



## Think Technology: Closed Loop Customer Targeting

### Closed Loop Customer Targeting: Interview With The CEO Of Xactly

#### Reason for Report:

#### Industry Update

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#### THINK SUMMARY:

We had an opportunity to interview Chris Cabrera, Founder and CEO of Xactly, a leading provider of a sales performance management suite delivered as a service. The company's flagship product, Xactly Incent (sales compensation management), has gained a foothold across verticals especially with small- and medium-sized organizations (and increasingly with larger organizations), including PepBoys, Informatica, Cablevision, PayPal, Redback Networks, Data Domain, and John Hancock. Xactly's strategic product breadth that has been built out and integrated with Incent represents a source of differentiation and a lever for sales growth intermediate term, according to Mr. Cabrera. We see sales performance management as a key component of a broader closed loop customer targeting system, helping to drive alignment across an organization (sales, service, marketing, and other functional areas) to optimize sales performance.

#### KEY POINTS:

Xactly is a provider of an affordable, sales performance management suite delivered as a service. The offering is true multi-tenant, and the company's flagship product, Xactly Incent, addresses a significant pain point—compensation—that is ineffectively and inefficiently managed today in Excel, according to Mr. Cabrera. Usability appears to be a strong point, and Incent enables sales and finance executives to easily design, implement, manage, analyze, and optimize sales compensation management programs.

The company has gained a foothold across industry verticals and especially with small- and medium-sized organizations; the company's product vision could serve the company well as it pushes upstream with a more-strategic, broader value proposition.

The compensation solution market is less than 1% penetrated, largely because there has been no cost effective solution available, historically, according Mr. Cabrera. Demand drivers spurring spending decisions include increased focus on compliance issues and on improving sales productivity through improved visibility. Armed with on-demand/subscription pricing (which requires little upfront costs) and strong ROI proposition, Xactly appears well-positioned to tap the emerging opportunity.

Despite macro headwinds, Xactly has seen growing demand for automated compensation management solutions for companies of all sizes and is bullish on this trend increasing in the future, which likely reflects the health of secular trends, credibility of Xactly's offering, and the size of the opportunity.

We see sales performance management as a key component of a closed loop customer targeting system, helping to optimize alignment across an organization (sales, service, marketing, and other functional areas) and even outside an organization to optimize sales performance.

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Michael Huang, ThinkEquity (TE): Please explain your business, the problem you solve, and why customers and investors should care about Xactly?

Christopher Cabrera, CEO, Xactly (CC): If you look at what Xactly is about, it starts with compensation. Compensation is a tremendous pain area. It's an area that's completely managed today in Excel. But compensation is just the gateway that gets us to these customers and from there, we create a whole series of solutions that allow our customers to do analytics, non-cash rewards and, ultimately, sales management, and that's where Xactly becomes a very strategic vendor. We sell primarily to the finance organization, but it is always around sales performance and how to get sales people selling more stuff and being more effective.

TE: Are you focused on any vertical or segment of the market; Enterprise, small/midsize?

CC: Our application is extremely horizontal. Just about every company across every industry has sales people, which is a given, and the second given is that they're generally paying those people some type of variable comp, and the third given is that they're using Excel to manage it. So it's a very universal problem and cuts across segments and verticals. Having said that, I ran the worldwide sales and marketing organization at Callidus and it's a great company, and they have a great product, but they're very focused on the giant companies like Sprint, Verizon, and the DirecTVs, that are willing to pay \$5 million and have 100,000 users--that's not the market that Xactly is going after. We have artificially set a limit of 2,000 subscribers and below because that part of the market is so underpenetrated.

TE: And when you're talking subscriber base, is it the number of sales people or is it the number of users who are going to use?

CC: One of the great things about our solution is that it's not just for sales people. It's anybody and everybody within the company or even outside the company, who gets paid variably. And so, it absolutely includes all the sales people, but it also includes all the management up the chain, that's getting any kind of variable override and also the dealer network. So it's very common for salesforce.com and us to do a joint sale where they might pull say, 100 seats and we might get 130. Also, with our non-cash Rewards application, we see many different user types including, marketing teams, agents in call centers, support staff, etc.

TE: What are the other modules you offer besides compensation management, and who are the customers for these modules?

CC: We took modular approach because not all the customers need every one of our modules out of the box. So we want to be able to sell them our flagship product Xactly Incent, and then different modules, depending on what they want to do, what data they want to bring in, what kind of data management they need. We have modules for analytics, modeling, credit assignment, data management, and we recently launched a non-cash reward application, Xactly Rewards.

TE: In terms of product roadmap, are there any new products due out over the next year that we should be excited about?

CC: Absolutely. In addition to continuing to enhance our existing portfolio of products including our flagship product Xactly Incent, Xactly will continue to broaden its Analytics module to provide even deeper sales performance analytics including sales forecast accuracy, total cost of sales and post sales analytics to understand and explore what products were sold through which channels etc. In addition, Xactly plans to expand its non-cash Rewards, point-based incentive solution for broader application and distribution. Other planned modules include Quota and Territory Management solutions.

TE: Do you believe that compensation structure should or could be a source of differentiation for companies?

CC: I'm 100% convinced that compensation should be and can be a strategic weapon to differentiate competitors. I've visited Nike and Adidas, who you would think that they are selling effectively the same products to the same people through the same channels, but you will be amazed at how differently they compensate. There are a number of companies who dumb down their compensation structure, because their systems are Excel-based, and they'll pay the same compensation on all products, regardless of the profitability or the strategic importance of each product. We allow them to pay differently for different products and incent different behaviors, e.g., for discounting best practices. And that's where this becomes very strategic.

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TE: As more and more organizations embrace the sophisticated compensation management solutions, do you think that their competitive advantage via sales compensation structure is minimized?

CC: First of all, the penetration of compensation management solutions is miniscule. The three big companies have probably tapped 1% of the market or less and so, I don't think we're anywhere near a point where the differentiation is mitigated. Having said that, we have many companies, that are direct competitors, buy incentive compensation solutions from us. But then it's how you use the system and how you create the compensation plans. So, we're providing the vehicle and the tool to be able to create the plans, and it's all how they use it.

TE: What are the key demand drivers for Xactly?

CC: Compliance is a big one, and if you just do the back of the envelope math, let's say a 200-person company, paying say, \$50,000 per rep in variable comp, and you're talking about a \$10 million cost center that is not automated, has no audit trails, has known error rates. So, clearly compliance is one of the big drivers and we've had many CFOs buy our product primarily for compliance issues. The second and probably more exciting thing is that sales organizations are recognizing that if they can provide their sales people with some Web-based access so the sales people can see how they're doing, if they can provide better comp plans that drive better behavior, if they can create contests and to get the competitive juices going, they will be able see a dramatic increase in their top-line revenue. That's where the big draw is, these companies are trying to find ways to differentiate from their competitors and trying to get their sales people selling more stuff. And now, because we've cracked the code on doing this in an on-demand way and we've now made it affordable for every company of every size, that's why you're seeing this marketplace explode and why so many customers are flocking to Xactly.

TE: It seems like the value proposition is fairly well understood by customers. But, have people been budgeting for sales comp, and how does that compare to say a couple of years in the past and how would you expect that to trend over the next couple of years?

CC: A couple points, we're talking about a few thousand dollars a month with very little up-front cost. So, even if it's not budgeted, if we get to the right person, they immediately know that they need something like this. It's really more of a question of education. We're still at an early stage in this market, where people are not familiar that there is a solution that's affordable in this space. Our sales cycles are running about 92 days on average, which is ridiculously short. And so, we don't see budgets necessarily being a big issue.

TE: What is the kind of ROI that you've been able to deliver to your clients?

CC: ROI generally falls into three different buckets. You've got the savings from a finance perspective by reducing inaccuracies; you can manage these systems with less people. There's a lot of hard dollar savings which by itself justifies our system. The second area is increasing sales. By giving better visibility to sales people on what they can make by closing an additional five deals in this month, you can drive certain behavior and increase sales. The third area has to do with companies that have multiple product lines and they want to sell some products more than others.

TE: Help us understand what is your secret sauce and what makes your product special?

CC: There are a number of architectural differentiations; we are the only company in this marketplace with a true multi-tenant application; we're the only vendor in this space that has patented technology. And then there's just a lot of product road map differentiation. We're not looking at this just as a comp solution; we are looking at this as this much broader Sales Performance Management offering. We are adding quota and territory management and price management and some forecasting planning. The secret sauce is that we have cracked the code on a rules-based, multi-tenant application that creates this data mart and allows us to deliver these additional modules. Nobody else is talking about a roadmap like that. Nobody is viewing the market the way we view it and nobody else is getting the traction that we're getting.

TE: Who represents your greatest competition currently, and looking out a couple years, who could represent the strongest competition?

CC: The strongest competition across all industries is non-automation, or companies managing the very complex process of sales compensation in spreadsheets. Some of the shortcomings of spreadsheet-based sales compensation management include its error-prone nature, the lack of meaningful reporting and analysis capabilities and how it handicaps sales ability to

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collaborate and share information designed to motivate behavior and results. Looking out a couple of years, we still see this as the primary competition. In the wings, we see the legacy, on-premise vendors jumping on the "on-demand" bandwagon with hosted solutions attempting to automate sales compensation at a far greater risk to customers without the true benefits of a 100% SaaS sales performance management solution.

TE: Do you believe that performance management is a standalone suite of products or do you see it rolled into one with kind of CRM application?

CC: Certainly these are opportunities for us to do deeper stuff and broaden our platform, which to me is a standalone business. You're talking about well over \$100 per subscriber per month and if you look at the traction that we're getting in the marketplace, every single customer that has a CRM application is a candidate. So, I cannot be convinced that this isn't a standalone market, and that's just for the sales compensation product. Then you start adding these other things: the quota and the territory management and it becomes much bigger. At the same time, our customers are different from CRM customers. We sell to finance and they're not CRM users. So, it's not something that would be a natural up-sell for example, for Salesforce.com. It really is a different area.

TE: What is your sales model?

CC: We go to market with inside sales as well as field sales; we've got some great partnerships, and now we're working with a couple reseller partners.. For small opportunity, say, a 50-person company, we can generally handle that entirely on the telephone in a short selling cycle. If we're talking to a Fortune 500, that's probably going to be a little bit longer selling cycle and probably require a face-to-face visit. Every one of our customers pays us at least one year in advance; often we're getting two and even three years in advance.

TE: Help us understand your view on infrastructure investment for building redundancy and security.

CC: One of the decisions we made early on, and this is another area that differentiates us from competitors, is that we recognize that we do have the family jewels in terms of the data we aggregate for our customers to automate the process of compensation. And so right from the start, we used a telco-grade hosting facility on the West Coast, and we are the only vendor in the space that has both a type I and type II SAS70 certification for security and redundancy. We've closed many deals, especially with the larger public companies--in large part because our customers realize that their data is more secure at our data center than where they keep it themselves.

TE: Given macro headwinds, what type of impact either negative or positive have you seen on the business?

CC: Given the overall economy and the recent news of a recession, now more than ever, companies of all sizes need to deliver greater performance from their front-line sales personnel. Xactly is uniquely positioned to help companies be more successful in driving top-line results. As companies look to reduce their bottom-line expenses and maximize their top-line revenues, sales performance management solutions can help companies motivate behavior to improve performance. We have seen a growing demand for automated compensation management solutions for companies of all sizes and are bullish on this trend increasing in the future.

TE: Could you give us a sense of size of company in terms of headcount? How fast have you been growing, and what do you expect next year?

CC: Xactly is a 3.5 year old company with about 100 employees today in the U.S. and EMEA. We have seen steady, high-double-digit headcount growth in the past two years and expect to see even greater growth in the coming quarters.

TE: Where is the biggest challenge for you over the next couple years?

CC: I think it's just market awareness. We need to get the word out to those sweet spot companies which are these two- and three-hundred person sales teams to know that (a) there's a system out there and (b), there is a great return on it. We're still scraping and clawing to evangelize and get customers, and we need to get this thing to be more mainstream and that's just a process of educating everybody. These organizations have been doing compensation management in Excel for their whole history and they just have no notion that there's a solution out there, or if they do and they've looked at it in the past



and it was a million dollars. So part of it is just getting them to understand that there's an affordable solution out there.

TE: Thank you for your time and perspectives.

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Company	Exchange	Symbol	Price	Rating	Price Target
Data Domain, Inc.	NASDAQ	DDUP	\$16.25	Buy	\$30.00
salesforce.com, Inc.	NYSE	CRM	\$29.07	Buy	\$36.00

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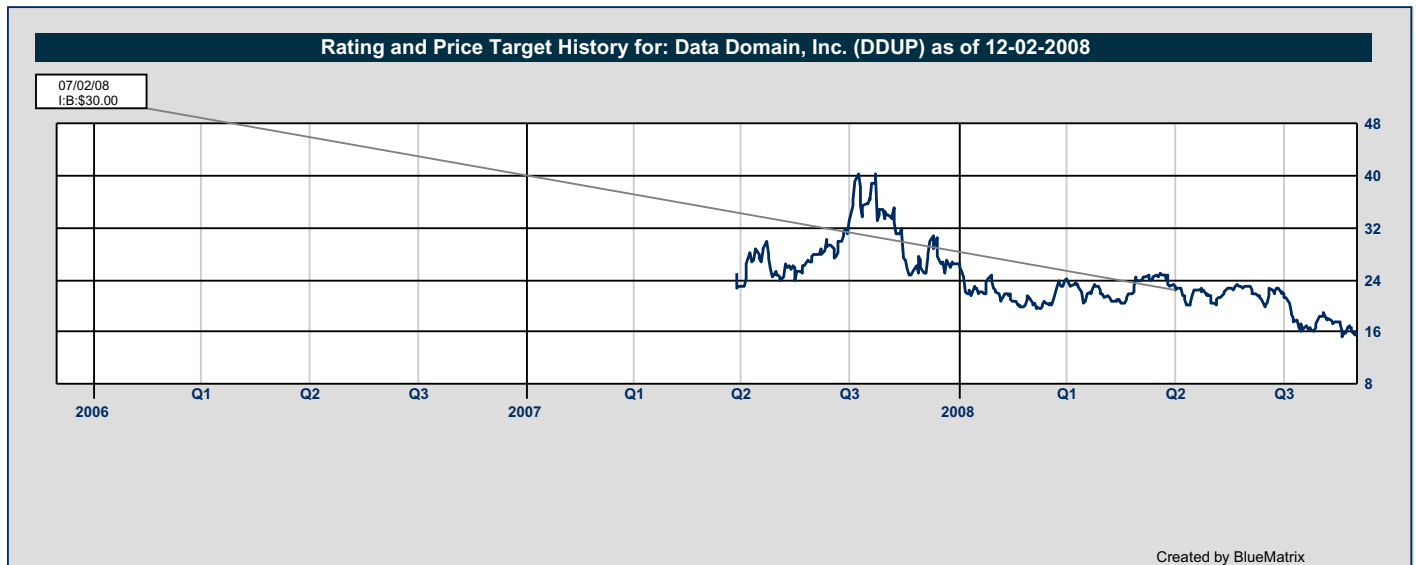
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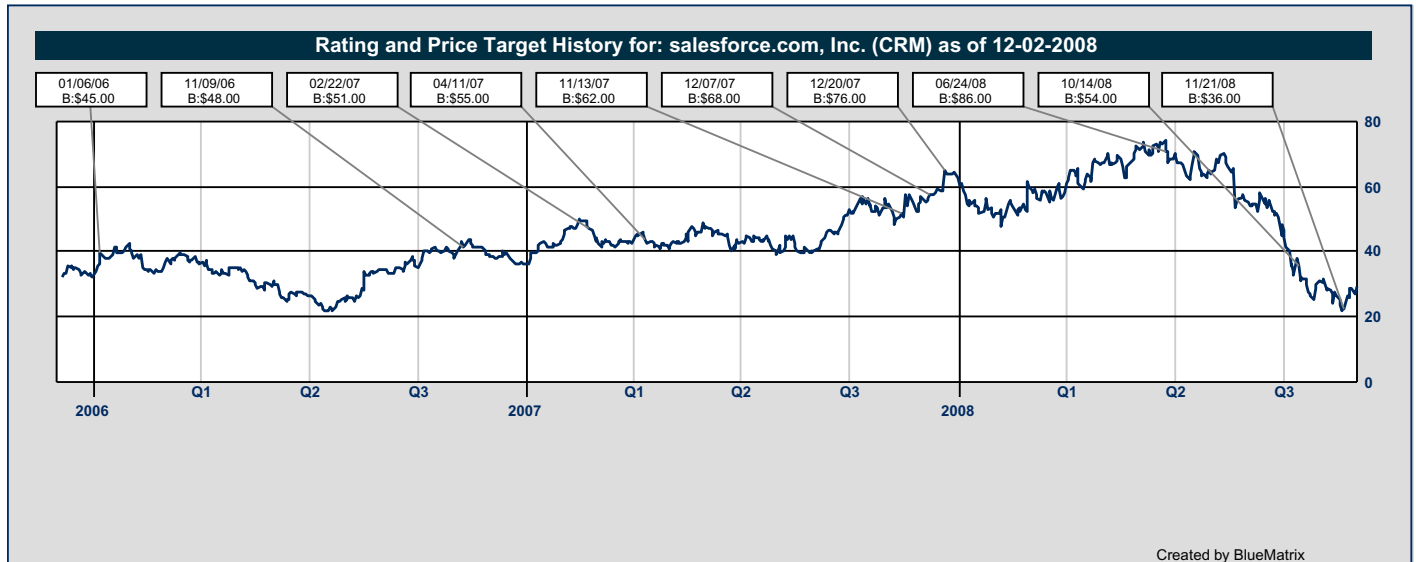
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Rating	Count	Percent	IB Serv./Past 12 Mos.	
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