

**Cloud Storage Thoughts (Interview w/ Nirvanix Co-Founder), HDD Pricing Update (Some Declines Thus Far in 1Q11), Intevac Sees HDD Equip. Pushouts, & More...**

Aaron C. Rakers, CFA  
Matthew Nahorski  
Patrick Newton, CFA

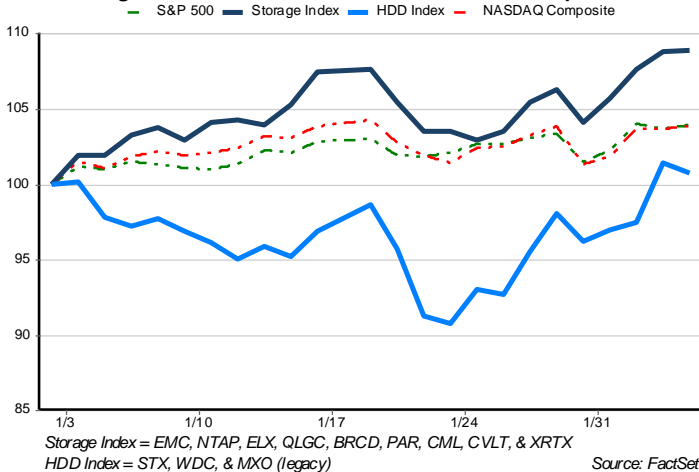
[rakersa@stifel.com](mailto:rakersa@stifel.com)  
[nahorskim@stifel.com](mailto:nahorskim@stifel.com)  
[newtonp@stifel.com](mailto:newtonp@stifel.com)

(314) 342-8401  
(314) 342-2792  
(303) 291-5345

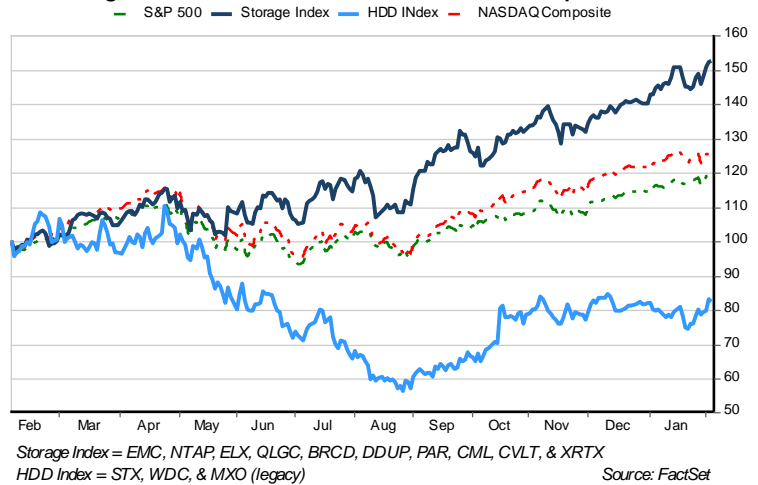
**Summary:**

- Cloud Storage – Discussion with Nirvanix Co-Founder Highlights Changing Storage Landscape?** We recently had an interesting discussion with Geoff Tudor, Co-Founder and Senior Vice President of Strategy and Business Development, at Nirvanix, a privately held provider of cloud-storage solutions. We found our discussion to be quite timely when considering the focus being placed on cloud-computing/storage (e.g., EMC’s Atmos/Isilon focus, Amazon’s S3 ramp, Verizon/Terramark, etc.). Nirvanix has become an increasingly well-known/emerging player in the cloud-storage market with seven global data centers and its hNode virtual file system technology, having over 700 customers (NBC Universal, Cisco, VMware, GE, etc.). Nirvanix’s cloud storage offerings are offered to consumers, SMB, and enterprise customers on a user-based pricing model; storage capacity is deployed as a service. The company highlights differentiation as based on the company’s ability to offer industry-leading *guaranteed* Quality of Service (QoS) levels and user-based pricing model (vs. Amazon’s S3 offering noted as providing best-efforts QoS capabilities and EMC’s Atmos solutions). We found Nirvanix’s hNode technology as the most interesting part of our discussion - we believe this is the most meaningful differentiator of the Nirvanix story. This is the company’s intelligent virtual file system technology (Nirvanix’s Internet File System, or IFS), enabling up to 500 different LUNs to be integrated into a single node with scalability to seven nodes under a single global namespace. As highlighted below, hNode (Web Services Layer) supports existing/heterogeneous file system environments. Please see pgs 2-5 for a more detailed discussion.
- Other Topics. (1) HDD Pricing Update.** Checks indicate low-single-digit price declines thus far in C1Q11 vs. average blended prices in C4Q10; low-single-digit MoM declines in 2.5” at STX and in 3.5” in WDC while HGST checks indicate pricing relatively unchanged. STX 2.5” declines across all capacity points (160GB-500GB) while WD 3.5” showed greater MoM declines in higher capacity drives. **(2) HDS’ Storage Results (Incremental Tidbits).** In addition to our report last week, we would note that HDS posted hardware growth in the mid-30% seq. range for C4Q10, in which high-end revenue grew in the high-20% yr/yr range (vs. EMC’s 19% yr/yr Symm growth) with the new VSP array product cycle kicking in (conversations noted that >90% of VSP deployments thus far going into new installed environments). HDS saw a significant increase in SSD adoption with the new VSP arrays – now having up to 5% of capacity on SSDs, ~30% in SAS 10K/15K RPM (high-perf.) enterprise drives, and the remaining ~65% in SATA drives – NT positive for STEC; LT negative for Seagate. **(3) Intevac Results/Outlook Highlight HDD Industry Capacity Pull-Back.** Intevac reported a systems backlog decline to \$46.7M exiting December vs. \$64.9M exiting September, reflective of only 2 Lean (HDD media sputtering) systems, down from six systems exiting the prior quarter. Intevac expects no shipments into HDD industry in C1Q11, noting that the industry would likely see 8-16 systems deployed in 2011 to support 10%-15% ship growth; it is seeing four system deployments delayed by one-quarter in C4Q10 and two systems moved out into latter 2011. **(4) Week Ahead.** Focus on EMC’s Analyst Event (Feb 8<sup>th</sup>) – expect focus on storage virtualization, new midrange product cycle, cloud-storage (hardware/software provider or more longer-term?), and big-data (Atmos, Isilon, & Greenplum), and Stifel’s Tech Conference (Feb 9-11<sup>th</sup>).

Storage & HDD Indices vs. S&P500 & NASDAQ Comp. - YTD



Storage & HDD Indices vs. S&P 500 & NASDAQ Comp. - 12-Months



Past performance should not and cannot be used as an indicator of future results

**Stifel Nicolaus does and seeks to do business with companies covered in its research reports. As a result, investors should be aware that the firm may have a conflict of interest that could affect the objectivity of this report. Investors should consider this report as only a single factor in making their investment decision. All relevant disclosures and certifications appear on pages 32-33 of this report.**

## Highlighted Industry News/Thoughts:

### Nirvanix - Conversation with Co-Founder Highlights Evolution of Cloud Storage; Details of Competitive Positioning vs. Amazon S3 and EMC's Atmos

We recently had an interesting discussion with Geoff Tudor, Co-Founder and Senior Vice President of Strategy and Business Development, at Nirvanix, a privately held provider of cloud-storage solutions. Below we highlight a few of the key takeaways from our conversation:

- **Nirvanix Background.** Based in San Diego, CA, and thus far raising more than \$23 million in venture funding from investors such as Intel Capital, Mission Ventures, Valhalla Partners, Windward Ventures, and the European Founders Fund, Nirvanix is becoming an increasingly well-known/emerging player in the cloud-storage market. Nirvanix's cloud storage offerings are offered to consumers, SMB, and enterprise customers on a user-based pricing model; storage capacity is deployed as a service. The company highlights differentiation as based on the company's ability to offer industry leading guaranteed Quality of Service (QoS) levels (vs. Amazon's S3 offering noted as providing best-efforts QoS capabilities).

Nirvanix views Amazon's S3 and EMC's Atmos (partner with AT&T) as its primary competitors. The company notes that Amazon's EC2 offering provides cloud computing capabilities, whereas Nirvanix is solely focused on storage. The company highlights the cost differentiation of its offering to enterprise customers relative to traditional deployment maintenance fees and technology refresh requirements. The company views its offerings as being positioned at the enterprise-class of cloud computing offerings in the market today. In November 2010, Nirvanix announced the appointment of storage industry veteran Scott Generuex as its President and CEO, as well as a \$10 million additional round of venture funding. Mr. Generuex had previously served as Senior Vice President of Sales at QLogic.

- **Nirvanix's Three Offerings.** Nirvanix highlights its portfolio as consisting of:

1. **Storage Delivery Network (SDN).** This reflects Nirvanix's co-located seven global datacenters (using data center facilities from Equinix, Digital Realty Trust, etc.), which compares to Amazon's single datacenter in Seattle, Washington. This consists of globally distributed/full-redundant datacenters (nodes) in Los Angeles, Dallas, New Jersey, Tokyo, Frankfurt, and two in Switzerland. We believe this model raises questions relative to the late-1990s/early-2000s timeframe when we saw names such as Storage Networks emerging as an outsourced storage provider with its Storage Points of Presence (SPOPs). Nirvanix highlights its ability to leverage a global/virtualized file system technology across commoditized low-cost (predominately Dell) x86 hardware and networking rather than high-end/expensive networked storage. The company's ability to leverage virtualization allows for significant resource utilization and a scale-as-needed cost structure. **Nirvanix charges customers an initial list price of \$0.25/GB.**
2. **Cloud NAS Gateways.** This is an optional solution for customers as a gateway providing file-level data migration into the company's SDN. From what we can gather about Nirvanix's Cloud NAS Gateway offering thus far, we question whether this could be considered a competitive/comparative solution to Riverbed's new Whitewater solution, albeit not providing deduplication functionalities like Riverbed. Nirvanix notes that competitive offerings are unable to monitor both ends of the cloud network and are not able to guarantee end-to-end QoS levels.
3. **hNode.** We believe this is the most meaningful differentiator of the Nirvanix story – hNode refers to the company's intelligent virtual file system technology (Nirvanix's Internet File System, or IFS), enabling up to 500 different LUNs to be integrated into a single node with scalability to seven nodes under a single global namespace. As highlighted in a slide from the company's presentation below, Nirvanix notes that its hNode (Web Services Layer) supports existing/heterogeneous file system environments. hNode is focused on allowing enterprise customers to leverage the company's functionality across their own private cloud (data center), as well as to transfer data into Nirvanix's SDN for business processes and workflow using the company's policy-based replication capabilities. The standard configuration has two hNodes (clustered) with a minimum of 200TB of storage each and scales to multiple petabytes per location using 2TB 7200 RPM SATA drives.

# Integrate the Nirvanix Web Services Layer Atop ANY File System (hNode™)

Brings granular usage-based storage services to existing storage assets and makes them *cloud-enabled*



Nirvanix Confidential



Source: Nirvanix

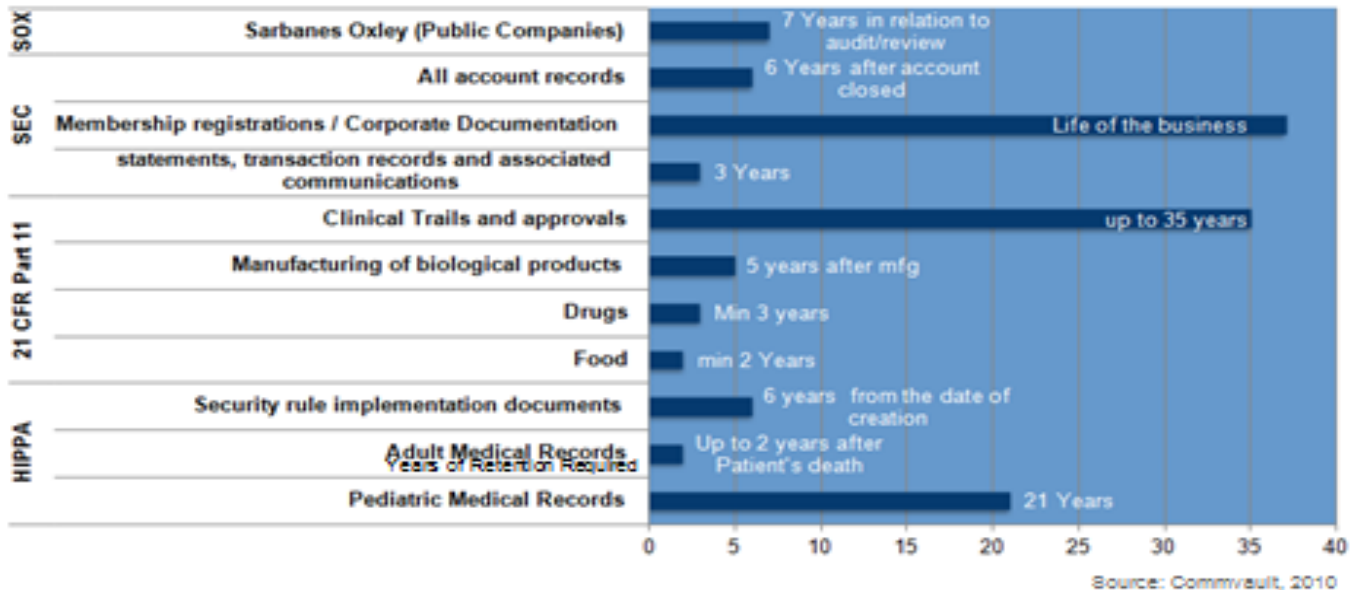
- Significant/Expanding Customer Base, Reseller Relationships with HP and Dell, and Patents.** Nirvanix notes that it currently has more than 700 cumulative customers. The company highlights NBC Universal as one of its flagship customers – increasing from its initial Digital Archiving deployment of 40TB to more than 1.5PB over the past year. Other highlighted enterprise customers include: Logitech (planning to use over 200TB under one node in Europe and LA; expect further expansion post initial digital archiving transfer), Cisco (using Nirvanix’s SDN for its Global Tech Support organization for log file storage on open customer cases), General Electric (offsite data protection and content collaboration/distribution), Amylin (biopharma company using Nirvanix’s SDN for server image storage; retained under strict FDA requirements), and others (VMware, NASA, Arizona State University, among others).

Also quite notable, in our opinion, is the fact that Nirvanix has established reseller relationships with HP and Dell – interesting as we would expect investors to question the role of hardware vendors in the evolution toward cloud going forward (i.e., maintaining a hardware vendor approach or potentially looking to expand into cloud offerings). The company also has relationships with Symantec (only vendor to thus far integration with Symantec’s NetBackup offering), CommVault, and Riverbed, as well as channel partners such as Avnet, Forsythe, SwissCom, Verizon, and others. Nirvanix has 11 pending patents with significant intellectual property around the company’s Virtual File System technology for massive content files, leveraging a single global namespace (we believe some could question this as compared to Isilon, HP/Ibrix, NetApp Data ONTAP 8, etc., as well as Google’s implementation of its own proprietary scalable file system technologies).

- Unstructured Data Growth = Significant Driver for Cloud Storage?** Nirvanix, like others in the storage industry, sees the substantial growth potential in unstructured digital content as a significant positive driver for those well positioned over the coming years. We continue to find the following chart as interesting (via Nirvanix’s presentation and citing CommVault figures). Nirvanix highlights expectations that overall digital content would grow at a 10x rate over the next five years, in which 95% (we have heard previously ~80%-plus) would be unstructured content. With this said, Nirvanix sees its addressable market as reflecting a 27 petabyte opportunity looking into 2012, or seeing cloud storage grow from an estimated ~9% of total cloud spending to 13% by 2014 of a total \$55.5 billion addressable market (or ~\$7.2 billion) – see second and third slides below.

# Explosive Growth in Unstructured Data

- Enterprises experiencing explosive growth of data they must store
  - 10X in 5 years, 95% of it unstructured**
  - Problem is only exacerbated by burdensome long-term compliance retention requirements



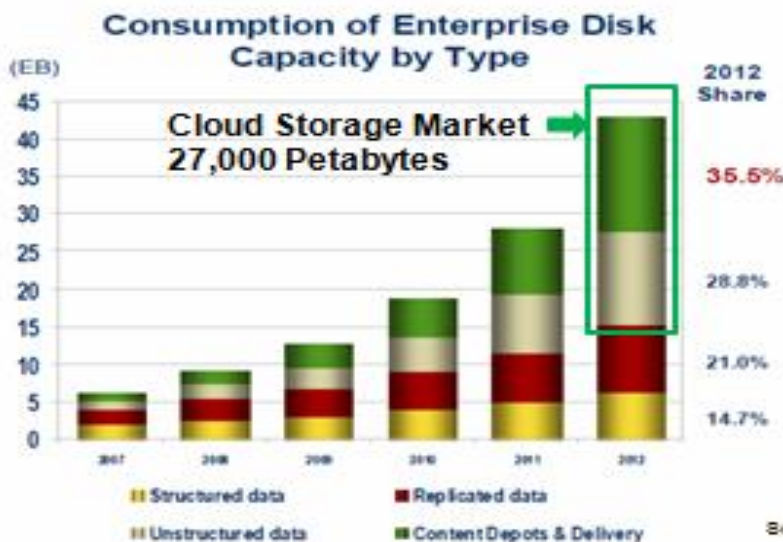
Nirvanix Confidential



Source: Nirvanix

# The Immense Business Opportunity

## Changing Information Profile: Content Delivery Driving Storage Growth



Content archive and delivery is the primary storage use case

Consequences:

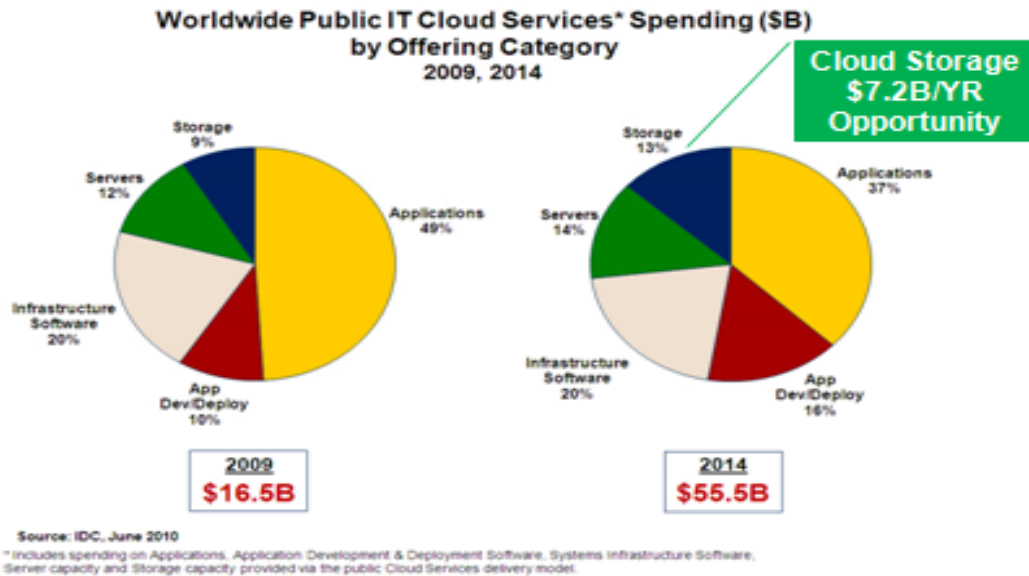
- Shift to file-based storage systems
- Redefinition of storage performance
- Resetting the bar for scale and density

Nirvanix Confidential



Source: Nirvanix

# Massive Growth: A \$7.2B Cloud Storage Market within Just 3 Years



Nirvanix Confidential

Source: Nirvanix

**Additional Note: Amazon S3 – \$750 Million in Revenue in 2011, Growing to 262 Billion Objects.** As an additional note to our Nirvanix discussion, we would highlight last week’s news that Amazon has reportedly estimated a revenue contribution of up to \$750 million in revenue from its Amazon S3 offering in 2011. The company also recently reported that it now stores roughly 262 billion objects, up over 100x relative to the year-ago 102 billion objects. Amazon is said to now be receiving more than 200,000 requests per second. Articles note that Amazon’s S3 offering provides 99.99% availability of objects in a year. The article also highlights that CommVault’s Simpana 9 platform enables customers to tie directly into cloud environments such as Amazon’s S3.

## Industry Pundit, Steve Duplessie, Highlights the Drive Toward Virtualization in Storage; A Likely Key Theme at This Week’s EMC Analyst Event

In an article written by well-known storage industry veteran Steve Duplessie last week, it is well articulated how critically important virtualization is for the enterprise storage market. The article notes the evolution of having virtualization as the foundation of cloud-computing environments (private, public, or hybrid) and the drive toward IT utility services, in which he views storage as an impediment. He notes that server virtualization is just the tip of the iceberg, though a *mighty tip* at that. The article notes that server virtualization serves as a great enabler, but is only the start toward all compute/infrastructure resources becoming ultimately virtualized and orchestrated holistically. **In the end, the conclusion made is that server virtualization is merely the starting point for other levels of virtualization across the enterprise data centers, and Mr. Duplessie’s view is that storage is the next IT industry ripe for these revolutionary moves – a dynamic we would expect to hear more about at this week’s EMC Analyst Event.** Mr. Duplessie, we believe correctly, highlights the need for storage architectures to become virtualized, dynamically distributed and orchestrated, and ultimately commoditized such as the server market.

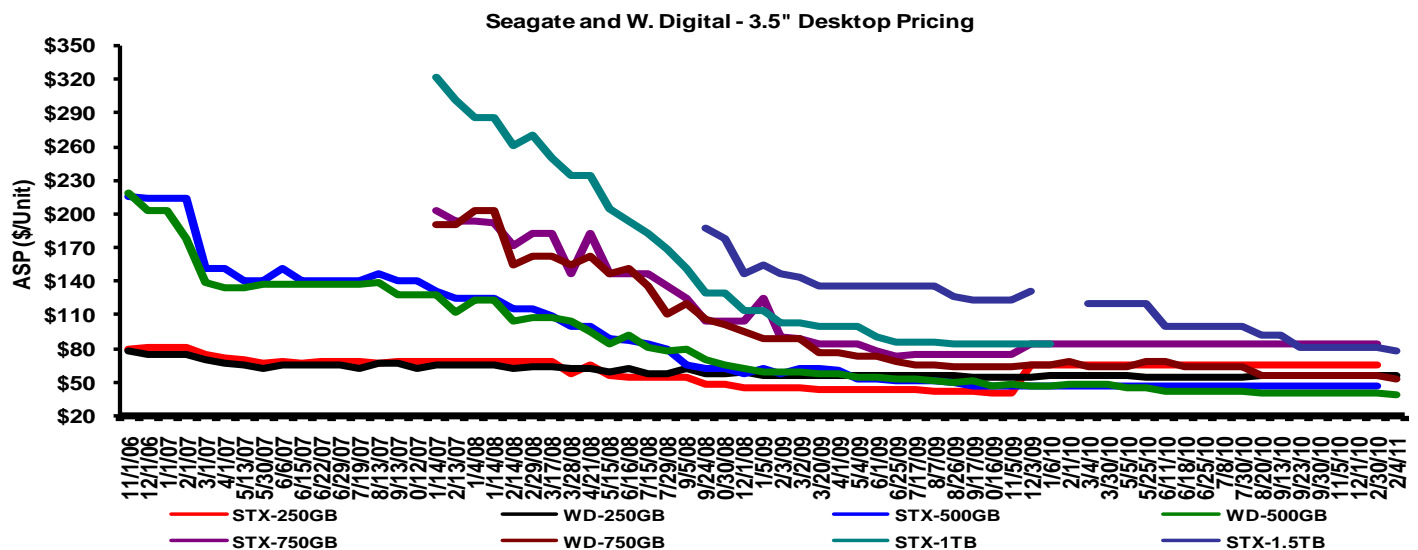
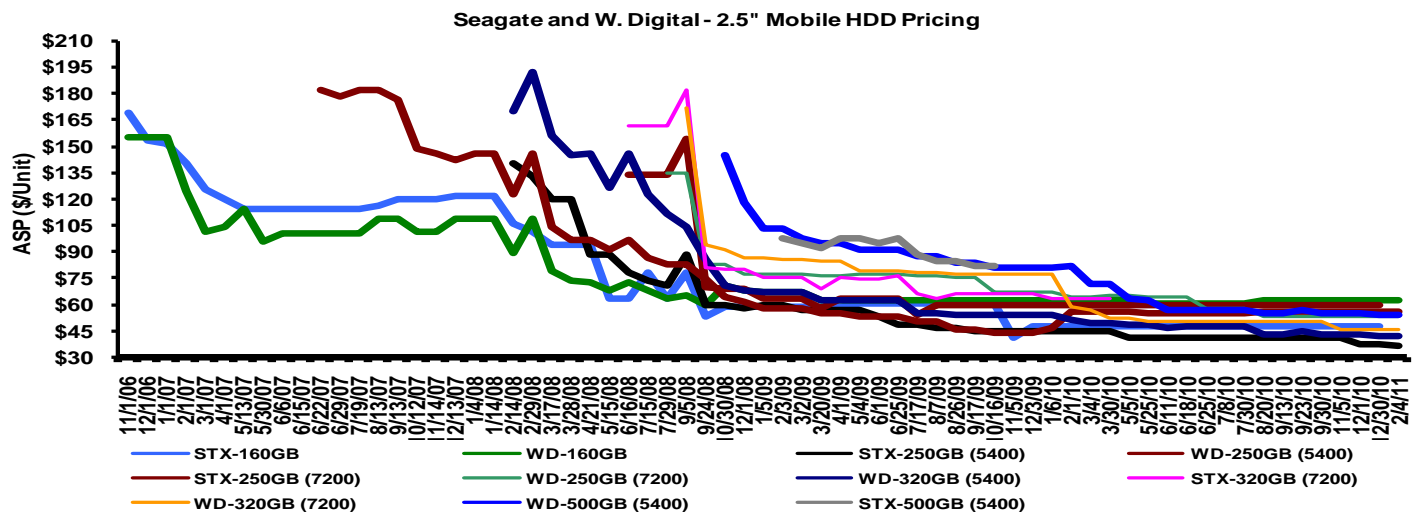
## HDD Pricing Checks – Our Checks Indicate Low-Single-Digit Declines Thus Far in C1Q11 vs. Average Blended Prices in C4Q10; Low-Single-Digit MoM Declines in 2.5” at STX and in 3.5” in WDC

Given the start of the month of February, we thought it would be useful to provide an update on pricing thus far into the March 2011 quarter. **Our pricing data thus far in the March quarter indicates blended ASP declines in the low-single-digit sequential range at Seagate and Western Digital compared to blended average levels exiting the December quarter with Hitachi showing only very slight declines at this point (~1%).** As a reminder, both Seagate’s and Western Digital’s underlying guidance for the March quarter reflected an expectation of like-to-like ASP erosion in the 5% sequential range (in-line with typical seasonality). **We would point out that while the pricing for the majority of drives at Seagate was flat MoM, we did see some 2%-3% MoM declines in 2.5” mobile drives, while at Western Digital we saw low-to-mid-single-digit declines across most of its 3.5” desktop drives (while all other drives remained essentially flat MoM).** Below we highlight some of the pricing data:

- **2.5” Mobile Drives.** Our pricing data for Seagate’s 2.5” mobile drives at the beginning of February indicates price declines in the 2%-3% range compared to levels exiting December. Overall pricing thus far in the March quarter compared to blended average pricing exiting the December quarter indicates a sequential decline of 3.1%. Our checks indicate that these declines were spread out

fairly evenly across several capacity points, ranging from 160GB-500GB. As a reminder, our checks had indicated that 2.5" pricing at Seagate remained relatively unchanged throughout the September and December quarters on an average blended basis. Turning to **Western Digital's** 2.5" drives, our checks indicate that WD did not change any prices for its 2.5" drives during January, similar to the trends we saw in both November and December. Given the steady pricing points in January, this implies that thus far in the March quarter, average blended prices are down about 5% sequentially compared to average blended prices exiting the December quarter (majority of pricing activating in C4Q10 took place in October, according to our checks). Our checks indicate that **Hitachi's** mobile drive pricing was essentially unchanged on a MoM basis during the month of January (down 0.2% MoM), marking the third consecutive month of little to no change in 2.5" pricing, according to our checks. Thus far into the March quarter, overall blended 2.5" pricing was actually up 0.6% sequentially, which compares to a 4% sequential decline in C4Q10. In this, we would note that while a handful of drives were down 1-2% sequentially, two drives (with capacities of 500GB and 750GB) were up 4% sequentially.

- 3.5" Desktop Drives** – Taking a look at **Seagate**, overall pricing for the month of January was unchanged compared to levels exiting the month of December. This did reflect one 1.5TB drive declining 3.8% MoM that was offset by one 500GB drive increasing 4.1% MoM. Looking at pricing thus far in the March quarter compared to average blended pricing exiting C4Q10, Seagate's prices are down 1.5% sequentially. As we have noted in the past, this is driven by some low-single-digit declines in a few high-capacity drives. For **Western Digital**, the company was very active on the 3.5" pricing front in January, with average prices declining 2% MoM (price declines ranging from 1%-5% MoM across all capacity points). Given overall pricing on a month-over-month basis was down 2%, Western Digital's overall blended pricing was down about 2% sequentially for 3.5" drives thus far in 1Q11 compared to blended pricing exiting the December quarter, again driven by low-to-mid-single-digit declines across all capacity points. **Hitachi** 3.5" drive prices were essentially flat (down 0.6%) on a MoM basis compared to levels exiting the month of December. Our checks indicate that Hitachi only lowered pricing on one drive during the month – lowering a 1TB drive by approximately 5%. Thus far into the March quarter, average blended pricing is down approximately 0.7% compared to average levels exiting the December quarter. This is driven primarily the previously mentioned 1TB drive.

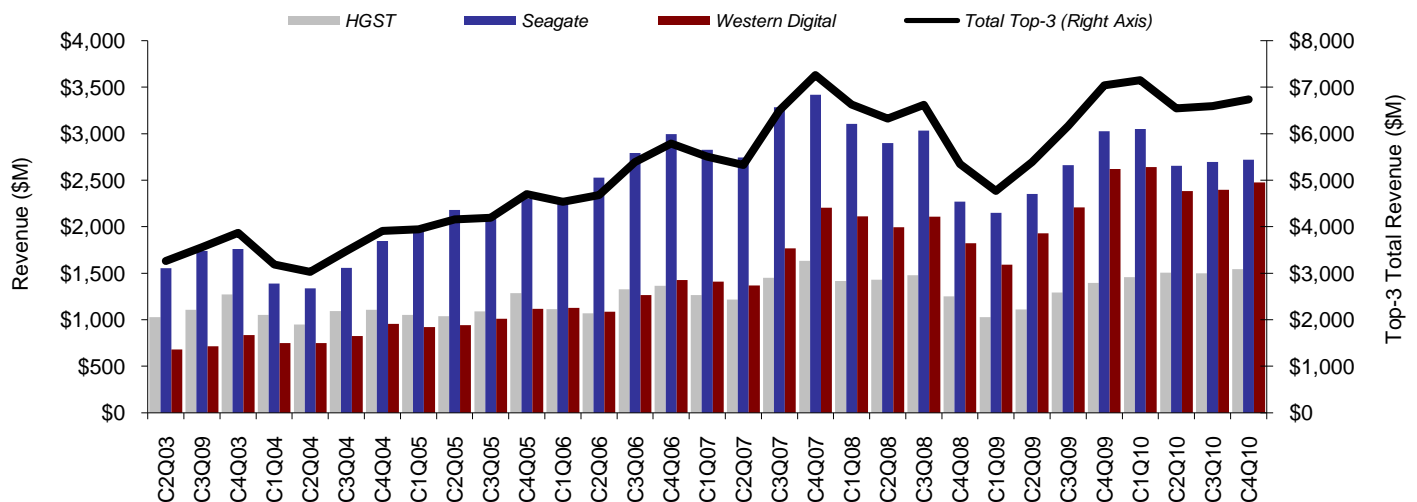


**Hitachi Results – Hitachi Global Storage Technologies (HGST) Gains Shipment Share; Remains Profitable**

Hitachi reported its results for the December quarter (F3Q10) last week. Below we provide some quick takeaways as it pertains to the company’s reported HDD results (HGST; Seagate and Western Digital implications) and the company’s Storage Solutions results (EMC, NetApp, HP, 3PAR, etc. implications). **Given its ongoing work toward a possible initial public offering, Hitachi did not provide an updated representation with regard to Hitachi Global Storage Technologies (HGST) results for the December quarter - only providing the shipment, revenue, and operating margin detail as provided in Hitachi Ltd.’s release.**

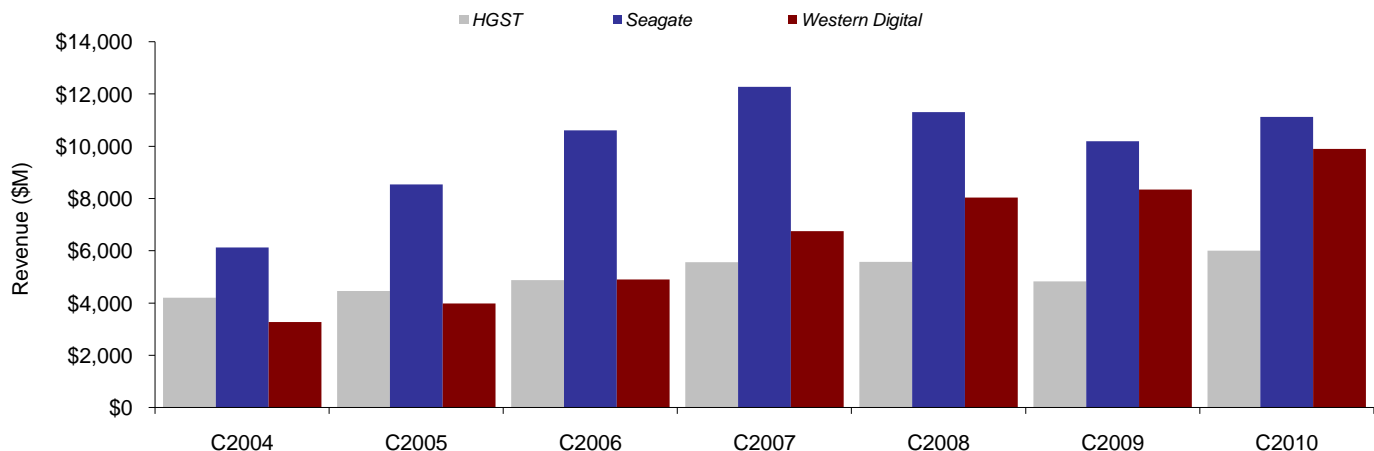
- HGST Revenue.** Hitachi Ltd. reported HGST revenue of \$1.542 billion, +11% yr/yr and +3% sequentially (¥127.4 billion, up 2% yr/yr). This compares to the company reporting 16% yr/yr growth and a 0.4% sequential decline in revenue for the prior quarter. This compares to Seagate reporting revenue of \$2.719 billion, -10% yr/yr and -3% sequentially, and WD reporting revenue of \$2.475 billion or -5.5% yr/yr and up 3% sequentially for the December quarter. As we have highlighted/discussed in recent reports, HGST has posted positive performance relative to its competitors during the past two quarters. On a combined basis (HGST + Seagate + WD), HDD revenue totaled \$6.736 billion for the December quarter, declining 4% yr/yr and reflecting a 2% sequential increase. On a relative revenue basis, HGST’s share stood at ~23%, roughly flat sequentially and up from approximately 20% in the year-ago quarter. The charts below provide comparisons between HGST, Seagate, and WD reported quarterly revenue.
- HGST Operating Margin. Implied Gross Margin in the ~20% Range?** HGST reported operating income at \$104 million, or 6.7% operating margin. This compares to the company reporting \$138 million operating income, or a solid 9.2% operating margin, in the September quarter and \$137 million, or 9.8%, in the year-ago quarter. Seagate had reported operating income of \$214 million, or 7.9%, in its December quarter, while WD had reported operating income at \$235 million, or 9.5% operating margin, during its December quarter. With an estimated opex structure that reflects a similar 3% sequential increase relative to revenue, our model would imply HGST running its HDD operations with a gross margin of approximately 20%, slightly ahead of Seagate and Western Digital reporting 19.5% and 19.2% gross margin during their respective December quarters.

**Quarterly Revenue - HGST, Seagate, & Western Digital**



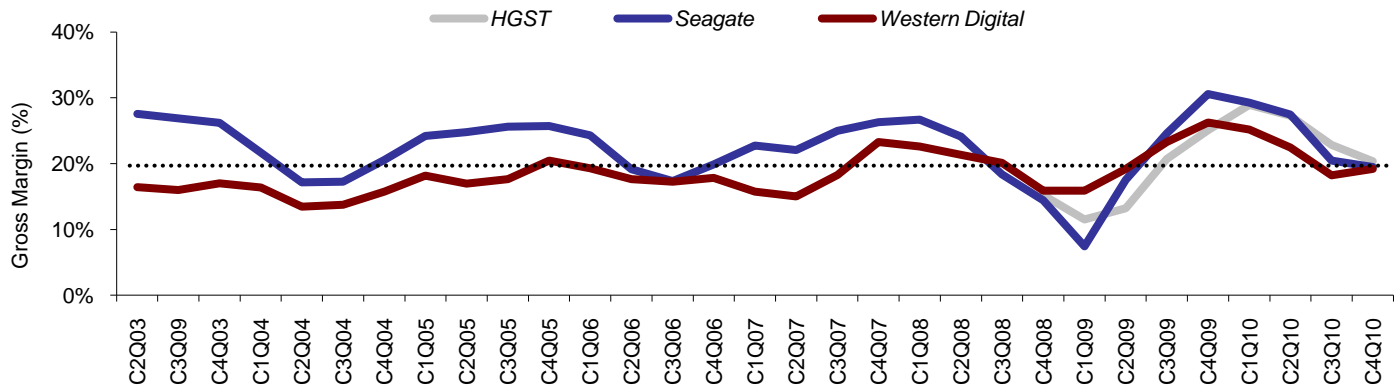
Source: Company Data, Stifel Nicolaus Estimates

**Total Revenue - HGST, Seagate, & Western Digital (Calendar Years; \$M)**



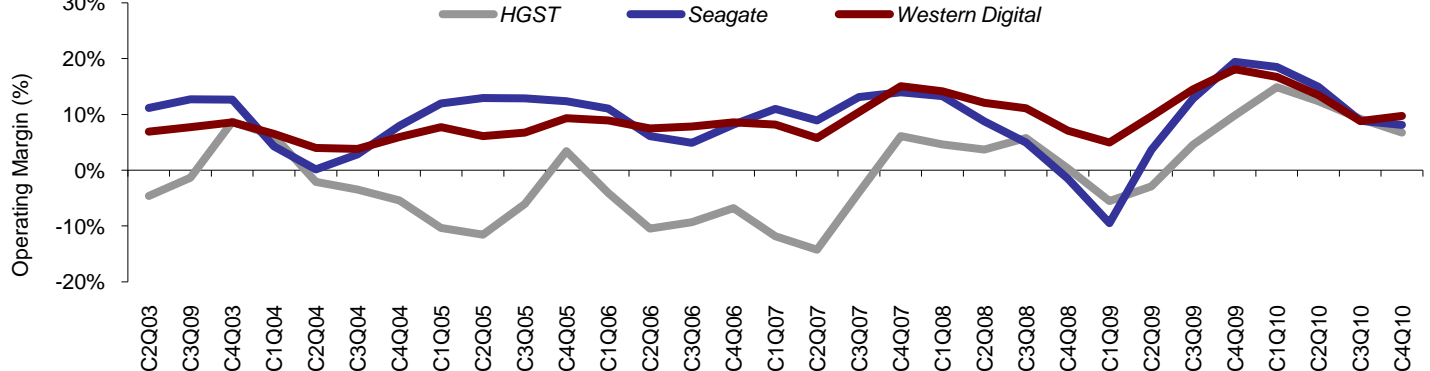
Source: Company Data

### Quarterly Gross Margin - HGST, Seagate, & Western Digital



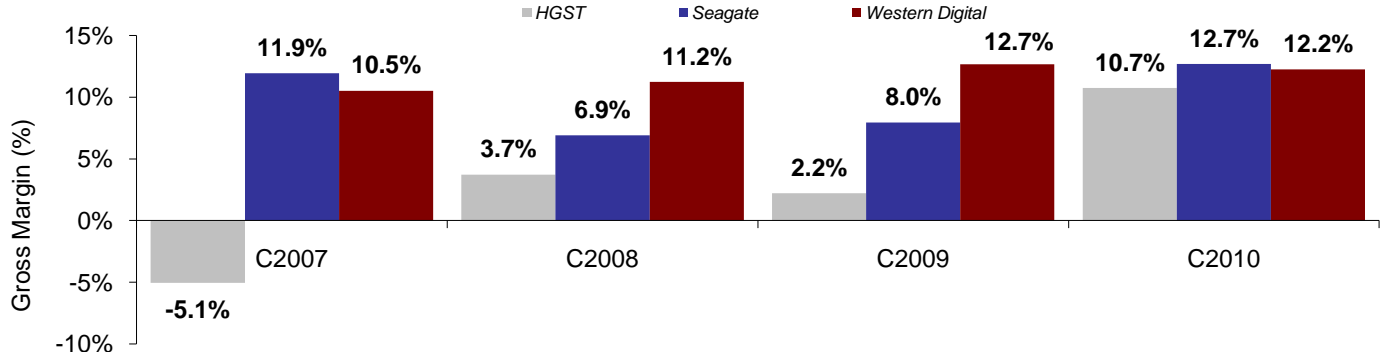
Source: Company Data; Stifel Nicolaus Estimates

### Quarterly Operating Margin - HGST, Seagate, & Western Digital



Source: Company Data; Stifel Nicolaus Estimates

### Operating Margin - HGST, Seagate, & Western Digital (Calendar Years)



Source: Company Data

- HGST Shipments – Strong Performance in Enterprise and 3.5” Desktop.** HGST reported total shipments of 30.3 million for the December quarter, growing a solid 22% yr/yr and 5% sequentially. This compares to total industry shipments at an estimated ~167.5 million, or up only 4% yr/yr and 2.5% sequentially. This compares to HGST’s total shipments growing 15% yr/yr and 2% sequentially in the September quarter versus total industry shipment growth estimated at approximately 8% yr/yr. As a reminder, Seagate shipped 48.9 million drives in its December quarter, down 2% yr/yr and 1% sequentially, while Western Digital’s shipments at 52.2 million were up 5.5% yr/yr and up 3% sequentially. **Like our analysis of Toshiba’s shipment results for the December quarter last week (see our Enterprise Hardware & HDD Weekly report published Monday, 1/31), HGST’s results again raise our questions with regard to Seagate’s shipment share loss in C4Q10.** Toshiba had shipped approximately 18.0 million HDDs during its December quarter, declining 14% yr/yr and 3% sequentially.

With this data (using the ~167.5 million shipment estimate), we find Seagate’s shipment share to have stood at 29.2% for C4Q10, down from 30.1% and 31.1% in the prior and year-ago quarters, respectively. Western Digital’s total industry shipment share stands at approximately 31.2%, roughly flat on a sequential and yr/yr basis, while HGST’s share at 18.1% reflects an increase from 17.2% and 15.5% in the prior and year-ago quarters, respectively. Toshiba’s shipment share stands at approximately 10.7%, down from 11.3% and 13.1% in the prior and year-go quarters, respectively.

- 2.5" Commercial/Consumer (Mobile HDDs – Portable PCs and Consumer Electronics). Seagate Ship Share Loss in Focus?** HGST shipped 16.3 million 2.5" drives, up 13.2% yr/yr and down 3.0% sequentially (vs. 17.5% yr/yr and +1% seq. in the September quarter). This compares to Seagate reporting mobile compute shipments (i.e., not including 2.5" drives shipped into consumer electronics applications) at approximately 11.8 million for its December quarter, declining 14% yr/yr and 12% sequentially. Western Digital reported total notebook computer HDD shipments at 17.4 million in its December quarter, reflecting a 2% yr/yr decline and up 5% sequentially. Toshiba shipped approximately 11.8 million 2.5" mobile/notebook HDDs for its December quarter, which was down 15% yr/yr but a 25% sequential increase. **Again, we believe the key highlight within these results is the relative underperformance of Seagate's 2.5" mobile shipments in the December quarter.**
- 3.5" Commercial/Consumer (Desktop HDDs) - Solid Relative Performance.** HGST shipped 9.6 million 3.5" drives in the September quarter, up a very strong 35% yr/yr and 14% sequentially. This compares to Seagate's 19.8 million computer desktop drive shipments for the December quarter, reflecting a 7% yr/yr decline, or down approximately 1% sequentially. If we were to include Seagate's 3.5" nearline (SATA enterprise) shipments, we would estimate a decline of 4% yr/yr and flat sequentially. Western Digital reported total desktop shipments of 20.4 million in its December quarter (ex-SATA drive shipments into enterprise), which reflects 6% yr/yr growth and a 2% sequential decline. Our checks remain stable with regard to 3.5" pricing.
- 2.5"/3.5" Enterprise Drives - Strong Share Gains at HGST and Stable at Seagate; Implies Sharp Decline in Toshiba/Fujitsu Share.** HGST reported that it shipped 2.3 million enterprise-class drives (servers/enterprise), which is up a strong 35% yr/yr and 28% sequentially. This compares to HGST shipping approximately 1.8 million enterprise (mission-critical FC/SAS) drives during its prior quarter, up 20% yr/yr and down 5% sequentially. This compares to Seagate's approximate 4.8 million mission-critical enterprise drive shipments for its December quarter, which reflects 4% yr/yr growth and a 3% sequential increase. Toshiba reported that it had shipped approximately 1.06 million enterprise-class drives during its December quarter, up from 850,000 and 1.34 million shipments in the prior and year-ago quarters.

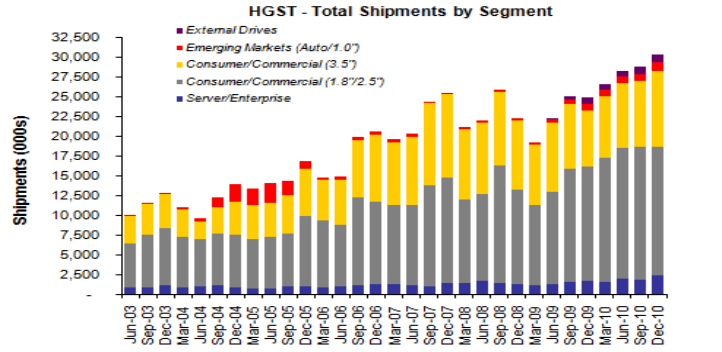
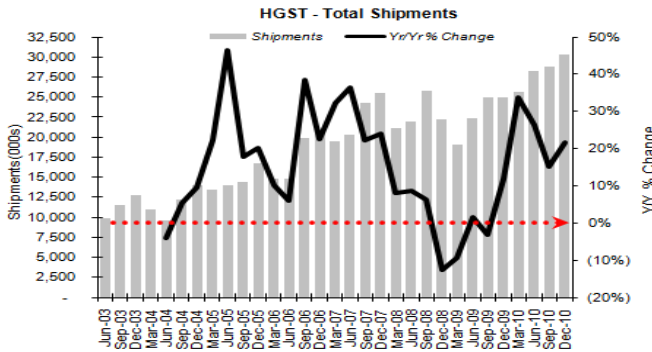
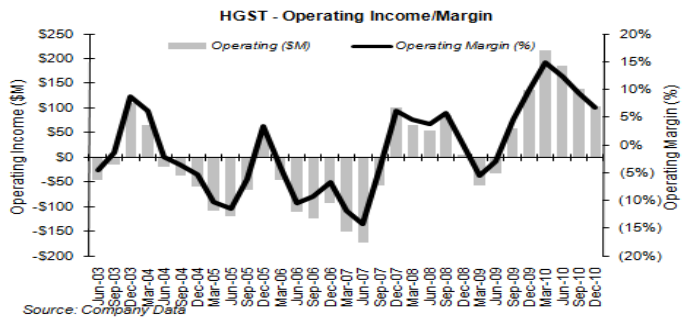
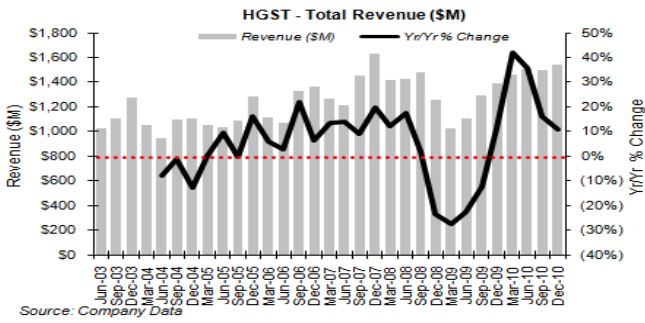
Using industry estimates that the industry shipped approximately 8.3 million mission-critical enterprise drives during the December quarter, our estimates are unchanged in that Seagate's shipment share declined to approximately 58% versus 63% and 60% in the prior and year-ago quarters, respectively. **HGST's shipment share rose to nearly 28%, up from 25% and 22.5% in the prior and year-ago quarters, respectively,** while Toshiba's share stands at slightly below 13% versus 12% and approximately 18% in the prior and year-ago quarters, respectively.

- External Drives – Western Digital Continues to Dominate this Fastest Growing HDD Segment.** HGST, which had acquired Fabrik to push into the external drive market, reported that it had shipped approximately 1.04 million external/retail drives during the December quarter, up from 960,000 and 880,000 in the prior and year-ago quarters, respectively. This compares to Western Digital reporting 7.43 million total external drive shipments for its December quarter, while Seagate had shipped approximately 4.1 million external drives. This would imply Western Digital having a shipment share of approximately 59%, followed by Seagate at approximately 33%, and HGST at approximately 8% on a relative basis. These share trends have remained relatively stable on a yr/yr and sequential basis.

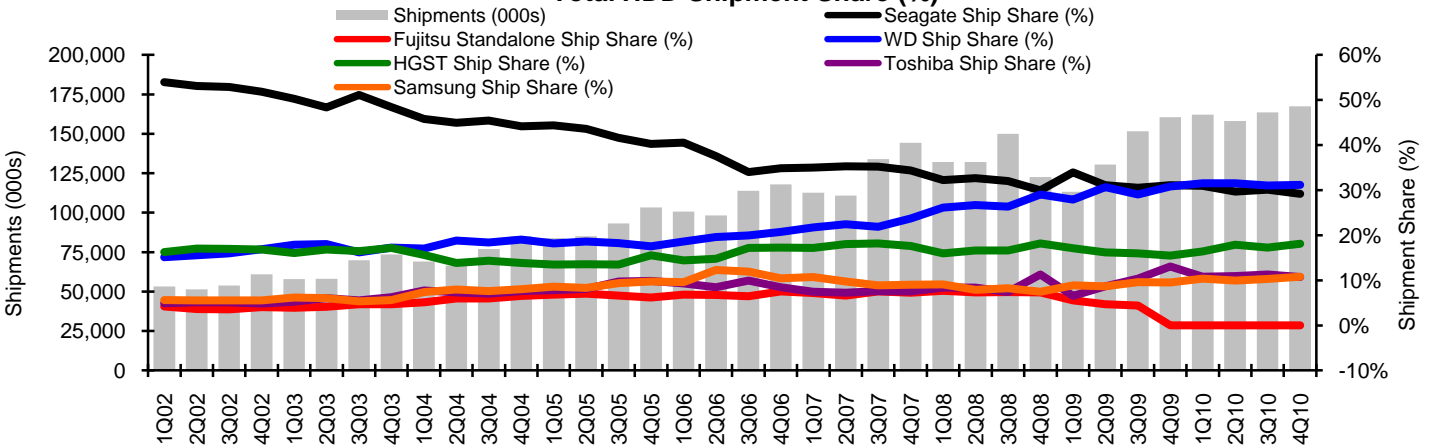
**Reminder: HGST Long-Term Financial Model Focus.** Although HGST did not provide an updated presentation on its HDD operations specifically, we believe the company's results, relative to Seagate and Western Digital, would likely result in a reiteration of the company's previously disclosed long-term target model expectations. As a reminder, HGST has highlighted Seagate's and WD's long-term focus on generating GM% in the 22%-26% and 18%-23% ranges and operating margin in the 10%-14% and 8%-14% ranges, respectively (note: only change was 8%-14% for WD vs. prior 10%-14% range per WD's recent commentary). Capex is estimated to be 6%-8% of revenue. HGST has previously noted that its transformation efforts continue with improving trends in sustained profitability and cash flow; focusing on responsible and profitable growth.

As a reference, the charts below summarize HGST's quarterly revenue, operating income/margin, and shipment trends by segment over the past several years. We also highlight the shipment share trends for total HDDs, 2.5" mobile/CE HDD shipments, and the enterprise-class HDD market.

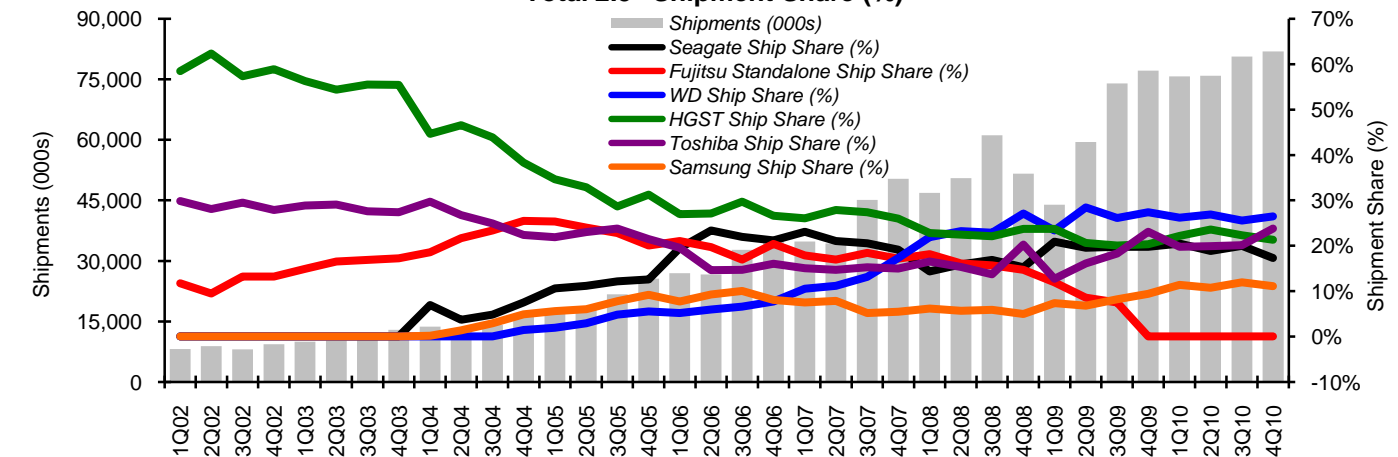
**HGST - Quarterly Revenue; Operating Margin**

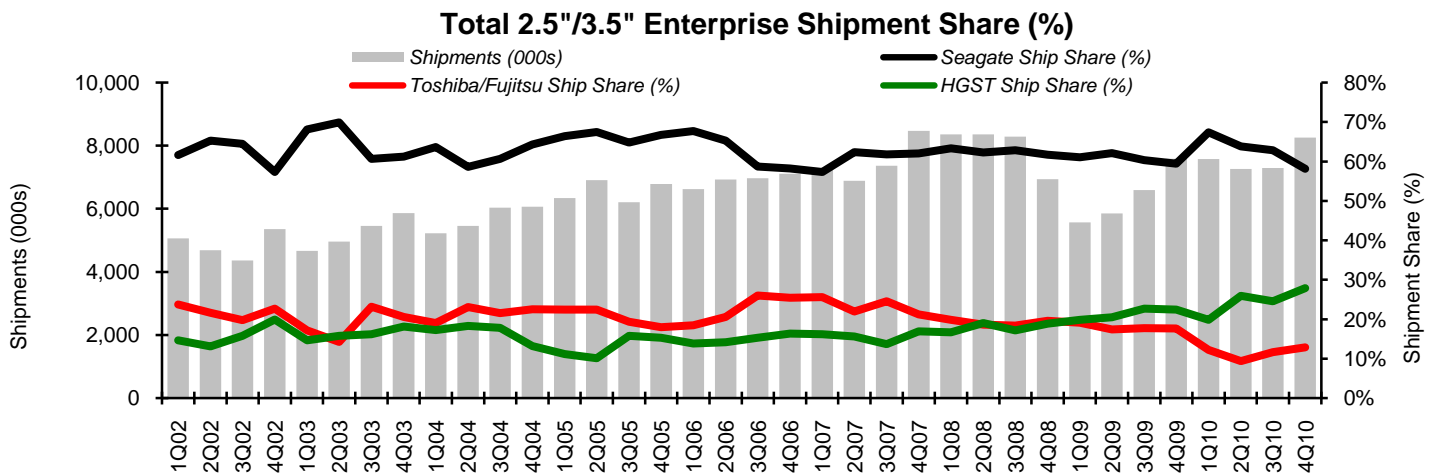


**Total HDD Shipment Share (%)**



**Total 2.5" Shipment Share (%)**





Source: IDC, TrendFocus, and Stifel Nicolaus Estimates

**Hitachi Storage Solutions (HDS plus Hitachi Storage Japan) – High-End Product Cycle; Heightened SSD Adoption (STEC Near-Term Positive, Seagate Long-Term Negative)**

Hitachi Ltd. reported that its total Storage Solutions revenue totaled ¥87 billion, up 6% yr/yr and a solid 18% sequentially. Using the stated ¥/US\$ FX rate of 81, this would imply yr/yr revenue growth of 20% yr/yr and 22% sequentially. Hitachi’s press release notes that the company saw *robust* results in its storage solutions for the December quarter, particularly overseas (i.e., Hitachi Data Systems, or HDS – Hitachi’s SAN/NAS offerings ex-Japan). **We would note that Hitachi’s F2010 (ending March 2011) forecast for the Storage Solutions segment now stands at ¥305 billion, which reflects a modest increase from the ¥300 billion forecast exiting the September quarter.** This would imply only ¥70 billion in the current quarter, which we view as quite conservative.

From our conversations with HDS’s management regarding the company’s December quarter results, we would highlight:

- **Strong Hardware and Software Growth – High-End Product Cycle Kicking In.** Driven by a high-end product cycle, HDS reported that hardware accounted for 55% of the company’s total revenue, up from 50% in the prior quarter and implying a mid-30% sequential growth rate. Software revenue increased to 20% of total revenue, also implying a mid-30% sequential growth rate. Services revenue, at 25% of total revenue, declined approximately 4%-5% sequentially for the December quarter.

In this, the company reported that its high-end systems revenue growth stood in the high-20% yr/yr range, and its modular/midrange revenue growth was in the high-single-digit yr/yr range. This compares to a down low-single-digit yr/yr and low-20% yr/yr growth rate disclosed in the September quarter. In our discussions, the company had noted that **it was seeing more than 90% of its new Virtual Storage Platform (VSP) deployments going into new installed environments versus upgrade environments relative to the company’s legacy USP/USP-VM installed base.**

- **Solid State Drive (SSD) Adoption Ramping with VSP High-End; Flipping the HDD Ratio between Mission-Critical (10K/15K SAS/FC) and High-Capacity (7200RPM SATA) Drives.** In our conversations, HDS’s management did note that it has seen a positive adoption of SSDs with the ramp of its new high-end VSP solutions – driven by its SAS architecture and the enhanced sub-LUN level tiering functionalities (vs. EMC’s launch of FAST-2 in its high-end Symmetrix arrays just over the past few weeks). **From a quantitative standpoint, our discussions suggested that the company has seen an increase of up to 5% of total system capacity being in SSDs with the new VSP offerings, relative to our estimate of a 1% capacity contribution in the prior generation USP/USP-V offerings.** We also estimate that the company sees a ~30% capacity contribution for SAS (10K/15K RPM) high-end drives in its new VSP with the remaining 65%-70% of disk drive capacity shipped per system being via low-cost/high-capacity SATA drives. We would estimate that the prior generation USP/USP-V solutions would have had a ~10%-15% SATA drive contribution with the remaining 85%-90% being the 10K/15K RPM drives.

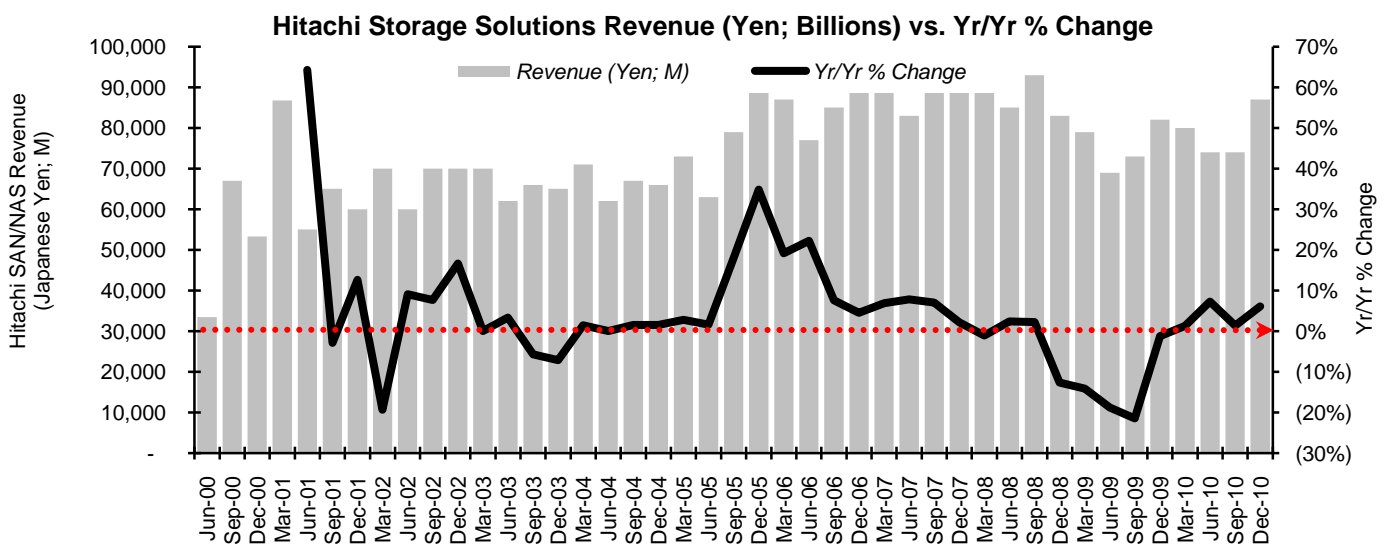
**STEC and Seagate Implications.** We would view this as a clear **positive for STEC**, in which we have estimated HDS to account for ~\$12-\$15M in revenue for STEC’s December quarter, albeit our conversations continue to point to additional SSD supplier relationships to develop over the coming quarters. Additionally, as we have reported in the past, we would view the changing dynamics between the use of high-RPM SAS/FC drives and SATA drives within the enterprise storage market as having **negative long-term implications for Seagate’s important enterprise HDD segment.**

- **Geography.** According to our conversations, HDS saw broad-based growth from a geographical basis – growing 19% yr/yr in Americas, 18% in EMEA, and 25% yr/yr in Asia-Pac (ex-Japan). This compares to the company reporting 10% yr/yr growth in Americas in the September quarter. EMEA grew only 4% and 3% yr/yr in the June and September quarters, respectively. Asia-Pac revenue grew 19% and 20% yr/yr in the June and September quarters, respectively.

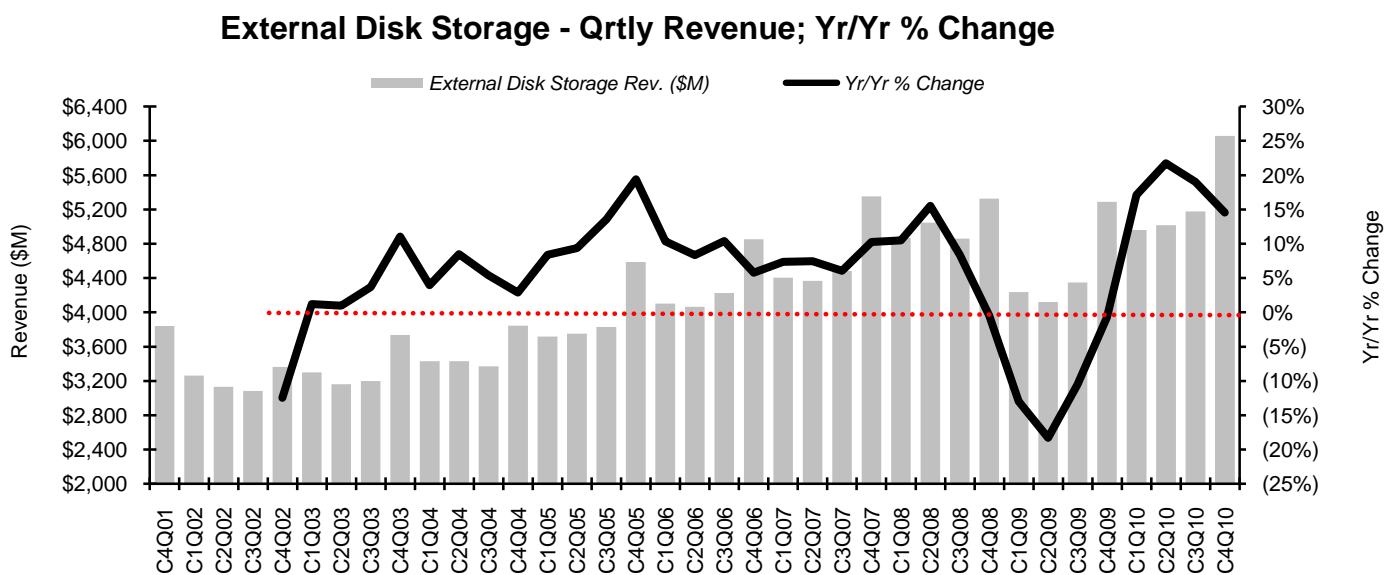
**EMC/NetApp Thoughts.** Although HDS has continued to ramp its midrange offerings, we believe most investors continue to view the company as competitive with EMC’s high-end Symmetrix offerings. While we do not view HGST’s results as changing our

positive thesis on EMC’s competitive positioning in the high-end storage market, we believe it will be increasingly important to monitor Hitachi’s new high-end product cycle over the coming quarters. As a reminder, HDS has historically seen as much as 20% of its revenue derived from its OEM relationship with HP, which we believe could come under some pressure as HP looks to integrate/ramp/push its 3PAR solutions. EMC reported that its Symmetrix revenue grew 19% yr/yr (we estimate up ~9% sequentially) for the December quarter. Our discussions with the company have highlighted an expectation that its high-end Symm revenue could grow in the mid-single-digit yr/yr range in 2011 and we believe it remains important to note that when looking at the robust growth seen in 2010, we still only arrive at a revenue estimate that is roughly flat with 2008 levels.

The charts below highlight Hitachi’s Storage Solutions revenue over the past several years, as well as our estimates for total external disk storage revenue. As shown, we estimate that the total disk storage market grew a robust ~ 17% sequentially and yr/yr for the December quarter. **If accurate, this would leave the total external disk storage market posting approximately 18% yr/yr in 2010, far surpassing our initial expectation of 9%-10% yr/yr growth. We would highlight the relative growth comparison between vendors for 2010, using our estimates for those that have not yet reported. We would characterize the overall C4Q10 demand data points on the storage market to be very positive for NetApp – making our/consensus current ~6% sequential growth estimate for the January quarter look particularly conservative, especially when considering our ongoing positive checks on NetApp’s current midrange/high-end product cycle.** We also highlight the relative external disk storage revenue share over the past several quarters (thru C3Q10; C4Q10 estimates not yet published), per IDC’s estimates.

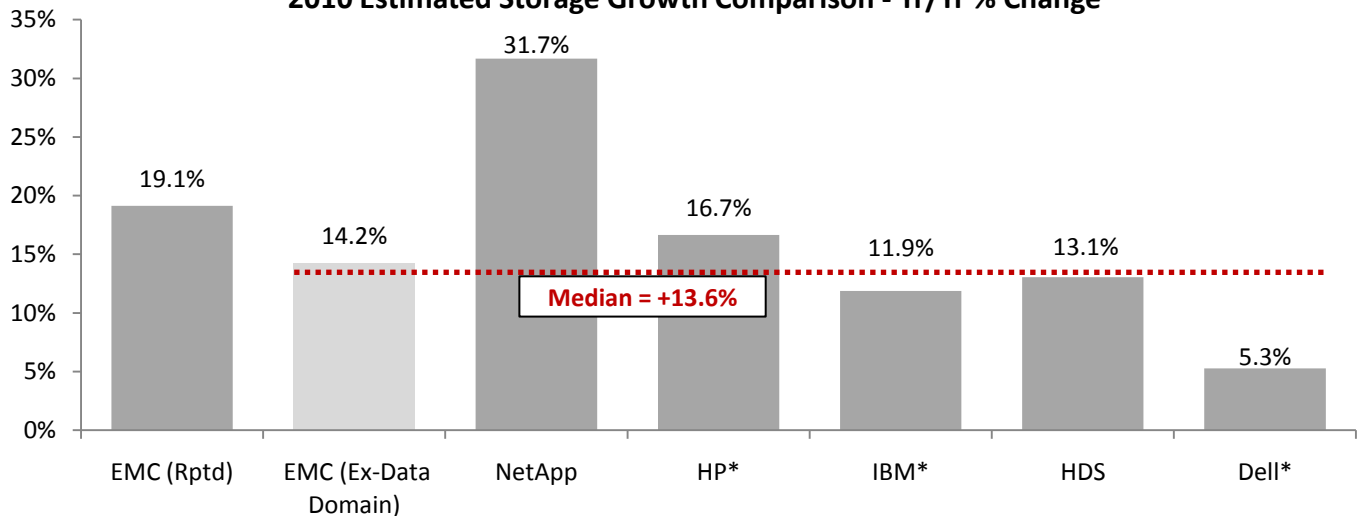


Source: Company Data



Source: IDC and Stifel Nicolaus Estimates

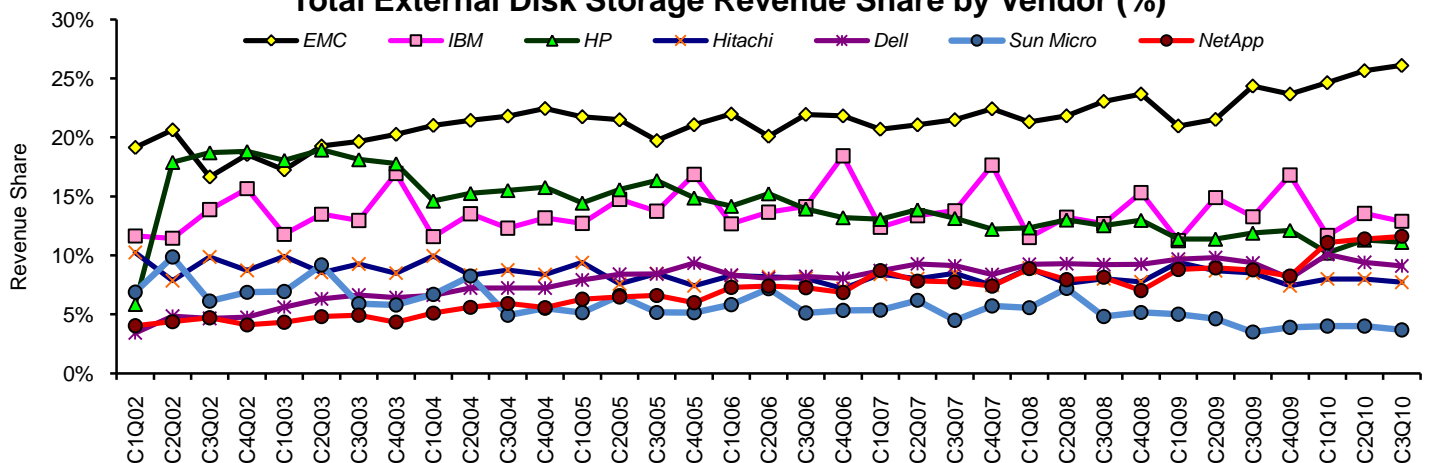
### 2010 Estimated Storage Growth Comparison - Yr/Yr % Change



Source: Company Data; Stifel Nicolaus Estimates

\*Note: We are including EqualLogic in Dell, LeftHand in HP, & XIV in IBM

### Total External Disk Storage Revenue Share by Vendor (%)



Source: IDC, Company Data, Stifel Nicolaus Estimates

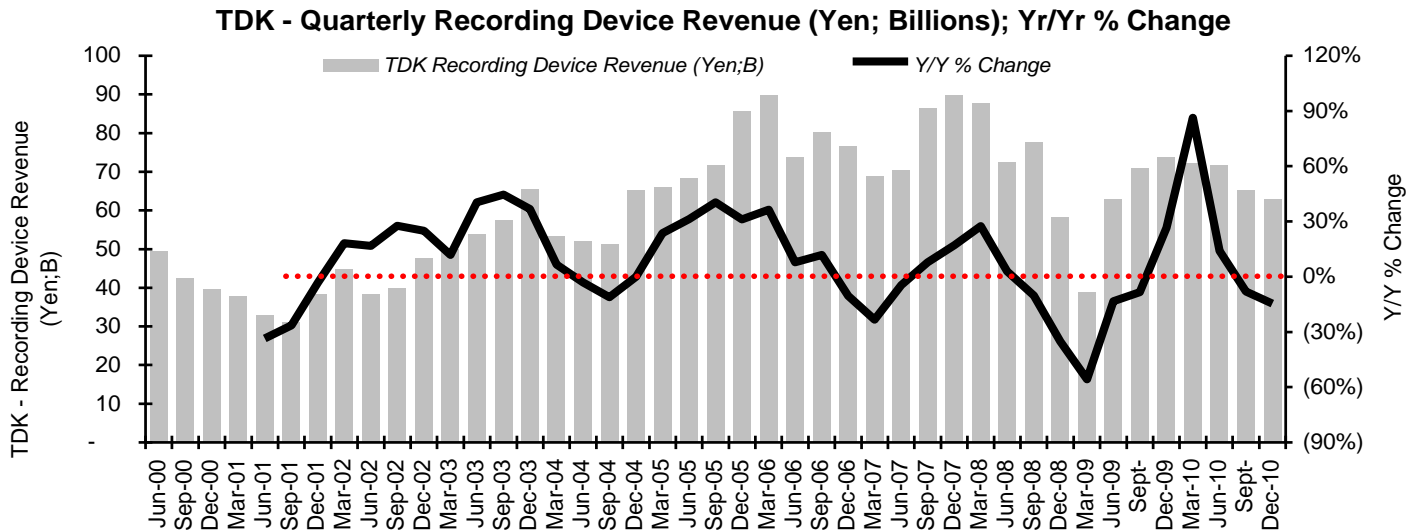
### Fusion-io has shipped 15TB of Enterprise PCIe Solutions over Past 12 Months

Fusion-io, which is a privately held leader in the PCIe SSD market, recently announced that it **shipped more than 15 petabytes of its enterprise PCIe module offerings over the past 12 months**. The company also notes that it has seen more than 2,000 end users choosing its solutions, including more than half of the Fortune 50 enterprises. Fusion-io's ioMemory and Virtual Storage Layer (VSL) technology primarily plays in the server market with its offerings with strong relationships with Dell, IBM, and HP; articles note that this is an indication that the industry is moving from the incorporation of NAND flash in the server market from leading edge application environments to mainstream enterprise computing applications. The company notes that the incorporation of its offerings have often enabled workload performance improvements by as much as 500% with higher utilization rates in virtualized server environments. In November 2010, Fusion-io introduced its newest offering – ioDrive Octal – that provided 6.2GB/s bandwidth and up to 5.7TB of linear-scaling capacity per PCIe slot. As a reference, per Dell's website, a Fusion-io 640GB MLC ioDrive carries a list price of \$11,832, or nearly \$18.50/GB – clearly not a cheap offering on a per GB basis; however, focus should be on IOPs improvements. A 320GB SLC-based ioDrive Duo carries a list price of \$17,487, or approximately \$54.60/GB.

### TDK Results (HDD Implications)

TDK, the sole merchant provider of read/write recording heads and suspension assemblies, reported recording device (primarily HDD heads) segment revenue of ¥200B (\$2.445 billion) for the first 9 months of F2011 (April 2010 – December 2010), which is down 3.7% yr/yr. This would imply revenue of ¥63.039B for the December quarter, which is down approximately 15% yr/yr and 3.5% sequentially. The company reported that the decrease for the first 9 months of F2011 mainly reflected a slight decline in sales volume of HDD heads, some Yen appreciation against the Dollar, and price erosion. Like last quarter, TDK is maintaining its original overall top/bottom-line forecast for its F2011 (ending March 2011), targeting sales of ¥880 billion, operating income of ¥60 billion, and net income of ¥45 billion. **TDK management did note that magnetic application products for recording devices saw a lack of growth in notebooks in the quarter.** TDK is targeting recording device sales of ¥57.9 billion for F4Q (March), noting that second half revenue is now targeted to be ¥120.9 billion compared to the prior forecast of ¥110.9 (up 9% from the prior view). The guidance

calls for an 8.2% sequential decline in recording device revenue and a 19.9% yr/yr decline – noting that FX has a large negative impact on the outlook. We view TDK’s results and outlook as generally in-line with Seagate and Western Digital targeting March quarter TAM to decline by roughly 5% and 7.5%, respectively.



Source: Company Data

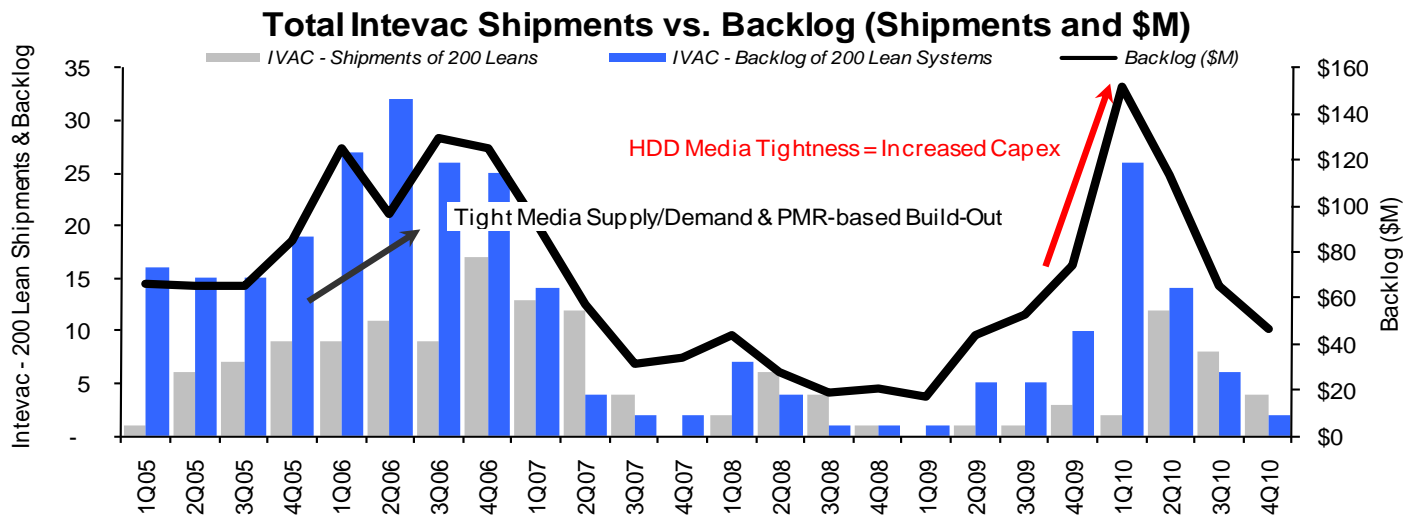
**Intevac Reports 4Q10 Results; Assumes Conservative Estimate of 10%-15% Yr/Yr HDD Growth in 2011**

Intevac, a provider of media sputtering/disposition equipment into the HDD industry, reported revenue of \$36.2 million, up 5.7% yr/yr and down 44% sequentially. This compared to the consensus estimate of \$37.0 million and the company’s guidance of \$36-\$37.5 million. Intevac’s HDD equipment revenue at \$26.799 million was up 74% yr/yr and down 52% sequentially. The company reported that it had recognized revenue on four systems shipped during the December quarter, down from eight systems shipped in the September quarter. **Of particular interest, the company reported that its order backlog totaled \$46.7 million exiting the December quarter, down from \$64.9 million exiting the prior quarter. This includes a backlog of approximately two Lean systems and two Lean Solar systems, which compares to six Lean systems exiting the prior quarter and 10 from the year-ago quarter. Looking into C1Q11, Intevac expects revenues of \$13.5-\$16.5 million, which includes no 200 Lean or Solar systems recognized in the quarter. For 2011, Intevac is expecting a conservative outlook for HDD shipments to be up 10%-15% yr/yr and the number of 200 Lean Gen II systems needed to support this growth would range from 8-16 systems.** As shown in the chart below, Intevac’s backlog continues to decline following the peak of the HDD supply/demand tightness exiting 1Q10.

Intevac noted that while 2010 began with an assumption of a 20% yr/yr growth rate in HDD shipments, this forecast had declined to approximately 15% by midyear. In response to this, customers modified delivery schedules to manage their capacity and **four systems were delayed by a quarter to 4Q10 with two systems deliveries moved to 2011.** Intevac believes the industry shipped a total of 655 million drives during 2010, resulting in yr/yr growth of approximately 17%, which is roughly in-line with our prior estimate.

**Turning to 2011, Intevac believes that HDD growth is still firming up with some initial estimates calling for about 700 million drives in 2011, or yr/yr growth of about 7%, with most of the growth expected in 2H2011.** The company believes this growth will drive additional capacity requirements for its customers. In assuming normal seasonality and relatively flat unit volume in 1H2011, the implied unit volume for 2H2011 is approximately 390 million drives, according to Intevac. In this, C4Q11 shipments could reach as much as 200 million, representing yr/yr growth of 18%-20%. In terms of the average number of disks per drive, Intevac believes the number will remain unchanged at 1.7 for 2011 due to the continued proliferation of high-capacity multi-terabyte drives, the desire for higher capacity drives on laptops, and the move to smaller disk and enterprise drives offset by magnetic aerial density increases.

The company noted that in addition to adding capacity systems to support growth in 2011, additional systems may be required to replace legacy systems. Intevac noted that its customers have over 60 legacy systems in production that manufacture primarily 3.5” aluminum disk. Looking into 2011, some industry estimates call for media growth to be dominated by 2.5” disk. While noting that the actual number of legacy systems being retired is hard to predict, in 2010, approximately half of the production systems shipped by Intevac were replaced legacy systems. With that said, the incremental capacity needs of Intevac’s customers in 2011 will be partially met by the four systems that were shipped in late 2010 and given that, Intevac does not expect to ship as many HDD manufacturing systems in 2011 as it did in 2010. Management did note that customers can wait until the end of 2Q11 to place orders for their peak capacity requirements given Intevac’s lead times and likely timing needs for 3Q11 installations.

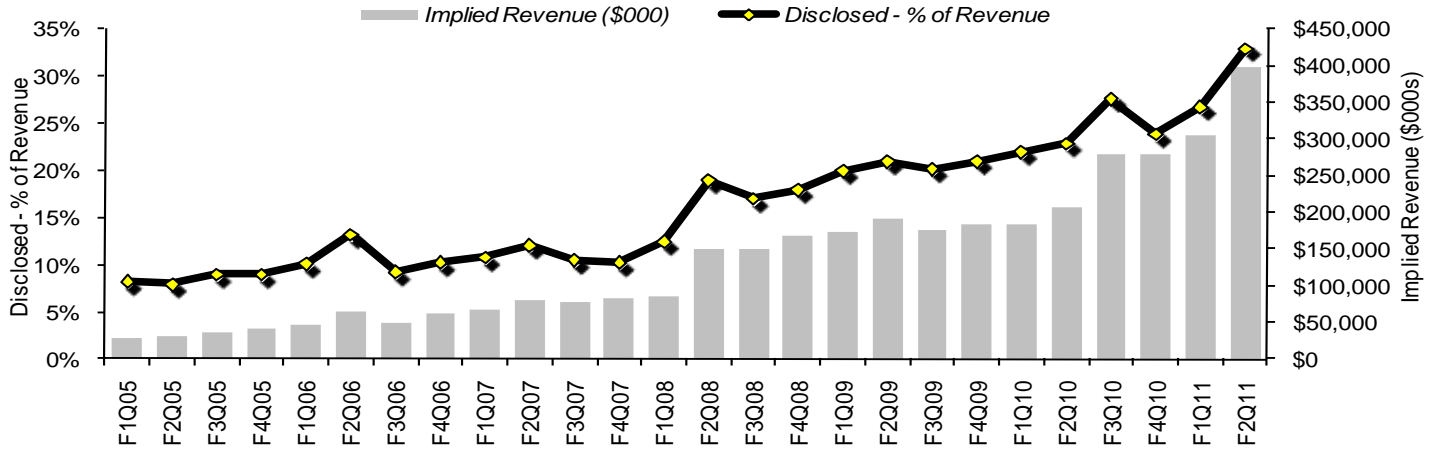


Source: Company Data

**Arrow Electronics Reports 4Q10 Results – Highlights Double-Digit Growth in Industry-Standard Servers and Storage**

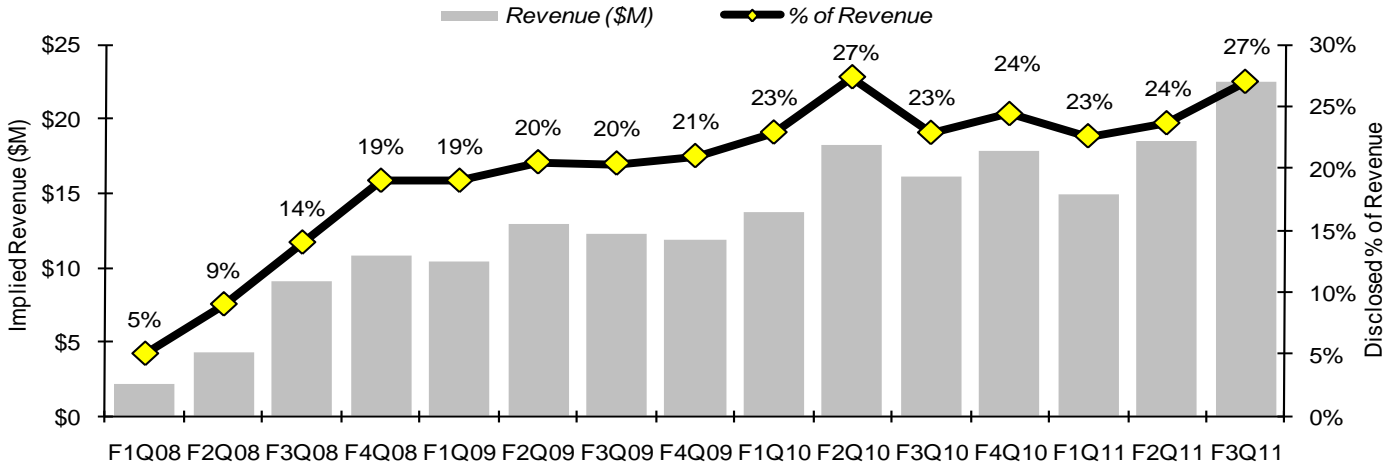
- Arrow reported total revenue of \$5.238 billion, which compares to the company’s guidance of \$5.0-\$5.4 billion and the consensus of \$5.492 billion. In this, the company reported: **(1) Global Components** – revenue totaled \$3.438 billion, up 28.9% yr/yr and down 2.7% sequentially. This compared to the company’s guidance of \$3.325-\$3.525 billion. **(2) Enterprise Computing** – revenue totaled \$1.894 billion, up 17.7% yr/yr and up 55.3% sequentially. This compares to the company’s guidance of \$1.675-\$1.875 billion in Enterprise Computing segment revenue for the December quarter. The company noted the enterprise computing solutions, total sales were well ahead of normal seasonality with extremely strong double-digit sequential growth in all products. Industry-standard servers were up 60% sequentially, proprietary products were up 55% sequentially, storage was up 40% sequentially, and software was up 65% sequentially. The company also noted very strong double-digit yr/yr growth in ISS, storage, software, and services.
- From a geographic perspective, the company saw growth in the Americas (+40% yr/yr), European (+43% yr/yr; +52% yr/yr excluding FX), and core Asia-Pacific (+29% yr/yr) regions in the **Global Components** business, which was partially offset by a slowdown in low-end handset business in Asia-Pac. Lead times are noted as returning to more normal levels, with the exception of a few specific areas, and there were no meaningful changes in cancellation rates. Management noted that its survey of over 300 customers in North America indicated that the outlook for purchase requirements heading into C1Q11 remained positive and that the majority of the surveyed customers believe they have the appropriate level of inventory heading into the March quarter. The **Enterprise Computing** business saw sales growth well ahead of normal seasonality in the Americas driven by strong performance in storage, software, industry-standard servers, and services. In Europe, sales growth was ahead of normal seasonality, led by strong performance in the U.K. and Nordic regions.
- **Guidance:** Looking forward, Arrow is guiding its 1Q11 revenue to be \$4.75-\$5.15 billion, ahead of the prior consensus estimate of \$4.841 billion. In this, Arrow is guiding: **(1) Global Components** - \$3.55-\$3.75 billion, midpoint implying just over 6% sequential growth, **(2) Enterprise Computing** - \$1.2-\$1.4 billion, midpoint implying down 31% sequentially. The guidance does not include the pending acquisition of the RF, Wireless & Power Division of Richardson Electronics. Management noted that for the Global Components business, the Americas region is expected to have organic growth at the low end of normal seasonality, the European region is expected to be in-line with normal seasonality, and the Asia-Pacific region is expected to be in-line with the high end of normal seasonality (although visibility is limited given the impact of the Chinese New Year). For the enterprise computing business, Arrow expects sales to be in-line with normal seasonality.
- **Derivative Thoughts.** As it relates to our coverage universe, we would note that IBM, HP, and historically Sun have accounted for the largest contributions in the server market (although dynamics with Sun changed during C2010 given the acquisition by Oracle), while EMC and NetApp have been the company’s largest storage partners. **NetApp** derived approximately 14% of its total revenue via Arrow in its F2010 (April 2010), equating to approximately 20% of NetApp’s total indirect revenue. Avnet accounted for ~11% of NetApp’s total revenue, leaving combined Arrow + Avnet at ~24% of total revenue, or approximately 35% of NetApp’s indirect revenue (see chart below). We estimate that Arrow and Avnet combined to account for roughly 33% of total revenue in the October 2010 quarter (18% from Arrow and 15% from Avnet), or approximately 46% of total indirect. NetApp’s indirect revenue accounts for ~70% of total revenue, consistently representing a key growth driver over the past several years. **CommVault** derived approximately 27% of its December quarter revenue through Arrow (see chart below). We believe Arrow’s in-line results could be viewed as a net-neutral/slightly positive data point for CommVault especially as the company utilizes its recently restructured sales force. **EMC** has not explicitly talked about its relationship with Arrow; however, the company has noted that it sees up to 75% of its total mid-tier revenue flowing through channel partners (note: EMC did recently announce its VNX/VNXe mid-tier product refresh and we believe the Data Domain business remains strong). In terms of servers, Arrow’s consistent positive comments on industry-standard (x86) server strength could be viewed as a positive for **HP** (leader in x86 servers w/ ~50% share) as well as for **Dell**.

**NetApp - Arrow + Avnet Contribution - % of Total Revenue (Disclosed)**



Source: Company Data

**CommVault - Implied Arrow Revenue; Disclosed % of Total Revenue**



Source: Company Data

Enterprise Hardware & Hard Disk Drive Coverage Summary

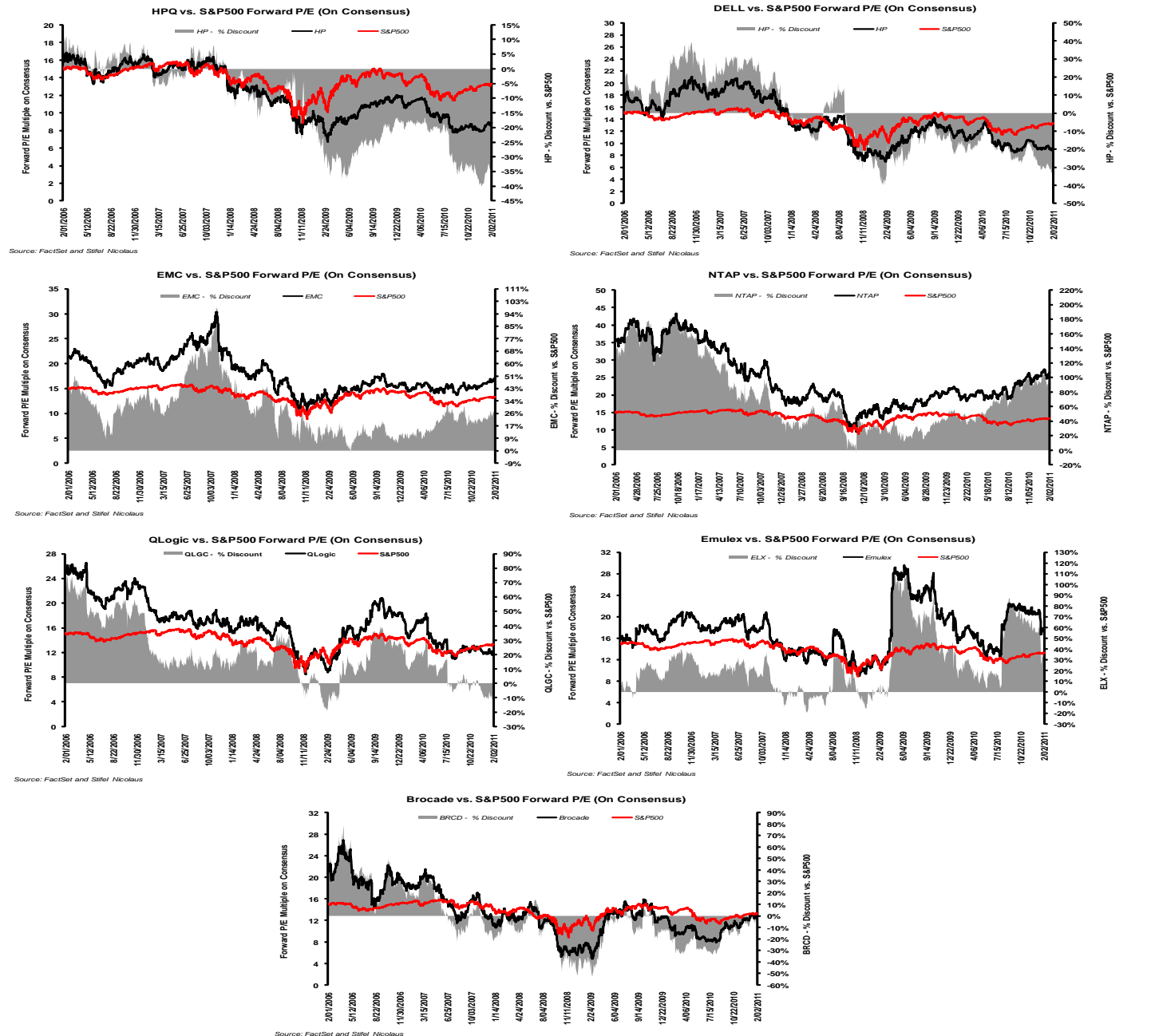
Ticker	Price 2/4/2011	Market Cap.	Ent. Value	Share Performance					Valuation on Consensus/Trailing					
				% Ch. YTD	% Ch. 12-Months	% Ch. 3-Months	% Ch. 1-Month	% Ch. 1-Week	Forward P/E (C2011)**	Forward P/E (C2012)**	MC/Sales (Trailing)	EV/Sales (Trailing)	EV/Sales C2011	EV/EBITDA (Trailing)
EMC (Hold to Buy = 1/4/10)	\$25.69	\$53,159	\$51,996	12.2%	50.6%	19.7%	11.2%	4.9%	18.27	16.78	3.10	3.06	2.79	12.76
NetApp (Hold to Buy = 12/20/10)	\$57.93	\$20,930	\$17,671	5.4%	36.8%	7.9%	0.9%	7.2%	26.61	22.86	4.47	3.90	3.17	20.43
Hewlett-Packard (Initiate Buy = 8/6/09)	\$47.43	\$104,531	\$116,233	12.7%	-2.7%	8.3%	11.0%	4.2%	9.18	8.47	0.87	0.92	0.74	6.70
Dell (Initiate Buy = 1/5/10)	\$13.89	\$26,808	\$19,390	2.5%	4.0%	-4.1%	1.5%	5.6%	9.23	8.92	0.45	0.32	0.31	4.48
Broadcom (Buy to Hold = 2/23/10)	\$6.08	\$2,805	\$3,398	14.9%	-9.3%	-1.1%	12.1%	8.6%	16.16	11.12	1.30	1.62	1.59	8.56
QLogic (Initiate Buy = 3/25/09)	\$18.14	\$1,924	\$1,581	6.6%	3.5%	2.5%	5.2%	2.8%	12.29	10.94	3.37	2.68	2.57	8.79
Emulex (Initiate Hold = 3/25/09)	\$11.74	\$992	\$914	0.7%	-3.7%	7.2%	-0.1%	5.5%	18.10	13.34	2.29	1.93	1.66	14.50
Compellent (Hold = 3/26/09; Pending Acq. By Dell on 12/13)	\$27.69	\$882	\$822	0.4%	36.8%	12.1%	0.4%	0.0%	84.91	58.30	5.97	5.60	4.28	110.53
CommVault (Buy to Hold = 7/13/10)	\$33.73	\$1,450	\$1,256	17.9%	50.6%	16.6%	14.4%	12.8%	37.03	31.02	4.86	4.21	3.78	33.23
Xyratex (Upgrade to Buy = 6/24/09)	\$13.50	\$409	\$318	-17.2%	-3.1%	-17.1%	-17.9%	2.7%	5.96	5.68	0.25	0.20	0.20	2.18
Seagate (Buy to Hold = 10/28/10)	\$14.33	\$6,766	\$6,780	-4.7%	-23.9%	-2.4%	-4.3%	3.8%	8.64	6.38	0.62	0.61	0.62	3.11
Western Digital (Hold to Buy = 4/22/10)	\$36.21	\$8,401	\$5,641	6.8%	-10.6%	8.8%	6.1%	6.7%	12.78	9.41	0.84	0.57	0.63	3.18
FS Networks (Hold; Wadhvani)	\$123.64	\$9,982	\$9,496	-5.0%	145.0%	0.0%	-8.0%	12.8%	32.49	27.34	10.31	9.89	8.08	18.16
IBM (Not Covered)	\$164.00	\$203,747	\$220,847	11.7%	30.5%	13.8%	11.2%	3.0%	12.54	11.37	2.08	2.21	2.05	9.07
Apple (Buy; Doug Reid)	\$346.50	\$319,139	\$292,162	7.4%	73.9%	10.8%	5.1%	3.1%	14.61	12.87	4.15	3.83	2.51	12.75
Cisco (Buy; Sanjiv Wadhvani)	\$22.05	\$122,973	\$99,346	9.0%	-4.4%	-7.0%	7.6%	5.4%	12.96	11.60	3.00	2.38	2.20	7.97
Juniper (Buy; Sanjiv Wadhvani)	\$40.06	\$20,877	\$18,591	8.5%	58.2%	20.1%	7.6%	10.4%	25.85	21.20	5.11	4.54	3.77	19.56
S&P IT Consulting & Services	\$123.64	\$9,982	\$9,496	-5.0%	145.0%	0.0%	-8.0%	12.8%	32.49	27.34	10.31	9.89	8.08	31.90
S&P Semiconductors	\$37.11	\$5,454	\$5,288	5.5%	223.8%	26.2%	-1.9%	4.4%	44.18	32.84	9.75	9.58	6.96	67.73
Average Return:				6.8%	39.8%	8.5%	4.5%	6.1%	22.65	17.78	3.52	3.24	2.65	20.82
Median Return:				6.8%	30.5%	8.3%	5.2%	5.4%	16.16	12.87	3.10	2.68	2.51	12.75

Highlighted = Stifel Buy Rated Stocks

\* Forward P/E = On Next 12-Month Consensus Estimate  
 \*\* Forward P/E = On C2011, C2012 = On Stifel Estimates (Except Stocks Not Followed)

Source: FactSet; Stifel Nicolaus Estimates

ENTERPRISE HARDWARE COVERAGE - LARGE/MID-CAF FORWARD P/E (NTM; CONSENSUS) VS. S&P500



# Noteworthy News Review – Stifel Nicolaus Thoughts/Analysis

EMC Corporation

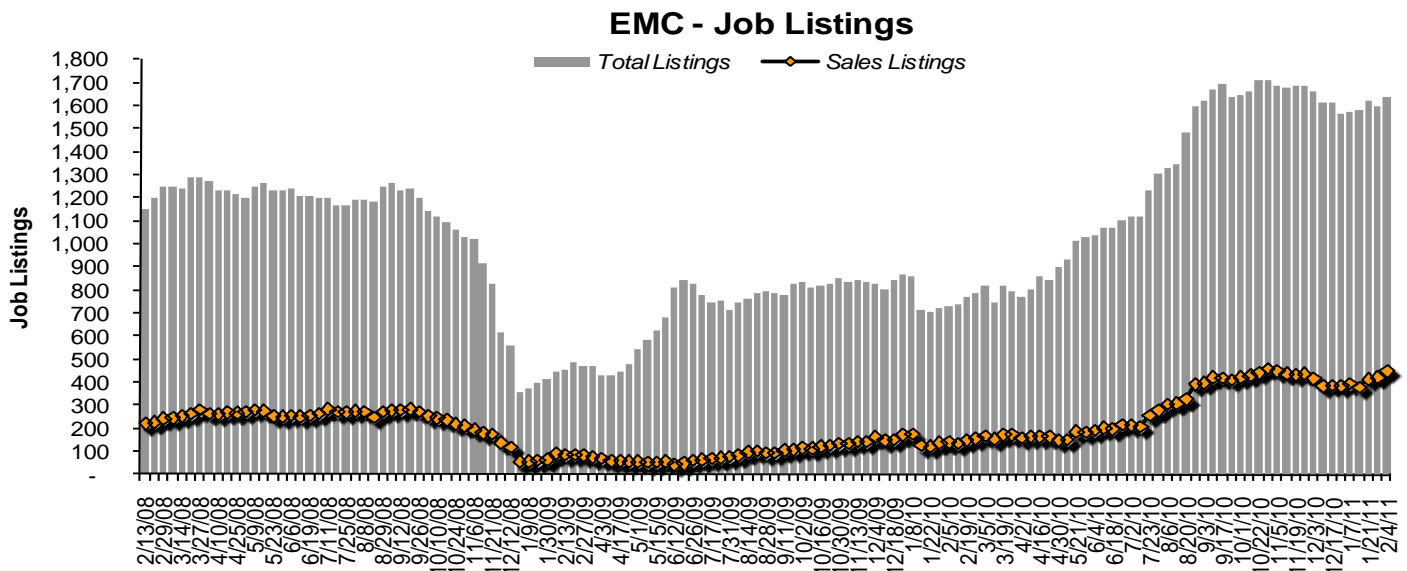
(EMC – NYSE - \$25.69 – Buy)

## 2/1/11: EMC Unifies eGRC Strategy for Enterprise Governance, Risk and Compliance Programs

EMC has announced its enterprise Governance, Risk and Compliance (eGRC) strategy that is designed to allow organizations to become more agile, gain greater visibility into their data, and drive an operational framework across the enterprise, according to EMC. The new strategy includes an open platform, technology solutions, a user community and partners to provide a holistic view of an organization’s total risk and compliance profile. The new strategy focuses on four key areas: (1) Business Solutions, (2) Information Governance, (3) Business Continuity and Disaster Recovery, and (4) Advanced Security Management. EMC has also announced the next-generation of its RSA Archer eGRC management platform that is designed to support cross functional collaboration across IT, operations, legal, and finance areas. It should allow organizations to have centralized views into enterprise risk, automated and repeatable business processes, integrated systems, and information as well as flexibility to evolve as an organization’s needs change.

## EMC Job Listings Update

As of last week, EMC’s job listings totaled 1,640, which are up from 1,595 last week and now up 75 from levels at of the beginning of 2011. In this, there were 325 total core EMC listings, increasing by 15 openings compared to last week and now up from 317 at the beginning of January. In terms of total sales listings, there were 450 openings, increasing by 27 listings over the last week and up from 385 at the beginning of the year. Total professional services listings were 115 at the end of last week, increasing by 8 from levels in the previous week, while software engineer listings totaled 277, decreasing by 9 over the same time period. EMC’s Data Domain job openings, which came in at 18, were down 1 compared to the prior week. The Data Computing Division (Greenplum) now has 120 openings – down 2 from last week. The figure below highlights EMC’s job listings over the past several months.



Source: Company Data

NetApp Inc.

(NTAP – Nasdaq - \$57.93 – Buy)

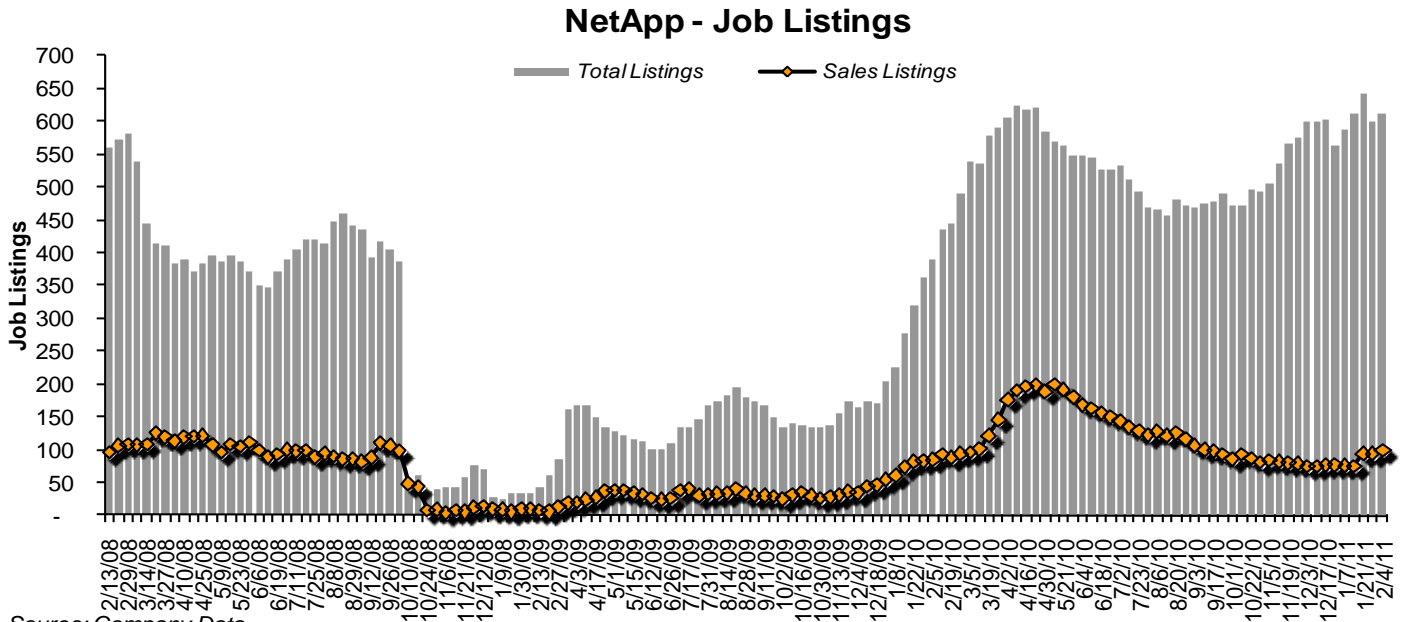
## 2/1/11: NetApp Completes Acquisition of Akorri Networks

NetApp announced that it has completed the acquisition of Akorri Networks, a privately held company, for approximately \$60 million. The press release notes that Akorri was able to grow its customer base by more than 100% in 2010 by helping enterprises adopt and expand their use of server virtualization technology. NetApp notes that Akorri will extend the NetApp OnCommand management software suite with performance capacity analytics and optimization for greater visibility across the IT stack, including applications, servers, networks, and storage. Akorri’s main software offering is called BalancePoint, which helps customers identify performance bottlenecks, improve storage capacity planning, and free up time, people, and budget resources needed to run virtual environments. It complements NetApp SANscreen in order to help customers improve IT flexibility and efficiency through functions that help operate and analyze virtualized, share IT infrastructures.

## NetApp Job Listings Update

NetApp’s job listings increased by 12 openings over the past week, increasing again after the downturn we saw in the prior week – job openings came in at 613 vs. 564 at the beginning of January. We would point out that NetApp has stated on numerous occasions its plans to target a long-term operating margin at 16% and if the company were to run above this level, it would invest for growth in the company (obtained 19.8% operating margin in October 2010 quarter, vs. LT guide of 17.5% +/- 50bps; management noted an expectation of 18.5% for January 2011). The company’s current listings have 99 sales openings, which is up 5 openings compared to last week and up 22 from 77 listings at the beginning of 2011. The company has 203 openings for software engineers, which is down 2 compared to last week and down 9 from 212 listings on 12/31/10. Customer support engineering listings decreased by 2 openings to

come in at 67, which is down 3 compared to levels in the beginning of the year. The figure below highlights NetApp’s employee job listing trends over the past several months.



Source: Company Data

**Hewlett-Packard (HPQ – NYSE - \$47.43 – Buy)**

**2/3/11: BMC Software Results – Cisco UCS Ramp Remains Slower than Anticipated**

Last week, BMC Software announced its F3Q11 earnings, with our focus on Cisco-related commentary, specifically focusing on UCS data points. In prepared comments, BMC noted that it recently entered into an alliance with Cisco that targets new solutions for large-scale cloud-computing infrastructures, and is already delivering products. The product was described as a new integrated cloud delivery platform consisting of technology from both BMC and Cisco, with a good portion of cloud wins for F3Q stemming from the Cisco partnership.

In regard to a question during the Q&A portion of BMC’s earnings call inquiring about the Cisco UCS initiative, **BMC Software noted that UCS is “a little behind” where BMC thought it would be at this time, although noting that the UCS business is growing nicely off of a small base.** UCS is seen as a building block that can drive large-scale cloud wins. Previously (June 2010 quarter), BMC had noted that it had over 100 customers through its OEM relationship with Cisco, noting that the April 2010 quarter was too early to give any color around the expected impact, and no update in the December quarter.

**2/3/11: HP Set to Refresh Midrange EVA Storage Arrays?**

Although we believe HP’s long-term focus will be on the company’s 3PAR solutions/architecture moving down market going forward (sub-\$100k price points), a short story published on *Storage Newsletter* reported that HP may be readying some refreshed midrange EVA solutions. The article suggests that HP could introduce two new configurations, the EVA P6300 that will support 5 or 10 SFF (small form factor, 2.5” HDDs) disk shelves, while a higher-end P6500 would support 10 or 18 SFF disk shelves. **The article also notes that these offerings will support long-awaited enterprise-class SSDs.**

**2/3/11: HP Cautious on 1Q11 Notebook PC Shipments**

According to a *DigiTimes* article published last week, and likely further supported by Intel’s quality issue announcements with regard to the Sandy Bridge processors, HP is apparently more cautious on notebook PC shipment trends in 1Q11. The article cites an expectation of 7%-10% yr/yr growth to 10.1-10.4 million units shipped, reflecting a tempering outlook given a softening in Asia-Pac demand – per upstream component providers. The article notes that HP sees a 15%-20% decline in Asia-Pac demand, from which China was noted as the primary driver. The story notes that HP has had well-known quality issues on some of its consumer notebooks in China.

**Dell, Inc. (DELL – Nasdaq - \$13.89 – Buy)**

**1/31/11: Compellent and Dell Reach Memorandum of Understanding and Amend the Agreement and Plan of Merger**

Last week, Compellent filed an 8-K in which the company and Dell reached a memorandum of understanding relating to several putative class action lawsuits related to the merger. **As a result, Compellent expects the special meeting date to approve the adoption of the Merger Agreement to be postponed until February 22, 2011.** As part of this understanding the two companies have agreed to amend their Agreement and Plan of Merger. The following changes have been made:

- Dell and Compellent will eliminate the requirement that Compellent have a stockholder rights plan and Compellent will redeem the rights outstanding under the prior rights plan and that this amendment will not give Dell the right to terminate the merger agreement or receive a termination fee under the merger agreement.
- Dell and Compellent will amend Section 4.3 (No Solicitation) to include the following exemplary changes: (a) Compellent and Dell agree that Compellent will not be required to enter into a standstill agreement with future bidders, if any; (b) Compellent and Dell will agree to eliminate or shorten certain time periods regarding future bids, if any; (c) Compellent and Dell will agree to reword the determination that must be made in order for Compellent’s board of directors to enter into discussions or negotiations or share confidential non-public information with a potential bidder; (d) Compellent and Dell will agree to modify the type of information that Compellent would be required to supply to Dell relating to a future bid, if any; and (e) Compellent and Dell agree to revise the applicability of subsection (g) relating to a breach of Sections 4.3 (No Solicitation) and 5.2 (Company Stockholders’ Meeting) of the Merger Agreement
- Compellent and Dell will revise the definition in the Merger Agreement of “Triggering Event”, which includes the following exemplary changes: (a) Compellent and Dell will agree to eliminate the reaffirmation of the board recommendation upon request provision; (b) Compellent and Dell will agree to delete the triggers relating to the Rights Plan and the standstill provision previously set forth in Section 4.3 (No Solicitation); and (c) Compellent and Dell will agree to add a materiality condition to subsection (f), relating to a breach of Section 4.3 (No Solicitation).
- Compellent and Dell will amend the Merger Agreement to provide that the termination fee referred to in Sections 8.3(c) and 8.3(d) of the Merger Agreement will be reduced to \$31,100,000.
- Compellent will agree to delay the meeting of the stockholders for the stockholder vote to approve the adoption of the Merger Agreement with respect to the merger (the “Merger”) so that it does not occur prior to 21 days from the date the terms set forth in the preceding bullet points are disclosed to the public on a Current Report on Form 8-K.

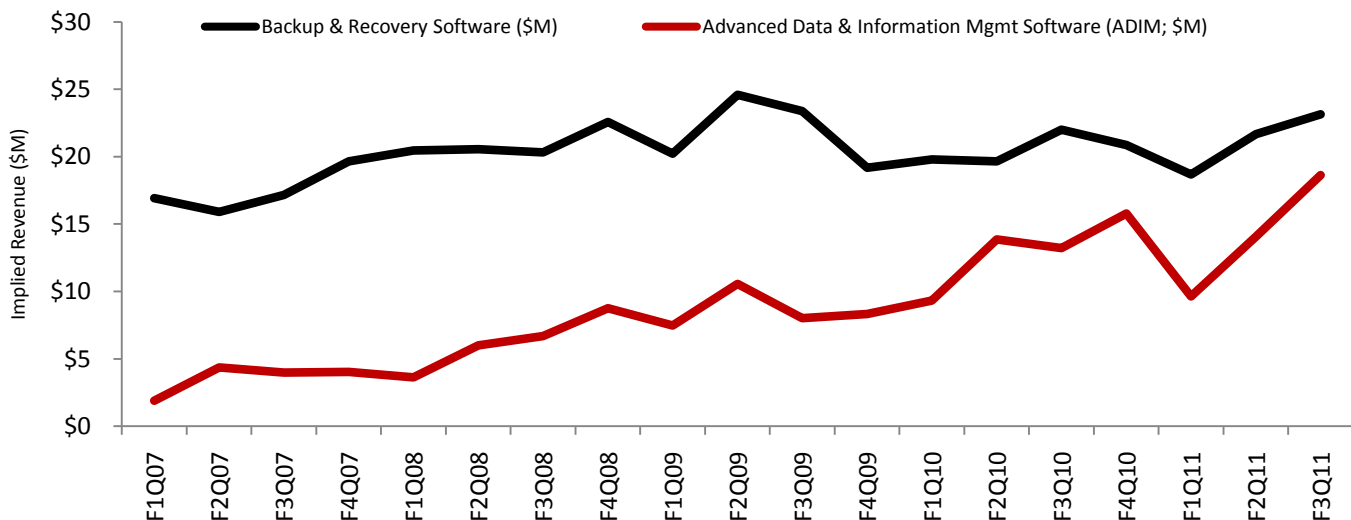
**CommVault Systems**

(CVLT – Nasdaq - \$33.73 – Hold)

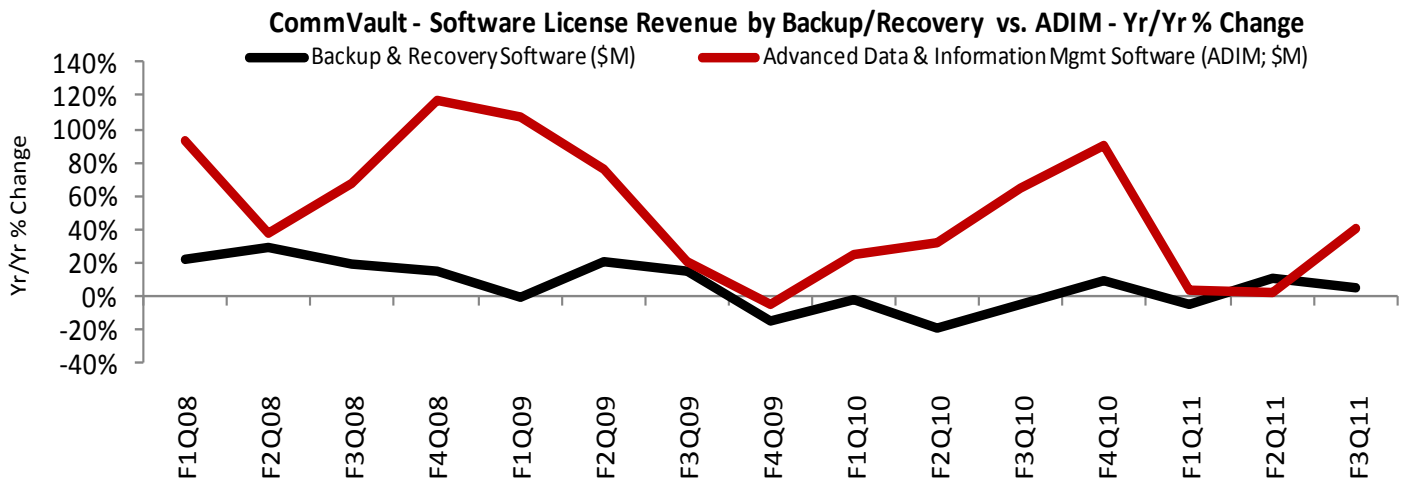
**2/4/11: Quick Notes on F3Q11 10-Q Filing – Impressive ADIM Growth; Strong OEM Uptick**

• **Software Breakdown – Strong Yr/Yr and Seq. Growth in ADIM License Revenue.** As reported, CommVault’s 10-Q filing discloses that the company generated approximately 60% of its total software license revenue from sales of Backup and Recovery solutions during the nine months ending December. **We find it notably interesting that this would imply a roughly ~55% contribution for the December quarter, or rather reflective of an increase in the company’s Advanced Data and Information Management (ADIM) offerings to 45% of software license revenue from an implied 39% contribution in the prior and year-ago quarters.** This implies ADIM revenue grew a strong 41% yr/yr (vs. Backup and Recovery +5% yr/yr), or up approximately 32% sequentially (vs. Backup and Recovery license revenue +7% sequentially). The charts below illustrate CommVault’s quarterly software license revenue trends over the past several quarters. We would also highlight CommVault’s disclosure that software revenue growth of 19% yr/yr reflected a 24% yr/yr increase in revenue outside the U.S. and a 15% yr/yr growth rate for revenue generated within the U.S. (vs. disclosed 21% yr/yr and -1% yr/yr in the prior quarter, respectively).

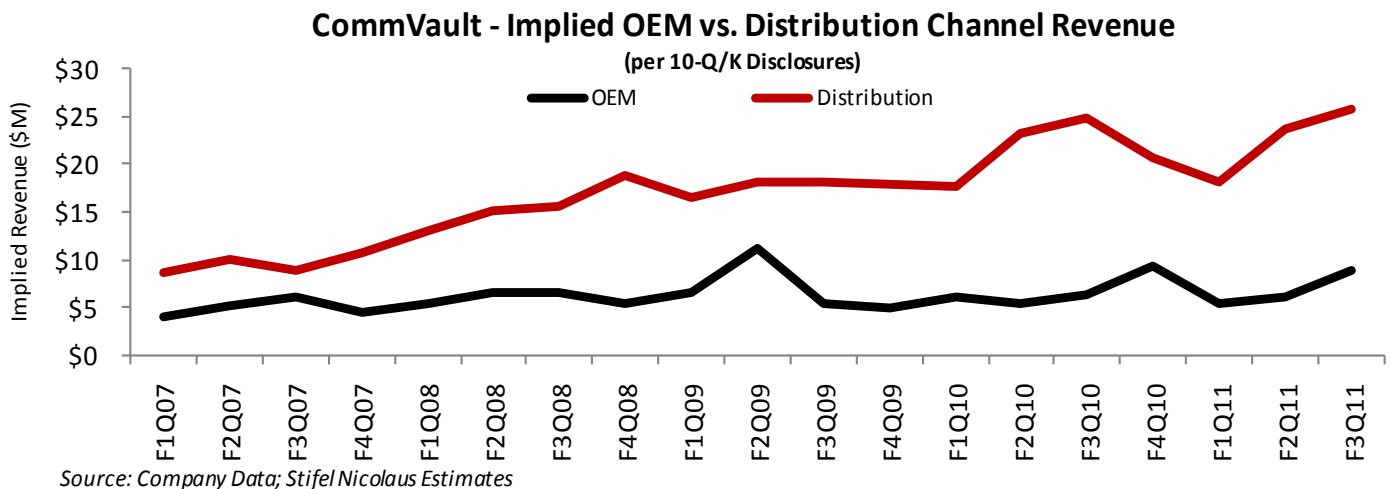
**CommVault - Software License Revenue by Backup/Recovery vs. ADIM**



Source: Company Data; Stifel Nicolaus Estimates



- Indirect vs. Direct Revenue; OEM Revenue.** CommVault again reported that it had derived approximately 83% of its total software license revenue from indirect channels for the nine months ending December 2010. Using these 10-Q disclosures, we can roughly conclude total indirect channel software revenue at \$34.7 million for the December quarter, growing 12% yr/yr and 17% sequentially (or disclosed at +\$3.6 million). Within this, the company disclosed that its **OEM software revenue contribution stood at 9% of total revenue for the nine months ending December, which would imply a ~11% contribution for the quarter, or roughly a 41% yr/yr increase and up more than 45% sequentially (again in using prior quarterly cumulative disclosures).** This would also imply total distribution channel revenue (ex-Services) at approximately 31% of total revenue for the December quarter, growing 3% yr/yr and approximately 9% sequentially for the December quarter, according to our model. As a reminder, the company disclosed that Arrow accounted for ~27% of total revenue for the December quarter, growing 42% yr/yr and 28% sequentially. The company's 10-Q notes that its Avnet contribution was not material for the nine months ending December. Direct revenue grew \$2.9 million yr/yr, or 76% yr/yr for the December quarter (vs. 10% yr/yr growth in the prior quarter).



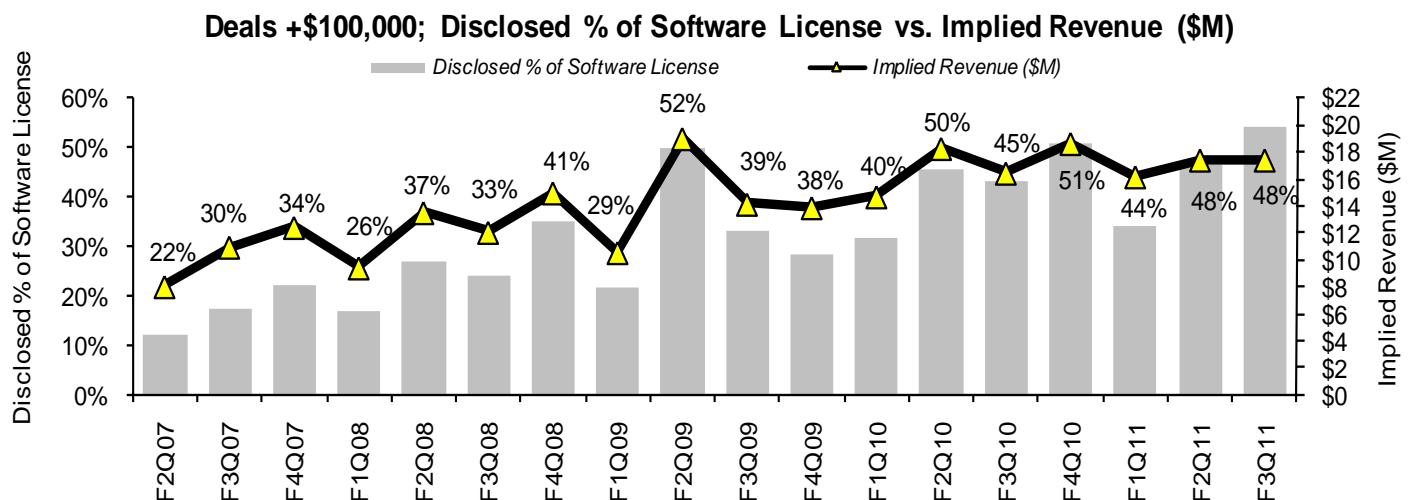
- Enterprise Deals.** As previously disclosed, approximately 48% of CommVault's F3Q11 software revenue was derived from deals in excess of \$100,000, reflecting an absolute revenue increase of \$4.3 million or 27% yr/yr for the December quarter. Revenue from deals less than \$100,000 grew 12% yr/yr, or \$2.2 million (vs. a 13% yr/yr increase reported for the prior quarter). **The company's 10-Q filing reiterates that the company had seen a 35% yr/yr increase in the number of enterprise deals, which compares to a 17% yr/yr increase in the prior quarter.** The average deal size of >\$100k deals stood at \$219,000 (as previously reported), down from the ~\$230,000 average deal size reported in the prior quarter and ~\$233,000 in the year-ago quarter.
- Currency (FX) Impacts – No Impact.** CommVault's 10-Q filing discloses that it had generated approximately 38% of total revenue from international markets during the nine months ending December, or approximately a 40% contribution for the December quarter. The company's filing also discloses that revenue would have been higher by approximately \$300,000 for the December quarter, or equating to approximately a 40bps impact to yr/yr revenue growth, per our model. Cost of revenue and opex would have been impacted by less than \$100,000 and \$200,000, respectively. This results in no impact to the company's bottom-line EPS, according to our model.
- Dell & Arrow Revenue and Accounts Receivables Contributions.** In addition to noting that Dell and Arrow accounted for 23% and 25% of revenue for the nine months ended December 31, 2010 (disclosed 20% and 27% for F3Q11, respectively), the filing also

discloses that Dell and Arrow accounted for 21% and 33% of the company’s accounts receivables balance exiting the December quarter. This implies a sequential decrease of nearly 18% at Dell and an increase of just over 59% sequentially at Arrow. On a yr/yr basis, CommVault’s Dell accounts receivable balance declined 14% and Arrow accounts receivables balances increased 61%.

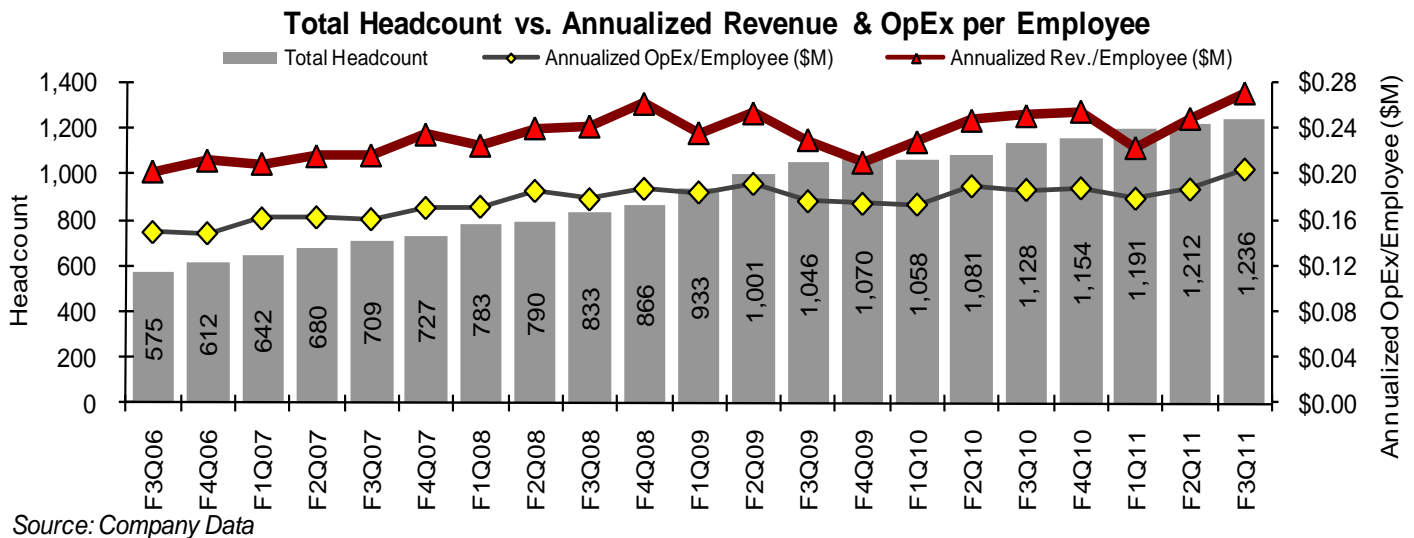
- **Deferred Revenue Breakdown.** As reported earlier this week, CommVault’s total deferred revenue balance of \$103.167 million grew 24% yr/yr and 6% sequentially. The company reported short-term deferred revenue of \$90.833 million, which was up 22% yr/yr and up 4% sequentially. The 10-Q filing discloses that this consisted of \$377k in deferred software license revenue, down from \$533k in the prior quarter but up from \$197k in the year-ago quarter, leaving the remaining \$90.456 million in deferred services revenue. This was up 21.5% yr/yr and roughly 4% sequentially. Long-term deferred revenue of \$12.334 million was up 46% yr/yr and up 18% sequentially.
- **Other. (1) New vs. Existing Revenue.** CommVault’s filing again reiterates that in recent fiscal years it has generated approximately 62% of revenue from existing customers, leaving approximately 38% of total revenue from new customers (similar commentary given in previous 10-Q). **(2) Cumulative Customer Base.** CommVault’s 10-Q reiterates the company’s prior disclosure of exiting the December quarter with approximately 13,500 total employees, up from ~13,000 exiting the prior quarter, or noted to reflect an additional ~400 customers. **(3) Share Repurchase.** CommVault’s 10-Q reiterates the fact that the company exited the December quarter with \$48.252 million remaining in its current share repurchase authorization; this equates to a ~1.5 million repurchase authorization, or approximately 3% of total shares outstanding. As a reminder, CommVault did not repurchase any shares during its December quarter.

**2/1/11: Solid F3Q11 Results; Focus on Simpiana 9 Growth and Continued Sales/Distribution Investments**

- **Maintain Hold; Focus on Simpiana 9 Adoption, Continued Investments and Ramping/Expanding Opportunities.** While we continue to consider CommVault a well-positioned story looking forward with a very favorable view on the company’s Simpiana 9 product suite, we maintain our Hold rating at this time. We remain positively focused on CommVault’s new Simpiana 9.0 product cycle, expanding enterprise deal pipeline/funnel (enterprise sales up 24% sequentially and accounted for 48% of license revenues vs. 48% in F2Q11; noting an increase in 7-figure deals), ramping/expanding distribution partnership base (Hitachi, Avnet, and other unnamed distribution partnerships ramping), although we believe investors should pay close attention to ongoing investments in the company’s sales force and distribution base going forward as it relates to operating margin expansion (company now forecasting 50-75bps expansion in F2012). While our investment thesis continues to reflect no expectation of CommVault being acquired in the near term, we would expect shares to see downside risk support given recent M&A activity/expectations in storage/data management/cloud-computing. Shares of CVLT now trade at ~38x and ~34x our C2011 and C2012 estimates, or more importantly 3.6x and 3.3x EV/Sales on our C2011 and C2012 estimates.
- **Estimates – EPS Lowered Given Ongoing Investments.** Our F2012 estimates are now \$359.9M/\$0.83. (vs. prior \$338.5M/\$0.95), and we have introduced a F2013 estimate at \$396.5M/\$0.99. C2011 and C2012 estimates are \$349.9M/\$0.83 and \$387.9M/\$0.94 with non-GAAP operating/EBIT margin estimates at 17.7% and 19.1%. We would note our EPS changes also reflect a raised pro forma tax rate assumption from 34% to 36% in F2012 as well as increased share count. CommVault did not provide specific guidance, but did again note that it remains comfortable with double-digit top/bottom-line growth in F2011 and F2012; it also stated that it viewed Street estimates as being prudent. CommVault also noted an expectation of operating margin increasing 50-75bps in F2012, but did provide a somewhat conservative tone citing the timing of certain large deals, some lingering international uncertainty in F4Q11, as well as uncertainty regarding the timing of the impact of new distribution opportunities (citing Avnet as being below expectations in the U.S. in F3Q11).



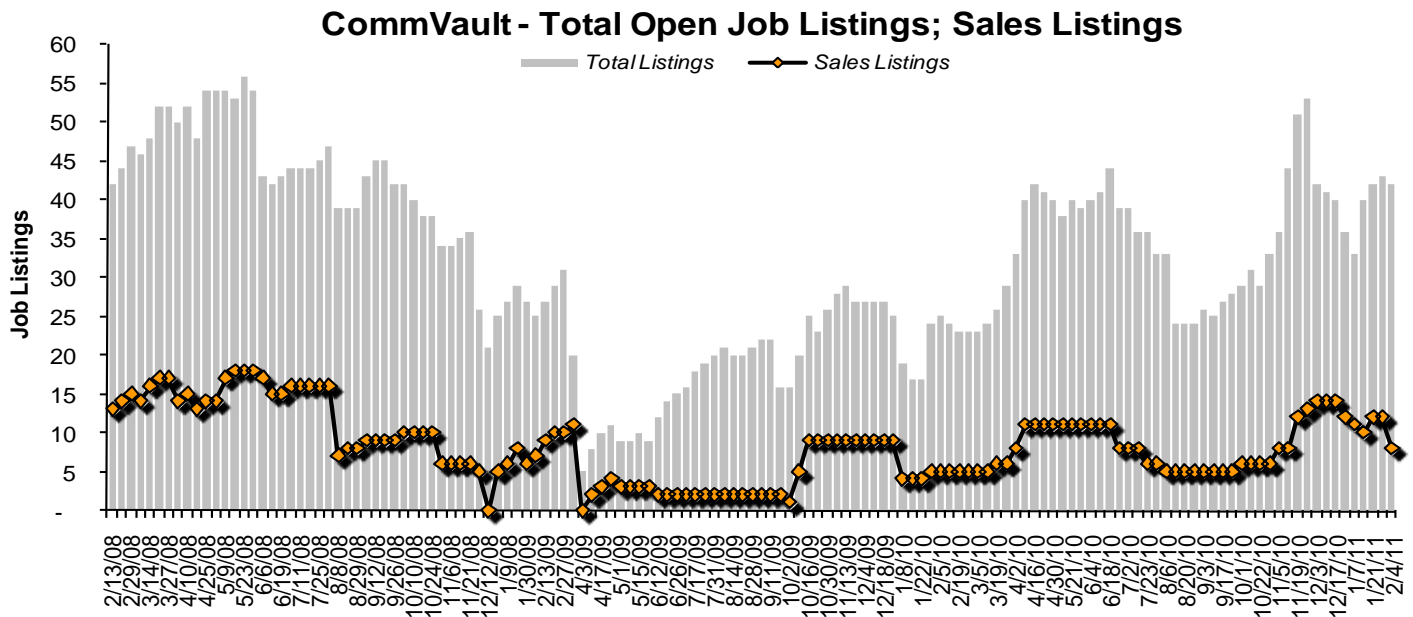
Source: Company Data



Please see our detailed report published on 2/1/11 for more information

### CommVault Job Listings Update

CommVault's total job listings decreased by 1 opening last week when compared to our checks in the prior week. Total listings were at 42 exiting last week, up 6 from the beginning of 2011 (total listings ranged from 29-53 over C4Q10). In this, the company has 8 sales openings, 5 openings in professional services, no openings in technical services, and 4 listings in technical support. This compares to 12, 5, 0, and 4 openings in the week prior, respectively. We would point out that management noted on its F3Q11 (December 2010) earnings call that the company would continue to add headcount going forward, most likely as it pertains to its enterprise sales force. The figure below highlights CommVault's job listing trends over the past several months.



### QLogic Corporation

(QLGC - Nasdaq - \$18.14 - Buy)

#### 2/3/11: F3Q11 10-Q Review - No Surprises; Focus On Inventory, China, Share Repo & More

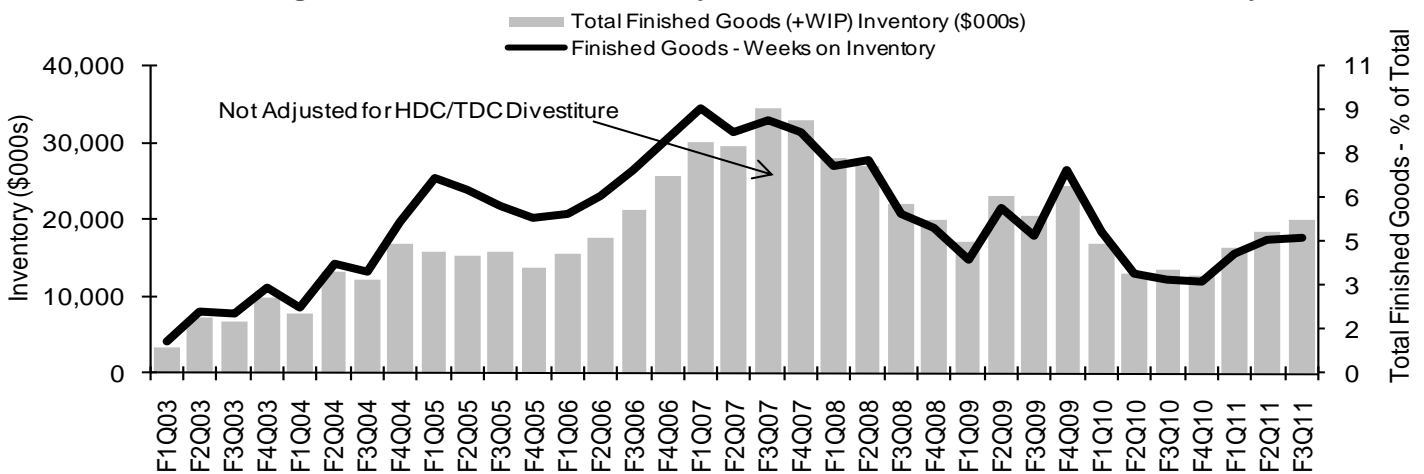
**(1.) Additional Product Details.** QLogic's filing discloses little incremental color with regard to the company's 2.8% yr/yr increase in Host Product segment revenue - only noting that the company saw this being driven by an increase in the quantity of adapters sold (same commentary given in last quarter's 10-Q filing). As a reminder, the company's filings are no longer providing specific color on unit growth within the company's Host Product segment (73% of total revenue in F3Q11), though we continue to believe that overall like-to-like pricing remains relatively benign (we estimate 1%-2% sequential decline range). As we mentioned in the QLogic F2Q11 10-Q review report (published 11/1/10), our conversations noted that the company did not provide explicit color given the immateriality of this data. However, the company's filing does note that the 5.5% yr/yr increase in the company's Network Product segment revenue (19% of total revenue) reflected a 17% yr/yr increase in FC switching units sold, partially offset by an 8% yr/yr decline in ASPs (vs. a 17% yr/yr increase in units sold and a 9% decrease in ASPs last quarter). Silicon Product revenue was noted to

have increased given an increase in the quantity of chips sold during the quarter. QLogic's top-10 customers again accounted for 84% of total revenue (disclosed for the cumulative nine months ending December). This would imply roughly a flat yr/yr contribution but 10% sequential growth for the December quarter to \$133.7 million (roughly 86% of F3Q11 revenue). This contribution compares to an 88% contribution for the same time frame a year ago (nearly 90% of F3Q10 revenue).

**(2.) China Disclosure.** In its geographical disclosures, QLogic again (started during the F1Q11 10-Q filing) disclosed its revenue contribution being derived from China. For the December quarter, the company generated \$23.9 million in revenue from China, which compares to \$22.2 million in the year-ago quarter and \$18.8 million in the September quarter. Therefore, China accounts for 15.3% of total December quarter revenue, up from a 12.8% contribution in the prior quarter and 14.9% in the year-ago quarter – a trend we believe could potentially become more interesting over time (especially as the company has mentioned Huawei as a potential FCoE switching partner going forward). No countries outside of the U.S. and China account for more than 10% of total revenue.

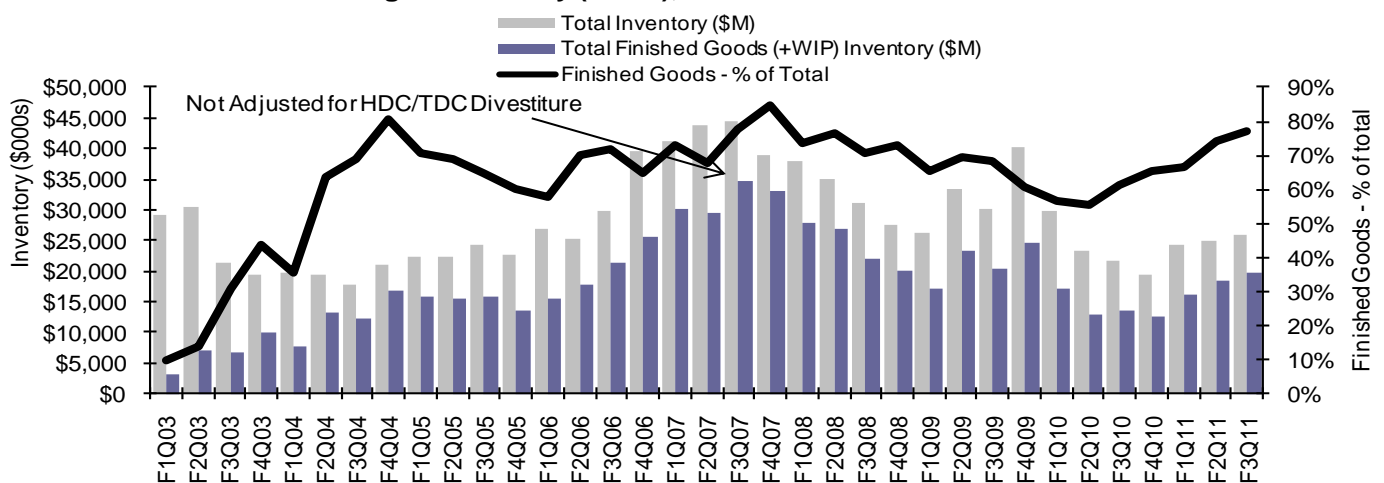
**(3.) Inventory – Finished Goods Inventory Continues to Increase.** In QLogic's reported \$25.857 million in inventory (up 4% seq.), the company reported finished goods inventory at \$19.893 million, which compares to the company's finished goods inventory balance standing at \$18.405 million exiting the September quarter. Therefore, the company's 8% sequential finished goods inventory increase builds off of a 13% sequential increase in the September quarter. For F3Q11, finished goods as a percentage of inventory came in at 76.9%, which was up from 61.5% in the year-ago quarter, and up from the prior quarter's level of 74.0% (see figure below). The second figure below also illustrates QLogic's finished goods inventory balance versus weeks of finished goods inventory. As we can see, the company exited the quarter with approximately 4.7 weeks of inventory, up from 4.5 weeks exiting the prior quarter and up from 3.2 weeks a year ago. Raw materials inventory at \$5.964 million exiting the December quarter compared to \$6.452 million exiting the September quarter. This 7.6% sequential decline follows a 21% sequential decrease seen in the September quarter.

**QLogic - Finished Goods Inventory vs. Weeks of Finished Goods Inventory**



Source: Company Data

**QLogic - Inventory (\$000s); Finished Goods as % of Total**

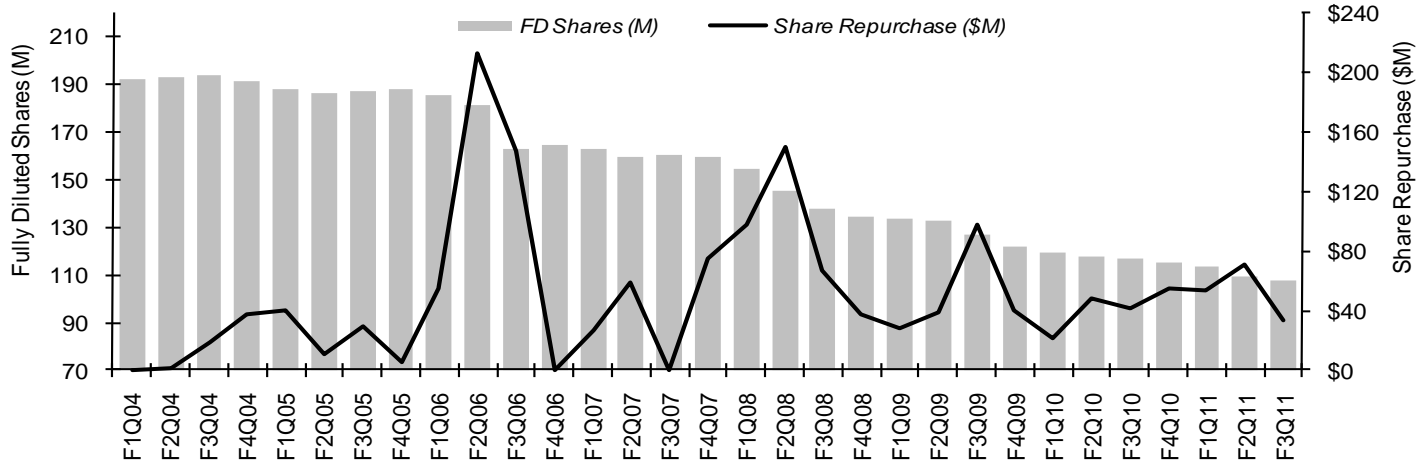


Source: Company Data

**(4.) Share Repurchase.** According to the company's filing, QLogic has spent \$154.9 million to repurchase approximately 9 million shares during the nine months ended December 2010. The filing notes a spend of roughly \$31.2 million to repurchase approximately 1.792 million shares during the December quarter (vs. \$70.9 million spent on ~4.4 million shares repurchased during the September quarter; cash flow statement indicates a spend of \$32.986 million in C4Q10). This filing notes an average repurchase price of

\$17.57/sh. vs. \$16.23/sh. spent during the prior quarter. Since F2003, QLogic has repurchased approximately 101.5 million common shares for an aggregate of approximately \$1.6 billion out of a total \$1.75 billion in available authorization. QLogic continues to predominately leverage its consistent FCF generation to repurchase shares, remaining one of the most active companies on the share repo front in overall tech on a relative basis. The company has reduced its fully diluted share count by nearly 44% since the inception of its share repurchase authorizations. The figure below highlights QLogic's quarterly share repurchase activity over the past several years. QLogic has an existing share repurchase authorization at \$147 million exiting the December quarter.

**QLogic - Quarterly Fully Diluted Shares; Share Repurchases (\$M)**



Source: Company Data

(5) **Other.** Additional quick notes include: (1) **Purchase Obligations.** QLogic's non-cancelable purchase obligations totaled \$63.8 million exiting the December quarter, roughly unchanged from \$63.6 million exiting the prior quarter. (2) **International Cash.** QLogic's 10-Q filing again discloses the company's international cash/investment balance. The company sees approximately 60% of its total cash and investments held internationally, down from 61% in the prior quarter. We would note that company reported a 49% and 47% contribution in the June and March quarters, respectively. (3) **FCoE – Similar to last quarter's filing,** while QLogic continues to ramp its FCoE solutions in the market, like with most emerging technologies the company anticipates the market for FCoE will take a number of years to mature. The filing also notes that QLogic expects products based on the FCoE protocol to supplement, and perhaps replace, certain products based on the Fibre Channel protocol (similar commentary given in prior 10-Q filings).

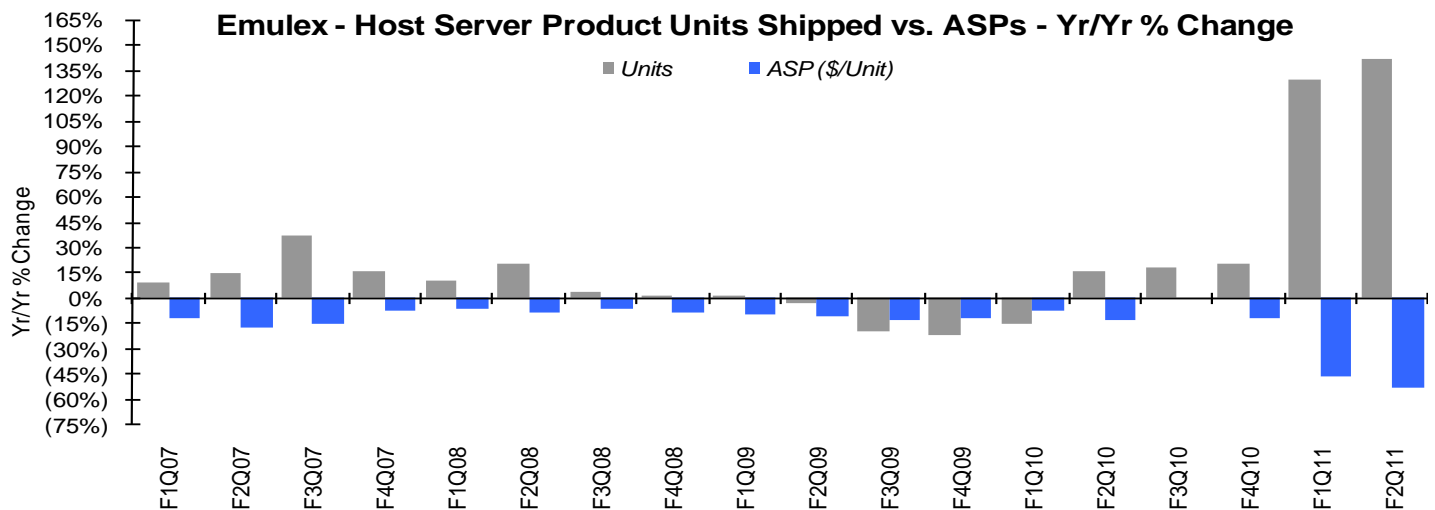
**Emulex Corporation**

(ELX – NYSE - \$11.74 – Hold)

**2/3/11: F2Q11 10-Q Review: Customer Contributions, Segment Details, Cash Flow and More**

**Segment Details**

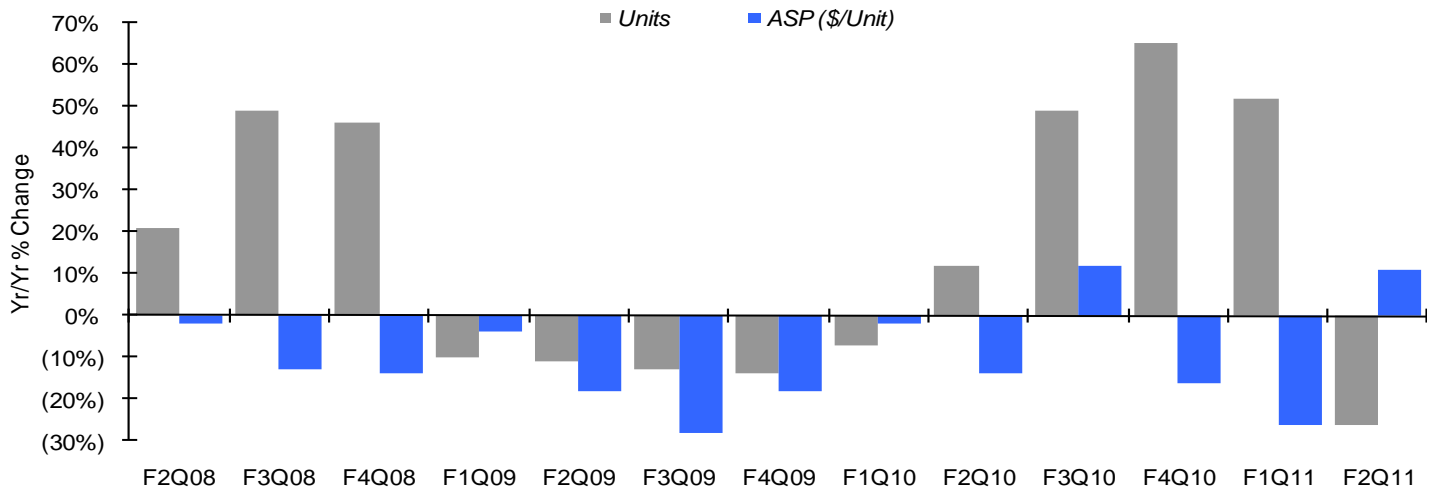
• **Incremental Host Server Product (HSP) Metrics** – Emulex's 10-Q notes that the company's HSP revenue increase of 12.5% yr/yr reflected a 142% yr/yr increase in units shipped, partially offset by a decrease of approximately 53% in average selling price (ASP). The filing notes that the significant increase in units shipped and decrease in ASP were due to the inclusion of ServerEngines, which accounted for no revenues in the year-ago quarter and had significantly lower ASPs compared to other Emulex products. This compares to unit shipments increasing 130% yr/yr in the prior quarter and ASPs falling 46% yr/yr.



Source: Company Data, Stifel Nicolaus Estimates

- Incremental Embedded Storage Products (ESP) Metrics** – Emulex's 10-Q notes that the ESP revenue decrease of 17.2% yr/yr reflected a 26% yr/yr decrease in units shipped (versus a 52% yr/yr increase in the prior quarter) and an ASP increase of 11% yr/yr (vs. -26% yr/yr in the prior quarter). The decrease in units shipped was primarily due to lower demand for ESP products while the increase in ASP was primarily due to the migration from 4Gbps to 8Gbps I/O controller products.

**Emulex - Embedded Storage Product Units vs. ASPs - Yr/Yr % Change**



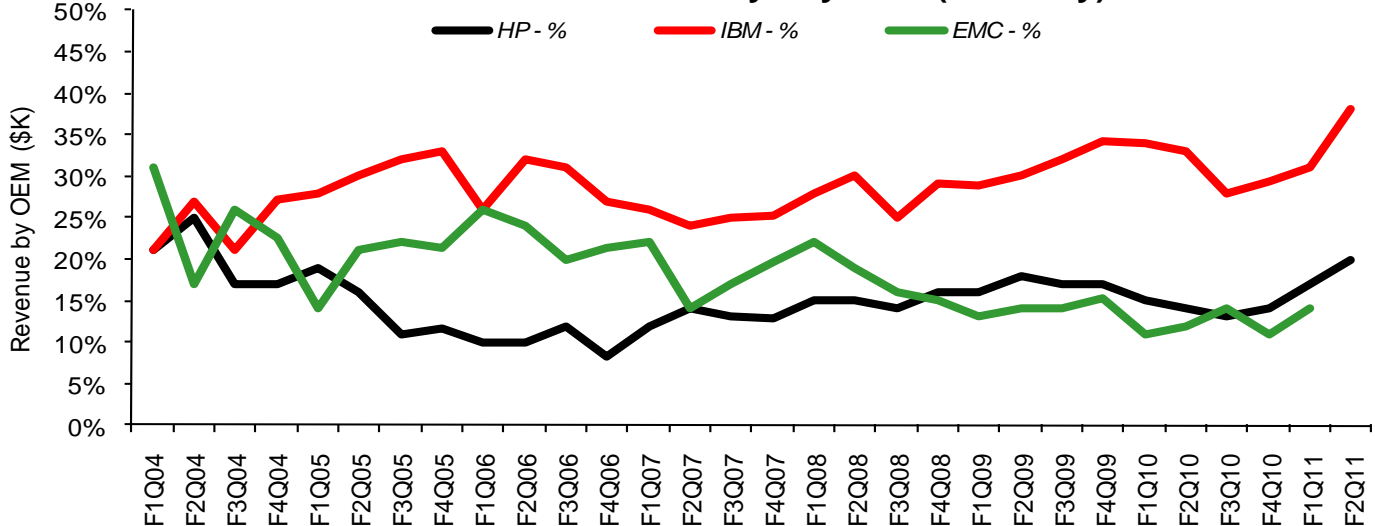
Source: Company Data, Stifel Nicolaus Estimates

**Key Customer Breakdown (HP, EMC, and IBM)**

Emulex's 10-Q highlights the following with regard to its key customer breakdown (using OEM + Distribution channel):

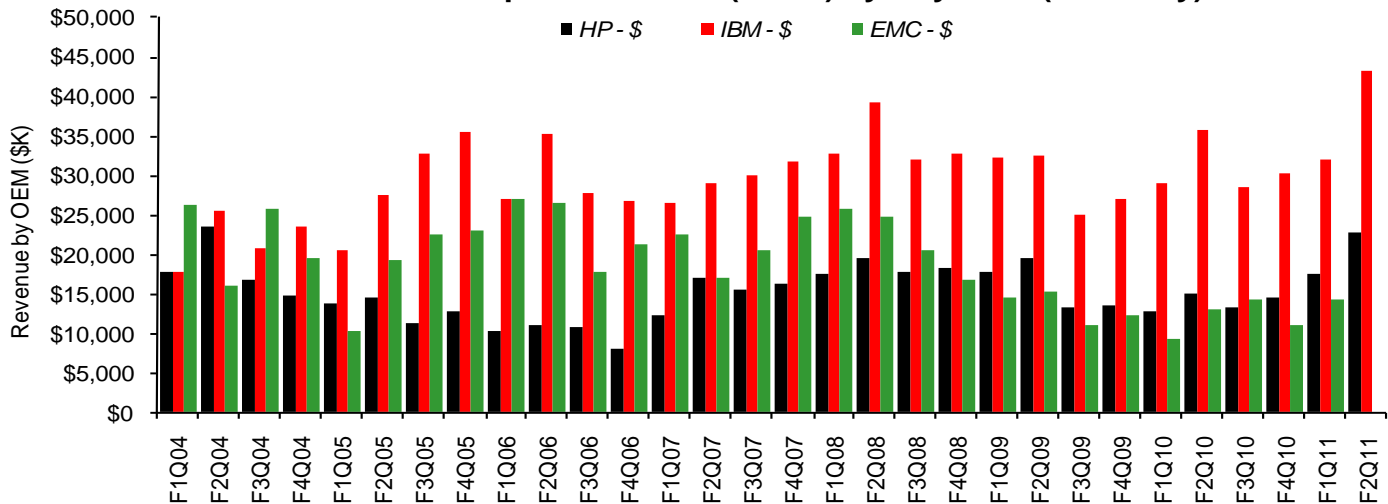
- EMC** – Was a sub-10% customer for the first time. This compares to a 14% contribution in the prior quarter and 12% in the year-ago quarter.
- Hewlett-Packard** – HP accounted for 20% of Emulex's total revenue, up from 17% in the prior quarter and 14% a year ago. This implies HP revenue increased 50% yr/yr and 30% sequentially (versus up 37% yr/yr and up 20% sequentially in the prior quarter).
- IBM** – IBM remains Emulex's largest customer at 38% of total revenue in the December 2010 quarter, up from 31% in the prior quarter and up from a 33% contribution in the year-ago quarter. This implies a 21% yr/yr increase and a 36% sequential increase (versus +10% yr/yr and up 6% sequentially in the prior quarter).
- Emulex's 10-Q notes that revenue from its top-five largest direct customers accounted for 68% of total revenue, which compares to a 58% contribution in the prior and year-ago quarters. This implies a revenue increase of 23.4% yr/yr and an increase of 29.6% sequentially. The filing notes that the increase in concentration was primarily due to significant increases in revenue from IBM and HP. Direct and indirect sales to the company's top-5 customers accounted for 80% of total revenues during the December quarter, up from 72% a year ago. The figures below highlight Emulex's implied quarterly revenue by key customer over the past few years.

**Emulex - Revenue % by Key OEM (Quarterly)**



Source: Company Data

**Emulex - Implied Revenue (\$000s) by Key OEM (Quarterly)**



Source: Company Data

**ServerEngines Commentary**

The 10-Q filing highlights the company's acquisition of ServerEngines that was completed on August 25, 2010. While the commentary is pretty much the same as in the previous filing, the numbers around the acquisition have changed slightly. The December 10-Q filing notes that the aggregate preliminary purchase price was \$135.7 million, down from the prior filing's price of \$136.5 million. In the \$135.7 million, \$54.793 million was paid in cash, \$67.367 million in stock, \$11.500 million in contingent consideration, and \$1.995 million in options assumed. This compares to the prior filing noting \$54.791 million in cash, \$67.367 million in stock, \$11.966 million in contingent consideration, and options assumed of \$2.355 million. Included in the common stock issued and contingent consideration is 2.2 million shares of Emulex stock to be held in escrow for 18 months from the acquisition date subject to certain standard representations and warranties defined in the merger agreement.

The contingent consideration relates to 4 million shares that are issuable upon achievement of two post-closing milestones. Approximately 2.5 million shares are tied to the employment of certain recipients, and therefore Emulex accounts for them as stock-based compensation. Emulex recognized approximately \$10.6 million during C3Q10, \$3.2 million during C4Q10, and expects to recognize approximately another \$8.3 million of stock-based compensation expense through F2012. The first post-closing milestone was met during C4Q10.

**Cash Flow**

Emulex's 10-Q provides details on the company's cash flow generation that were not presented when the company announced its quarterly earnings. The company generated CFO of \$6.531 million during the December 2010 quarter, versus \$10.481 million and \$8.949 million generated in the prior and year-ago quarters, respectively. FCF (CFO less Capex) totaled \$1.995 million, lower than the \$6.018 million generated in the prior quarter and versus \$6.075 million a year ago. FCF/share stood at \$0.02 versus \$0.107 and \$0.08 in the prior and year-ago quarters, respectively. This also compares to the company reporting non-GAAP EPS of \$0.13 during the December quarter (adjusted for tax benefit).

**Inventory (Raw Materials vs. Finished Goods)**

Emulex reported that its inventory was up 10.3% sequentially in the December 2010 quarter when compared to the September 2010 quarter (\$15.851 million vs. \$14.372 million). In this, finished goods inventory decreased 3.9% sequentially to \$10.184 million, while raw materials inventory increased roughly 50% sequentially to \$5.667 million. We would also point out here that the company has entered into various agreements for professional services, joint-development, non-recurring engineering, and purchases of inventory with the company's purchase obligations exiting the September quarter at approximately \$71.1 million, up from \$63.5 million in the prior quarter.

**Headcount Detail (Yr/Yr R&D and S&M Headcount Increases)**

Emulex reported that its overall headcount stood at 961 employees exiting the December 2010 quarter. This is compared to 765 employees exiting the year-ago quarter and 964 employees exiting the prior quarter. In this, the company reported: (1) Engineering & Development – headcount increased yr/yr from 450 persons a year ago to 616 exiting the December quarter (down 3 sequentially). This increase reflects the acquisition of ServerEngines. This has increased expenses by approximately \$6.5 million yr/yr, partially offset by a decrease in performance based compensation of approximately \$500K. (2) Selling & Marketing – Emulex reported that it had a total of 135 employees in its Selling & Marketing organization exiting the December 2010 quarter. This is slightly up from the 133 total employees exiting the prior quarter, and up from 121 a year ago (expenses increasing \$600K yr/yr). (3) General & Administrative – headcount totaled 140 total employees exiting the December 2010 quarter, flat with the prior quarter and up 12 from a year ago. The yr/yr increase resulted in an increase of approximately \$400K in salary and related expenses compared to the year-ago quarter.

**Share Repurchases**

The filing notes that since the company reinitiated its share repurchase plan in July 2009, the company has repurchased approximately 6.1 million shares for an aggregate purchase price of \$58.3 million, or an average price per share of \$9.55. The filing goes on to note that of these 6.1 million repurchased shares, approximately 4.1 million were repurchased during the six months ended December 26, 2010. Given that no share repurchases occurred during C4Q10, this means that all these shares were repurchased during the September 2010 quarter for approximately \$40.1 million, or an average of \$9.76/share. Emulex has \$41.7 million remaining under the repurchase program, which equates to roughly 3.58 million shares, or approximately 4.1% of diluted shares outstanding.

**2/1/11: Emulex Unveils Next Generation OneConnect UCNAs**

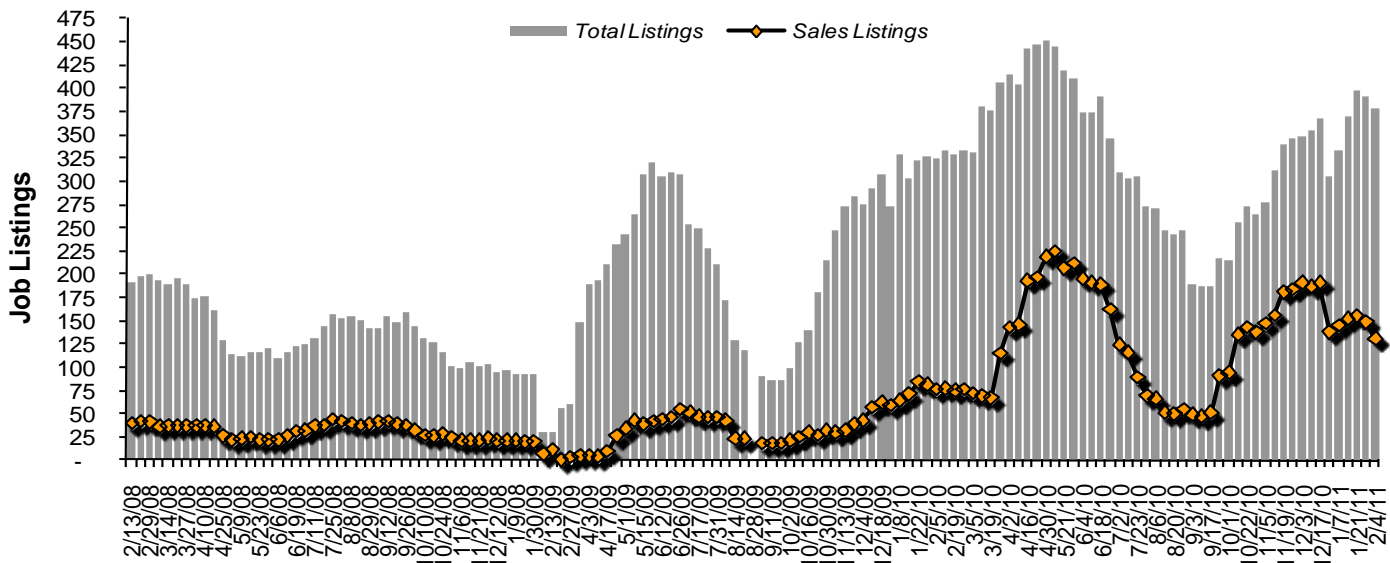
Emulex has announced the availability of its newest OneConnect OCe11000 family of UCNAs. These are based on the BladeEngine 3 (BE3) 10GbE I/O Controller (IOC). BE3 is a single-chip, dual-port 10GbE IOC that allows network and storage resources to be virtualized into multiple hardware-isolated and protected virtual network and virtual storage interfaces. The press release notes that Emulex was the first to ship its third generation UCNA product and has over 250K ports shipped in the past six months. The new OCe11000 features improved VM performance with SR-IOV support (SR-IOV allows PCIe devices to appear as multiple physical devices), lower opex with power savings, more VMs per CPU with Emulex vEngine, next generation virtual networking, and optimized networking performance.

**Brocade Communications Systems** (BRCD – Nasdaq - \$6.08 – Hold)

**Brocade Job Listings Update**

As of last week, Brocade’s overall job listings totaled 378, which were down from 391 last week and are up 73 openings from levels at the beginning of the year. In this, there were 130 total sales listings, which had decreased by 18 openings over the past week. We would note that after seeing a dramatic drop in jobs at the end of the year, Brocade is now seeing job listings track at similar growth levels that were seen during the majority of C4Q10. While it is hard to guesstimate what the underlying driver of the fluctuations in sales openings is, we believe some could question whether this reflects the company’s need for additional incremental investments in sales coverage or if this is reflective of current turnover in the company’s sales force (management noted at its Analyst Day on 9/16 that it has the right sales teams in place). Services openings were down 1 compared to last week at 29, while support listings increased by 2 openings to come in at 12 total openings. Engineering listings came in at 122 openings, up 5 over the same time frame. The figure below highlights Brocade’s job listings over the past several months.

**Brocade - Total Open Job Listings; Sales Listings**



Source: Company Data

**Xyratex** (XRTX – NYSE - \$13.50 – Buy)

**\*\*No Specific Company News; See Above Related HDD Thoughts (Intevac Results Highlighting HDD Capacity Investments)**

**Western Digital** (WDC – NYSE - \$36.21 – Buy)

**\*\*No Specific Company News; See Above Related HDD and PC Thoughts**

**Seagate Technology** (STX – NYSE - \$14.33 – Hold)

**Seagate Names Michael Cannon to Board of Directors**

Seagate announced last week that it has named industry veteran, Michael Cannon, to its board of directors. Mr. Cannon was formerly the president of Dell’s Global Operations – retiring in January 2009. Prior to Dell, Mr. Cannon was the CEO of Solectron and had previously served as the CEO of Maxtor, which Seagate had acquired in May 2006.

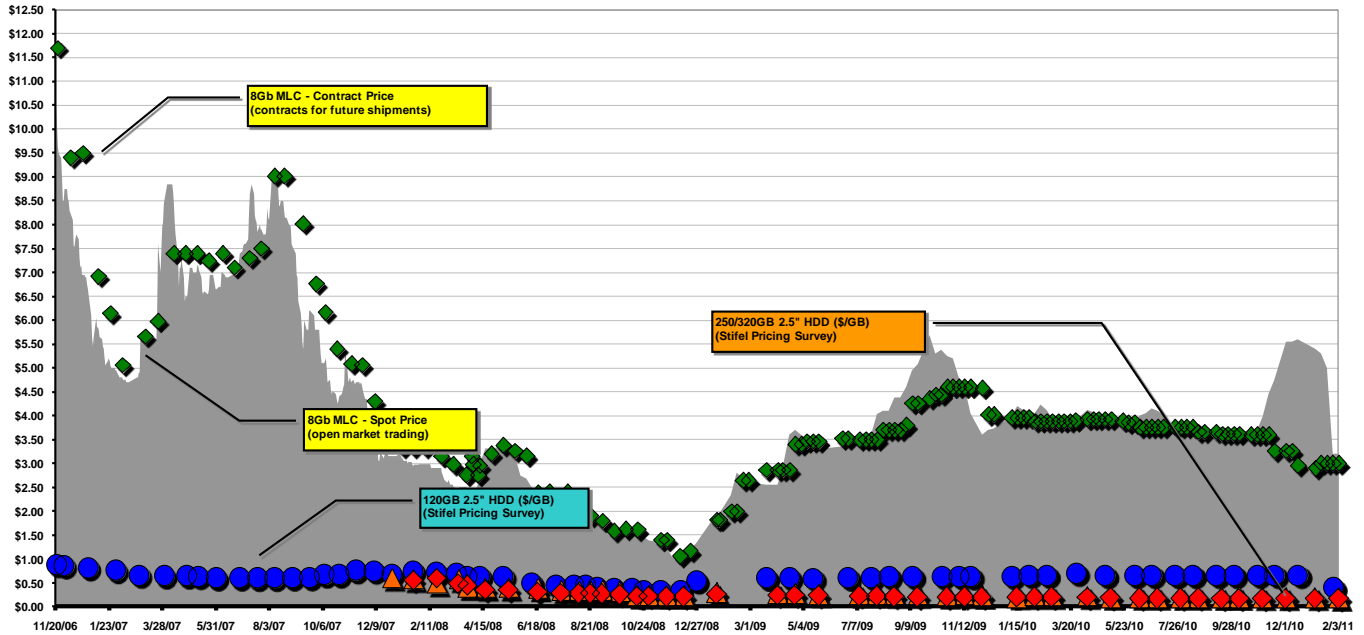
STEC Inc.

(STEC – Nasdaq - \$23.13 – Hold)

**NAND Flash vs. 2.5” HDD Pricing Update**

As shown in the figure below, 8GB MLC-based NAND Flash spot pricing carries a roughly 19.0x price premium when compared to current 320GB 2.5” mobile HDD prices, as measured by \$/GB. This is up slightly from the 18.3x premium we saw last week. We would note that this compares to the 21.5x premium we saw in late May/early June 2010. We continue to note that this does only reflect the cost of the NAND Flash component, which we estimate to account for as much as 80% of SSD build-of-material costs. We continue to assume limited penetration (less than 10%) by SSDs into the notebook market through 2010; however, we believe pricing trends remain very important.

**NAND Flash (8Gb/1GB MLC) Spot Price vs. Monthly 2.5” HDD \$/GB Pricing (120, 250, & 320GB 2.5” HDDs)**

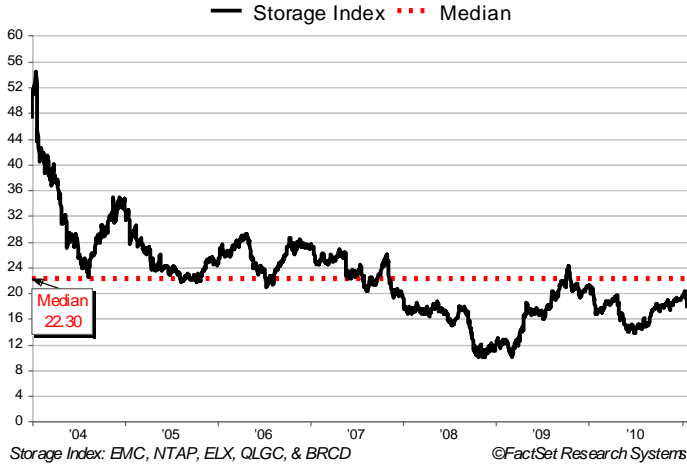


Source: DRAMeXchange, Stifel Nicolaus Estimates

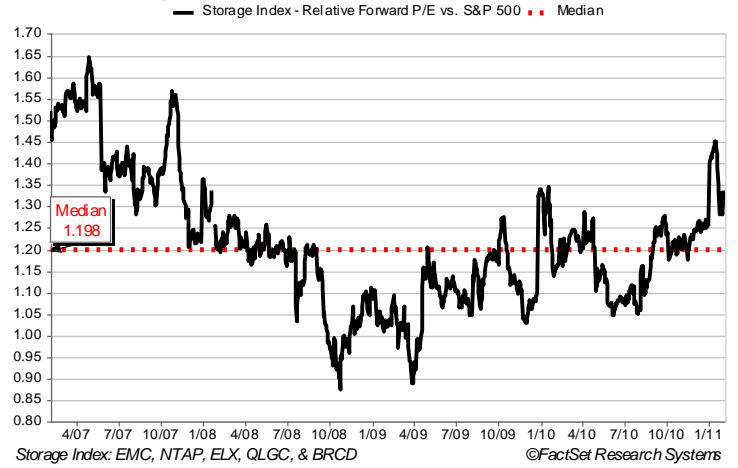
Pricing as of 2/4/11.

# Enterprise Storage Industry Indices

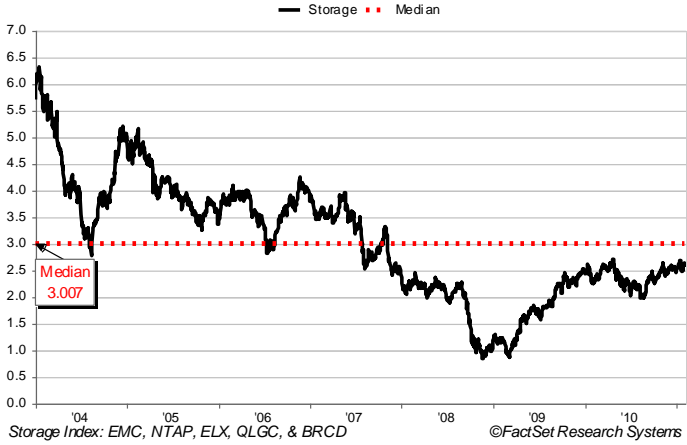
**Storage Index - Forward P/E - 2004 - Present**



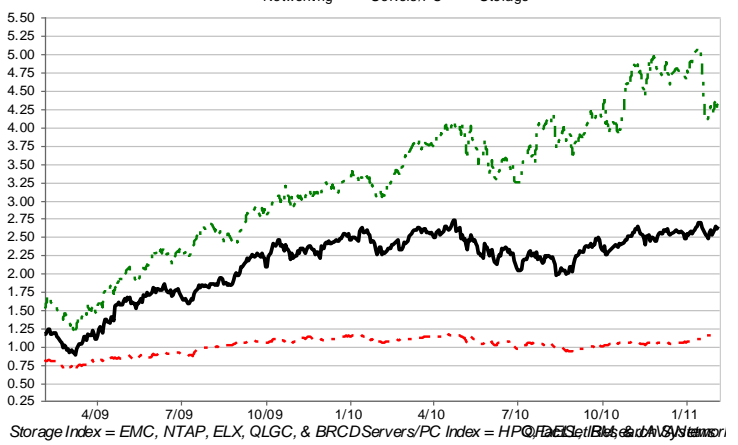
**Storage Index - Relative Forward P/E vs. S&P500**



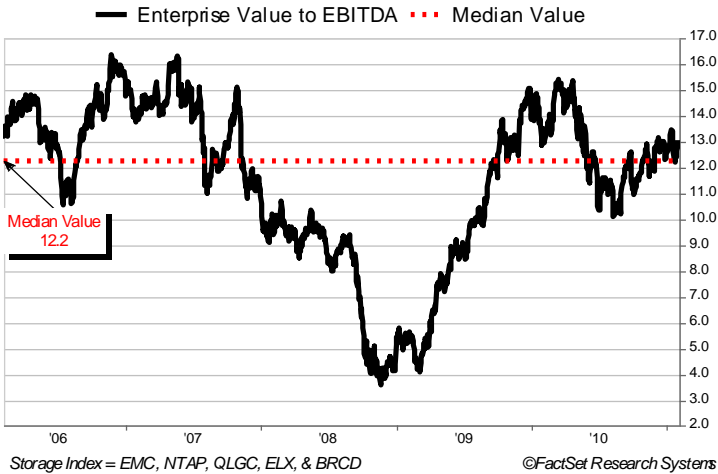
**Storage Index: EV-to-Sales - 2004 - Present**



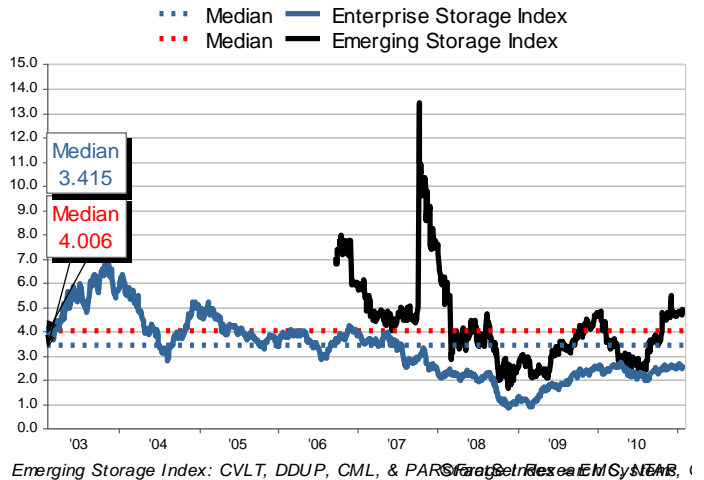
**Storage, Servers/PC, & Networking Index - EV-to-Sales - 2-Years**



**Storage Index - EV-to-EBITDA (Trailing)**



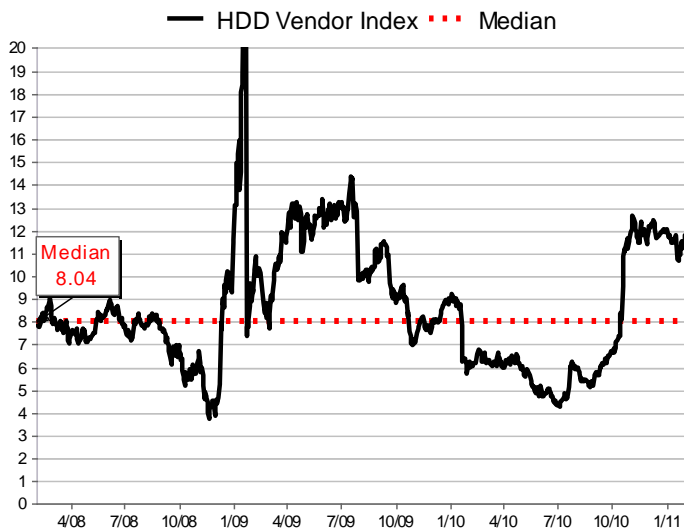
**Emerging Storage Index: EV-to-Sales - 2006 - Present**



Source for All Charts: FactSet and Stifel Nicolaus  
 Past performance should not and cannot be used as an indicator of future performance

# Hard Disk Drive Industry Indices

**HDD Vendor Index - Forward P/E - 2004 - Present**



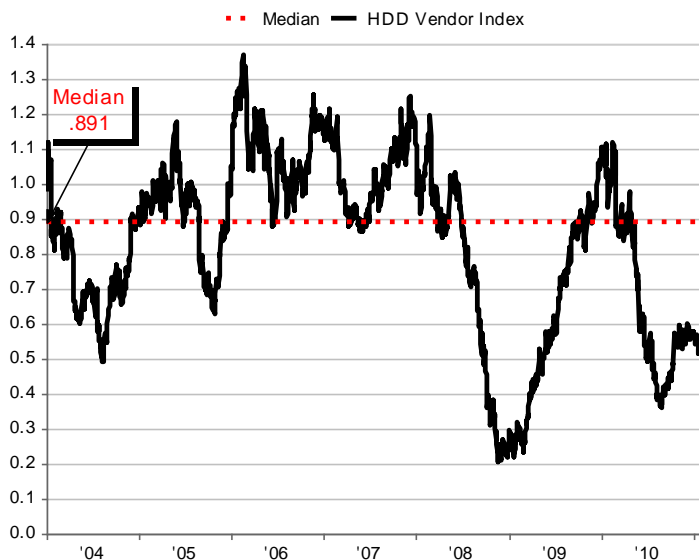
Storage Index: STX, WDC, & MXO (legacy) ©FactSet Research Systems

**HDD Vendor Index - Relative Forward P/E vs. S&P500**



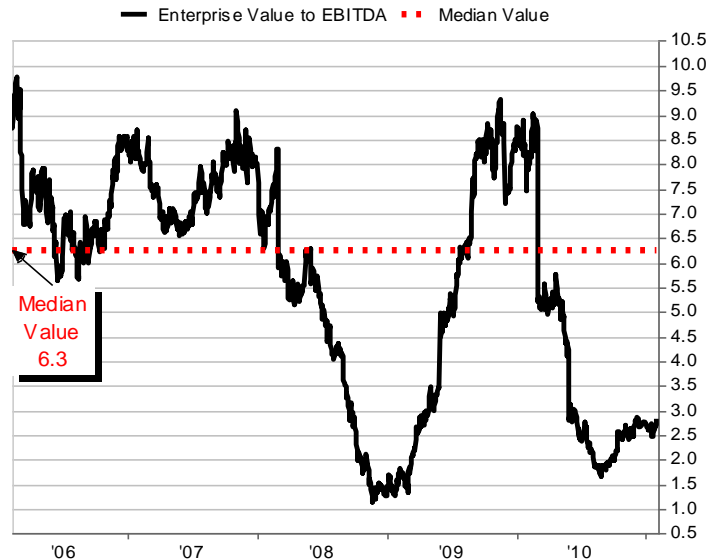
Storage Index: STX, WDC, & MXO (legacy) ©FactSet Research Systems

**HDD Vendor Index: EV-to-Sales - 2004 - Present**



Storage Index: STX, WDC, & MXO (legacy) ©FactSet Research Systems

**HDD Vendor Index - EV-to-EBITDA (Trailing)**



HDD Vendor Index = STX, WDC, & MXO (legacy) ©FactSet Research Systems

Source for All Charts: FactSet and Stifel Nicolaus

Past performance should not and cannot be used as an indicator of future performance

Note: All statements in this report attributable to Gartner represent Stifel Nicolaus interpretation of data, research opinion or viewpoints published as part of a syndicated subscription service by Gartner, Inc., and have not been reviewed by Gartner. Each Gartner publication speaks as of its original publication date (and not as of the date of this report). The opinions expressed in Gartner publications are not representations of fact, and are subject to change without notice.

### Important Disclosures and Certifications

**I, Aaron C. Rakers, CFA, certify that the views expressed in this research report accurately reflect my personal views about the subject securities or issuers; and I, Aaron C. Rakers, CFA, certify that no part of my compensation was, is, or will be directly or indirectly related to the specific recommendation or views contained in this research report.**

**For our European Conflicts Management Policy go to the research page at [www.stifel.com](http://www.stifel.com).**

For applicable current disclosures for all covered companies please visit the Research Page at [www.stifel.com](http://www.stifel.com) or write to the Stifel Nicolaus Research Department at the following address.

Stifel Nicolaus Research Department  
Stifel, Nicolaus & Company, Inc.  
One South Street  
16th Floor  
Baltimore, Md. 21202

Stifel, Nicolaus & Company, Inc.'s research analysts receive compensation that is based upon (among other factors) Stifel Nicolaus' overall investment banking revenues.

Our investment rating system is three tiered, defined as follows:

**BUY** -For U.S. securities we expect the stock to outperform the S&P 500 by more than 10% over the next 12 months. For Canadian securities we expect the stock to outperform the S&P/TSX Composite Index by more than 10% over the next 12 months. For other non-U.S. securities we expect the stock to outperform the MSCI World Index by more than 10% over the next 12 months. For yield-sensitive securities, we expect a total return in excess of 12% over the next 12 months for U.S. securities as compared to the S&P 500 and Canadian securities as compared to the S&P/TSX Composite Index.

**HOLD** -For U.S. securities we expect the stock to perform within 10% (plus or minus) of the S&P 500 over the next 12 months. For Canadian securities we expect the stock to perform within 10% (plus or minus) of the S&P/TSX Composite Index. For other non-U.S. securities we expect the stock to perform within 10% (plus or minus) of the MSCI World Index. A Hold rating is also used for yield-sensitive securities where we are comfortable with the safety of the dividend, but believe that upside in the share price is limited.

**SELL** -For U.S. securities we expect the stock to underperform the S&P 500 by more than 10% over the next 12 months and believe the stock could decline in value. For Canadian securities we expect the stock to underperform the S&P/TSX Composite Index by more than 10% over the next 12 months and believe the stock could decline in value. For other non-U.S. securities we expect the stock to underperform the MSCI World Index by more than 10% over the next 12 months and believe the stock could decline in value.

Of the securities we rate, 48% are rated Buy, 50% are rated Hold, and 2% are rated Sell.

Within the last 12 months, Stifel, Nicolaus & Company, Inc. or an affiliate has provided investment banking services for 31%, 21% and 17% of the companies whose shares are rated Buy, Hold and Sell, respectively.

### Additional Disclosures

Please visit the Research Page at [www.stifel.com](http://www.stifel.com) for the current research disclosures applicable to the companies mentioned in this publication that are within Stifel Nicolaus' coverage universe. For a discussion of risks to target price please see our stand-alone company reports and notes for all Buy-rated stocks.

The information contained herein has been prepared from sources believed to be reliable but is not guaranteed by us and is not a complete summary or statement of all available data, nor is it considered an offer to buy or sell any securities referred to herein. Opinions expressed are subject to change without notice and do not take into account the particular investment objectives, financial situation or needs of individual investors. Employees of Stifel, Nicolaus & Company, Inc. or its affiliates may, at times, release written or oral commentary, technical analysis or trading strategies that differ from the opinions expressed within. Past performance should not and cannot be viewed as an indicator of future performance.

Stifel, Nicolaus & Company, Inc. is a multi-disciplined financial services firm that regularly seeks investment banking assignments and compensation from issuers for services including, but not limited to, acting as an underwriter in an offering or financial advisor in

a merger or acquisition, or serving as a placement agent in private transactions. Moreover, Stifel Nicolaus and its affiliates and their respective shareholders, directors, officers and/or employees, may from time to time have long or short positions in such securities or in options or other derivative instruments based thereon.

These materials have been approved by Stifel Nicolaus Limited and/or Thomas Weisel Partners International Ltd., authorized and regulated by the Financial Services Authority (UK), in connection with its distribution to professional clients and eligible counterparties in the European Economic Area. (Stifel Nicolaus Limited home office: London +44 20 7557 6030.) No investments or services mentioned are available in the European Economic Area to retail clients or to anyone in Canada other than a Designated Institution. This investment research report is classified as objective for the purposes of the FSA rules. Please contact a Stifel Nicolaus entity in your jurisdiction if you require additional information.

The use of information or data in this research report provided by or derived from Standard & Poor's Financial Services, LLC is © 2011, Standard & Poor's Financial Services, LLC ("S&P"). Reproduction of Compustat data and/or information in any form is prohibited except with the prior written permission of S&P. Because of the possibility of human or mechanical error by S&P's sources, S&P or others, S&P does not guarantee the accuracy, adequacy, completeness or availability of any information and is not responsible for any errors or omissions or for the results obtained from the use of such information. S&P GIVES NO EXPRESS OR IMPLIED WARRANTIES, INCLUDING, BUT NOT LIMITED TO, ANY WARRANTIES OF MERCHANTABILITY OR FITNESS FOR A PARTICULAR PURPOSE OR USE. In no event shall S&P be liable for any indirect, special or consequential damages in connection with subscriber's or others' use of Compustat data and/or information. For recipient's internal use only.

**Additional information is available upon request**

© 2011 Stifel, Nicolaus & Company, Incorporated One South Street Baltimore, MD 21202. All rights reserved.