

FINAL TRANSCRIPT

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Morgan Stanley - Analyst

PRESENTATION

Adam Holt - *Morgan Stanley - Analyst*

Hello, everyone. This is my first presentation of the day, or conversation, I should say. So if I haven't met you, my name is Adam Holt; I run the software group at Morgan Stanley. And I'm very happy today to have with us James Beer, who is the Chief Financial Officer from Symantec. James is going to give a little bit of an overview about Symantec and then I'll get into some Q&A. So thank you for coming.

James Beer - *Symantec - EVP & CFO*

Great, thank you, Adam. Yes, just a couple of minutes, then, on our strategy. We are a company very much oriented around securing and managing information and identities. There are five key areas of thrust behind that strategy. So the first of those -- device security. You can think of that as the traditional antivirus business that grew up at the endpoint around a desktop, but increasingly is serving the needs of all the different devices that are proliferating today, particularly mobile devices as well as the traditional laptops and so forth. So first of all, device security.

Second, information security and protection. So this is still a security theme, but also broadly covering the backup and recoverability of the information itself.

Third theme, identity security, becoming increasingly important as we see e-commerce spread, but not only e-commerce, as we are seeing more and more the explosion of information generally, but also the coming together of consumer information, often times on the same device as corporate information, that driving more requirements around the IT departments to be able to understand who you are. Are you really who you say you are, when you are trying to access a particular area of information and so forth. So identity a particular driver for the future, in our view.

Fourth item, context and relevance is something we talk about. And here we are getting at the real explosion of particularly unstructured data that is occurring around us and our ability to help companies sift through these vast quantities of information to find the specific nugget that they need for a particular task. So it's around things such as intelligent archiving, the ability to offer e-discovery tools in the legal context has been an important driver of this, particularly in the United States in recent years.

Fifth driver, the cloud, from a couple of perspectives. First of all, from the view of us delivering our software as a service in addition to the traditional on-premise type delivery. But then second from the perspective of us helping outfit their providers who are setting up shop in the cloud to deliver computing resources. Oftentimes, virtualization is a big part of their strategy, and so our ability to play as well in the physical world as we do in the virtualized world becomes very important there.

So those are the key themes that underlie the overall strategy. Very much, though, an ongoing focus on persistent execution. I'm pleased to be able to say that in the last quarter that we reported, the September quarter, we were able to over-perform on each of the five key financial metrics that we track and be able to guide ahead of the consensus at that time. We are particularly pleased with how our operating cash flow has held up in this tough macroeconomic period that we've all been working through,

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and that very much underlies the ongoing value of the products that we sell and the underlying renewal stream that is represented in our base business.

So that cash flow, two primary uses of it -- first of all, we've had a very consistent record of buying back our shares. In fact, over the last four years, none of our software company peers have bought back as great a percentage of their market cap as we have, and we remain very committed to buyback going forward. Second use of that operating cash flow, acquisitions -- that has been a traditional part of how the Company has evolved over time, and we are very pleased with the results so far of the acquisitions that we've entered into in this last 12-month period that have center around encryption capability and identity security.

So with that, I'll take a chair and start with the questions.

QUESTIONS AND ANSWERS

Adam Holt - *Morgan Stanley - Analyst*

All right, well, thank you. The first question -- given all of the diversity of businesses that you are in, you've got a nice view across the enterprise on spend. Can you give us your latest thoughts on how the environment is, what your expectations are for a budget flush, if you will, and what your preliminary thoughts are looking at calendar 2011 from an IT spending perspective?

James Beer - *Symantec - EVP & CFO*

Yes. I'd say nothing terribly different to what we've seen in commentary around various industry players in recent times, a cautious rebuilding of spending and optimism versus the real lows of late 2008, first half of 2009. We would expect a typical budget flush, I don't think anything out of the ordinary. We were quite pleased with how our September quarter ended in terms of the US federal sector. It's their year end, and they certainly are an entity that is spending on, particularly, security, but also storage technologies as well. And so that was an illustration of a certain degree of firming of demand.

But it's still tough out there, I think particularly for small/medium-sized businesses. That's a sector that we've seen having a hard time to get into recovery mode.

Adam Holt - *Morgan Stanley - Analyst*

If we go through what you think are the key growth drivers for next year, you broke down your businesses effectively. But some of the businesses are more mature and are generating a lot of cash. Others are higher-growth businesses. To you, what are the two or three keys to accelerating your current growth rate over the next 12 to 18 months?

James Beer - *Symantec - EVP & CFO*

Yes; I think the highest-growth parts of our business will come around our hosted offerings, where we are already in the market with an e-mail security, Web security and endpoint management, which is in essence a centrally managed security offering. So we continue to see good take up there. We'll be bringing other hosted offerings into the marketplace over the next year or two, but we are seeing nice double-digit growth around our software-as-a-service businesses.

On the security side, thinking on-premise now, the data loss prevention products that we have available are oftentimes the ones that are really driving the conversation, that are following through to data loss prevention sales but also allow us to broaden out the discussion with the customer around other security technologies as well. So I think those will be particularly important.



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Other growth opportunities for us -- the consumer business continues to grow steadily, and we think that there is more opportunity for us there. The backup and archiving business has also been growing very nicely. We refreshed our product set in the backup arena at the start of this calendar year, and we have been very pleased by the take up around de-duplication capability, virtualization support and the integration of our backup and archiving capabilities.

So I think those are going to be the items that will help drive our top line.

Adam Holt - Morgan Stanley - Analyst

Why don't we drill down on the consumer business for a minute? It's a question I get all the time. I was going to do an impromptu audience survey to see how many folks use antivirus, but it's a market that has been around for a while. You have tens of millions of customers.

James Beer - Symantec - EVP & CFO

Yes.

Adam Holt - Morgan Stanley - Analyst

How do you grow that business, and what is the impact of a potentially slowing PC environment?

James Beer - Symantec - EVP & CFO

Well, we've been able to grow the business, as I was mentioning just a moment ago, even in a really tough macroeconomic environment for consumers. And we've been doing this in a variety of ways. But two important themes are around up-selling customers to the higher end products, particularly Norton 360. That has gone exceptionally well since it was launched about four years ago. And secondarily, the ability to, in essence, extend out the average life of a customer. We are now enjoying more than a four-year average life, and that is driven as a result of a variety of renewal initiatives that we have undergone in recent years and are now being underpinned by our new e-commerce platform capability that we have developed in-house.

We used to outsource this capability. We now have a much greater ability to granularly go after specific sub-segments of our customer base as we look to offer them new products at the end of their subscription life and so forth. So it's those sorts of things, as well as attracting new customers up front, either from OEM relationships, retail or ISPs, that is really driving the business.

Adam Holt - Morgan Stanley - Analyst

One area of real differentiation that you have on the consumer side is the hosted backup business. Could you talk about how significant that is and where you think penetration can go over time?

James Beer - Symantec - EVP & CFO

Yes. I think this has been an important part of the success of Norton 360. That is really the key difference between the Norton Internet Security product and the Norton 360 product. And so we've seen this large take-up of the 360 offering, and what we've also found is that when customers are looking to us not only for their security needs, but for their online backup needs, it becomes a stickier relationship. Those renewal rates rise. Obviously, that's a healthy thing from our perspective.

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So as a standalone product per se, it's a relatively modest part of the overall consumer revenue mix. But as a driver of Norton 360, and 360 as a driver, in essence, of our revenue premium, it has been very important.

Adam Holt - Morgan Stanley - Analyst

Let me ask a follow-up question that touches on the consumer but is an enterprise question as well. A lot of questions I get about not just the consumer security market but also the desktop software market have to do with the proliferation of new devices -- tablets, cell phones and in general, devices changing on the point side and application changing on the cloud side, so more applications moving to the cloud and being accessed by different kinds of devices.

How does that impact the consumer business, and how does that impact your total security business?

James Beer - Symantec - EVP & CFO

Well, it is making life more complex, if you will, for consumers and for businesses. And in many ways, that's a good thing for our business. We are very much about managing that complexity for our customers because, as I was mentioning when I was up at the podium there, increasingly we are seeing customers' individual devices coming into workplace. We are increasingly seeing a device contain both corporate and personal information. The devices that you are using today are probably not going to be the devices you are using in a year or two's time. You are potentially going to have more devices that you are using tomorrow than you've had said yesterday.

And so there is this overall operation that is a real issue for the IT departments of companies to manage because they've got to be just as sure that whatever device is being used by an employee is just as secure and in compliance with the way in which they are looking for corporate information to be used within their specific environment.

And so the game is changing rather rapidly. Gone are the days where the IT department pretty much dictated what you used and how you used it. They are now having to react to much more of a commingling of activity. And that's going to enhance the need for their ability to be able to do things like, when a device is lost or an employee leaves the company, to be able to wipe that data that is owned by the corporation off that device while potentially leaving the personal information on the device.

So you've got a variety of new needs that evolve around the notion of management of these devices and management of the information that we will very much be looking to serve as things evolve here.

Adam Holt - Morgan Stanley - Analyst

So how does that impact your product set? In particular, I want to drill down on the VeriSign acquisition and why you did it and how that changes your positioning as applications move to the cloud, but also operating systems may move to the cloud with desktop virtualization.

James Beer - Symantec - EVP & CFO

Yes; I think the notion of identity is going to become much more important for IT managers to be able to be sure about. They've got to be much more agile in their ability to be able to serve an application, serve the data, oftentimes in a virtualized way, to a particular device. And it's going to be a lot more complicated than this has been in years past. And yet, at the same time, security threats are becoming ever more so, because the attackers are very well-funded, very creative and so forth, and very focused on a monetary objective now.

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So it's a very different and fast evolving landscape, in this regard. It's going to be some interesting opportunity for us. And I think identity is going to be right in the middle of it. It's going to be much more important to be able to verify that you are who you say you are when you are trying to access a particular information set within an organization. Organizations are much more focused now on which are the key elements of their information set. That's what has been driving the growth of data loss prevention as a security tool. And identity is going to be a very close cousin of that type of security outlook.

Adam Holt - Morgan Stanley - Analyst

Just a couple more questions on the security business, and then I want to move to the enterprise. You made a decision awhile ago to get out of the network security business. Another question I get with some regularity is, as we move into more distributed environments, does that change the way that you think about network security? Is there a reason to believe that you should be in the firewall business or intrusion detection, intrusion protection, any of the network areas?

James Beer - Symantec - EVP & CFO

We are not planning to make a big shift in this direction. We exited that business in part because we didn't want to be focusing on an area where Cisco and Juniper were very much focused. And now we have a little bit of an investment in this regard in that we have a joint venture that we've built with Huawei over the last three or four years, and that business is focused on a building appliances, both for the storage side and the security side of the business. So they are in the network security business, but that's really a second derivative, if you will, of our primary core.

Adam Holt - Morgan Stanley - Analyst

McAfee, arguably your biggest competitor on the security side, is in the process of being acquired by Intel. What does that mean for you from a competitive perspective?

James Beer - Symantec - EVP & CFO

Well, I think there may be some opportunity here, as there is a certain amount of distraction value in the process of bringing two rather different cultures together. And so we will continue to have our sales teams go aggressively after all of the opportunities in the security landscape. We feel very good about where our product set is. I think the timing of this transaction is helpful from our perspective and that we are very much riding the wave of a product cycle. So I think there's going to be every opportunity for us to get out to customers and really talk to our depth of capability, breadth of capability and real focus on security.

I think, technically, the notion of trying to burn a lot of security capability into the chip level is not a terribly practical one. The threats evolve way too quickly. We reissue our software multiple times a day, so the notion of trying to build your defenses in at the chip level, I think, is certainly not sufficient. There may be some limited applicability, technically. And indeed, our own encryption products have just been recently integrated with Intel's architecture at the chip level. But this is not something that we see being a dominant technical driver here of the business at all. It's just moving too fast.

Adam Holt - Morgan Stanley - Analyst

Let me touch on the backup business and the storage business for a little while. On the backup side you obviously have some product cycles. You mentioned earlier the impact of de-duplication. How do you think about the sustainable growth rates in backup? And where are you in some of these product cycles?



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James Beer - Symantec - EVP & CFO

Yes; we think that over the next three years backup can grow in the mid-single digits. I think that's going to be very much driven by items such as de-duplication. Clearly, the IT departments are under enormous budget pressure and de-duplication is just a very straightforward way of saving money. It is remarkable the number of duplicate copies of digital information that are traditionally backed up and archived and so forth. So there's a real clear ROI opportunity there. So that's going to be important.

Virtualization capability -- we are exceptionally well-positioned there in terms of having the leading backup software for virtualized environments. We seem to win the VMware award on a regular basis. And so there will continue to be an uplift for us. And then bringing together the archiving world with the backup world is proving to be another very helpful driver of that business. So I think those are going to be the themes over the next few years.

Adam Holt - Morgan Stanley - Analyst

The archiving business has been a terrific business for you. Obviously, it's something that you acquired recently. Are there other areas that are adjacent to the core backup space that you think you need to be, like the next kind of archiving opportunity?

James Beer - Symantec - EVP & CFO

Well, I think archiving is itself going to continue to evolve around this theme that I was talking about earlier of context and relevance, because that unstructured information is just growing so quickly there is going to be a premium put on the most intelligent way to be able to pick and choose from this massive information. And so you see areas like e-discovery continuing to evolve, for example. There already have been first-generation products that we've had in the marketplace now for a couple of years, but I think these are literally sciences that will just continue to accelerate in terms of the capability because the need is very clear and the task is only getting more difficult as these volumes continue to expand.

Adam Holt - Morgan Stanley - Analyst

As we look at the key drivers of the backup business, how tied are you to server growth? And as we see penetration of virtualization increase, is there any sort of correlation directly there on the backup side, or is it still too early for that to be the case?

James Beer - Symantec - EVP & CFO

Well, we have been taking to market different business models, if you will. The traditional business model was around a per-server type motion. We found customers getting interested in per-terabyte pricing models as well, in part because customers are finding that that is easier for them to predict their cost curve over time, as they have some sense for their overall volume of storage and how that is projected out into the future. So we found about a quarter of our customers have moved from a per-server type model to a per-terabyte model for our net backup products, so the higher end backup offering that we have. And I would expect that that will continue to expand the per-terabyte style.

Adam Holt - Morgan Stanley - Analyst

Let's shift to the storage business. The storage business has been impacted to some extent over the last couple of years but what has happened on the Solaris front, not only the Oracle acquisition but also, to some extent, the degradation of Solaris share. Can you give us a sense for how we should expect to see that business evolve and, if and when you start to see stability in Solaris, how storage begins to grow again?

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James Beer - Symantec - EVP & CFO

Well, you're absolutely right. The Solaris platform -- it used to be almost the entirety of the storage management business. Over the years, clearly Solaris was losing share. And so we have been working to move as much of our storage management business onto UNIX/Linux platforms and so forth. So today we are at about half and half, and I would expect the trend to keep moving towards the Linux side of the equation.

So we're able to continue to bring out new products that will support that part of our business. Last quarter, we rolled out a couple of products that we've codeveloped with VMware for the virtualized environments, one that is all oriented around high availability for applications, the other for optimizing storage in virtualized environments. So there are opportunities for us to get some uplift here.

That said, I mentioned at our analyst day back in May that I would expect over the three-year horizon that the storage management as this would be flat to down low-single digits. Now, we'll obviously work hard to beat that type of projection, but that just gives you a sense for the reality that people are moving more of their applications off the Solaris platform and that that's still, today, about half of the business.

Adam Holt - Morgan Stanley - Analyst

So I'll ask the question just because it's the obvious next question, which is, to the extent that the storage business may end up being flat to down for the next several years, how strategic is it to you? And more broadly, what can you say or what can you do about potentially breaking apart some of the pieces to maximize shareholder value?

James Beer - Symantec - EVP & CFO

Well, obviously there has been a lot of talk, reports written about this topic and so forth. And I should just say that we are, as a management team, as you would expect, very much focused on portfolio issues. That's just a regular part of running a business. And so we are regularly thinking through these types of things. And as we do that, we are thinking it through from the perspective of the strategy that I was outlining at the start of our discussion here, so what fits best with our goal of securing and managing information and identities.

So the acquisition's that we have made in this past year obviously very much are oriented to fit with that strategy. And so we'll think through our portfolio on a very regular basis. But as you say in your note, Adam, there are a variety of issues as you consider portfolio that always come into play here -- be they contract issues, be they sales force management issues, be they tax issues. So these are complicated topics that are very much worthy of serious thought. And that's absolutely what they get at Symantec.

Adam Holt - Morgan Stanley - Analyst

I've got a few more questions, and we've got just a few minutes left. Are there any questions in the audience?

James Beer - Symantec - EVP & CFO

The other thing I'd say on that last point, of course, is that while there is a need to continue to think about portfolio issues, it is really important that we keep our overall team focused on consistent execution. That is clearly going to be a key driver for our share value, and we've got to deliver that time and time again. September was a good quarter for us. We've got to do exactly that sort of thing for the next three or four quarters. That's where we need all of our people at the Company focused, day in and day out. So that's a really important part of this overall perspective.

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Adam Holt - Morgan Stanley - Analyst

And that was, I guess, my next question, which is, as you look at the keys to consistent quarter-to-quarter execution, what are the things that you think that you have made progress on? And what are the areas that you think are a continued work in progress as you think about the next year?

James Beer - Symantec - EVP & CFO

I think we've made real progress around product quality, and that's obviously where it all starts because a salesperson is only going to have the confidence to sell well into a customer if they feel as though they can really stand behind the product that they are putting their personal reputations on the line for at that Company. So I think it all starts with product quality, and our portfolio is in, I think, the best shape it has been in the 4.5 or so years that I've been at the Company. So it all starts there.

And I think the sales team has, as we have talked about the statistic of our larger deals that includes both security and storage sales within a single contract, that is now oftentimes up into the 40% mark. That is reflective of the progress that the sales team has made in cross-selling this broad portfolio of products that we have. So I think we've made progress in that regard, as demonstrated by that stat.

And then around the cost structure, we continue to focus on driving efficiencies and effectiveness. And of course, that frees up funds for us to put more effort behind the highest growth opportunities that we see in front of us, things like hosted, DLP, consumer and backup.

Adam Holt - Morgan Stanley - Analyst

So on the cost side, let's talk about margins a little bit. There have been some puts and takes on the margin side. You've done a great job reallocating, being more efficient on the positive side. On the negative side, the PC market has weighed on margins, obviously, the e-commerce platform -- how should we think about margins evolving from here?

James Beer - Symantec - EVP & CFO

Yes; what we have said is that over a three-year period, we can take margins to around the 30% mark. So in this last quarter, when you back out the various purchase accounting modifications associated with the VeriSign and the encryption transactions, we are running at an operating margin of about 27.5%. So I think it's important to do that conversion, and we are certainly, in our conference calls and so forth, going to continue to lay that out as explicitly as we can so that people understand the accounting effects associated with the acquisitions in the first year, year and a half or so after a deal closes. So we will look to be as transparent as we can with that. So there's a couple of points of margin opportunity over the next three years or so.

Adam Holt - Morgan Stanley - Analyst

With that, we are out of time. Thank you very much.

James Beer - Symantec - EVP & CFO

Okay, thank you.

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