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Deal Spotlight
January 2010

EMC Acquires Archer Technologies

Compliance Software Consolidation Wave Continues - Who's Next?

On January 4, 2010, EMC announced its plans to acquire Archer Technologies in an effort to broaden its exposure to the highly coveted, rapidly growing market for Governance, Risk Management and Compliance software (GRC). The acquisition adds best-in-class, IT-centric GRC capabilities to EMC's RSA Security product line and enviably positions the company against infrastructure software competitors IBM, HP, CA, McAfee and Symantec, who have remained on the sidelines in GRC M&A. The Archer deal is the latest in a GRC consolidation wave that has precipitated in the acquisitions of Paisley Consulting, Cura, Axentis and Brabeion over the past twelve months. Archer is one of the top three pureplays remaining in the GRC sector and its acquisition will unequivocally have transformational implications for the industry. We expect the larger enterprise software incumbents to follow suit as the pool of viable GRC platform targets continues to shrink. As the window of opportunity closes, the more ambiguous question is who will move the most quickly to establish a formidable presence in what continues to evolve into one of the most mission-critical software categories of the next decade.

Transaction Highlights

- EMC is acquiring 100% of the equity of Archer for an undisclosed sum.
- All of Archer's executives are expected to stay with the company, which has 138 employees across its two offices in Overland Park, KS and Reston, VA.
- Archer closed 2008 with $23 million in revenue and was growing at 30% annually. The company has been profitable since its inception in 2001.
- The transaction is expected to close in Q1 2010.
- Archer will remain in Overland Park and will operate as a part of EMC's RSA Security Division as a wholly-owned subsidiary.
- Archer's software will be wrapped into EMC's product portfolio and will be offered as a standalone product.
- Archer's growth profile, customer base, product defensibility, the valuation multiple on the 2008 round, the fact that Archer was an existing EMC partner and the company's "opportunistic" leverage all contributed to a highly attractive transaction multiple.

Archer Background

- Archer's product set enables highly regulated companies to reduce enterprise risks, manage and demonstrate compliance, automate business processes, and gain visibility into corporate risk and security controls.
- The company raised its first round of institutional funding with Bain Capital Ventures in September of 2008, when it placed a minority stake for $29 million.
- Its customer base spans 25% of the Fortune 100 and 36 of the top 40 US financial services institutions. The company is vertically agnostic with traction in financial services, telecom, technology, healthcare, media and government.
- Archer's solutions can be deployed on-premise, with a managed service provider or via SaaS.
- The company was founded as a security management solutions vendor. As market demand for IT-centric GRC tools proliferated, the company redirected its offering to capitalize on the trend.
- Archer acquired rival IT GRC vendor Brabeion Software in January of 2009, bolstering the company's policy management tools with Brabeion's IT compliance content library. Brabeion specialized in leveraging content from PricewaterhouseCoopers to help customers map risk events to business risks and link IT controls to governing sources beyond laws and regulations.

Synergies

Strategic Fit with RSA – From a headline perspective, Archer's IT centric approach to compliance was an ideal fit for EMC's RSA division. Archer provides GRC solutions that manage the lifecycle of corporate policies, analyzing and managing business risks and demonstrating compliance. Its product set addresses Policy, Risk, Compliance, Enterprise, Incident, Vendor, Threat, Business Continuity and Audit Management. The technology, coupled with RSA's solutions for data loss prevention and security information and event management (SIEM), will provide customers with a more comprehensive IT-GRC offering that spans policy automation, security controls, security event management and remediation.

The fundamental driver behind the convergence of traditional security tools and GRC is that customers have shifted from an IT-based approach to a policy-driven approach that leverages technology to enable policy enforcement and compliance. As such, corporate governance initiatives, audit requirements and compliance legislation are now creating pull through revenue opportunities for traditional security tools that allow CISOs to automate processes surrounding policy and procedure management and the associated reporting requirements. Compliance has continued to evolve into a board level topic, which has blurred the lines between a business decision and a technology decision. Archer provides the content, framework and process automation to ensure that customers are addressing their policy, risk and compliance management requirements. RSA offers the underlying IT infrastructure to enforce these initiatives – essentially bridging the business policies to the controls. The thesis behind this transaction is that EMC customers will be better positioned to manage their security issues, address compliance and ultimately report on the outcome in a business intuitive manner.

Strategic Fit with the Broader EMC Organization – The long term opportunity extends beyond the RSA business unit into various other layers of the EMC software stack. Archer's tools are likely to be a critical component of the vision for EMC's recently acquired Ionix unit. Ionix is the systems management platform that customers use to automate their IT configurations across servers, networks and storage environments. There is also a compelling synergy between the Archer product set and EMC's traditional storage, backup and business continuity capabilities – particularly in heavily regulated industries such as healthcare and financial services where legislation is creating demand for more robust storage infrastructures. Eventually, VMware will leverage Archer's functionality as demand for addressing compliance in virtual environments becomes ubiquitous.

We also believe that Archer's technology positions EMC Global Services (EMCGS) to generate incremental consulting revenue as it relates to GRC strategy formulation, benchmarking, implementation and integration. GRC remains a highly consultative business, with two-thirds of the $30 billion industry being spent on services. With Archer as a beachhead, EMCGS will have an opportunity to create a lucrative GRC services practice around the technology. While this appears to be a logical outcome conceptually, it will require a focused effort on the part of Archer's executive team and EMC. GRC is an extremely complex domain that varies widely by vertical, legislation and customer. The successful pureplays have differentiated themselves by speaking the language of the customer's CRO, CFO, CCO or CISO more effectively than traditional software players. It will require a Herculean effort on the part of EMCGS to compete effectively with the specialists in this regard.

A more cryptic product synergy relates to the fit with the Documentum business line. Documentum's tools are frequently used in GRC related domains, particularly in situations where traditional ECM and BPM tools are used to address specific customer requirements. Documentum's acquisition of ProActivity provided robust process modeling tools, which are instrumental in GRC. That said, Archer was not built to address business-focused GRC. It has made solid progress in recent years in building out a more holistic enterprise GRC suite. However, it is still behind industry leaders BWise, Open Pages and Paisley (Thomson Reuters) in this regard. Given EMC's track record, we suspect that it will make a GRC acquisition that is a better fit with the Documentum business and can be seamlessly integrated with the Archer platform under a cohesive GRC umbrella.

Critical Mass in GRC – We believe that this transaction is exactly what the GRC sector requires to facilitate the long anticipated growth explosion in the industry. Compliance content players such as Thomson Reuters, Wolters Kluwer and Moody's have been aggressive acquirers on the business side of GRC. In the IT GRC area, there has not been a meaningful transaction of scale that involved an enterprise software acquirer since the acquisitions of Virsa and Logical Apps by SAP and Oracle, in 2006 and 2007, respectively. In typical EMC form, the software giant has once again led the market and established a front runner position in a sector that is characterized by colossal market demand.

Archer will benefit from EMC's broad distribution capabilities, marketing prowess, partner base and international data centers for those customers deploying SaaS. It also stands to gain from the strength of EMC's services and support teams, which will enable Archer to remain focused on building market awareness, improving the product set and integrating the offering across the EMC organization. If executed properly, EMC has an opportunity to bring GRC functionality deeper into the software ecosystem and wider into the marketplace. The caveat is that acquisition integration rarely goes this smoothly inside of large organizations such as EMC. The primary risk to the deal, in our view, is that Archer's vision is defocused as a result of the bureaucratic issues that plague most large software companies. GRC is far too complex and rapidly evolving for management to become distracted and competitors will catch up quickly if this dynamic prevails.

Customer Synergies – RSA President Art Coviello reported that customers have been asking for policy management, audit and compliance tools as a part of their broader security offerings. To address these requirements, RSA forged a partnership with Archer that has resulted in several joint customers in the financial services sector. As such, the combined value proposition was apparent from the outset – an arrangement that was likely a critical driver in the transaction and in the valuation. Archer's customers include 25 of the Fortune 100 - aligning with EMC gives the company firsthand access to most of the remaining 75. This is likely to generate tangible cross selling opportunities for the business.

Symbiotic Relationship Between GRC and SaaS – One of the primary growth impediments for the SaaS delivery model has been concern over security, data privacy and compliance. Given the nature of the buying audience in GRC (i.e. Chief Risk Officers, General Counsel, Chief Compliance Officers, Chief Security Officers, etc.), this trend is not surprising. Bridging security with GRC in a formidable enterprise solution is likely to appease many of the concerns that have slowed the widespread adoption of cloud based computing. It is logical to believe that the maturation of integrated GRC and security offerings will facilitate broader acceptance of the SaaS delivery model. In turn, the cost efficiencies of SaaS are likely to breed broader demand for hosted GRC solutions, particularly in the middle market. EMC is enviably positioned to lead the market in this regard.

Challenges for EMC

Lack of Domain Expertise – EMC's foremost challenge will be to provide first rate integration services and ongoing support for its GRC customers. Compliance software has historically required lengthy deployment cycles, customer hand holding and a network of software partners that provide integration into the broader software environment. The coordination of these efforts, coupled with the need to have dedicated GRC consultants that have relevant experience, creates complexities that are foreign to most software genres. EMC will need to scale this talent pool effectively to fully capitalize on the strength of Archer's offering.

Market Encroachment and a Fiercely Competitive Industry – The IT GRC market is highly competitive, a dynamic that historically has stretched sales cycles in the sector. There is a small handful of pureplays that offer product sets that are comparable in sophistication to Archer, including Agiliance, Modulo, Relational Security, SailPoint Technologies and

The GRC Software Landsacpe

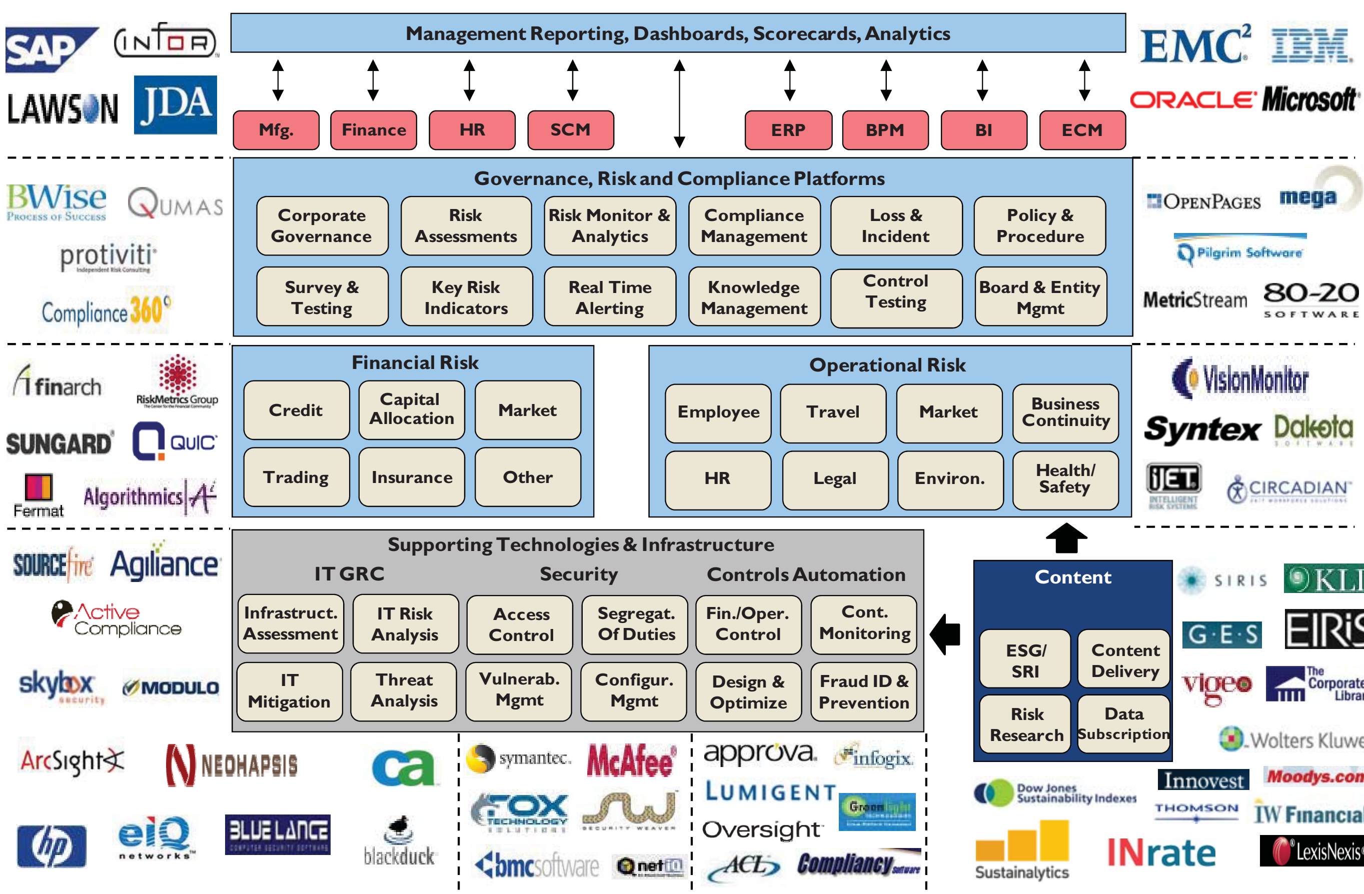

Diagram Source: Forrester; Logo Placement: TM Capital eIQnetworks. There are also larger vendors, such as Symantec and CA, which have made significant inroads in the IT GRC area with their broader infrastructure stacks. 2010 will be a pivotal year for the industry as product sets fully mature and sales execution becomes paramount. We expect that several of the smaller pureplay vendors will be acquired as a reactionary measure to the Archer deal.

Competitive Partnerships and Loss of Independence – In addition to RSA, Archer has partnered with security vendors McAfee and Symantec historically. It is likely that these partnerships will be phased out at some point, which may be disruptive to Archer's customer base depending on how RSA handles these relationships. More importantly, it is feasible that Archer's independence and security vendor agnosticism have created revenue opportunities historically. This may create hurdles going forward at customers whose loyalties lie with Symantec, McAfee, IBM or CA.

EMC's Acquisitions in 2008 and 2009

Date	Target	Description	Deal Size ($m)
09/01/09	Kazeon Systems Inc.	eDiscovery, security and GRC solutions	NA
08/31/09	FastScale Technology Inc.	Virtualization and provisioning solutions for enterprise class Web farms	NA
08/07/09	SpringSource Inc.	Software tools that build, run and manage Java applications	$446
06/01/09	Data Domain Inc.	Deduplication storage appliances for disk-based backup, archiving and network disaster recovery	$2,645
05/27/09	Configuresoft Inc.	Enterprise configuration management solutions	$87
01/02/09	SourceLabs Inc.	Open source infrastructure software systems	NA
11/26/08	Tungsten Graphics Inc.	Graphics software consultancy that develops graphics and infrastructure solutions on Linux	NA
10/31/08	Trango Virtual Processors	Embedded processor virtualization solutions	$64
09/30/08	Blue Lane Technologies Inc.	Vulnerability shields for physical and virtual server infrastructure	$15
05/28/08	B-hive Networks Inc.	Virtual environment management solutions	NA
04/04/08	WysDM Software Inc.	Data protection management software	NA
04/01/08	Conchango Plc	Consultancy with emphasis on application development and system integration	$83
03/10/08	Infra Corp. Ltd.	Web architected solutions that automate IT service management processes	NA
03/05/08	Iomega Corp.	Storage and network security solutions for small businesses	$211
02/21/08	Pi Corp.	Personal information management solutions	NA
01/15/08	Thinstall Inc.	Application virtualization software	NA
01/09/08	Foedus LLC	Virtualization infrastructure technologies and services	NA

Acquisition Indigestion – EMC acquired six businesses in 2009, including Configuresoft, Data Domain, FastScale, Kazeon, SpringSource and SourceLabs. This activity followed 11 acquisitions in 2008. Through M&A, EMC has successfully transformed its image from a data storage business into an end-to-end infrastructure management software vendor. Most of these acquisitions have been in areas where EMC was already present or in domains that were extensions of an existing solution. We argue that GRC is a fairly green area for EMC that is a full degree of separation from its traditional markets. EMC will need to pay particular attention to the integration of the business and ensure that it is not lost in the shuffle of the broader acquisition funnel.

Delivery Model – Archer currently uses IBM as its hosting partner for its SaaS customers. Although EMC has announced that these customers will not be affected by the transaction, it is likely that this will cause some disruption. EMC intends to phase in SaaS and hosting services to support Archer's multi-tenant architecture over time and the current plan is to offer customers multiple hosting provider alternatives, with EMC being one of the options. We suspect that EMC will find ways to encourage customers to make the transition. That said, their ability to manage the transition and retain customers throughout the process will have a meaningful impact on customer loyalty and attrition levels.

TM Capital Commentary and Industry Implications

In an era of heightened governmental oversight and the anticipation of an onslaught of new compliance initiatives in 2010, the GRC software sector is well positioned for sustainable growth in the coming years. These regulations are posing major challenges for boards, who continue to search for affordable, repeatable technologies that secure business information, control enterprise risks and comply with legislation. These underlying dynamics will continue to foster growth in the GRC market for the foreseeable future.

EMC's acquisition of Archer demonstrates its recognition of the addressable market opportunity in compliance. We believe that Archer represents the ideal target for EMC as its cornerstone acquisition in the space. This position is predicated on the basis that Archer represents the strongest, largest, IT GRC pureplay in the sector. Given EMC's historical reputation as a "boiler room" technology vendor, Archer was a logical selection if EMC was looking at compliance through an IT lens. We speculate that EMC will continue to build out its GRC platform with incremental acquisitions that are additive to the Archer suite. This consolidation is likely to occur in the business centric GRC area with targets that have the frameworks and process-based tools to address either specific forms of legislation or specific verticals. This acquisition needs to be led by the Documentum business unit so that EMC can bridge IT GRC and Enterprise GRC into a single, holistic platform that addresses the full spectrum of customer GRC requirements – from corporate policy all the way down through security controls. Ownership of a top flight, business-centric GRC platform would provide an "end run" option around players such as Oracle and Microsoft, who own infrastructure, systems and security components alongside their enterprise applications. It would also strengthen EMC's position against SAP, who has taken a highly transaction-centric approach to compliance software, leveraging controls automation extensions of its ERP system. We applaud EMC's foresight and first mover initiative, particularly if this is the opening move in a much larger chess match.

The net of these forces is a colossal "squeeze" that is being placed on the pureplay compliance industry – a trend that is expected to facilitate a shakeout in the space. Larger enterprise software acquirers will require the best-of-breed functionality, built-in domain expertise and vast services experience of an industry pureplay that has weathered the storm over the past decade and understands the constantly evolving compliance initiatives. This inertia will catalyze consolidation in the marketplace.

The good news is that there is a small handful of pureplays in the market with cutting-edge technologies, world class consulting teams and robust compliance suites that represent viable acquisition targets for the industry bellwethers. The bad news is that there is a much larger universe of buyers who recognize the importance of these solutions, many of which will miss the window.

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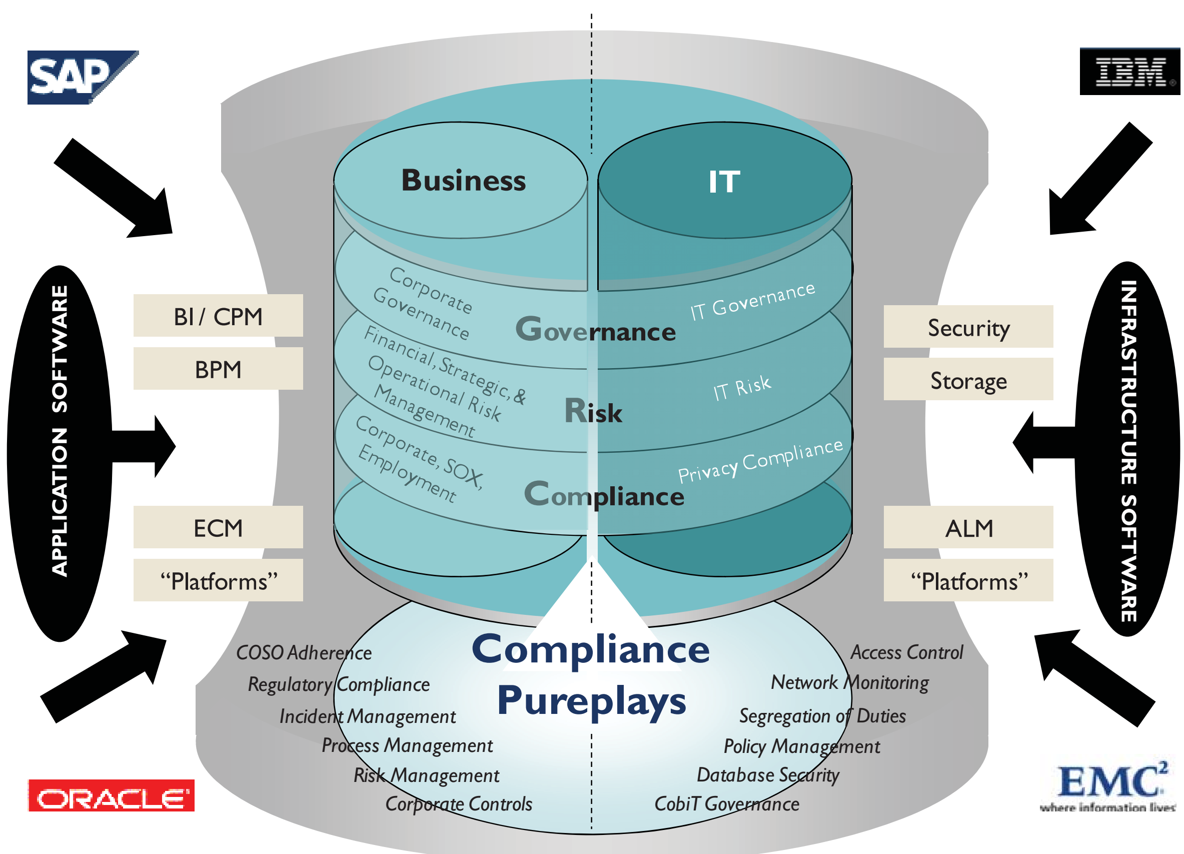
Pureplay GRC Squeeze



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