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<<Patrick Walravens, Analyst, JMP Securities>>

So why don't we go ahead and get started. We are delighted to have Taylor Rhodes here with us. Taylor has a huge week this week in San Francisco, so we really appreciate you taking an hour of your time and coming to chat with us. And Taylor is going to walk us through may be 20 minutes slides, maybe little less and then we'll sit down and have a chat.

<<Taylor Rhodes, President and Chief Executive Officer>>

Thanks for time. I'm going to stand up a little bit because I talk about our standing. So it's Taylor Rhodes, I have the honor of being the fairly new CEO of Rackspace. I've been in the job for about six months and been at the company for about eight years. So I'm going to talk to you today about where we are, where we've been and where we're going, what market we operate in, how do we compete.

But my boss and one of my mentors is Graham Weston. Graham is the founder of Rackspace. He is the current Chairman of Rackspace and one of my favorite pieces of wisdom from Graham is the notion that everyone needs to be famous for something. So Graham will tell you, if you talk to him, that in early days of marketing he worked with Jack Trout. I don't know if any of you know who Jack is, but he wrote the book Differentiate or Die. And Jack's fundamental piece was you need to be famous for something. If you are an individual or company, identify what's your world class in delivering and focus on it, because that becomes part of your brand.

And today, I'd like to talk about what we are famous for at Rackspace, but I'll also spend some time talking about some speed bumps we hit in 2012, 2013 that got us off our game, how we refocused, what we are refocused on and how we are playing to our true strengths. So quite simply what we are famous for at Rackspace is called Fanatical Support. It is being world famous for delivering the best customer outcomes in the tech hands now.

And in the early days of Rackspace in the late 1990s, early 2000s, Graham actually started the company and what he calls is denial of service model. He was a real estate guy, he said, wow, tech is kinda like real estate, it's buy a piece of land, rent a server, get an opex stream, avoid service at all cost because that's how you lose your margin. And that's how they started the company out. But early on in the early days of the web and web apps, they started getting deluge with customers who actually said, I'll pay you more to solve my problems. I will actually pay you not to work on inputs but to create outcomes, I'll pay you more to treat my business as your own. And out of this realization came the notion there was a gap in the market for premium service and premium profit margin for people who wanted to pay you to create great outcomes for them.

Technology has always been hard and it always will be it, always breaks. Skills are always a scarcity, especially as technology change happens in the market space. So this ability to spot opportunities to build what we call economies of expertise and wrap a great customer outcome around them is how we've always competed. So we decided to plant our flag there and that remains the core essence of how we differentiate in the market today. We have lots of skeptics along the way. I remember in our 2008 IPO road show everyone said, well, service isn't scalable, how you do this. You'll lose it as you get big. It depends on you having a great culture. Companies lose their culture when they get big. And I want to tell you a little bit about our culture because it underpins our long-term differentiated scalable model.

Our model is all about creating what we call customer promoters. Promoters are customers who the science will show you stay longer, buy more, tell other people about you. So they increase the lifetime value of a customer, your churn stays very low and it reduces your acquisition costs on new customers. And this has really been at the heart of our model for a long time, installed base growth being a very healthy part of how we grow the business.

Now, this is a picture of a rare commodity. This is a Linux tech who is actually smiling. And for those of you who know Linux techs, smiling Linux tech is actually usually an oxymoron, right. They like to work in the dark a lot, they don't like to talk to customers very much, they like to write code, they like to solve problems. So, for us to build this model we knew that great text with great bedside manner is going to be tough. So the next realization we had was we had to build a great place to work. We had to become a recognized place where smart people could come, solve problems, have a very decentralized flat model, be entrusted with a lot of authority and be treated like grown-ups essentially to create great customer outcomes.

This Linux tech happens to be wrapped up in a straitjacket. A straitjacket for us is the ultimate sign of customer service excellence at Rackspace. It's a peer nominated award. Once a month one Racker wins it. And as for people who are spotted by their peers and by their customers it's creating those outcomes that nobody else can create. So for us at the heart of this is this differentiated position in the industry. Just Friday night in Las Vegas the annual Stevie Awards were held. Stevies are the customer service awards that span many, many industries.

And on Friday night, Rackspace won three more Stevies, we win these every year and we don't take them for granted because every year we submit a new category. This year, we wanted to press a lot on how technology is enabling our customers to do more things for themselves which helps us elevate Rackers further up above the API and create the next level of value. So this year, we were nominated again and won the People's Choice Award for best tech innovation in the service model. And for us that's very fitting because over time, we have continued to drive change in the way we do business through technology and through innovating service levels.

On the one hand, we are the founders and the inventors of the managed hosting industry. In the early 2000s, we've coined the term managed hosting and we became the largest pure play managed hosting provider in the world. We came from a very small SMB web hoster to becoming a very large enterprise grade dedicated hoster. On the other hand, we were an early entrant into cloud. We actually launched our first cloud in 2005. We called it the hosting system and in 2005 late in the year, we rebranded and launched a company called Mosso, which was one of the world's first clouds. In fact AWS launched the cloud in 2006 as well.

So then we drove on from there, and ultimately we became the founders of OpenStack. And these two vectors have come together in our model today and what we call managed cloud, which takes the best of dedicated single tenancy and multi tenancy and lets us really create the best-fit outcomes for our customers. Along the way and this invention of OpenStack it's been a blessing and a curse for Rackspace. I want to tell you a little cautionary tale. I mentioned we got off our game a little bit. OpenStack has been one of the most valuable disruptive innovations in tech in the last 10 to 20 years. Today, OpenStack is backed by everybody and their brother. We've got IBM, HP, Cisco, everybody in it.

But for us, when we OpenStack in 2010, it was a defensive move, visionary at the time. That said, we will lose the race to innovate and develop software against the likes of Amazon and others who have many more dollars and many more developers than we do. But the world preferred Linux ultimately over Windows operating systems and Sun for Web apps at the time Android was beginning to outship iOS and our vision was that the world would prefer to have an open cloud operating system alongside the closed proprietary stack. So we open sourced, we built the community, but we also knew we had to lead the community. So from 2010 to 2012 and a half, we put all our time, money and effort into building the world's first OpenStack cloud.

And in that process, I believe we got a little bit punched down on OpenStack and we misinterpreted what it was for us because after we rebranded the company, the open cloud company in 2012, we decided the right thing to do was to go fight a platform war, OpenStack versus AWS. Let's go fight a game on their turf and economies of scale for an early adopted cloud market populated by developer decision makers who do not value support and who did not understand our offer.

That took us off our game in 2012 and 2013. Our revenue growth decelerated in that time from 28% to 17% as we focused on the wrong market with the wrong offer and the wrong economics for the wrong outcomes. So we realized this. We had sort of what I call our Apollo 13 moment. Remember the moment when they dump everything on the table and they say that's all I got to get those folks down here. We needed to go back to basics. We needed to get back to understanding who our customers were, what assets we had to serve them better than anybody else. We had to get back to focusing on what we were famous for and find those buyers with the right value proposition.

I think Mr. Cramer represents well the voice of the Bayer against Rackspace over time. He has been at Bayer ever since we were at four bucks and he was at Bayer all the way to 80 and then he was a rejoicing Bayer all the way down to 26 and now he sort of goes well with the hell. But his Bayer thesis was simply this. Cloud is all commodity, technology displaces humans, no more need for them, therefore Fanatical Support has no place and in the market Rackspace is left with an infrastructure rental business, infrastructure is going to zero, game over, any questions, right. That's the Bayer thesis that took hold in the market from 2013 into what I call mid-2014.

But for us, our realization came in that time frame that falling cloud infrastructure prices rather than being the death of Rackspace actually assured in this next decade of enormous growth opportunity for us and here's why. Falling cloud infrastructure prices remove a lot of barriers to entry into the market. Any smart dove with a credit card and an idea can write an app today procure cheap cloud infrastructure, spin it up and start to offer it to the world. So this ubiquity of cheap infrastructure has led to an explosion that is really accelerating of software and tools designed for the cloud, and this in turn creates a lot of complexity for you and me. People are trying to operate and run businesses and make decisions as these tools evolve and evolve and evolve. It's very hard, it's a tough landscape. It creates complexity for business decision makers.

And really now CapEx in slow moving and high-cost infrastructure used to be the scarcity. Now that that is the ubiquity, the scarcity has shifted once again to smart cloud engineers who know how to make the infrastructure and the apps that run on a network. When we talk to our customers, they tell us, if I have a marginal dollar to spend, I sure as heck would like to spend it on something that is differentiating for me, a great engineer that's writing code and shipping product for me, a great marketer who really helps us place our product well. I would rather not spend money on my payroll with engineers running clouds that don't differentiate me.

So this notion of staying fast and lean and focused on core is really at the heart of our opportunity. And what we call this is, we call this economies of expertise. Amazon is all about economies of scale and those are important in the equation, but what we're finding more and more as the mainstream market accelerates in the cloud and this complexity and skills gap emerges, this value on economies of expertise to make it all work is really a key part of the equation for many, many buyers.

So here is a great example, real life. This is Zack Rosen. Zack is the CEO of a San Francisco based tech company called Pantheon. Pantheon employs about 15 very high priced super talented engineers building a platform for Drupal web hosting. You look at Zack and you'd say, man he's a bona fide cool kid, he's a techie, he's got a beard, he lives in San Francisco, he must be an AWS customer. Zack is actually the poster child for understanding the value of economies of expertise in making a business decision. Zack was recently approached by one of our competitors and said, hey, you want a 40% price cut sight unseen we’ll cut your infrastructure bill by 40%. And Zack said he did not take the meeting, and here's why. Zack employs 15 software engineers. They get to go write code, ship product that makes Drupal more competitive on their platform.

If he had to do what Rackspace does for him, he says he would have to double his staff and more importantly he'd be valuable engineering opportunity cost away from what is core and differentiated for him. The infrastructure component of the total cost stack is only a fraction. You still have to solve for the people cost and other parts, and what Zack understands that buying these economies of expertise from us in a variable cost model is a great way for him to stay focused on his core business.

So find that this is a business proposition that all companies have to consider, right. Whether you're borne on the cloud company like Pantheon or Tinder or DigitalFilm Tree or you are an established company like Under Armor, Mazda, Oakley, all businesses have to make this decision. It’s not about leaders or laggards, it’s about staying focused on what is core to your business. And so we see the market is clearly separating and the market is starting to speak this language.

Cloud went through early hype days as all markets do. Now it’s moving from hype to wisdom. And in this shift to wisdom, two clearly demarcated value propositions are models are emerging. The first is called unmanaged cloud and it has two components. The first is their technology stack. So this is a closed proprietary stack of technology that you can write your apps to via APIs which you have to solve for the people equation. And they can be your people, they can third-party contractors you come in, but somebody must manage and make the applications work. Somebody has to take out owner's manual and say, I will figure out how to make the 96 APIs work here, I'll take care of the cloud the 2 o'clock in the morning, et cetera. So this is the value proposition for unmanaged cloud and it is very valid for a large part of the market and this will be the volume part of the market.

The other part of the market though is what's called managed cloud and this is where Rackspace is the reference leader. This model is different in two important ways. The first part is about leading technology choice. One of the things that is really been valuable to Rackspace over time is that we have remained technology-agnostic. We can meet our customers on the technologies that they want us to run. We can avoid taking the risk on new technologies and let someone else take that risk. We will put them in a great service model and productize and run them. So we can meet our customers with technology choice.

The second piece though is the people piece and not just any people, it’s our Rackers. Remember, our Rackers are world-famous for being customer service fanatics. So not only are they going to be gee whiz smart guys and ladies about cloud technologies as they evolve, they are actually going to treat our customers' businesses as if they were their own and that's a very important differentiator. Gartner is the kind of consumer reports of our industry and Gartner this year had a good insight. We agree with them. They split their Magic Quadrant in our industry into two parts. The first part is called IaaS, Infrastructure-as-a-Service and in this landscape they only consider multi-tenant public cloud infrastructure, no hybrid choice of options and no services. And in this world Amazon is the king. This is a pure economies of expertise game and they are undoubtedly the kings of this game.

But when you change the landscape to the managed cloud quadrant, you see that it shifts dramatically in our favor. The first thing to note is that Amazon, Google and Microsoft are not on this contract. They are offering a different model with a different value proposition. We are on this quadrant in a very favorable leadership position. And even more exciting for us is the people we compete with in this space are legacy, big tech companies who are really struggling with disruption to their own models in cloud. You'll have seen stories recently about IBM and HP and everybody else and cloud models are extremely disruptive to large companies who have to figure out how to shift their product investments, their sales models. Everything from soup to nut in a cloud model is disruptive. And so in this space we feel very competitively advantaged as the service leader with hybrid option.

So great two markets separating identifiable agreed by Gartner, is it worth it. We get this question a lot, how big is this thing, can you guys make money, and is it profitable. There's a new report out this week from 451 research, total adjustment market in the managed cloud and essentially it comes to a few conclusions. The first is that is big, okay, $17 billion by their estimate growing to $43 billion in the next four years. And ultimately they are seeing a shift as the mainstream comes into cloud that the model that combines infrastructure options and services starts to grow much more quickly than the infrastructure only market and this makes sense, right.

We have seen these shifts before, mainstream starts to move, skills gap emerge to participate in cloud, the barrier to entry today is understanding how to make it work. And so this notion of buying infrastructure and services as the preferred model for the majority of the market will follow IT as it has always evolved. And finally for us the good news is while they recognize that AWS is the undenied leader in the IaaS only space, Rackspace is the leader in the managed cloud space. So it's a big market, it's growing quickly, it's picking up. A lot of the market will prefer managed services plus infrastructure. But we don’t want to focus on infrastructure. We think that infrastructure is a commodity in fact.

The real value-add is moving up above the infrastructure and solving meaty problems that really matter to CMOs, CIOs and CTOs. So we have shifted our focus and moved our resources up into areas where we can go talk to a CMO about digital marketing, solving making their e-commerce system run better, making it work better with their content management system delivering big data solutions that actually help CMO spend their money more wisely. So our move into practice areas or solution areas around digital marketing, big data and the analytics, cloud scale applications, cloud office which for us is productivity and email solutions, and finally IT transformation which helps CIOs adopt private clouds and get their virtualized workloads into hybrid models. These are our focus areas where we get out of the fray talking about the cheapest price of a bit of infrastructure and into the high value conversation with business decision makers.

We are also sharpening our focus of differentiated by being a hybrid cloud leader. The big unmanaged cloud players tell you all you need is a multi-tenant public cloud that will solve all your problems. And in the long run, I may agree with that. In 10 years, I think most applications will actually be in a multi-tenant public cloud context. But on the way due to a number of factors that will be a journey to that end through hybrid. It fits the logic doesn't it? Most CIOs have a big portfolio of apps and to think that one form factor is the right fit for all of those is absurd in my mind. So when we about one size doesn’t fit all, we are talking about hybrid portfolio options.

Many applications will perform better in a multi-tenant public cloud environment, but many others will perform better in a single tenant dedicated private cloud environment. And interestingly for us our biggest customers now are connecting across both of these environments to use single-tenancy and multi-tenancy together. I'll give you a simple example, Domino's Pizza is one of our large retail customers. They run websites with us that host all of their e-commerce. They do an incredible amount of business through it.

They want a secure single tenant backend where they keep this customer data where the database transactions happen, but they want to use the front end public cloud to burst for the times when they make an offer on TV and they have a high inbound volume spike. In the past, they have to manage that in a very cumbersome and an expensive way. Today in the cloud, they can check that box on security and performance and they can also burst very, very easily and we manage that for them. So this is a very practical hybrid use case that's driving a lot of our growth.

I mentioned before that we've always been technology-agnostic. That's a little bit of a lie. When we got of course, we actually became very bias toward OpenStack and we started to try to pick a winner. And what we realized along the way is that OpenStack is just one of the choices of leading technologies that our customers will want us to run. But when we can meet them with offers around VMware private clouds, Microsoft private clouds and OpenStack private clouds, you offer that choice, you cover more of the market and you come in with much more credibility because you're not trying to solve the problem each time with a particular technology.

We also recently announced our support for Google Apps for Work. That's an experiment, quite frankly, to see if we can take Fanatical Support on top of another cloud provider's infrastructure and capital and product, and find a market that values us running those things for them. So this notion of meeting customers with choice is a key part. So our Rackspace Solve series is a ongoing road show where we have our customers on stage telling our story. We have found that in 2012 and 2013, we also took the hand off the handle on marketing. We did not do effective marketing. We got confused about our message. We have found that our message is clear, we just need to go and tell it in more places, and the best spokespeople for us are our customers. So this Solve road show in 2015 will cover these cities on these days.

And in fact our first solve show of 2015 is in San Francisco and it's held tomorrow. It will be at the Fine Arts Palace, the Innovation Hangar. We expect a sold out event, but you all are welcome to come if you let us know today, there is a website there and you will hear companies like Tinder and DigitalFilm Tree borne on the cloud companies or established companies like VMware or WalmartLabs and these companies will talk about real practical use cases about ecommerce and big data and those solutionaries I talked about. So if you can make it tomorrow, we'd love to have you and you will hear some amazing people doing crazy things in tech and talk about why they prefer the managed cloud model.

So a couple of takeaways before I turn it back over to Pat and he gets to grill me. Look the first thing is, we are the early leader in the big and exciting market called managed cloud. It just makes sense that as the cloud moves from early adopter to mainstream more and more companies are going to want and need help and they are considering who is trustworthy and capable of giving them the best help. The second is, we are clearly differentiated. When you think about us versus AWS, we always get asked the question, how do you $7 billion market cap company compete with them. And I go back to Jack Trout and I say Differentiate or Die. Find your customers, do something amazingly different and better than they can, stick to it, reinvest and let them go. So for us, we are clearly differentiated by our focus on specialized expertise in those practice areas, hybrid infrastructure options and Fanatical Support.

Finally, over the years, we have a proven business model, proven sustained growth, profit and shareholder value and we're back, we're back in our game, we're executing our model, you are seeing three quarters now of sequentially improving growth quarter-over-quarter and importantly also we are starting to see an expansion of our business market into enterprise where we are winning more and more large deals as the large traditional competitor struggle with being dislocated by cloud. We are getting an opportunity to take on more and more of those very profitable larger deals.

So those are my comments. Pat, I'd love to sit on and chat with you and hear with questions we have from the audience.

<<Patrick Walravens, Analyst, JMP Securities>>

So, how is business Taylor?

<<Taylor Rhodes, President and Chief Executive Officer>>

Business is good. Yeah. Thank you. So, how is business for you, Pat?

<<Patrick Walravens, Analyst, JMP Securities>>

Two good days. Have we had you here before, we haven't. Okay, good. Where are you from? Where were you born?

<<Taylor Rhodes, President and Chief Executive Officer>>

Phoenix, Arizona.

<<Patrick Walravens, Analyst, JMP Securities>>

Okay.

<<Taylor Rhodes, President and Chief Executive Officer>>

I live in San Antonio, Texas now. One of the things Graham would tell you if he was here is, when he founded Rackspace he said, we're going to be in the heart of the – the mouth of the Rio Grande Valley, not Silicon Valley. So we are going to be different by design. I said that sounds real crazy Graham and he's a little bit crazy, but he is a genius founder.

<<Patrick Walravens, Analyst, JMP Securities>>

I like his sayings too, like one of those other ones was something about – what is it about working with your friends? I heard that one from Jason. Alright, so you were born in Phoenix, where did you go school?

<<Taylor Rhodes, President and Chief Executive Officer>>

I went to the University of Arizona undergrad which is called the Harvard of Tucson, Arizona, and – look, there is a competing institution there called Pima Community College and we are better. And then I went to Marine Corps for a number of years and then I went back and got an MBA at Carolina Chapel.

<<Patrick Walravens, Analyst, JMP Securities>>

The Marine Corps was how long?

<<Taylor Rhodes, President and Chief Executive Officer>>

It was five years.

<<Patrick Walravens, Analyst, JMP Securities>>

Five years. That was when to when?

<<Taylor Rhodes, President and Chief Executive Officer>>

That was 1995 to 2000.

<<Patrick Walravens, Analyst, JMP Securities>>

1995 to 2000. What was going on in 1995, 2000?

<<Taylor Rhodes, President and Chief Executive Officer>>

A lot of Bill Clinton chicanery. We were the force. We got to go, distract the market from Monica Lewinsky if you remember that.

<<Patrick Walravens, Analyst, JMP Securities>>

Remember Desert Fox, 1998?

<<Taylor Rhodes, President and Chief Executive Officer>>

Yeah. I missed Christmas for that. Thank you.

<<Patrick Walravens, Analyst, JMP Securities>>

And so you come back in 2000 and where do you go?

<<Taylor Rhodes, President and Chief Executive Officer>>

Got out of the Marine Corps, went to an MBA school. And then my first stop out of MBA school was at EDS.

<<Patrick Walravens, Analyst, JMP Securities>>

Actually, it was like 2002 then?

<<Taylor Rhodes, President and Chief Executive Officer>>

Yeah, 2002. And so, EDS had bought A.T. Kearney and I was joining A.T. Kearney and ultimately ended up joining EDS, in the Corporate Strategy Group there and did M&A divestiture and business line planning and a lot of that nonsense for about 18 months and then moved out into service delivery and management. My last role at EDS was managing our relationship with big airline and transportation companies like American Airlines and U.S. Airways etc. And really at that point, you're running major systems that airlines absolutely depend on. We can't push airplanes, they can't sell tickets if you are not running yourself well.

<<Patrick Walravens, Analyst, JMP Securities>>

And where are you based when you are doing the EDS stuff, are you moving around?

<<Taylor Rhodes, President and Chief Executive Officer>>

I was up in Dallas, but on planes a lot.

<<Patrick Walravens, Analyst, JMP Securities>>

And so – did you go from EDS straight to RAX?

<<Taylor Rhodes, President and Chief Executive Officer>>

I did.

<<Patrick Walravens, Analyst, JMP Securities>>

What year what that?

<<Taylor Rhodes, President and Chief Executive Officer>>

Late 2006.

<<Patrick Walravens, Analyst, JMP Securities>>

And how does that come about, did you get a phone call?

<<Taylor Rhodes, President and Chief Executive Officer>>

Yes, Lanham was a friend of a friend and Lanham Napier was our CEO at the time and he was one of the early stage guys there. He was the CFO initially, became the CEO and Lanham was looking for help moving Rackspace out of being a pure small business web hoster to more kind of enterprise grade stuff. And you had met Lanham several times. He is a real visionary and had a powerful effect. And when I went down, you go from the big beautifully EDS campus, Ross Perot land in Dallas and at the time Rackspace was $200 million company, a stinky little building it San Antonio and you think to yourself, is this a good trade, and you meet Lanham and he has got this vision for this company and his passion about building a great place to work and all of those things and he tricked me and I went.

<<Patrick Walravens, Analyst, JMP Securities>>

And so initially your role was what?

<<Taylor Rhodes, President and Chief Executive Officer>>

I came into run at the time we had two business units, one was called managed which was for our small customers and one was called intensive which was our first step up into a more enterprise grade SLA, where we would take at the time big customers like Atari and run their stuff. And so I came into run intensive and start to build our more sophisticated end of the business. I had sales and operations and Fanatical Support all of that.

<<Patrick Walravens, Analyst, JMP Securities>>

And you did that for how long?

<<Taylor Rhodes, President and Chief Executive Officer>>

It was about, let's say, that was almost two years when the global financial crisis hit and Lanham and I were sitting, having breakfast one day today and he said, we're either go out of business because we have a lot of small business customers who are going to got a business themselves or this is going to be that crazy opportunity that ignites new growth streams for Rackspace. So what he was talking about was we were having breakfast and talking about enterprise and what enterprise customers were accounting us. If you remember, we went public on August 8, 2008. So actually Zack Nelson was sitting in that chair earlier.

<<Patrick Walravens, Analyst, JMP Securities>>

Was he?

<<Taylor Rhodes, President and Chief Executive Officer>>

And he goes, yes – he goes, people forget this, but we were the last company to go public before the window closed in 2008 and he goes actually it's not true because Rackspace came after us. There was only a few tech IPOs that year. We were one of them and so we got out a month before. And just what has happened at that time is two things, one, because we are now NYSE listed and we've been growing, we had a little bit of brand awareness flickering up into the mid market of the enterprise and lots of those companies were in distress, right.

They were saying, gosh, I got to fire IBM, I got to close my data center, I got to fire my people, I've heard of you, my risk tolerance is up, come try, once you come more to this. So we actually started seeing this inbound motion from medium and large-size customers, we needed something different. And at the same time also here remember, we bought Slicehost in early 2008 and that was the code base of our first cloud and risk tolerance.

<<Patrick Walravens, Analyst, JMP Securities>>

And got by the way Slicehost.

<<Taylor Rhodes, President and Chief Executive Officer>>

Yes, that's right. Slicehost was a very cool hip cultural deal. That was one of the early clouds. And also because of global financial crisis with risk tolerance up, people started to actually be willing to experiment on cloud models as well. So those two things, the ability to start moving up into the mid-market and enterprise who start to sell cloud actually came out of what we thought might be the end of Rackspace. So that's pretty cool.

<<Patrick Walravens, Analyst, JMP Securities>>

Yes, I never realized [indiscernible] might be in the Rackspace. Stock went to like $4 though.

<<Taylor Rhodes, President and Chief Executive Officer>>

It came out at $12 and mopped down to $4.

<<Patrick Walravens, Analyst, JMP Securities>>

They go down to $4. Okay, what I am trying to get to is, why don't you go to international, when did that happen?

<<Taylor Rhodes, President and Chief Executive Officer>>

We founded our enterprise business unit for two years then I went to international in 2011 and spent almost three years overrunning our operations in Europe and Asia and building out the business there. We got about 1,200 people outside of London now. We've got people now on the continent as well and over in Asia Pacific, and so we really launched and put a lot of new revenue engine line over there.

<<Patrick Walravens, Analyst, JMP Securities>>

Yes. And so this whole – we were going all in and OpenStack thing came out, how did the international growth hold up?

<<Taylor Rhodes, President and Chief Executive Officer>>

It's kind of funny. I know you've not talked about it. But I used to say my best job without working overseas was the Atlantic Ocean and six time zones, right, you just got to kind of do your own thing. And when the corporate was making decisions you didn't necessarily agree with. You could modify your approach to how you carried out the orders. And I actually thought…

<<Patrick Walravens, Analyst, JMP Securities>>

Your approach is how you carried out the orders. I love that. I need to do that at work more.

<<Taylor Rhodes, President and Chief Executive Officer>>

What happened was this time when we got crazy at OpenStack, what was working in the European market at that time was absolutely Fanatical Support with hybrid options. It was not open, open, open, and the European market is always 24 months behind the U.S. anyway in new technology adoptions. So this notion of OpenStack was even more for in there than it was here and so we kind of just said, look that's not right for us, we're going to go run the place Fanatical Support with hybrid option than we grew 30% plus in the year that U.S. decelerated significantly, and that was a big lesson learned for me when I took the President job and the CEO job.

<<Patrick Walravens, Analyst, JMP Securities>>

We have to get that point out. So I am just going to skip ahead because everybody wants me to ask you about third-party cloud. So what we'll do we'll just skip all the other stuff, we can get back to it if we have time. So there is a little bit of a concern from investors that [indiscernible] when everyone started getting really excited about OpenStack and the stock went to $80, right. There is a lot of chatter about the third-party cloud. So just high level, what is it that people don't know, what is it that people are excited about and then we will try to figure out what the reality is?

<<Taylor Rhodes, President and Chief Executive Officer>>

Well, people are excited about is that a lot of the world prefer to Amazon technology and the cloud, right. And just like we said historically, we have always gone where people – to the technology our customers prefer. Now we've stay focused on and done too many at one time but whether that was starting with Linux and then adding Windows, moving into VMware early when it became clear they were going to the leave the virtualization market etc. we have always followed where the leading technologies are, right. And what we've done is in product types and really played to our core DNA which is making a great service experience out of those.

And again taking that burden of having people on your own payroll who have to say certified in that stuff and keep up with changes, they motivated etc. So the exciting part is potentially moving into a Fanatical Support model on somebody else's cloud technology is very consistent with our routes in our history and how we have done things historically. So it's potentially every exciting because there is a big part of the market that prefers those technologies, but really want to need someone to manage things on top of that before them. So that's the potential. I think the caution is we have to make the business more work and you have to make Fanatical Support working that. And so we are openly pushing and exploring this.

We think it is well versed on a time to go, check it out and be serious about it, but we are far from being able to say we have a launched model in market and we are confident that we can add value and be sticky and not be the middleman that can cut out easily. I would call an R&D project that has serious potential but as I've said openly on the call, we have to go and figure out how to make it Fanatical and how to make it economically attractive.

<<Patrick Walravens, Analyst, JMP Securities>>

Okay. Great. So now that we've properly lowered expectations, let's raise it back up. So, let's go through just sort of AWS, Google and Microsoft and think about how those offerings might be suited or not well suited to working with you in this way. We'd start with Microsoft.

<<Taylor Rhodes, President and Chief Executive Officer>>

Look Microsoft is a company that historically has been a software company. They generally have done a lot of their selling motion through channel partners and they are finding that Azure is – it really is a very good set of technologies that is maturing and they've made a lot of progress. But they have a lot of their customer base who historically have done what we call support figures. Customers who are used to buying service around technology and who are accustomed to Microsoft being able to say either we natively Microsoft can support you on this technology or here is a great set of channel partners who can support you on these technology.

So they naturally have an opportunity I would call it to drive as or even further into the market by having a great partner who does a Fanatical Support service on top of their technologies. And then I think they realized that. I think they are opened to working on that. I think that's a very natural motion for them because again they are historically a channel-enabled company. So that's how I think about Microsoft.

<<Patrick Walravens, Analyst, JMP Securities>>

Yes, those are all positives. Any negatives on the Microsoft side?

<<Taylor Rhodes, President and Chief Executive Officer>>

If you have to make it work. I mean, these relationships are complex, right. Many a time it becomes a two-party deal. You have – what's their strategy, what are their priorities, what are ours, do they match up, how do you get sales people compound, all those things. So there is lots of work to go there.

<<Patrick Walravens, Analyst, JMP Securities>>

But those kinds of conversations are happening?

<<Taylor Rhodes, President and Chief Executive Officer>>

Yes. I can't comment specifically on them, but we do work with Microsoft a lot.

<<Patrick Walravens, Analyst, JMP Securities>>

You kind of have a big relationship anyway, right?

<<Taylor Rhodes, President and Chief Executive Officer>>

I have to say yes. We have always been one of Microsoft’s largest channels, right. You can sneak in a few…

<<Patrick Walravens, Analyst, JMP Securities>>

Okay, and how about Google? Maybe we should do Google, okay, let's do Google next.

<<Taylor Rhodes, President and Chief Executive Officer>>

Yeah I think Google is…

<<Patrick Walravens, Analyst, JMP Securities>>

You have already got something, right?

<<Taylor Rhodes, President and Chief Executive Officer>>

Yes, we're doing the pilot and we're doing the limited availability of the Google app store. Look I think Google is still trying to figure out who the market is for their product. We are seeing heavy levels of interest in Google but not a lot of adoption there. But I think even Google will tell you that Google technologies are very different. The way Google technologies work is not, they work for Google to adopt them and use them as an enterprise who is used to B2C type offers, it's a different proposition. And so Google has I think a lot of work to do to find who their market is and who is going to buy their cloud, and then they have to figure out how they will support customers because Google again is a B2C company, they don’t have a B2E or Business to Enterprise type model that allows customers to work with them on how would you solution this, how would you implement it, how do I migrate there, how do I roll along the other side. So I think that they are an emerging cloud and they need to solidify who their target customers are.

<<Patrick Walravens, Analyst, JMP Securities>>

Okay. So negatives for Google, their technology is different, they have to figure out who their market is, it's more of a B2C. Positives, I would throw out –

<<Taylor Rhodes, President and Chief Executive Officer>>

They’re Google.

<<Patrick Walravens, Analyst, JMP Securities>>

They're Google and their culture, I think, fits reasonably well with you. Is that fair? When you walk around San Antonio and you walk around Google's headquarters [indiscernible].

<<Taylor Rhodes, President and Chief Executive Officer>>

I don’t see any reason why we couldn’t work together. I just think that’s still an early stage technology, an early stage product.

<<Patrick Walravens, Analyst, JMP Securities>>

Okay. Alright. Now AWS.

<<Taylor Rhodes, President and Chief Executive Officer>>

Well, they are clearly the effective leader, right. And so they have the market share and volume of preference. I think that AWS interesting, this is my observation, no conversation with them. My observation is that they are realizing that to cross the CASM into the enterprise, they’re going to need a human support layer around their product, both in terms of sales motion as well as in terms of offering managed cloud. On the other side, at their re:Invent conference last November in Vegas they didn't announce a price cut for the first time in a very long time, but did announce lots of investment in channel partner enabling to support on top of their cloud. So you see small companies today that are growing rapidly by data parts who have taken advantage of this opportunity and the thing that we have to determine there, the market need to observe in AWS is will AWS want to go build all those capabilities itself or will they prefer to partner up for people who can do it for them.

<<Patrick Walravens, Analyst, JMP Securities>>

Capabilities like what?

<<Taylor Rhodes, President and Chief Executive Officer>>

Like support and having the ability to go out and engage in the sales motion with customers around how would you solution, what should I use it for, which option go where etc. all of those frontend heavy enterprise side things are things that you would have to build that scale to continue penetrating the enterprise or they have to partner up for.

<<Patrick Walravens, Analyst, JMP Securities>>

And what's your sense?

<<Taylor Rhodes, President and Chief Executive Officer>>

My sense is I think the reinvent, they are talking a lot about their partners.

<<Patrick Walravens, Analyst, JMP Securities>>

No way, right. No way, no way, no way. I mean let someone else who can run on that business. I just can't see it. And so are you – what relationship do you have with AWS now?

<<Taylor Rhodes, President and Chief Executive Officer>>

We have conversation that I’m not going to comment real specifically on that. I think we want to determine if this works or not, and so you can rest assure the work is underway to determine if they can work.

<<Patrick Walravens, Analyst, JMP Securities>>

And what do you need from them in order to provide the level of support that you want to provide?

<<Taylor Rhodes, President and Chief Executive Officer>>

Conceptually you would need very close escalation type relationships with their technologist. You would need visibility into their APIs and their infrastructure so that you can actually tell customers what’s going on. You can leverage a lot of their native tools that are available to customers today who are savvy enough to be able to operate them but there would be additional layers of sort of product and engineering integration to happen. And then of course there would need to be a lot of go-to-market orchestration done as well. How do you stay out of each of each other's way, how do you not create conflicts in their sales force to our sales force, those types of things would be top of mind.

<<Patrick Walravens, Analyst, JMP Securities>>

Cool. I have a bunch of more questions, but maybe we will open it up and see if anyone in our audience does.

Question-and-Answer Session

<A - Taylor Rhodes>: No, we did such a good job.

<Q - Pat Walravens>: No, no, they will. Give them a minute.

<Q>: [Question Inaudible]

<A - Taylor Rhodes>: Yes. So the current offer is for Fanatical Support on Google Apps. And think about that consistently, we have a very large email and productivity business natively. We offer our managed exchange, we offer our managed email. So this is a very

close cousin, it's just again slopping the technology out. I would say it’s going moderately well. Like I mentioned, I think Google is still a brand that has to be merged in the B2B context. And so you find that there are still lots of pockets of education we have to do on what is their technology, how does it work, I think office 365 is the factor of standard in that space and many more people know about that. So I would just call it Google’s technology start to emerge and find market traction.

<Q - Pat Walravens>: How important does it seem to them?

<A - Taylor Rhodes>: Well, that’s always the billion-dollar. I have lot of money and tons of smart people who are working on a lot of stuff, is this going to be more important than self driving cars, I don’t know and I am not saying that to be historic yet. When you talk to people who are at Google or formerly from Google, they are very open about the fact that one year something is very important, the next year is just not. I think cloud is important to them, I think that it is important to them for a couple of reasons. The first is they don't want to let bases run away with that. They view data on platform for them as a natural value adding to their core search business and so there is lots of reasons for them to take it seriously. I just think they have a very long view to get there, lots of money and smart people, and they don’t patiently try to figure out how to get it to market.

<Q>: [Question Inaudible]

<A - Taylor Rhodes>: Sure. So our pricing model, we have two forms of pricing. One is a subscription or contractual base model where most of our customers will sign up for just call average 24 month contract with us. For that, they get a predictable monthly cost that includes infrastructure plus services. On the utility side, customers can sign up for pure utility usage based model and that is denominated in a price that is broken into cost per unit of infrastructure based on the gigabyte hour as well as a service cost, so that you can see this is Fanatical Support means, this is what we’ll do and here is what it costs. We made a significant change to our pricing model last July because prior to that we had bundled our pricing model with infrastructure and services under one unit. And what it did is it made the market misunderstand us and was in hindsight not great. So you came to our site and you saw there was actually $0.60 per gigabyte hour. AWS has got $0.30 per gigabyte hour. But for us, what we were explaining is that in addition to the infrastructure you’re getting a whole set of managed services on top in SLA. So we unbundle that, now you can get the clear picture that the infrastructure is competitively priced and you can make inform buying decision on what we will do for you, for what cost on the service side.

<Q>: [Question Inaudible]

<A - Taylor Rhodes>: We do what we call racker engagement which is a measure of loyalty or disengagement. We do it twice a year. We were one of the early companies to start doing this at scale with Gallup and ultimately what we want to know is two simple questions. One, a scale of 1 to 10 how likely are you to recommend Rackspace as a place to work to your friend or colleague and two, on a scale of 1 to 10, how likely are you to

recommend your manager as a leader to work for. Those two things and then verbatim comments and we can get lots of rich data out of that.

<Q - Pat Walravens>: We should do that. It's a great idea.

<Q>: [Question Inaudible]

<A - Taylor Rhodes>: Yeah. So my dissatisfaction was that, in August of 2012, we rebranded the company to open cloud company and that was very confusing. Before we had a very clear message, Fanatical Support, Fanatical Support, Fanatical Support. Open was a confusing message because people didn't know what it meant, right. Okay, you're open so how does that solve by problem, is your product worth, what you actually do. And so we’ve gotten of our game and gotten very confused, spent a bunch of money on open. If you went to SFO, we had a big digital billboard, we open source the cloud and it was sort of good thought provoking thought leadership type marketing but it had zero correlation with demand generation and differentiation. And we have built a lot of our muscle around that and kind of abandoned the players that actually worked, right, articulating what we do, what are we best in the world, that world is Fanatical Support. And that coincided with a period of time when we made a poor hire. We had a CMO, that smart gentleman just wasn’t a good fit for us in our model. And so during that period of time, I think our marketing really sucked, frankly. And so we had to get back out there and start to build the message. So it’s a multi-faceted thing. The Gartner's agreement with us in that deal, happy coincidence whether lucky or good, I’ll take lucky but the ability to get out on the road, they start spending more intelligently around those solutions rather than trying to buy horizontal words like cloud and hosting, you get a much better effect when you can target around particular problems you’re trying to solve. So we have a multithread marketing program going on right now, our Chief Revenue Officer, Todd Cione is sitting right behind you, and he's in charge of it. So you can drill him on that after we’re done here.

<Q - Pat Walravens>: Okay. I've got two more questions and then we'll wrap up. Can you flip back on your slides to your growth chart?

<A - Taylor Rhodes>: Yeah.

<Q - Pat Walravens>: Yes, all right, so can you keep accelerating?

<A - Taylor Rhodes>: Yes. Look, I think if we don’t we're underplaying to the market size, the growth rates that I just showed you there, but I don’t think it’s easy slam-dunk, right. You don't get nearly broken for nothing. When you get nearly broken, you realize you’ve been investing in some of the wrong things for few years and you have to rebuilt. So for us 2014 was about turning around and starting to get this sort of quarterly rhythm back. And 2015 is about now deepening our pray in those practice areas where we can get the flywheel going.

One of our best success stories in 2014 has been in digital, where we are winning more and more of the big ecommerce internet 1,005 sites. And when you get a flywheel into that, you become self referencing as the leader. We get channel partner who prefer us, we get CMOs who heard is the other CMO. So we have to build a few more of those fly wheels out that takes product work, it takes market work, it takes channel partner work and so I think the good news I always tell Rackers we are not opportunity constrained. We are execution constrained. We got to run after this thing especially while the big guys normally were sort of the managed cloud leaders are struggling.

<Q - Pat Walravens>: Write that down, not opportunity-constrained.

<A - Taylor Rhodes>: It's using too many opportunities. If we stick to many of them, we will screw it up.

<Q - Pat Walravens>: And then last one, I think is – so as far it's not a guidance, but sort of how fast do you want to grow this business aspirationally, what would you like to see it building?

<A - Taylor Rhodes>: At one point, we were at 50% grower, right. I think for us aspirationally we want to get back within the next couple of years to being a 20% plus growth company with good margin and our mission on this also profitable growth, right. We are not trying to suck out the profit of the company but we want to find those workloads. If we are doing our job right, here here's how you'll know it, one, we're selling where we don't get caught up in the conversation of the lowest price for gigabyte of storage or compete.

Two bigger deals which drive profit scale on our business and referenceability. Those are the two sort of telltales, right. If we are out shopping for the wrong kind of deals, when competing against Amazon, there again we are going to do stupid on profitable deals where it's all about infrastructure and we had no value on top. So I think finding three or four of these big slices of the market going deep vertically and becoming software referencing leader can get us back in a reasonable timeframe to 20% plus growth.

<Q - Pat Walravens>: Last one, so under what circumstances would this business be sold?

<<Taylor Rhodes, President and Chief Executive Officer>>

I hope none after 2014. Look, I have to give you the standard public company CEO answer on that. We are not for sale. Someone showed up with the crazy offer, we would have to seriously entertain it.

<<Patrick Walravens, Analyst, JMP Securities>>

Alright. Thanks so much. Taylor, it's great having you here, really appreciate it.