

## **Progress Software Corp. (PRGS – NASDAQ - \$20.15 – Buy)**

### **Third Quarter 2004 Results**

Progress reported revenues for the third quarter of fiscal 2004 of \$89.3 million, up 15% from \$77.7 million in the third quarter of fiscal 2003. Software license revenue increased 21% from \$27.2 million to \$32.9 million while maintenance and services revenue increased 12% from \$50.5 million to \$56.5 million. Within this segment, maintenance revenue increased 17% and services revenue declined 11% due to lower consulting revenue. For the third quarter DataDirect contributed \$7.0 million of revenue, ObjectStore contributed \$5.1 million and Sonic contributed \$6.6 million. In the year earlier quarter there were no revenues from DataDirect, which was acquired in the first quarter of fiscal 2004, \$3.6 million from ObjectStore and \$5.8 million from Sonic.

International revenues were 58% of the total in the third quarter of fiscal 2004, the same as in the third quarter of fiscal 2003. Currency added about 5% to reported revenues in the most recent quarter. Due to a modest shift in the mix of where profits are made, the effective tax rate in the third quarter of fiscal 2004 was 33.4% bringing the full year rate to 32% compared with the previous expectation of 31%. The company repurchased 403,000 shares of its stock during the quarter and ended the period with \$185.4 million of cash and short-term investments and no long-term debt.

Net income for the third quarter of fiscal 2004 was \$8.5 million, or \$0.22 per share diluted, compared with \$7.3 million, or \$0.19 per share diluted, in the prior year period. Diluted pro forma earnings per share, excluding amortization of purchased intangibles, were \$0.25 in 3Q04 compared with \$0.20 in 3Q03.

Progress has continued to record steady growth although a number of enterprise software companies have reported softening demand. We believe that the lower total cost of ownership of the Progress database, the company's concentration on mid-sized businesses through application partners, and the growth of its newer businesses account for this above-average performance. We expect these favorable trends to continue.

For the fourth quarter of fiscal 2004 we project revenue of \$95 million and pro forma diluted earnings per share of \$0.30. For the full year we expect revenue of \$361.5 million and pro forma diluted earnings per share of \$0.98. Although we have lowered our revenue forecast for the quarter and the year, our EPS estimate for the fourth quarter is unchanged and for the year is up \$0.02 due to the strength of the third quarter earnings. We are not making any changes in our estimates for fiscal 2005; revenues are expected to be \$407 million with pro forma diluted EPS of \$1.10. We believe the majority of the revenue growth will come from DataDirect, ObjectStore and Sonic.

#### *Disclosure*

*I, Jean W. Orr, certify that (1) the views expressed in this report reflect my personal views on all of the subject companies and securities and (2) my opinions are not affected by my compensation which is derived solely from brokerage trade commission(s) which may or may not be of securities discussed in this report.*

Progress has recorded good revenue and earnings growth during the last three years and, in our opinion, is positioned to continue to achieve a 15% growth rate in earnings. At the current price, the stock is selling for 20.6x our fiscal 2004 estimate and 18.3x our fiscal 2005 estimate. We believe the stock offers good value for investors and re-iterate our **Buy** recommendation on the stock.

*Jean W. Orr, CFA  
Nutmeg Securities, Ltd.  
847.658.3253  
September 16, 2004*

Additional information is available upon request.

*Note: The author holds a position in the common stock. Nutmeg initially rated the stock Buy on March 5, 2002 when the stock was selling for \$17.76 per share and the NASDAQ Composite Index was 1859.32 (closing prices on March 4, 2002). We currently rate three stocks Buy (75%) and one stock Hold (25%). Nutmeg Securities has not acted as manager or co-manager for any equity offering, nor received investment banking fees from Progress Software.*

#### **DEFINITION OF OUR RATING SYSTEM**

In general, we have three basic ratings of followed securities: Buy, Sell and Hold (Not Rated is a term we use where a security is not followed, or if followed, where not enough information is currently available to base an opinion).

**BUY** – is our rating for a stock that we consider currently attractive for purchase for most technology investors. It is a stock that we believe will outperform the market, as measured by the NASDAQ Composite, in a six to eighteen month timeframe. The recommendation could be based on industry or company fundamentals, on equity prices, or any one of a host of other factors, as assessed by the analyst.

We have also formed additional sub-categories of “BUY” rated stocks to make our position clearer. The most common of these are listed below:

- **STRONG BUY** – where the analyst feels a stock is especially attractive, in some cases due to recent price declines, in some where conventional wisdom on prospects is viewed as wrong, in some where there is a visible catalyst that will call attention to the security.
- **LONG-TERM BUY** – where the analyst considers the stock as fundamentally attractive but where fruition appears extended over a longer than normal period of time, or where the stock price currently is higher than levels where the analyst would rate the stock “BUY”.
- **SPECULATIVE BUY** – where the analyst considers the stock as very attractive on the price and the fundamentals but where well above average risk must be assumed by the investor.

**HOLD** – is our rating for a stock where prospects appear more or less in line with the market, or where we feel a compelling case cannot be made either for BUY or for SELL.

**SELL** – is our rating for a stock that in our opinion is likely to underperform the market as measured by the NASDAQ Composite in a six to eighteen month time frame.

This report has been prepared from original sources and company data that we believe to be reliable, but make no representation as to its accuracy or completeness. This report is published solely for informational purposes and is not to be construed as an offer to sell, a solicitation of an offer to buy any security, or the provision of or an offer to provide investment services in any state where such an offer, solicitation, or provision would be illegal. Any opinions expressed herein are statements of our judgment on this date and are subject to change without notice. Recommendations contained in this report represent a high degree of risk and may not be suitable for all investors. Nutmeg Securities, Ltd., its affiliates, its subsidiaries, and/or its officers and employees may from time to time acquire, hold, or sell a position in the securities mentioned herein. Additional information on subjects in this report is available upon request. Member NASD, SIPC and Chicago Stock Exchange. All rights reserved by Nutmeg Securities, Ltd.