

## **Tescom Software Systems Testing Ltd. (“Tescom” or “the Company”)**

Interim Results for the Six Months ended 30 June 2007

Tescom Software Systems Testing Ltd. (Symbol: TSCM), the international quality assurance and software testing service provider, announces its interim results for the six months ended 30 June 2007.

### **Highlights**

- Revenues amounting to \$27.5m, versus \$26.8m in 2006
- Gross margins were 34.0%, compared to 32.1% in 2006
- Profit before tax was \$1.4m, versus \$1.1m in 2006
- Diluted earnings per share were \$0.06, versus \$0.05 in 2006
- Strengthening of senior sales and account management personnel in the UK, US and Israel
- Continued emphasis on European activities, which comprise over 54% of consolidated revenues, versus 51% in 2006

Ofer Albeck, CEO of Tescom, said: “Tescom’s H107 results reflect an improvement in gross margins, alongside stability in revenues. During H107, we re-focused our efforts on large-scale, long-term projects, which resulted in improved gross margins, alongside a decrease in revenues in the short term. We have also significantly enhanced our investments in sales and marketing resources on a global basis. These actions, which were taken for their long-term benefits to the Company, are expected to result in a relatively modest increase in our top line and a decrease in operating profitability for the remainder of 2007.

The Company expects to benefit from its continued emphasis on the European market, now representing more than 54% of its total revenues, which has significantly higher gross margins. Tescom continues to focus its efforts on growth from new large-scale, long-term contracts, as well as on cultivating its well established account management with existing customers.

We expect to leverage our investments in sales and marketing, along with our previous investments in infrastructure and management, in order to achieve consistent, sustainable long-term growth in both revenues and profitability”.

### **Enquiries:**

#### **Tescom**

Ofer Albeck, CEO	+ 972 3 535 0990
Phil Serlin, VP Finance	+ 972 3 535 0990
Ravit Halevy, VP Corporate Development	+ 972 3 535 0990

#### **Landsbanki Securities (UK) Limited** (Nominated Adviser)

Tom Hulme	+44 (0)20 7426 9593
-----------	---------------------

## **Chief Executive's Review**

Tescom's revenues for H107 of \$27.5m remained stable in comparison to revenues of \$26.8m in H106. These figures reflect the weakening of the US dollar against the major currencies of the Group of approximately 10% on a weighted average basis for H107 in comparison to H106.

Gross margins have increased to 34.0% from 32.1% in the corresponding 2006 period, as we begin to see the effects of improved account and delivery management. As part of our continuing efforts to improve our margins, we have also invested in establishing a "near-shore" operation in Israel. This operation is expected to bring results in 2008. We anticipate that our near-shore experience from this operation will enhance our global off-shore capabilities in the future.

During H107, we made a strategic decision to significantly enhance our sales and marketing efforts on a global basis, as we believe our previous investments in delivery management have provided us solid delivery capabilities and the necessary infrastructure for expansion. As part of this decision, we have focused our investments in enlarging and upgrading our sales force in most of our territories.

Overseas activities have grown to represent over 54% of consolidated revenues, in comparison to 51% for the same period in 2006, and this percentage is expected to increase.

Within the framework of the Company's enhanced sales and marketing efforts, we recognized an opportunity to compete on a substantial tender for Tescom in the European market. This tender, while consuming significant resources and management attention, resulted in our entering into new alliances and refining our marketing tools. This experience will serve the Company in realizing similar opportunities in the future. We are proud of the efforts invested by our local and global resources to produce a high-quality submission. We are currently waiting to receive formal notification with regard to the tender.

Tescom continues to make progress in the US, and has invested in new senior sales and delivery management. These investments are expected to have a positive effect on long-term revenue and profitability growth. In the Asia-Pacific region, Tescom has increased its off-shore contract activities.

Tescom Israel has re-focused its efforts on large-scale projects for the long term. These actions are expected to result in improved gross margins in the long term, alongside a decrease in revenues in the short term. The Company has recently established a low-cost, near-shore operation in Modi'in Elite, which has successfully completed training of the first group of new employees. This operation is part of an Israeli-government subsidized programme to provide employment and training to certain segments of the population. The Company has also been successful at gaining new contracts in the insurance sector and has won the principal tender for testing issued by the IDF (Israel Defence Forces)

We expect to leverage our investments in sales and marketing, along with our previous investments in infrastructure and management, in order to achieve consistent, sustainable long-term growth in both revenues and profitability.

I also wish to thank our employees for their continued efforts on the Company's behalf.

## **Financial Review**

### **Results**

Revenues for H107 of \$27.5m remained stable in comparison to the corresponding period in 2006. Revenue increases in Europe, the US and Asia-Pacific, mainly as a result of new contracts in these locations, were offset by a decline in revenues in Israel.

Pre-tax profit amounted to \$1.4m, versus \$1.1m in 2006. Gross profit margins increased to 34.0% from 32.1% in the 2006 period, mainly as a result of higher margin contracts in Israel, the US and Australia. G&A expenses increased slightly, to \$5.8m from \$5.7m in 2006. Sales and marketing expenditure increased by 13.6%, to \$1.9m from \$1.6m in the 2006 period.

The Company's revenues and operating profit were positively affected by the weakening of the US dollar against the major currencies of the Group (Pound Sterling, Euro and Israeli Shekel) of approximately 10% on a weighted average basis for H107 in comparison to H106.

Net financial expenses increased by \$0.1m, as a result of fluctuations in the exchange rates between the NIS, the dollar and the other operating currencies in the various Group locations.

The Company generated \$0.5m in cash from operating activities during H107, versus utilizing \$1.1m in H106. The increase in operating cash flows results primarily from a smaller increase in trade receivables, as opposed to the corresponding period last year. The Company's cash balance at 30 June 2007 was \$1.7m, which reflects the payment of a \$0.9m dividend during the second quarter. The Company maintains short-term bank credit lines in both Israel and the UK in the aggregate amount of approximately \$8.0m. \$3.0m had been drawn against these credit lines as of 30 June 2007.

### **Dividends**

The Company's dividend policy is subject to the future performance of the Company and its funding requirements. In March 2007, the Company declared a final dividend of \$0.9m on account of 2006, which was paid on 2 May 2007.

### **Outlook**

Tescom expects a relatively modest increase in its top line and a decrease in operating profitability for the remainder of 2007. Our focus on long-term, large-scale projects has resulted in improved gross margins, alongside a decrease in revenues in the short term. Our increased investments in sales and marketing, while reducing operating profit in 2007, are expected to bring results in 2008.

The Company expects to benefit from its continued emphasis on the European market, now representing more than 54% of its total revenues, which has significantly higher gross margins. Tescom continues to focus its efforts on growth from new large-scale, long-term contracts, as well as on cultivating its well established account management with existing customers.

The Board of Tescom continues to examine a number of strategic opportunities to expand its businesses in its current territories and enhance shareholder value.

**TESCOM SOFTWARE SYSTEMS TESTING LTD.****CONSOLIDATED BALANCE SHEETS****In thousands of US dollars**

	<b>December 31, 2006</b>	<b>June 30, 2007</b>
	<b>Audited</b>	<b>Unaudited</b>
<b>ASSETS</b>		
<b>CURRENT ASSETS:</b>		
Cash and cash equivalents	2,071	1,725
Trade receivables	13,830	14,424
Other current assets and prepaid expenses	1,227	1,733
Total current assets	17,128	17,882
<b>NON-CURRENT ASSETS:</b>		
Severance pay fund	2,267	2,245
Property and equipment, net	1,661	1,906
Deferred income taxes	1,379	1,504
Goodwill and other intangible assets	432	403
Total non-current assets	5,739	6,058
Total assets	22,867	23,940

The accompanying notes are an integral part of the consolidated financial statements.

**TESCOM SOFTWARE SYSTEMS TESTING LTD.**

**CONSOLIDATED BALANCE SHEETS**

**In thousands of US dollars**

	<b>December 31, 2006</b>	<b>June 30, 2007</b>
	<b>Audited</b>	<b>Unaudited</b>
<b>LIABILITIES AND EQUITY</b>		
<b>CURRENT LIABILITIES:</b>		
Short-term credit and current portion of long-term loans	2,506	2,987
Trade payables	1,336	1,508
Income taxes payable	293	587
Other current liabilities and accrued expenses	6,868	6,846
Total current liabilities	11,003	11,928
<b>LONG-TERM LIABILITIES:</b>		
Long-term loans	252	273
Accrued severance pay	2,691	2,709
Total long-term liabilities	2,943	2,982
<b>EQUITY:</b>		
Share capital	51	51
Share premium	10,480	10,516
Treasury shares, at cost	(328)	(328)
Foreign currency translation reserve	(732)	(717)
Accumulated deficit	(550)	(492)
	8,921	9,030
	22,867	23,940

The accompanying notes are an integral part of the consolidated financial statements.

August 30, 2007

Date of approval of the  
financial statements

Ofer Albeck  
CEO and Chairman of  
the Board of Directors

Philip Serlin  
Vice President, Finance

**TESCOM SOFTWARE SYSTEMS TESTING LTD.**

**CONSOLIDATED STATEMENTS OF OPERATIONS**

**In thousands of US dollars, except share and per share data**

	<b>Year ended December 31, 2006</b>	<b>Six months ended June 30,</b>	
	<b>Audited</b>	<b>2006</b>	<b>2007</b>
		<b>Unaudited</b>	
Revenues	53,437	26,760	27,490
Cost of revenues	35,808	18,171	18,146
Gross profit	17,629	8,589	9,344
Operating expenses:			
Selling and marketing	3,121	1,630	2,022
General and administrative	11,389	5,728	5,716
Total operating expenses	14,510	7,358	7,738
Operating income	3,119	1,231	1,606
Financial income	106	28	81
Financial expenses	(244)	(156)	(294)
Other expenses, net	(4)	(5)	-
Profit before taxes on income	2,977	1,098	1,393
Taxes on income	657	350	427
Net profit	2,320	748	966
Basic and diluted net earnings per share	0.15	0.05	0.06

The accompanying notes are an integral part of the consolidated financial statements.

**CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY**

**In thousands of US dollars**

	<u>Share capital</u>	<u>Share premium</u>	<u>Treasury shares, at cost</u>	<u>Foreign currency translation reserve</u>	<u>Accumulated deficit</u>	<u>Total equity</u>
Balance as of January 1, 2006 (audited)	51	10,881	(173)	(1,331)	(2,870)	6,558
Share compensation expenses	-	(401)	-	-	-	(401)
Shares repurchased by the Company	-	-	(155)	-	-	(155)
Foreign currency translation adjustments	-	-	-	599	-	599
Net profit	-	-	-	-	2,320	2,320
Balance as of December 31, 2006 (audited)	51	10,480	(328)	(732)	(550)	8,921
Share compensation expenses	-	22	-	-	-	22
Foreign currency translation adjustments	-	-	-	15	-	15
Exercise of options	-	14	-	-	-	14
Dividends	-	-	-	-	(908)	(908)
Net profit	-	-	-	-	966	966
Balance as of June 30, 2007 (unaudited)	<u>51</u>	<u>10,516</u>	<u>(328)</u>	<u>(717)</u>	<u>(492)</u>	<u>9,030</u>

	<u>Share capital</u>	<u>Share premium</u>	<u>Treasury shares, at cost</u>	<u>Foreign currency translation reserve</u>	<u>Accumulated deficit</u>	<u>Total Equity</u>
Balance as of January 1, 2006 (audited)	51	10,881	(173)	(1,331)	(2,870)	6,558
Share compensation expenses	-	123	-	-	-	123
Shares repurchased by the Company	-	-	(163)	-	-	(163)
Foreign currency translation adjustments	-	-	-	244	-	244
Net profit	-	-	-	-	748	748
Balance as of June 30, 2006 (unaudited)	<u>51</u>	<u>11,004</u>	<u>(336)</u>	<u>(1,087)</u>	<u>(2,122)</u>	<u>7,510</u>

The accompanying notes are an integral part of the consolidated financial statements.

**TESCOM SOFTWARE SYSTEMS TESTING LTD.**

**CONSOLIDATED STATEMENTS OF CASH FLOWS**

**In thousands of US dollars**

	Year ended December 31,	Six months ended June 30,	
	2006	2006	2007
	Audited	Unaudited	
<u>Cash flows from operating activities:</u>			
Net profit	2,320	748	966
Adjustments to reconcile net profit to net cash provided by (used in) operating activities:			
Share compensation expenses	(401)	123	22
Depreciation and amortization	442	275	221
Increase in accrued severance pay, net	121	90	43
Deferred income taxes, net	(131)	(144)	(119)
Increase in trade receivables	(1,279)	(2,774)	(456)
Increase in other current assets and prepaid expenses	(501)	(331)	(500)
Increase in trade payables	377	1,057	155
Increase (decrease) in other current liabilities and accrued expenses	(618)	(166)	163
Net cash provided by (used in) operating activities	<u>369</u>	<u>(1,122)</u>	<u>495</u>
<u>Cash flows from investing activities:</u>			
Additions to property and equipment	(462)	(70)	(214)
Proceeds from sale of property and equipment	-	8	-
Net cash used in investing activities	<u>(462)</u>	<u>(62)</u>	<u>(214)</u>
<u>Cash flows from financing activities:</u>			
Dividend payment	(1,050)	(1,021)	(908)
Short-term bank credit, net	576	807	351
Exercise of options	-	-	14
Shares repurchased by the Company	(155)	(163)	-
Repayment of long-term bank loan	(20)	(8)	(87)
Net cash used in financing activities	<u>(649)</u>	<u>(385)</u>	<u>(630)</u>
Effect of exchange rate changes on cash and cash equivalents	<u>199</u>	<u>61</u>	<u>3</u>
Decrease in cash and cash equivalents	(582)	(1,508)	(346)
Cash and cash equivalents at the beginning of the period	<u>2,653</u>	<u>2,653</u>	<u>2,071</u>
Cash and cash equivalents at the end of the period	<u><u>2,071</u></u>	<u><u>1,145</u></u>	<u><u>1,725</u></u>

The accompanying notes are an integral part of the consolidated financial statements.

**TESCOM SOFTWARE SYSTEMS TESTING LTD.**

**CONSOLIDATED STATEMENTS OF CASH FLOWS**

**In thousands of US dollars**

	<b>Year ended December 31, 2006</b>	<b>Six months ended June 30,</b>	
	<b>Audited</b>	<b>2006</b>	<b>2007</b>
		<b>Unaudited</b>	
(a) <u>Supplemental disclosure of cash flows:</u>			
Cash paid during the period for:			
Interest	180	72	92
Income taxes	1,679	548	330
(b) <u>Cash received during the period for interest</u>	37	25	45
(c) <u>Supplemental disclosure of non-cash transactions:</u>			
Property and equipment acquired on credit	340	229	226

The accompanying notes are an integral part of the consolidated financial statements.

**NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**In thousands of US dollars, except share data**

**NOTE 1:- GENERAL**

- a. These financial statements have been prepared in a condensed format as of June 30, 2007 and for the six months then ended. These financial statements should be read in conjunction with the annual financial statements of the Company as of December 31, 2006, and their accompanying notes.
- b. The interim condensed consolidated financial statements herein have been prepared in accordance with IAS 34, "Interim Financial Reporting", on the historical cost basis. The significant accounting policies and methods of computations applied in the preparation of the interim financial statements are the same as those applied in the annual financial statements as of December 31, 2006.

**NOTE 2:- EXCHANGE RATE DATA**

Following are data regarding the representative exchange rates of the New Israeli Shekel ("NIS") and the Pound Sterling in relation to the US Dollar:

<u>As of</u>	<u>Exchange rate of one US Dollar</u>	<u>Exchange rate of one Pound Sterling</u>
June 30, 2007	NIS 4.249	NIS 8.507
June 30, 2006	NIS 4.440	NIS 8.138
December 31, 2006	NIS 4.225	NIS 8.288

**NOTE 3:- FUTURE ACCOUNTING POLICIES**

*IAS 23 (Revised), "Borrowing Costs"*

IAS 23 has been revised to require that borrowing costs be capitalized if they are directly attributable to the acquisition, construction or production of a qualifying asset. A qualifying asset is defined as an asset that takes a substantial period of time to get ready for its intended use or sale and includes fixed assets, investment properties and inventories that require a substantial period of time to bring them to a saleable condition. The option to immediately recognize such costs as an expense is eliminated. The revised Standard is effective for annual periods beginning January 1, 2009. Early application is permitted.

The Company believes adoption of the revised Standard is not expected to have a material effect on its financial position, results of operations and cash flows.

**NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**In thousands of US dollars, except share data**

**NOTE 3:- FUTURE ACCOUNTING POLICIES (cont.)**

*IFRIC 8 – Adoption of IFRS 2 Regarding Share-Based Payments*

IFRIC 8 deals with share-based payment transactions where all or part of the goods or services are not specifically identifiable. These goods or services are measured upon the date of grant as the difference between the fair value of the share-based payment and the fair value of the identifiable goods or services. The Company believes adoption of IFRIC 8 is not expected to have a material effect on its financial position, results of operations and cash flows.

*IFRIC 10 - Interim Financial Reporting and Impairment*

IFRIC 10 disallows the reversal of an impairment loss recognised in the past in the interim financial statements with respect to goodwill, investments in equity instruments or financial assets presented at cost. IFRIC 10 will be adopted in the Group's financial statements beginning in 2007, and will apply to goodwill, investments in equity instruments and financial assets presented at cost from the date on which the Company first adopts the measurement principles of IAS 36 and IAS 39, retrospectively. The Company believes that adoption of IFRIC 10 will not have a material effect on its financial statements.

**NOTE 4:- SEGMENT INFORMATION**

*Six months ended June 30, 2007 (unaudited):*

	<u>North America</u>	<u>Europe</u>	<u>Israel</u>	<u>Other</u>	<u>Total</u>
Segment revenues	<u>2,839</u>	<u>14,922</u>	<u>7,872</u>	<u>1,857</u>	<u>27,490</u>
Segment results	<u>404</u>	<u>2,032</u>	<u>(58)</u>	<u>292</u>	<u>2,670</u>
Unallocated expenses					<u>1,064</u>
					<u>1,606</u>

*Six months ended June 30, 2006 (unaudited):*

	<u>North America</u>	<u>Europe</u>	<u>Israel</u>	<u>Other</u>	<u>Total</u>
Segment revenues	<u>2,556</u>	<u>13,747</u>	<u>8,834</u>	<u>1,623</u>	<u>26,760</u>
Segment results	<u>5</u>	<u>1,723</u>	<u>450</u>	<u>220</u>	<u>2,398</u>
Unallocated expenses					<u>1,167</u>
					<u>1,231</u>

**NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**In thousands of US dollars, except share data**

**NOTE 4:- SEGMENT INFORMATION (cont.)**

*Year ended December 31, 2006 (audited):*

	<b>North America</b>	<b>Europe</b>	<b>Israel</b>	<b>Other</b>	<b>Total</b>
Revenues:					
Segment revenues	4,831	27,604	17,216	3,786	53,437
Segment results	(241)	4,173	1,260	327	5,519
Unallocated expenses					2,400
					3,119

**NOTE 5:- DIVIDENDS**

In March 2007, the Company declared a dividend of approximately \$ 900 (\$ 0.06 per share), which was paid in May 2007.

**NOTE 6:- CONTINGENT LIABILITIES**

- a. In July 2007, a former senior employee of the Company commenced legal proceedings against the Company for amounts that he alleges should have been paid to him during the period of his employment. The financial statements include an accrual for these proceedings that reflects the best estimate of the Company's liability, based on the opinion of its legal counsel. No accrual has been made for an additional amounts claimed (approximately \$ 250), which management does not expect the Company to have to pay, based on the opinion of its legal counsel.
- b. In August 2007, the Company received notice of a legal claim made against it by a former supplier in the amount of approximately \$ 230. The Company is currently evaluating its response to the claim and has not yet filed a defense motion in respect thereto. At this early stage, the Company is unable to determine the likelihood of any loss in connection with the claim and, accordingly, no accrual has been made in the financial statements in respect of this matter.