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PRESENTATION

Operator

Good day or good afternoon, ladies and gentlemen and welcome to the Rackspace Hosting Second Quarter 2011 Earnings Release Conference Call. As a reminder, today's call is being recorded. At this time, all lines are in a listen-only mode to prevent background noise. After the prepared remarks, there will be a question-and-answer session. (Operator Instructions)

It is now my pleasure to introduce, Mr. Jason Luce, Vice President of Finance for Rackspace. Mr. Luce, you may begin.

Jason Luce - *Rackspace Hosting, Inc. - VP, Finance*

Good afternoon, thank you for joining Rackspace's second quarter 2011 earnings call. I'm here today with Lanham Napier, our CEO; and Karl Pichler, our CFO. We issued a press release after the close of the market today with our unaudited financial results for the second quarter of 2011. If you do not have a copy, please visit the Investors Section of our website at rackspace.com, where this call is also being webcast.

The primary purpose of today's call is to discuss the second quarter 2011 results. However, some of our comments today are forward-looking statements that involve risks, uncertainties, and assumptions. If the risks or uncertainties materialize or assumptions prove incorrect, our results could differ materially from those expressed or implied by the forward-looking statements and assumptions.

All statements other than historical facts are statements that could be deemed forward-looking statements. These risks, uncertainties, and assumptions are described in Rackspace Hosting's Form 10-K for the year ended December 31, 2010 and filed with the SEC on February 22, 2011 and in Rackspace Hosting's Form 10-Q for the quarter ended June 30, 2011, expected to be filed shortly.

These forward-looking statements speak as of today. Except as required by law, we assume no obligation to update these forward-looking statements publicly even if new information becomes available in the future.

During today's discussion, we will be using GAAP as well as non-GAAP financial measures such as adjusted EBITDA. Our GAAP results and GAAP to non-GAAP reconciliations can be found in the earnings release we issued earlier today, which is posted on our website as mentioned previously.

Following our prepared remarks today, we'll the open call for your questions.

Okay, Lanham?

Lanham Napier - *Rackspace Hosting, Inc. - CEO, President, and Director*

Good afternoon, and thank you for joining Rackspace's second quarter earnings call. This quarter, we are hosting our call from our international headquarters in London. It's been an insightful week here in the UK. We've met with a variety of existing prospective customers and it's clear that there's an insatiable force for cloud computing for businesses around the world. We think these businesses are looking to Rackspace to be the service leader in the cloud and to do so on a global basis.

At the beginning of the year, we communicated that our goals for 2011 are to accelerate revenue growth, while also investing to strengthen our business and improve our long-term economic model. At the halfway point in the year, we believe we have made excellent progress toward these objectives. Thanks to all the customers who trust us to run their mission-critical business applications and the tireless commitment of our rackers. We're happy to announce that we recently achieved $1 billion of annualized run rate revenue this past June. The opportunity ahead of us is massive and the atmosphere at Rackspace has never felt better.

Here are some of the highlights from the second quarter. Number one, revenue growth accelerated to 32% on a year-over-year basis and 7.5% on a sequential basis. We've been able to drive higher growth in 2011 through continued rapid growth in our public cloud business, which grew by 85% in Q2 on a year-over-year basis and improved traction in serving large enterprises, customers leveraging our enhanced portfolio products and services, and by a meaningful pick-up in sales to existing customers, which we measure as installed base growth.

Monthly installed base growth remained at 0.9% per month for the quarter. Although, we are not at pre-recession installed base growth, [we had] approximately 1.5% per month on average, 0.9% for the first six months of 2011, is higher than the 0.2% that we achieved in 2009 and the 0.5% that we averaged in 2010.

As you know, growing sales to our existing customers is a key pillar of our growth strategy and a tangible proved point that we used to measure the value we bring to our differentiated service model.

Three, in addition to accelerating growth, we are pleased with our investments and profits in the second quarter. In February, we outlined our plans to not only increase share in the massive cloud computing market, but also improve our long-term business model to deliver better profits and returns.

With the improvements made in the second quarter, we are on track to accomplish our goals for 2011.

In Q2, adjusted EBITDA was 31% year-over-year and our margin profile remained stable. Net income grew 57% with higher margins of 7.1%. Maintaining margins while improving capital efficiency leads to higher returns and as a result, return on capital improved to 14.4% in the second quarter.

Although it has taken us nearly 12 years to achieve our first billion dollars of run rate revenue, we believe that it will take a fraction of that time to attain the second. Before we hand the call over to Karl to go through the numbers in detail, we'd like to outline what we're doing to achieve this next milestone.

First, we believe that cloud computing era represents the biggest market opportunity in all technology; one that could represent a multi-billion dollar revenue stream for Rackspace and we've only just begun to tap into that opportunity.

While the overall size of the market opportunity for Rackspace is difficult to precisely calculate, we know that it is massive and growing rapidly. More and more corporations are discovering that using a specialized service provider is the better, faster, cheaper way to address their IT capacity needs; pay less and get more.

Second, we believe our strategy to be the dominant service leader in the cloud computing market will drive sustained growth. Rackspace's value proposition is focused on providing our customers with great technology results through the culture of customer service that we call Fanatical Support. Running mission-critical IT systems require us a complex combination of computing hardware, software management tools, as well as the technical staff that has expertise in a diverse range of technologies and is obsessed with customer service.

Fanatical Support combines these ingredients to deliver a world-class service experience to our customers. Fanatical Support leverages both the strengths of our systems and those of our employees to create the best technology service results in our industry. This service delivery strategy is the core of our differentiation and competitive advantage. We will continue to invest in this [goal] and improve the value delivered to customers. We believe the investments we make today will help us take full advantage of the huge market opportunity in cloud computing.

Our growth strategy involves operating expanding portfolio of products and services, all managed with Fanatical Support. Our portfolio approach allows us to service a larger share of our customers' IT needs and enhances our ability to grow with them over time.

One way to track the success of our portfolio strategy is through the growing number of customers that use a mix of our offerings. One example is Tetris Online, a developer and publisher of electronic properties. Its games can be played online on Nintendo Wii, Nintendo DS and Xbox Consoles, as well as on Apple devices in Facebook.

Rackspace hosts the company's main website as well as many of its social media games, including Tetris Battle and Feevo. We run these properties for Tetris Online using our recently introduced RackConnect product, which enables customers to build a scalable, flexible compute solution that offers the performance advantages of dedicated servers with the flexibility and scalability of our public cloud platform.

Just last month, we announced that Domino's, a leader in pizza delivery, also selected Rackspace's RackConnect offering. Using RackConnect will give Domino's a scalable, cost-effective platform to support the Company's ambitious international growth strategy. Domino's chose Rackspace because of our ability to be flexible and accommodate its evolving computing needs while allowing its internal IT team to focus less on the maintenance of its online properties and business applications and more on innovation.

Our portfolio strategy also helps us grow our footprint with large enterprises such as Newell Rubbermaid. Newell Rubbermaid, a member of the S&P 500, is a global marketer, consumer of commercial products with approximately $5.8 billion in sales in 2010.

Newell Rubbermaid boasts a strong portfolio of global brands, including Rubbermaid, Sharpie, and Graco. Rackspace provides the infrastructure that supports the online properties for many of these brands.

Newell Rubbermaid is also leveraging our private cloud, SharePoint hosting, and public cloud services. Our private cloud and SharePoint offerings had given us a great entry point into the enterprise market. Edelman, a global public relations firm has entrusted Rackspace to run a VMware-based private cloud for it, along with a SharePoint deployment.

One of our strategies with enterprise customers is to give them the door with a relatively small deployment, demonstrate the value of Fanatical Support, and earn the chance to run incremental workloads, thereby expanding our footprint within the organization. Once the companies to experience the value of Fanatical Support, they often want more. Or managed cloud offering continue to grow strongly in the quarter in what was only a second full quarter of availability.

Sales grew by more than 200% sequentially, and the average revenue per customer continues to be more than twice that for customer using our cloud server product without the managed service level. The managed cloud product combines the economic and flexibility benefits of our public cloud platform with the added value of our world-class Fanatical Support. Rackspace benefits because delivering the managed cloud service requires less capital for a given dollar of support revenue.

From an economic perspective, the result has improved capital efficiency and higher returns. The San Diego Zoo has chosen Rackspace's managed cloud service to host its main website, as well as a collection of global blogs. In addition, it has configured several servers to host web, development, and database workloads. This zoo is also taking advantage of Rackspace's new cloud load balancers product to help manage traffic.

More than 800 customers have adopted the cloud load balancer service since it became available in April. This product enables customers to cost effectively scale applications or deploy high-availability configurations with fault tolerance. Our cloud load balancers should help Rackspace address new areas of demand as well as improve capital efficiency.

In the last few months, we've made good progress driving adoption of the OpenStack cloud computing platform and gaining traction with our Cloud Builders business. More than 90 companies are now involved in the OpenStack Project, including Hewlett-Packard, which recently announced they were back in OpenStack. In May, Citrix announced Project Olympus, in which it will provide a certified version of OpenStack for enterprise customers that want to build private clouds using the same technology that will run Rackspace's public cloud.

Meanwhile, our Cloud Builders business, which helps companies deploy and manage OpenStack based cloud, is generating healthy interest. Cloud Builders is currently participating in several proof of concept projects with large enterprise sized organizations.

Recently, Dell announced its OpenStack cloud solution that combines service from Dell with services from Dell and Rackspace Cloud Builders. OpenStack and Cloud Builders are generating great traction in the market and we expect to have more to share with you about these exciting initiatives in the remainder of the year.

While we are very encouraged by our progress with accelerating revenue growth, we are also encouraged that we're able to do this while simultaneously investing for the future to improve our unit economics. Demand is not the constraint for growth, given the massive size of the market opportunity. Instead, we sometimes purposely restrain growth by only taking on new business that we believe improves our overall economic model. We are making strategic investments to maximize our long-term potential.

In the first half of this year, our investments have yielded new service offerings such as the UK cloud, managed cloud in the UK, and Cloud Load Balancers. Tomorrow, we will announce the launch of our Critical Sites service in the UK. Like its U.S. counterpart, Critical Sites is designed for applications that require the highest service levels of performance and availability and is backed by our most comprehensive service level agreement.

The Critical Sites service has been available to U.S. customers since October last year and we've welcomed customers including Mazda, BlackLine Systems and Hawaiian Airlines, who all rely on Critical Sites to keep their mission-critical sites up and running. Demand for Critical Sites service continues to grow, reflecting the importance of having great tools and engineers available to help deliver superior user experience to customers. We are excited to bring this service to the U.K.

Looking ahead, we are investing in a number of new projects such as the development of cloud block storage, firewall as a service, unified control panel, and of course, building out our Cloud Builders business. All of these projects are funded by our current operations within our investment framework, aimed at driving profitable growth and improved capital efficiency. In short, during the second quarter, we grew faster and generated higher returns while investing to help us become bigger and more profitable in the future.

Balancing growth, margins, and investments for the future is demanding for everyone at Rackspace and we are encouraged that the entire organization has responded to the challenge. Rackers have put in many hours of hard work and personal sacrifice in order to deliver on our commitments for the first half of 2011. And we want them to know that we recognize and greatly appreciate all of their efforts.

I'd also like to announce the addition of two new Board members: Sam Gilliland, Chairman and CEO of Sabre Holdings and Lew Moorman, our Chief Strategy Officer and President have joined our Board. Sam will serve on the Audit and Compensation Committee and Lew will join our Service and Strategy Committee.

Now, let me hand the call over to Karl, who will take us through the detailed financial results for the quarter. Karl?

Karl Pichler - *Rackspace Hosting, Inc. - Interim CFO*

Thank you, Lanham. For the second quarter, total revenue was $247 million, representing 7.5% growth from the first quarter and 32% growth compared to the second quarter of 2010. Shift in currency exchange rates quarter-over-quarter had a positive impact on revenue of approximately $1 million sequentially and a positive impact of $5 million on a year-over-year basis. On a constant-currency basis, revenue grew 7% quarter-over-quarter and 29% year-over-year.

Total installed base growth was 0.9% in the quarter, which is in line with the prior quarter and an improvement from 0.6% in the second quarter of 2010. Managed hosting revenue increased to $204 million, representing 5.9% sequential growth and 25% growth on a year-over-year basis. Growth in managed hosting continues to be driven by strong upgrade activity and new sales to enterprise customers. Public cloud revenue for the quarter was $43 million, representing 15.8% sequential growth and 85% growth on a year-over-year basis.

Consistent with prior periods, cloud growth was driven by a combination of new customer adoption, higher usage from existing customers, and growth of the new product offerings such as our managed service on the cloud and Cloud Load Balancer. In total, we added more than 10,000 new customers in the quarter, bringing our total installed base to more than 152,000 customers.

Moving on to profitability, adjusted EBITDA grew to $82 million in the quarter, representing 7.5% sequential growth and 31% growth on a year-over-year basis. Adjusted only for non-tax stock-based compensation, adjusted EBITDA margin was 33% in the second quarter, in line with the first quarter and the second quarter of 2010. Adjusted EBITDA and adjusted EBITDA margin were negatively impacted by a non-cash charge of $2.8 million for the quarter, relating to data center operating leases.

Depreciation and amortization expense came to $47 million in the quarter, as a percent of revenue depreciation and amortization represented approximately 19% of revenue in the quarter, which is consistent with the range it has been over the last two years of 19% to 21% of revenue.

Net income came to $17.6 million in Q2, representing growth of 27.1% over the first quarter and 57% from the second quarter of 2010. Second quarter net income was positively impacted by a lower effective tax rate and lower stock-based compensation expense. The effective tax rate for Q2 was 33.8%, which is down from 38.3% in the first quarter. Although our tax rate has fluctuated on a quarter-to-quarter basis, it has remained flat at approximately 35.1% for the prior two years and we expect it to be at a similar rate for the full year in 2011.

Net income also benefited from a decrease in stock-based compensation in the second quarter. Our stock-based compensation expense decreased to $6 million, in the second quarter from $7.8 million in Q1. We expect to issue additional stock-based compensation in August.

Capital expenditures totaled $95 million in the quarter. Of this amount, we spent $49 million on customer gear, $17 million on data center buildouts, $14 million on our office facility, and $15 million on capitalized software development and other projects.

Capital expenditures for both data center and office increased $19 million sequentially due to the building out of the final stage of our London data center, as well as our ongoing headquarters consolidation project. We expect to complete the London data center buildout, as well as the current phase of our headquarters consolidation project by the end of the year.

Looking ahead for the full year of 2011, we continue to expect total capital expenditures to be in the range of $275 million to $335 million. If we continue to grow at a rate consistent with the last few quarters, we expect the total capital expenditures will trend towards the high end of that range.

Adjusted free cash flow came in at a negative $18 million for the second quarter, primarily due to the higher capital expenditures for the data center and office projects that I just described. As Lanham indicated during his prepared remarks, return on capital improved in the quarter to 14.4%. This was driven by a combination of lower tax rate, lower stock-based comp expense, and continued improvement in capital efficiencies. Revenue per server and capital turns both increased for the eighth consecutive quarter.

Average revenue per server grew to $1,140 from $1,123 in the first quarter. And capital turns increased to 1.87 from 1.84 in Q1. We ended the quarter with a total cash balance of $132 million. Our total debt outstanding, including capital leases, was $139 million, which translates to a net debt position of approximately $7 million or net leverage of essentially zero.

In summary, during the second quarter, we made good progress toward our goal of accelerating revenue growth while strengthening the business. While we still have lots to accomplish throughout the year, we remain on the right track to achieve our goals for 2011.

With that, we'll take your questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions). Greg Dunham, Credit Suisse.

Greg Dunham - *Credit Suisse - Analyst*

Yes, thanks for taking my question. I guess, I want to hit on the installed base. That was pretty strong again for the second quarter in a row at 0.9%, up significantly from where it was in the recession, but still below that kind of 1.5% it has been historically, I guess, when you're a much smaller company, I would say. Where do you think that can go with some of the things you're doing out on the product front and how does the macro going to impact that number going forward? Thanks.

Lanham Napier - *Rackspace Hosting, Inc. - CEO, President, and Director*

Okay. This is Lanham. So I'll take a stab at that one. Installed base growth is our most profitable growth that we have inside the Company. It's a reflection of how our customers feel about us. In our industry, it's a kin to comp sales of a retailer. So this is literally a revenue measurement and metric that we provide that demonstrates the lift in traction we have with our customer base.

As we serve customers well and increase their loyalty, they buy more from us. So this is a number that's net of churn. When we think about installed base growth, during the good days pre-recession, it got up to 1.5% a month, which if you annualize is about 18% a year. And so that's a healthy number. And you're right. We are not back at that level.

I think if we looked to the depths of the recession, the installed base growth went to slightly positive. Last year, it got up to about 0.5% per year. This year, so far, the first half of the year is almost double that. So we're very pleased with that progress. We think that's been a good piece of work. What drives it right now, number one is our enterprise business. Our enterprise customers are the fastest growing customer cohort we have right now.

Second, our cloud. And that cloud is a cool technology. It's easy to consume. So, customers are consuming more and more of it. And then lastly, it's our SMB customer base. And as SMB economic activity picks up, you'll see installed base growth pick up as well.

So the second part of your question touched on how does the macro impact it? Where do we think it can go? We actually believe that in good economic times, we can get it back to where it was historically pre-recession. Right now, things are still a little bit choppy out there. So, we are pleased with our progress. And this metric is impacted by the macro, particularly that SMB portion of it. As we look at what we've done in this choppy environment, man, we're still up double year-over-year. The traction we've had with our enterprise customers has been really strong and the traction we had with cloud is really strong. If you see on the backs of those two groups, the installed base growth rate has doubled this year relative to last year.

Greg Dunham - *Credit Suisse - Analyst*

That's helpful. Thank you for taking the question.

Operator

James Breen, William Blair.

Louie DiPalma - *William Blair & Co. - Analyst*

Hi. This is actually Louie DiPalma on behalf of Jim Breen. Can you guys hear me okay, considering that you are in London.

Lanham Napier - *Rackspace Hosting, Inc. - CEO, President, and Director*

Yes.

Karl Pichler - *Rackspace Hosting, Inc. - Interim CFO*

Yes.

Louie DiPalma - *William Blair & Co. - Analyst*

Great. I was just wondering if you guys could provide any color on why you're doing the call in London besides the launch of Critical Sites and savory Domino's Pizza over there?

Lanham Napier - *Rackspace Hosting, Inc. - CEO, President, and Director*

Sure, yes, I'll take that. So as you may know, we have a -- significant portion of our business is coming from our international business, which is basically serving the EMEA market and the other parts of the world outside of the US. Our overall contribution from a revenue perspective is about 25%. And it grows very nicely. It grew extremely fast before the recession and even during the recession, while the UK economy was really suffering, we grew north of 20% annually, nicely through that time.

What's really important to understand is that this business here acts as a multiplier for all the work that we do in San Antonio on a centralized basis with respect to systems and product development. So, we centralized that work there. We developed those products. And then we have a sales marketing and most notably, a service extension over here to serve customers locally. And this has provided a very healthy contribution to the business and continues to be a pillar of our future success.

Louie DiPalma - *William Blair & Co. - Analyst*

Nice. And given your success in the London market and generally in Europe, have you investigated launching in any other international market?

Lanham Napier - *Rackspace Hosting, Inc. - CEO, President, and Director*

Yes, today, we have physical presence and operations in the UK, in the Netherlands, in Amsterdam and in China, in Hong Kong as well as Australia. So what's happening right now in the marketplace is there is a secular shift from people having to do IT themselves to purchasing as a service.

We believe that this is a global opportunity for our Company as we work to build a service leader in cloud computing. It is absolutely a situation where we feel pull from customers to go into new geographies. When we look at our roadmaps in the investment that we've made in our product roadmaps so far, it's exactly, as Karl just described in that, we centralized our activity, we [build a lot] in the US and then we roll it out on a global basis. So oftentimes, we will start the product launch in the US, get down the experience curve a bit, have our learnings and then roll it into new marketplaces.

From a cloud perspective, the US is the most mature market in the world. It's going through early adoption and rapid growth. But even though it has, I believe, a decade of growth ahead of it, it is still the most advanced market in the world. So we tend to cut our teeth in the US with new products and then take it internationally after we've gotten that experience and success. We've done that so far. If you look at what we've accomplished here over the past year in our roadmap, starting with Windows cloud then launching cloud in the UK, then doing managed cloud in the US, doing Critical Sites in the US, then we launched managed cloud in the UK, and now tomorrow, we're launching Critical Sites in the UK. So there's the pattern upon which we are executing, and we want to continue to do this on a global basis.

Louie DiPalma - *William Blair & Co. - Analyst*

Great. It's very helpful. Thanks, Lanham, Jason, and Karl.

Lanham Napier - *Rackspace Hosting, Inc. - CEO, President, and Director*

Yes. Thank you.

Operator

Jonathan Schildkraut, Evercore Partners.

Jonathan Schildkraut - *Evercore Partners Inc. - Analyst*

Great, thank you for taking the questions. Lanham, in the prepared remarks you talked about restrained growth and thinking implications there was that the demand in the marketplace continues to be really robust. This is the third consecutive quarter of accelerating topline. Could you kind of frame the argument for us as we think about what factors could come into play that might cause growth to slow down as we look out over the next 6 or 18 months?

Lanham Napier - *Rackspace Hosting, Inc. - CEO, President, and Director*

Sure. Okay. Well, let's just talk generally about what's driving our growth and how we see what's happening in the marketplace. I'd start with inside the technology today, there is a paradigm shift with how IT is and can be consumed. Historically, businesses that had to do with themselves, they've had to purchase the gear, hire the people, purchase the software, deploy the infrastructure, run it and make it happen.

With the advent of hosting and the technology advancement in cloud computing, it's now available for the companies out there to consume this as a service. So they don't have to do it all themselves, they can buy it as a service with Fanatical Support from us. So this type of shift, depending on which industry analysts we want to look at, is billions and billions of dollars playing out over years at high compound annual growth rates. So underneath us, as a company, we have a rising tide just because we are on the right side of this shift.

So that's what's happening at a macro level. If you look at specifically at Rackspace, we have a differentiated position around Fanatical Support. We bring a portfolio of services where we can provide high service levels on dedicated infrastructure, as well as cloud infrastructure. That portfolio is a big piece of the growth. The next piece is how we're targeting that portfolio to enterprise customers.

The advent of the recession a couple years ago really allowed us to position ourselves in a new set of dialogs and discussions with the Fortune 500 and FTSE 100 companies in a way that we just didn't have access to in the past. As CIOs, we're thinking about how to do more with less and we're exploring new ways to do things. So it starts with our portfolio. It gets into targeting that portfolio of enterprise customers, which ultimately results in strong installed base growth. We've seen the installed base growth double, approximately double at year-over-year basis. And that's being driven by enterprise customers buying more from us, the growth of our cloud and stabilized/improved conditions within our SMB business.

So what's happening here is, I believe we are better positioned and more competitive than we've ever been in the market. So there's the backdrop. To directly answer your question, [I look to] constrain the growth. I believe the biggest risk factor on us right now is our ability to execute. It's our ability to complete the roadmap.

And in the prepared remarks, we've talked about the products we've launched. In the previous question, I talked about some of those products either systems work underlying that, there's training Rackers underlying that, there's filling the market task underlying that. So, I think the number one risk for us is execution. I think the second risk is macro factors. We all lived through some craziness a couple years ago. During that craziness, our Company continued to grow because we were on the right side of the trade, but we did grow it slower. So, as so as we look at things today, I would say that the constrain today is really our ability to execute the roadmap and launch those products in a world-class, quick manner.

Jonathan Schildkraut - *Evercore Partners Inc. - Analyst*

If I could have a little deeper onto the macro side, in the past, at least over the last few quarters, we've talked about, maybe, an improving macro environment being a catalyst for the SMB side of your business. Today, I think most of the headlines are focused on kind of potential for the macro environment to get worse. At this point, are you guys seeing any evidence that the headlines that we read are making their way into your business?

Lanham Napier - *Rackspace Hosting, Inc. - CEO, President, and Director*

Yes, great question. I agree with you. I was in meetings today, but before the call, I logged on to check things out. And yes, there were some headlines today. So, I think, from our perspective, if you look at the numbers, our business -- last quarter is our best quarter in a long time. We're bigger, growing faster, we're making money, returns were up. We launched products. So everything here is going well and we're pleased with it. We have not seen any dramatic shift yet. Okay, we don't have anything to point to, to say that the headlines out there in the market have impacted our market have impacted our business yet. I think part of what happens on that though is because of the shift going on in technology, our Company is on the right side of the trade. So, we are the beneficiary as people want to explore new ways, save money, increase their service levels inside their business. So, I think that we're a little bit in a different spot relative to a lot of other providers and companies out there in the market.

Jonathan Schildkraut - *Evercore Partners Inc. - Analyst*

All right. Also if I could just sneak one more in here, there's been a ton of news flow around OpenStack. HP and Dell made adoption announcements recently. Could you help kind of frame how we should think about OpenStack either from a cost control or revenue growth opportunity?

Lanham Napier - *Rackspace Hosting, Inc. - CEO, President, and Director*

Sure. I'd say the net of OpenStack is that we believe OpenStack is going to be the open-source cloud system that an ecosystem is developing around it. When we go out to the community that's participating in OpenStack, there's hundreds of developers and many one-time contributing code. We've had a couple of releases. There are now over 90 companies supporting the project in the ecosystem. So, we believe that OpenStack is rapidly becoming the de facto open source standard for cloud computing. It's in our interest as a company to have a ubiquitous standard for the cloud. With standards-based computing, Rackspace can build services and provide Fanatical Support around that to capture opportunity and create revenue.

So that as we think about OpenStack today, there's some very important milestones to maintain our leadership in the project. Number one, I would say is completing our public cloud transition over to the OpenStack code, which we are targeting to happen by the end of this year. Number two, the size and pace and activity of the developer community that supports the project. Number three, the successful number of deployments that Rackspace Cloud Builders is seeding now in the marketplace.

As OpenStack becomes an accepted standard for an open-source cloud computing, we have a tremendous opportunity to build services and capture revenue around that. I would say the revenue is a mid to long-term opportunity, but the competitive impact and competitiveness for a company we've already felt today. Because what happens is as we are drawn into these conversations by CIOs about OpenStack when they're figuring out what their long-term architecture ought to be, it's a wonderful chance for us to talk to them about the portfolio we already offer. Help deploy OpenStack deployments for them, do proof of concepts around these deployments and in the process, sell some business today.

So what OpenStack is doing with our thought leadership there is just creating -- it's opening the door for us to have some really cool conversations with customers and prospects, earn additional business from them today, and I think over time, it will create a whole new revenue stream for us.

Jonathan Schildkraut - *Evercore Partners Inc. - Analyst*

Great. Thanks for taking the questions.

Lanham Napier - *Rackspace Hosting, Inc. - CEO, President, and Director*

Thank you.

Operator

Patrick Walravens, JMP.

Patrick Walravens - *JMP Securities - Analyst*

Hi, thank you. So, I guess, I have two questions. Just a quick one following up Lanham on OpenStack, would you expect us to start to see meaningful revenue in 2012? And then the second question is, can you help us think about the relationship between growth and free cash flow? I mean, at 32% growth, would you always burn cash or how should we think about that?

Lanham Napier - *Rackspace Hosting, Inc. - CEO, President, and Director*

Okay. This is Lanham. I'll handle the first one about OpenStack, and then I'll let Karl answer the capital question. So, with OpenStack, in terms of revenue generation, I would say based on our ability to have the conversations and sell services, not just OpenStack services, but the other services we already offer, it's already having a bit of a revenue impact. I agree with your timeline in that in 2012 as OpenStack is more broadly deployed. I think the revenue opportunity there for services outside of OpenStack improves. I also think that by the end of 2012, we will start to see some revenue traction around services for OpenStack itself. But I would not expect for it to be a step function different in what we're already doing. So, Karl, you might --

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Karl Pichler - *Rackspace Hosting, Inc. - Interim CFO*

Yes. Okay. So, yes, the relationship between revenue growth and cash burns means that we should breakeven from a cash flow perspective as growth rate is approaching 35%. So that relationship is based on the assumption that we continue to lease datacenter capacity rather than build it out. But as you know and as you heard from the prepared remarks, we are in the last buildout phase of LON3 facility here in London. And so, basically, that explains the current CapEx spend in mainly Q1 and Q2 of this year. And the long-term relationship between free cash flow and growth rate is basically driven by our return. So, as we become more capital efficient and increase our returns, our breakeven growth rate becomes even higher than that. And so that's that relationship.

Jonathan Schildkraut - *Evercore Partners Inc. - Analyst*

So, I guess, I'll just ask Karl, once you complete this buildout and as you look to your next one, do you think on the next one you will lease or you'll build something else?

Karl Pichler - *Rackspace Hosting, Inc. - Interim CFO*

Yes. We will lease.

Jonathan Schildkraut - *Evercore Partners Inc. - Analyst*

You will lease. Okay. Thanks very much.

Karl Pichler - *Rackspace Hosting, Inc. - Interim CFO*

Yes.

Operator

Simon Flannery, Morgan Stanley.

Simon Flannery - *Morgan Stanley & Co. - Analyst*

Thanks very much. Good evening. I wonder if you could address the margin trends. I think last quarter, you talked about margin trends probably not exceeding the previous year's levels. We've had them sort of stable Q1 to Q2. Are there any big puts or takes in the second half on the margin side compared to the first half? It would seem like as you continue to build your revenue, some of that should start to drop through to the margin side. And then any commentary, Lanham, around the competitive environment? We certainly see Century buying Savvis and AT&T and Verizon talking a lot about the cloud. Are you seeing any change from those [pairs] or others? Thanks.

Karl Pichler - *Rackspace Hosting, Inc. - Interim CFO*

Yes. So on the margin side, as we said in the past, we are aiming for flat margins relative to last year, which is basically what we're tracking towards the first half of the year. There may be some upside potential, but we are definitely determined to invest in building out our product and system sets to deliver higher growth rates. And that's what we're committed to, and that's what we're going to do. So that's the framework around that.

Lanham Napier - *Rackspace Hosting, Inc. - CEO, President, and Director*

On the competitive environment, Simon, I think it's a great question. I mean, our industry has gone through a pretty big wave of consolidation here. Admittedly, we focus a lot more on playing our game and executing our roadmap versus worrying too much about what the other guys are doing.

Generally, I think with consolidation like this, after a transaction goes through, there's a bit of, I guess, I'd call it distraction. As these companies try to integrate and get the cultures together, get the systems together, so they can start to execute again. So we have not seen a big shift in the competitive marketplace. I suspect it will take these companies a while to get organized. I remember when our industry went through this similar type of consolidation 11 years ago, and I basically think that as consolidation takes place, it creates more opportunity for us. Because what's happening is our Company's competitive advantage and position in the market is all around being the service leader, being identified as the brand with Fanatical Support.

And so customers select us based on the service levels we provide in our brand reputation.

So as these other competitors like Savvis and Terremark have been consolidated away, we are now much more distinct in the marketplace, actually. So when we looked as a specialist company, Rackspace versus Terremark, Terremark was a bit of a generalist and that they had colocation as well as managed offerings. But now they're part of Verizon, which -- while a much larger company with more assets, isn't specializing in cloud computing. So that when you look at service levels in a cloud and for that customer segment that wants to buy a world-class service experience, that wants help making this transition a cloud computing, the consolidation actually reinforces our uniqueness in the marketplace.

So, I think the consolidation actually tends to favor our competitiveness. The thought leadership we have in OpenStack also really helped. We are the thought leader of this project, which is becoming the open source de facto standard in cloud computing. So I feel like as a company, other voices in the marketplace have exited and our relative voice has increased.

Simon Flannery - *Morgan Stanley & Co. - Analyst*

Great. Thank you.

Operator

Scott Goldman, Goldman Sachs.

Scott Goldman - *Goldman Sachs & Co. - Analyst*

Hi, thanks and good afternoon, guys. Two questions. First, Lanham, I thought maybe you could address some the bandwidth activity we're seeing out there from some of your competitors, particularly Amazon and Microsoft. And just maybe you could address in terms of can you give us a sense for how much -- how much of your revenue is contributed by bandwidth and the bandwidth pricing, and whether or not there's a need to follow Amazon and Microsoft with some of the actions that they have taken? And then secondly, maybe you could just talk a little bit about the number of servers you guys added in the quarter. I think the last quarter, you added a very healthy number with the cloud UK launch. Maybe this one also a bit elevated with Critical Sites or is it more just to strengthen the business that's contributing to the servers added in the quarter? Thanks.

Lanham Napier - *Rackspace Hosting, Inc. - CEO, President, and Director*

Okay. Great questions. Thank you. Let's start with bandwidth and pricing activity. If you look at a company like AWS, I mean, they have cut prices over recent years here, year and a half, literally 16 times. Okay? So they are just playing a different game than we are playing. Specifically, when it comes to our pricing policy and how we think about that stuff, if you break down our Company, we are one part infrastructure and then one part integrated service.

If you talk to our customers and disaggregate our approach to the market, it's literally 20% to 25% of infrastructure and gear and three-quarters service. So that basically from our perspective, we've never been trying to make a lot of money on bandwidth anyway, okay? We consider that a more commoditized portion of the stack. I think this is manifested in the margins that network providers receive. And so we're not trying to make excess economic wins on bandwidth. I mean, where we hang our hat, differentiation and unit economics is really around Fanatical Support in the service that we provide. So for us, bandwidth is not a meaningful driver of our revenue. It's, obviously, an important component of what we provide because without it, no one can reach their stuff, but it's really not a revenue driver for us. It's not something that we feel is differentiable and that we try to differentiate on.

We just want to have a very reliable network with as many carriers as possible that has a competitive price in the market. And we feel like we deliver on that. In terms of the number of servers, our server count has gone up. You mentioned in previous periods how we had cloud rollouts in investment. I do think that part of what's going on here is as we look at the product launches we've had and the growth that we're experiencing, we are making investments on this and trying to provide ourselves some operating wiggle room in the event of a growth spike. So that when we look at our infrastructure today and we're talking about adding thousands of servers and stuff here on a quarterly basis, that's a lot of work. And we've automated much of this in the physical delivery.

But as we look at it, the last thing we want to do right now while we are experiencing rapid adoption into the cloud is to have capacity constraints at the basic compute level. So part of what's going on is we're providing a little more operating room for ourselves, because we've had conversations with customers. And every now and then, we get a glimpse of what our growth could be. So there are CapEx today as we look at it, and we look at the servers, it's success based. So we are doing this based on our fuel in the marketplace, based on business that we are winning, and we're just giving ourselves a bit more operating room.

Scott Goldman - *Goldman Sachs & Co. - Analyst*

Okay, and then just quickly, as a follow-up to that, I mean, does that give you -- I guess, is there any operating leverage you get by sort of pre-investing or giving you that wiggle room? I mean, I guess looking at it from both, you just mentioned CapEx side, but also from an OpEx side, is there any operating leverage that you would benefit from on quarters forward as those servers show up?

Lanham Napier - *Rackspace Hosting, Inc. - CEO, President, and Director*

In the long run, I believe that's yes. It's a little bit lumpy. The main thing though, just to clarify (inaudible) when I'm thinking about operating room, I'm thinking about SLAs and the customer outcomes that we're producing. I mean, right now, in a growth period like this, our brand reputation rides on the reliability and quality of the services that we provide. So when we think about the growth phase that we're in right now, we believe we are making the investments to build a multi-billion dollar revenue company that the opportunity in front of us in cloud is the biggest, coolest growth opportunity [intact].

So the investment we have today in gear like this is about providing capability in aggregate scale, not about trying to create operating leverage right now. I think there will be a time in our Company's maturity where we want to optimize more around operating leverage. But right now, what we're optimizing for is customer loyalty, scale, and making the investments to be the service leader in cloud computing. As we do this, we believe we will change the business model with things like OpenStack and the roadmap that we're rolling out to increase our service capability, create more value for customers and create more unit economics. So over time, I think you're right. I think that it will create operating leverage for us right now. This shows up in some of our metrics today when we look at capital turns and the revenue per server climbing sequentially, which just proves that we're adding more value per box. We're adding more value per input. So you'll continue to see some of that stuff. It will ebb and flow as we make investments and build the business. But right now, we're focused on customer loyalty, brand reputation, generating credible outcomes for customers and continuously improving our unit economics.

Scott Goldman - *Goldman Sachs & Co. - Analyst*

Great. I appreciate the color. Thanks for taking the questions.

Lanham Napier - *Rackspace Hosting, Inc. - CEO, President, and Director*

Yes.

Operator

Gray Powell, Wells Fargo.

Gray Powell - *Wells Fargo Securities, LLC - Analyst*

Hey, guys. Thanks for taking the questions. Just had a couple here. As you focus on the enterprise segment, where do you see more opportunities? Is it up-selling, existing customers on new products or winning new customers? And then can you just give us a sense as to what enterprise is as a percentage of revenue now, and how that growth compares to that of your installed base?

Lanham Napier - *Rackspace Hosting, Inc. - CEO, President, and Director*

Yes, okay. All right. So let's talk about enterprise. What's happening today inside of classic enterprise IT in the early adoption that we're having is that there is a long tail of applications. If you look inside a Fortune 500 IT department, that IT department, in many ways, is purpose built to run a handful of critical apps, their ERP system, their billing system, stuff like that, where we start to show up in this is that long tail of apps, where a lot of innovation is taking place, we are a perfect fit for that for these Fortune 500 companies.

I mean, there's basically -- this long tail of apps is growing rapidly. It moves at a fast pace. It is web-based. And so people are looking for Fanatical Support and a standard build and partner to help them with that. So this is where the conversation tends to start. Once we win an enterprise customer and we win one of those apps, we earn their trust. We have a metric around here, time to trust, and that drives the upgrade rate with enterprise customers.

As we win one app and do a good job, one app begets another. And right now, because we are -- it's a recent development for us to truly target Fortune 100 companies, Fortune 500 companies, our share of wallet there is very small. By definition, since we're starting at zero with half of them, and today we serve half the Fortune 100, so I think what happens is, we have a tremendous track record of growth with them.

In our remarks earlier, we talked about how enterprise is really part of the base here that's increasing the trajectory in our installed base growth rate. So the question about is it better, is it more growth with new customers, or more growth with existing customers? Here's how we think about that. Obviously, there are only 500 companies in Fortune 500. Okay? And so if you look at the top 100 of those, we only serve half of them. All right? So we have of a good opportunity with the other half. Because our share of wallet is low with these guys, boy, our upgrade rate with enterprise customers is exceptional.

So, today, I would say we have a great opportunity with each of them actually. And as we look at our growth metrics, we track each separately. We think about new customer acquisition and we have acquisition teams and sales designed to do that and only focus on winning new customers. And then once we have them in the door and enterprise service teams go to work, we look at developing that customer, doing great work with them to grow that business over time. So I would say today, it's actually kind of both.

Gray Powell - *Wells Fargo Securities, LLC - Analyst*

Got it. That's helpful. And then just one more, if I can.

Lanham Napier - *Rackspace Hosting, Inc. - CEO, President, and Director*

Sure.

Gray Powell - *Wells Fargo Securities, LLC - Analyst*

Just roughly estimating that I think cloud is about call it 20% to 25% of your US revenue and it's grown to that level in about three years. Given that you're launching service in the UK with just a much broader suite of products, is there any reason why you would not see a faster adoption rate?

Lanham Napier - *Rackspace Hosting, Inc. - CEO, President, and Director*

No. When we look at our adoption in the UK, it actually has tracked faster than what we experienced in the US. I think part of this goes to the roadmap discussion that we had earlier that we've had our experience in the US with these services first. So we just know how to go to market with them and serve them better. And ultimately, the driver in our business, all gets down to how our customers feel about us. When we win a customer and do great work for them, they [tell to their] friends. And so the sooner we do good work for them, the quicker they tell their friends and the more business and opportunity that ends up going our way. So we do believe that the adoption curves in the UK is attractive. So far, it's been tracking ahead of what we experienced in the US. And every market is a little bit different, right? So I think the cloud was really pioneered in the US. People in the UK had heard about and had some awareness of it before it got here. So I don't think it's entirely a fair criticism, it is not a fair criticism, a fair analysis around the adoption rate so far. But I'll tell you we're tracking ahead than what we did in the US and we're pleased with that.

Gray Powell - *Wells Fargo Securities, LLC - Analyst*

Got it. That's very helpful. Thank you very much.

Lanham Napier - *Rackspace Hosting, Inc. - CEO, President, and Director*

Yes, sir. Thank you.

Chris Larsen - *Piper Jaffray, Inc. - Analyst*

Chris Larsen, Piper Jaffray.

THOMSON REUTERS

Chris Larsen - *Piper Jaffray, Inc. - Analyst*

Hi, thanks. Actually a couple of follow-ups. Lanham, you mentioned earlier to a question about the OpenStack, about longer-term it driving revenue. Did you mean that you think you'll begin to charge for it or that it will just help bring in customers in the door? And then secondly, is there anything within the OpenStack that prevents perhaps a competitor of yours from starting up the Rackspace want to be and adopting OpenStack to let customers come on to their cloud? And then I have a couple of more follow-ups.

Lanham Napier - *Rackspace Hosting, Inc. - CEO, President, and Director*

Okay. All right. It sounds like you're loaded with questions. So on OpenStack, yes, let's clarify those remarks. That's a great question. Today, I would tell you that OpenStack is already driving revenue to Rackspace through other services that we talk about and sell while we were having an OpenStack conversation.

Today, we are driving OpenStack direct revenue as we build out OpenStack clouds for customers. And we've already done that. So the short answer is OpenStack is already driving revenue today. Part of what I was trying to clarify in the question earlier is I think the question from Pat, basically asked when is OpenStack going to be a significant driver of revenue, which in my mind means a big step function difference. Okay? And I just don't want to set crazy expectations out there in the marketplace.

I believe OpenStack is gaining traction at a high rate. And OpenStack is the de facto open-source cloud computing standard. As we roll out our cloud on OpenStack, we'll be the largest OpenStack cloud in existence. As we roll out our services around that, this creates a natural opportunity for us to sell services around every other OpenStack cloud that is developed out there. And that is a wonderful thing for our business model because the thing we focused on our business model allowed us to return on capital. Well the day where people deploy an OpenStack cloud on their gear inside of their own corporate data center and then we provide Fanatical Support on top in a service layer, we are now creating services and value and capturing that service margin with Fanatical Support, all on top of the customers' capital.

So in the long run, providing services on OpenStack inside of customer's data centers we think is another step function boost in our business model. So that I think in terms of having that significant impact, that adoption cycle, we see how that can take place. But we don't want to point to that as a near-term revenue impact. I think the near-term revenue impact today for OpenStack is literally helping customers to deploy OpenStack clouds and charging them for that. And it's also, as we have customers, have conversations with CIOs about OpenStack, CIOs often send us other business as part of the long-tailed applications, which we referenced earlier.

You asked a competitive question about is there anything to prevent Rackspace look-alikes or me-toos out there to try to build the next Rackspace on OpenStack. And from a technology point of view, OpenStack is available to everybody, including our competitors so they can certainly try to do that. I think we have some inherent advantages in it. Number one, we helped launch the project and partnership with NASA and others, so we have a knowledge advantage about it. Number two, as we deploy our cloud on OpenStack, we will have scale and be the largest OpenStack cloud in the world. Number three, we have a brand reputation and service capability with Fanatical Support that we believe today creates world-class outcomes and enables cloud adoption.

So going into it, I feel we have a number of advantages over somebody else who just wants to launch and do it. I think it will be difficult for them to compete with us because we bring these advantages. So we like our chances there.

Chris Larsen - *Piper Jaffray, Inc. - Analyst*

Great. And Karl, it's great to speak to you again. I think the last time we were talking, we were talking about Castle and you have to have a certain number of employees to get some tax credits. I'm assuming that you've hit those figures already, and is there any benefit that we might see in the numbers going forward as you begin to unwind the leases in the other facilities? And then second, within that, your ability to grow has really been constrained by just being able to add enough Rackers in some cases. And why don't you just give us an update on how that's going and you've got facilities now in Chicago. Is there a thought to set up a call center in Chicago and start adding some Rackers up there?

Lanham Napier - *Rackspace Hosting, Inc. - CEO, President, and Director*

Okay. Well, this is Lanham. While I start with the racker piece and Karl can follow-up on the taxes. Yes, I think that today culturing talent matters more than ever inside of our business. We have been able to hire people and be opportunistic around those skill sets and we've been successful at it. I think the, trick here and the secret here is that we do have a great culture and we're constantly investing our culture to make sure that we are the preferred employer.

In terms of opening up a call center in Chicago that's not on our mind. We consider ourselves support center not call center. We don't run like a call center. We have very different approach.

In terms of trying to distribute our offices and talents, we have opened an office in San Francisco, it's a office focused on specific engineering and development fields, which is why we're there. So the offices we open have a mission and purpose and identity and strategy around certain talents. So right now, we did not have plans to open a big office in Chicago, we have a facility there that's a datacenter and so we do have rackers there, but it's not a big footprint that we haven't seen in Antonia, Boston, or London for example.

Karl Pichler - *Rackspace Hosting, Inc. - Interim CFO*

Yes, on the tax side this is really a multi-year deal and the measurement point in time is still out sometime at the end of the year early next year where this test will be applied.

Chris Larsen - *Piper Jaffray, Inc. - Analyst*

Okay, great. And then is there any -- can we look for any expenses rolling off as the older buildings get decommissioned or deleased, yes, in San Antonia or are you still using those?

Lanham Napier - *Rackspace Hosting, Inc. - CEO, President, and Director*

Yes, there will be as we complete those migrations and those leases expires, yes, we will no longer be making those lease payments.

Chris Larsen - *Piper Jaffray, Inc. - Analyst*

Right and then, is it possible to give us a sense for what percentage of your servers are being used for cloud versus managed or dedicated?

Lanham Napier - *Rackspace Hosting, Inc. - CEO, President, and Director*

No, we haven't broken that out and I think part of the issue here is that there are certainly different technology form factors. From a customer perspective, our customers are utilizing multiple pieces of the portfolio today and so they may be using a cloud solution for part of their environment of dedicated solution for another. And so we haven't broken that, broken that out on our metrics.

Operator

Mitesh Dhruv, Bank of America.

Mitesh Dhruv - *Bank of America Merrill Lynch - Analyst*

Thank you, so much for taking my questions. Obviously, you had a great traction in the enterprise segment, Lanham. I was wondering how the capital efficiency metrics compare on the enterprise side vis-a-vis the managed hosting on the SMB side. Is there more customization required, have you catered to more intensive workloads in the enterprise side?

Lanham Napier - *Rackspace Hosting, Inc. - CEO, President, and Director*

The big difference if we think about moving up the stack is the service level that we provide. So if we go from a basic support package and management package to a Critical Sites for example, we create a lot more value for the customer Critical Sites and charge a lot more for us as well. So as we add service capability and increase service levels that actually tends to improve our capital terms.

Mitesh Dhruv - *Bank of America Merrill Lynch - Analyst*

On the enterprise side --

Lanham Napier - *Rackspace Hosting, Inc. - CEO, President, and Director*

Yes, that's true with the enterprise side it's true across the whole business. Okay? So when we talk about managed cloud having twice the ARPU versus our core cloud. And our core cloud has a service level that we think is excellent. All right? So as we add more service to it, we create more value and capture more value on top of that basic unit of investment, the server and related equipment. We do not do a ton of customization. We are a productized shop, so we want to create repeatable processes and outcomes with customers. So we resist customization.

Mitesh Dhruv - *Bank of America Merrill Lynch - Analyst*

Great and then if I look at the managed cloud side are very good sequential growth rate. Is there -- are those customers mostly customers who are adopting the quality of the Vanilla cloud and now going to the managed cloud side are now going to the managed cloud side are these new customers?

Lanham Napier - *Rackspace Hosting, Inc. - CEO, President, and Director*

Yes, It's a little of each, majority of them are new customers. Okay so that these are customers that as they transition to the cloud, want help. Want help. They want Fanatical Support and our job is to make it easy for them to sign up and get going and provide them that help. So the majority of the managed cloud customers are our new customers into our system.

Operator

We have time for one more question. Colby Synesael, Cowen & Company.

Colby Synesael - *Cowen & Co. - Analyst*

Hi, great. Thanks for fitting me in. Just two if I may. First off, I wanted to talk about your opportunity to grow revenues outside of hosting and most specifically I'm thinking about the virtual desktop offering that you launched recently. Is there more opportunities like those? And then the second question had to do with the integration of your more traditional managed segment with your cloud segment? I know there has been a focus on integrating the teams, integrating the systems, integrated the building. I was wondering if you could provide as with an update on all that. Thanks.

Lanham Napier - *Rackspace Hosting, Inc. - CEO, President, and Director*

Okay. Let's start with the first question around hosted virtual desktop. The way you framed it, around it being something outside of hosting, we actually don't think it is outside of hosting. We think it's part of it. So basically, what we've done is we go to market with a couple partners, it's on top of our infrastructure and maybe their virtual desktop code that [will work with them.]

So for example, Citrix is a company that we were closely with. So we view that actually as a bundled solution for customers. That's inside of our sweet spot. So we don't see it as something that's different. We do see it as an exciting opportunity. As I go on calls with enterprise CIOs, it is a regular topic with them because of the economic and performance advantages that we can provide for them.

So to your point, it's something that's pretty exciting. We are early in that investment. So far, we're happy with the results. We have a lot more work to do there and there's other things as we identify other things and opportunities that basically add more value on top of our base infrastructure, we will continue to go to market with it.

Your second question was the integration of our teams of managed and cloud, et cetera. Yeah, so let's talk for a second about our structure and what's going on there. We are organized in terms of customer segments. We are organized in segments to reflect the service delivery model that we have for customers and to increase our customer intimacy and understanding of customers. So when you asked a question about the integration of some of our managed teams and cloud teams and what's happening there, we have a number of customers that are consuming multiple services in our portfolio.

We segment them based on the complexity of the services. As we resegment ourselves around this, we make sure we integrate the teams and the systems so that we can provide Fanatical Support. So the basic driver here is we are a customer loyalty driven company. We want to create incredible outcomes for our customers to drive loyalty. So getting the tools, systems and Rackers aligned around a set of customers really enables this. It makes doing the work easy, so that we are building the right technology sets and integration to make that happen. This is where part of the investment we have to make in a company is our underlying foundational systems, because basically, you can't go out and purchase the systems we use to run this Company.

We have spent years investing on this, and really, it is a competitive advantage to run something at those scale we operate in. I mean, we think of ourselves as being the service leader in the cloud computing and operating truly at web scale. So with the integration efforts, it's about keeping our segments clear and distinct, knocking our customers' socks off, and aligning Rackers to make it easy for them to do that.

Colby Synesael - *Cowen & Co. - Analyst*

So all the systems, used to be before Rackspace cloud, I think it's called Mosso. All the integration that went into bringing into one cohesive team whether it is the systems or it is the billing practices or systems, those have all been completed at this point?

Lanham Napier - *Rackspace Hosting, Inc. - CEO, President, and Director*

No, sir. This work is ongoing. As our roadmap advances and as we serve a larger customer base, I basically think this work is never done. We will always be looking to refine the model and our systems to better serve our customers. And right now, as we look at this, we think we are uniquely positioned to do it. And OpenStack is helping out with this, because it's creating an ecosystem and a foundation of systems in our cloud. So we've made great progress. We're advancing quickly. I just think as the roadmap shifts, as the market opportunity shifts, you'll see us continue to organize ourselves and make adjustments to pursue growth opportunities.

Colby Synesael - *Cowen & Co. - Analyst*

Great. Thank you.

Lanham Napier - *Rackspace Hosting, Inc. - CEO, President, and Director*

Yes, sir. Thank you.

Operator

That concludes today's question-and-answer session. Mr. Napier, I'd like to turn the conference back over to you for any additional or closing remarks.

Lanham Napier - *Rackspace Hosting, Inc. - CEO, President, and Director*

Okay. Well, we just want to thank everybody for tuning into the call. And especially, we want to thank our customers that placed their trust in us for Fanatical Support. We take the work we do for you very seriously, and it's our honor to serve you. And then we want to thank the Rackers that make Fanatical Support real. They continue to produce incredible results for our customers, and it's just a pleasure to work with them. Thank you all for your attention and interest in us. Good-bye.

Operator

This does conclude today's conference call. Thank you for your participation.
