fiscal 2006.

Third Quarter Operating Expenses. We expect our overall operating expenses for our third quarter of fiscal 2006 to be approximately $20.5 million, compared to $19.5 million in the same quarter a year earlier. Compared to the third quarter of fiscal 2005, this increase primarily reflects our increased spending on course development, increased costs of sales compensation, and compensation expense related to stock options as a result of our adoption of FAS 123R, partially offset by the effect of changes in foreign exchange rates and savings in our marketing expenses. As noted earlier, we are focusing on ways to improve the efficiency of our spending on marketing, but we do not expect the results of those efforts will have any additional impact in our third quarter of fiscal 2006. We expect to spend approximately $0.8 million more on product development in the third quarter of fiscal 2006 than in the same quarter last year. These increased expenditures relate to our planned introduction of 15 new course titles in the third and fourth quarters of fiscal 2006 as well as the project to further enhance our management course offerings that I discussed earlier.

Third Quarter Interest Income. Our interest income reflects changes in interest rates, as well as changes in our cash balances. We expect our third quarter interest income to be approximately $0.8 million.

2006 Tax Rate. We estimate that our effective tax rate in the third quarter of fiscal 2006 will be approximately 46%, compared to an effective tax rate of approximately 67% for the third quarter of the prior year. The 67% effective tax rate for the third quarter of fiscal 2005 does not include the effect of a $1.1 million charge in that quarter due to the correction of an error on our fiscal 2001 income tax return.

Summary. In summary, we are looking forward to the results of our initiatives directed toward increasing revenues in both our management and IT product lines and reducing our costs. We are excited about the opportunities we see for significantly expanding our use of innovative instructional technology in our management curriculum, adding new courses at an increased rate, refining our marketing expenditures, and improving our gross margins.

Summary following discussion

Over the last 31 years, Learning Tree has built a strong position as the world's leading, vendor-independent provider of training for managers and technology professionals. Our instructors, our content, our classrooms and our worldwide delivery systems continue to raise the standards for quality and effectiveness in the industry. The goal of our quality processes and training methods is that each and every individual we train acquires the skills and knowledge needed to succeed in his or her job. We remain committed to the proposition that the long-term success of our customers depends in part on their investment in technology and in the training of their personnel to leverage that investment. We look forward to continuing to help our customers maximize the productivity and the effectiveness of their people.