

May 17, 2010

Software

Changing Consumer Security Economics: The Rise of Free

Conclusion: The rising importance of distribution plus the rapid penetration of free solutions into the consumer security software market is likely to further deteriorate profitability for paid vendors like MFE and SYMC, which see 35%+ of op. income from consumer. Free options have been available for some time, however our data points to 3 recent catalysts: 1) low cost/free alternatives have improved in quality, 2) consumers are more aware of low cost/free options and give free distribution higher priority in their purchase decisions, and 3) increasing saturation within consumer security. While the current PC cycle may represent a near-term tailwind for consumer security, the longer-term difficulty in sustaining the economics of these businesses likely pressures multiples for both firms. We are now neutral on both MFE and SYMC (see our separate note downgrading MFE).

Our survey of 2,500 US consumers revealed:

- 92% use security software on their home PCs, with 46% using free products.
- Overall renewal rates of 77% are solid, but 56% of non-renewals are moving to free solutions and 27% are turning off their security software, compared to just 17% moving to a competitive paid solution.
- 12.6% expect to move to a free solution when their current subscription expires vs. 5.4% moving to paid, suggesting a continued migration to free.
- Free trials were cited as the #1 reason for choosing consumer security software (26% of users), illustrating the importance and likely increasing competitiveness of distribution deals.

Where we differ: Renewal and conversion rates are key drivers of consumer security distribution profitability. Using our survey to hone our ests, we find that recent deals like MFE/Dell likely yield mid-20's contribution margins today. With their next PC purchase, only 47% of consumers plan to use their current security vendor, while 27% will use what ships on the PC, so distribution deals will likely remain very competitive.

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Changing Consumer Software Economics: The Rise of Free

Our recent survey of 2,500 US consumers highlights the changing economics within the highly penetrated consumer security market, changes we believe will continue to pressure profitability for paid vendors in the space. The rising importance of free trials for consumer security software is forcing vendors to compete aggressively for distribution deals. At the same time, the rapid penetration of free solutions is slowly shrinking the market of paying customers. Combined, these trends will likely exert negative margin pressure on the consumer security vendors for some time. Consumer security represents 37% and 31% of revs. for MFE and SYMC respectively, and between 35-40% of operating income for both firms. The 15%+ YoY unit growth we expect in the current PC cycle represents a near-term tailwind for consumer security billings growth, but the longer-term difficulty in sustaining the economics of these businesses will likely weigh on the multiples for both firms. Thus, we are taking our rating on MFE from Overweight to Equal-weight, inline with SYMC.

Survey Key Takeaway

We conducted a survey of 2500 US adults age 18+ using an Internet methodology in April 2010. The sample is balanced to be representative of the US adult population in terms of age, income, gender, and geography. Key takeaways include:

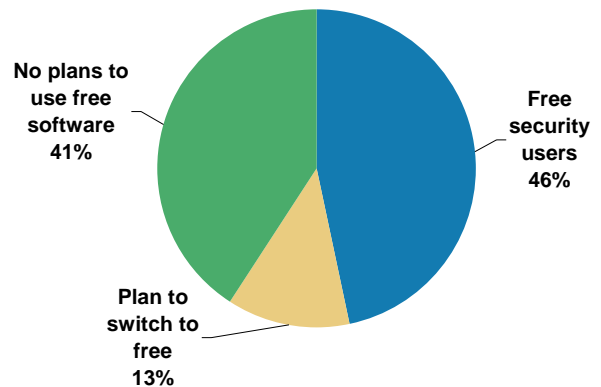
- **Consumer market will be largely driven by free solutions or distribution deals:** Free trials were the #1 reason cited for choosing consumer security software and 27% of consumers expect to use “what ships on their computer” when purchasing their next PC.
- **Free already a big factor in a saturated consumer security market:** >92% of consumers are currently using some security software, of these 46% report using free products today.
- **Migration to free expected to continue:** 12.6% of all users expect to move to a free solution vs. just 5.4% expecting to move to a paid solution. This implies a net 14% decline in the paid user base over the next 3 to 4 years.
- **Renewals higher than expected, but paid base is shrinking:** Overall industry renewal rates were solid at 77%, but the majority of non-renewals are moving to free solutions (56%) or turning off their security solutions (27%) vs. moving to a competitive paid solutions.

The Rise of Free

A new breed of security vendors have emerged, leveraging internet marketing and free-to-paid models to garner a large user bases. We were surprised to find 46% of U.S. consumers in our survey reporting to use free security software today. This includes both users of truly free software like avast! or Microsoft Essentials (23% of users) and consumers using free trials of paid software programs like McAfee and Norton (18% of users). Many of these free-to-paid consumer security vendors originated in Europe and we had assumed their large user bases were also in international markets. But 67% of US consumers reported being aware of free consumer security offerings and 37% had considered using an offering from a free vendor. This also speaks to the compelling value proposition of the free offerings as the current free user base at 23% of total users represents almost 62% of those who have considered using a free offering.

Exhibit 1

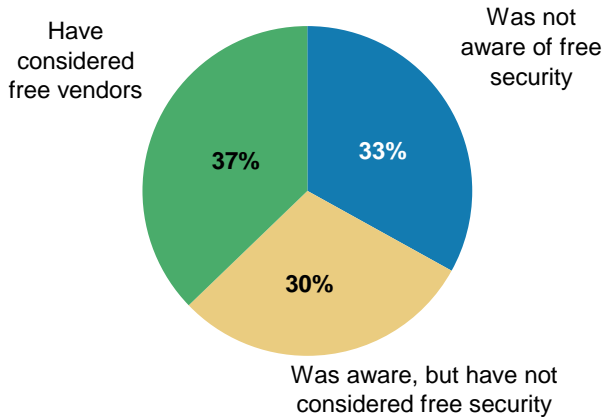
46% of Consumer Security Software Users Report Currently Using Free Versions – an Additional 13% Plan to Switch to Free



Source: Morgan Stanley Research, Alphawise

Exhibit 2

37% of Consumers Have Considered Using Software From Free Security Vendors



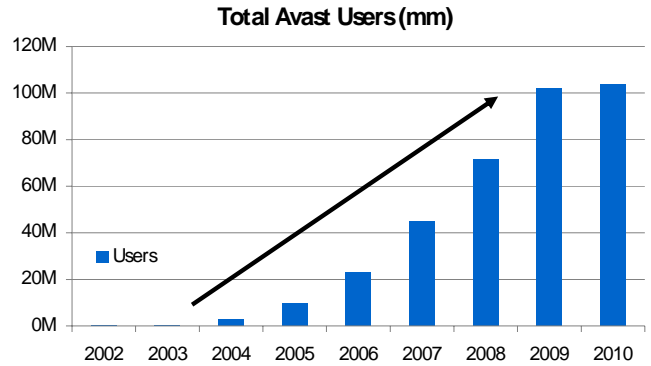
Source: Morgan Stanley Research, Alphawise. Note: Due to multiple responses, percentages may total to more than 100%.

The free-to-paid business model is not a new concept, however adoption of strategy within the broader software market has accelerated in recent years. With the help of low-cost online marketing, the free-to-paid model is being effectively implemented in new and disruptive ways to drive significant top-line growth. Free-to-paid security vendors generally offer entry-level free products, such as anti-virus and anti-spyware protection with the intention of up-selling and cross-selling paid product and services. The low-end solutions are offered for free to lower the barriers to product adoption and cultivate a user base into which paid products can be marketed. Having users who are familiar with and actually using the vendor's products helps to greatly reduce the sales efforts needed for the paid products.

Privately held avast!, an exceptionally fast growing security company, is a good example of the advantages gained from free-to-paid distribution. avast!'s dramatic growth in the security space has been primarily driven by its booming and active user community. By leveraging the benefits of the free-to-paid model, the company has been able to grow a 110M+ user-base in roughly 6 years, which serves as the basis for driving adoption of premium, paid products, technical advancement and community generated marketing.

Exhibit 3

Rapid Growth of the Avast User-Base is Key in Driving the Success of the Co's Free-To-Paid Model



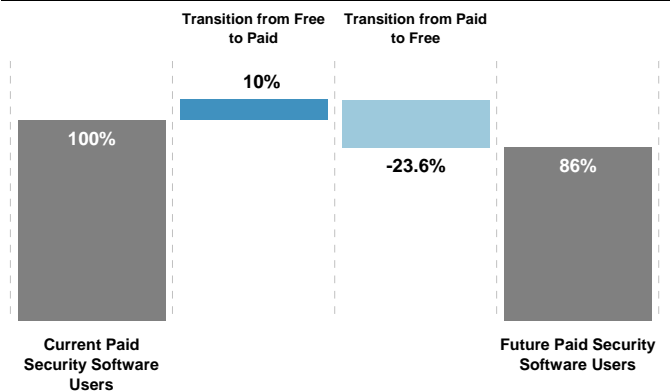
Source: Company data, Morgan Stanley Research

Slow Bleed of the Paid User Base

8% of current security users reported planning to move to a free solutions on their current computers and another 5% planning to switch to free offerings when they buy a new computer. This compares to 5% of current free users planning to move to a paid offering and 3% of users planning to begin using a paid offering when they purchase a new computer. Looking at this in context of the current paid security base within our survey (54% of respondents), this would represent a 10% increase in the paid base as users migrate from free to paid, but a 24% reduction from migration to free products. Together this implies 14% decline in the paid user base over the next 3 to 4 years.

Exhibit 4

More Consumers Expecting to Transition From Paid to Free Offering, Which Results in a Net 14% Decline in Paid Security Software Users

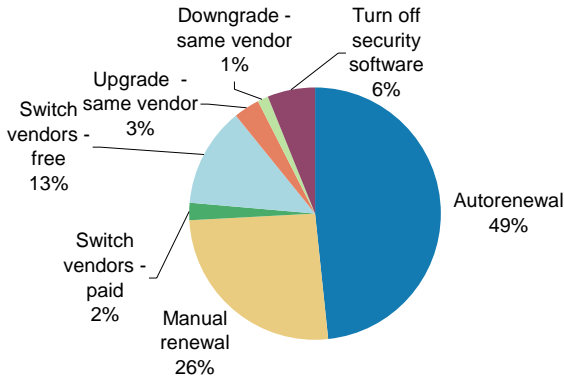


Source: Morgan Stanley Research, Alphawise

May 17, 2010
Software

Exhibit 5

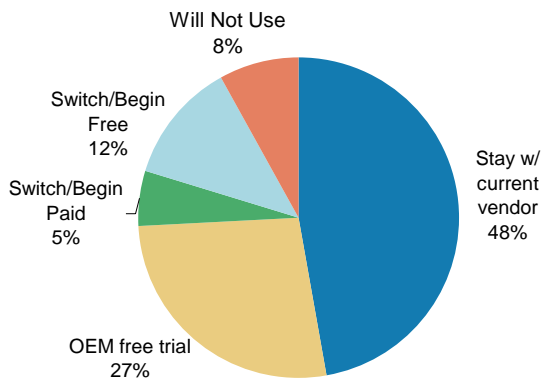
77% Renewal Rates Are Positive, but Non-Renewals Are Going to Free Solutions or Turning off Security Software versus Moving to another Paid Solution



Source: Morgan Stanley Research, Alphawise

Exhibit 6

Vendor Relationship Sustains Through New PC Purchases Less than 50% of the Time



Source: Morgan Stanley Research, Alphawise

Increasing Importance of Distribution

Distribution is now becoming increasingly important as differentiation in consumer security offerings becomes less apparent. Our survey results show distribution has come to trump performance or feature/functionality in consumer purchasing habits for endpoint security.

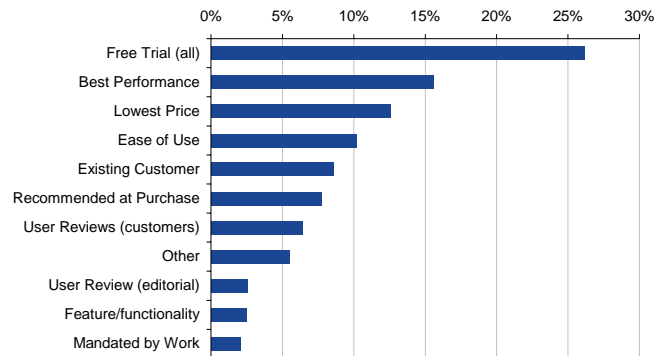
Free trials was the most cited number 1 reason for choosing a consumer security product. At the same time, independent lab tests fail to show significant differentiation between free and paid vendors in terms of product performance or effectiveness — and none of the products are 100% effective. Bottom line,

it's difficult for the consumer to readily identify a clear winner that consistently beats peers on performance and functionality and therefore it's easy for the consumer to go with the default choice on their PC.

Our survey shows that consumers most often choose to go with the vendor offered with their PC purchase **with 26% of respondents citing a free trial (either from an OEM, ISP, or other, such as a bank) as the number one reason for choosing their current consumer security software.** Richness of features and functionality ranked low, with only 3% citing it as the number one reason for choosing their software.

Exhibit 7

Free Trials are the Most Often Cited #1 Reason for Choosing Consumer Security Software



Source: Morgan Stanley Research, Alphawise. Note: Free trial responses include free trials from OEMs, ISPs, and others.

Only 47% of consumers plan to continue using their current security vendor after their next PC purchase, while 27% will use what ships on the PC, so distribution deals likely remain very competitive going forward. At the same time our survey suggests ~5-7% of the market is moving to free solutions annually, which could pressure renewal rates and conversion rates going forward.

How PC OEM distribution works

PC OEMs are the primary distribution channel for major consumer software security vendors like SYMC and MFE, contributing 60-70% of new customers, by our est. These partnerships are likely a source of high incremental profit margin for PC OEM manufacturers and their strategic importance to software companies gives advantages to PC OEMs in deal negotiations, which has caused pricing to erode — impacting consumer margins longer term. While MFE was more aggressive in 2008 forming partnerships, SYMC has re-asserted itself recently, announcing new partnerships with Samsung and Fujitsu on their last earnings call.

May 17, 2010
Software

Exhibit 8

Current Landscape of Top 10 PC OEMs Partnership With Consumer Security Software Companies

| | Asia, xJ | Japan | EMEA | NoAmer | LatAm |
|----------------------|----------|-------|------|--------|-------|
| HP | S | S | S | S | S |
| Acer | M | M | M | M | M |
| Packard Bell Gateway | S | S | S | S | S |
| Dell | M | M | M | M | M |
| Alienware | S | S | S | S | S |
| Toshiba | O | O | M | S | O |
| ASUS | S | S | S | S | S |
| Lenovo | M | M | M | M | M |
| Thinkpad | S | S | S | S | S |
| Sony | O | M | O | S | O |
| Samsung | S | S | S | S | S |
| Fujitsu | S | S | S | S | S |

Source: Company data, IDC, Gartner, Morgan Stanley Research. Note: 1) S = Symantec, M= McAfee, O = Others such as Trend Micro, 2) Apple has been excluded from the list. 3) Partnerships span desktops, laptops, and netbooks in most cases. 4) Symantec's partnership with ASUS is for netbooks only 5) Symantec's partnership with Samsung is for notebooks and netbooks only

PC OEM manufacturers pre-install software like security software for trial use on each PC (desktops, laptops, and netbooks) shipped. For these software packages, OEMs tend to partner with companies that offer the OEM not only good economics but also help differentiate their PCs in the market. When consumers buy new PCs they may elect to use these software packages for a limited period, typically 30-90 days, before they are enticed into purchasing the software. The economics of these partnerships are dependent on several variables and can be a combination of an upfront payment, payment for every shipment, payment for every registration or activation of trial software, or a revenue share arrangement based on the actual purchase price.

MFE typically pays OEMs upfront for deals, which means activations are quickly profitable. SYMC, on the other hand, bears expenses associated with units shipped in advance of activation – which means they may see margins pressured as the PC market accelerates. As PC volumes improve, the structure of the deals becomes more important – and MFE may see an earlier benefit from a PC recovery than SYMC.

HP's contract with SYMC is estimated to be up for renewal in 2011 and SYMC's management has stressed that the company will only do deals that make economic sense for SYMC. We think both SYMC and MFE will be rational about pricing, but will compete aggressively – and we could see the deal renew in CY10.

Profitability Framework for PC OEM Distribution Deals

While we do not know all the details of the large PC OEM distribution deals that MFE or Dell have signed, we have put together a profitability framework based on our best estimates to try to understand the sensitivities of key variables and give our best effort in assessing the economics of these deals. The key variables in our view include; average price, renewal rate, conversion rate, average customer life and of course the cost of the distribution deals. The survey results suggest average pricing around \$45 for paid consumer security, renewal rates of ~77%, conversion rates from free trials to paid offerings between 6-8% and an average lifetime for subscriptions between 3.5 to 4 years. These assumptions are included in the profitability framework below, sensitivity analysis follows in exhibit 4.

Exhibit 9

Estimated Economics of the MFE/Dell OEM Deal

| Assumptions: | |
|---------------------------|-------|
| Average Price | \$45 |
| Average Renewal Price | \$45 |
| Renewal Rate | 77% |
| PC Units/Year (M) | 10 |
| Conversion Rate | 7% |
| Contract Cost (3 Yr, \$M) | \$150 |
| Avg. Customer Life (yrs) | 4 |

| | Year 1 | Year 2 | Year 3 | Year 4 | Year 5 | Year 6 | Total |
|--------------------------|------------|------------|------------|------------|------------|------------|------------|
| PC Units Shipped (M) | 13.0 | 13.7 | 14.3 | | | | 41.0 |
| Conversion Rate | 7% | 7% | 7% | 7% | 7% | 7% | 7% |
| Renewal Rates | | 77% | 77% | 77% | 77% | 77% | 77% |
| Year 1 Subscribers | 0.9 | 0.7 | 0.5 | 0.4 | | | 2.6 |
| Year 2 Subscribers | | 1.0 | 0.7 | 0.6 | 0.4 | | 2.7 |
| Year 3 Subscribers | | | 1.0 | 0.8 | 0.6 | 0.5 | 2.8 |
| Total Subscribers | 0.9 | 1.7 | 2.3 | 1.8 | 1.0 | 0.5 | 8.1 |
| Average Price | \$45 | \$45 | \$45 | \$45 | \$45 | \$45 | \$45 |
| Total Billings | \$41 | \$75 | \$103 | \$79 | \$46 | \$21 | \$364 |
| Gross Margin | 85% | 85% | 85% | 85% | 85% | 85% | |
| R&D/G&A as % of Revs | 20% | 20% | 20% | 20% | 20% | 20% | |
| Contract Cost | \$150 | \$0 | \$0 | \$0 | \$0 | \$0 | \$150 |
| COR / Opex | \$14 | \$26 | \$36 | \$28 | \$16 | \$7 | \$127 |
| Cash Contribution | (\$123) | \$48 | \$67 | \$51 | \$30 | \$13 | \$87 |
| Cash Contribution Margin | -301% | 65% | 65% | 65% | 65% | 65% | 24% |

Source: Company data, Morgan Stanley Research

Exhibit 10

OEM Profitability — Sensitivity Analysis

Assumptions: \$150 million contract cost, 13 million annual units shipped, 35% COGs / Opex and 3 year average life

| | | Renewal Rate | | | |
|-----------------|-----|--------------|--------|--------|--------|
| | | 65% | 70% | 75% | 80% |
| Conversion Rate | 4% | -28.1% | -22.8% | -17.9% | -13.3% |
| | 5% | -8.5% | -4.3% | -0.3% | 3.3% |
| | 6% | 4.6% | 8.1% | 11.4% | 14.4% |
| | 7% | 13.9% | 16.9% | 19.8% | 22.4% |
| | 8% | 20.9% | 23.6% | 26.0% | 28.3% |
| | 9% | 26.4% | 28.7% | 30.9% | 33.0% |
| | 10% | 30.8% | 32.9% | 34.8% | 36.7% |

Assumptions: \$150 million contract cost, 13 million annual units shipped, 35% COGs / Opex and 4 year average life

| | | Renewal Rate | | | |
|-----------------|-----|--------------|--------|-------|-------|
| | | 65% | 70% | 75% | 80% |
| Conversion Rate | 4% | -21.6% | -15.3% | -9.4% | -3.9% |
| | 5% | -4.3% | 0.8% | 5.5% | 9.9% |
| | 6% | 7.2% | 11.5% | 15.4% | 19.1% |
| | 7% | 15.5% | 19.1% | 22.5% | 25.6% |
| | 8% | 21.7% | 24.9% | 27.8% | 30.6% |
| | 9% | 26.5% | 29.3% | 31.9% | 34.4% |
| | 10% | 30.3% | 32.9% | 35.3% | 37.4% |

Assumptions: \$150 million contract cost, 13 million annual units shipped, 35% COGs / Opex and 5 year average life

| | | Renewal Rate | | | |
|-----------------|-----|--------------|-------|-------|-------|
| | | 65% | 70% | 75% | 80% |
| Conversion Rate | 4% | -15.5% | -8.3% | -1.7% | 4.5% |
| | 5% | 0.6% | 6.3% | 11.7% | 16.6% |
| | 6% | 11.3% | 16.1% | 20.6% | 24.7% |
| | 7% | 19.0% | 23.1% | 26.9% | 30.4% |
| | 8% | 24.7% | 28.3% | 31.7% | 34.8% |
| | 9% | 29.2% | 32.4% | 35.4% | 38.1% |
| | 10% | 32.8% | 35.7% | 38.3% | 40.8% |

Source: Company data, Morgan Stanley Research

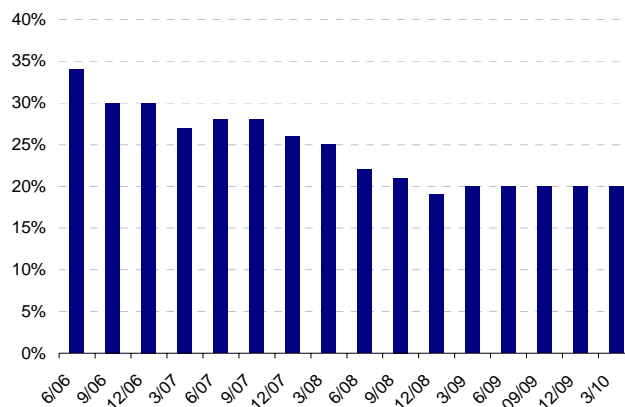
Retail exposure has been declining.

We have seen a marked shift in the consumer purchasing behavior over the last several years in terms of where they acquire security software. In the past, consumers typically bought security software products from traditional brick and

mortar retail stores like Best Buy or e-tailers like Amazon. However, this trend seems to have changed with more consumers now acquiring their security software either 1) directly from security vendors online stores, 2) activating trial version of pre-installed software that ships with new PCs, or 3) downloading software from business partners such as ISPs (AT&T, Comcast) and banks (Bank of America). As such, retail exposure has been on the decline. The retail channel contributes ~20% of consumer revenue for Symantec today down from ~35% 4 years ago, while McAfee garners <10% of consumer revenues from traditional retail channels. This shift also increases the relative importance of the PC OEM, ISP and other business partner distribution deals.

Exhibit 11

Retail Exposure For Symantec Has Declined To ~20% of Consumer Revenue from ~35%



Source: Company data, Morgan Stanley Research

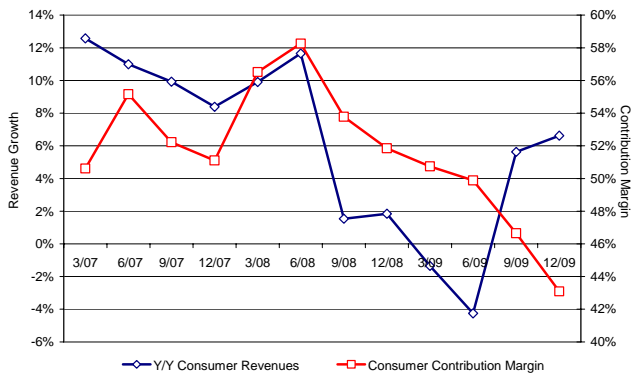
Partnerships with top 10 PC OEMs are increasingly important for market share, but eroding margins.

The top 7 PC OEMs shipped roughly 60% of the 159M consumer PCs (desktops, laptops, and netbooks) that were shipped worldwide during 2009, according to IDC. Three years ago Symantec enjoyed both ~50% market share within the paid consumer security market and contribution margins in that business in excess of 55%. At the same time McAfee garnered <20% market share with contribution margins of ~30%. In our view, the rising influence of distribution deals in consumer's security purchase decisions made Symantec's positioning difficult to defend. McAfee recognized this opportunity and became increasingly aggressive in striking OEM distribution deals, effectively doubling the percentage of PCs which ship with a trial version of their software from ~20% to ~45% within the top 10 PC OEMs. In order to defend their market share Symantec has had to get more aggressive with distribution deals, which was a large contributor to the nearly 14% point

May 17, 2010
Software

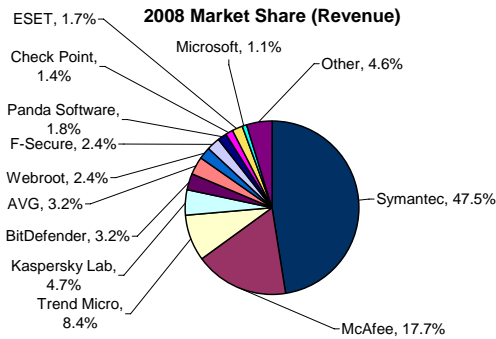
decline in contribution margins seen during this period. In Q4, SYMC announced new deals with Samsung and Fujitsu which should further weigh on margins in the short-term, as SYMC tends to take an upfront expense on OEM PC sales while revenue benefit comes 6-9 months as new users upgrade from trial to paid Norton products.

Exhibit 12
SYMC Consumer Margins Have Been Eroding For the Past 6 Quarters



Source: Company data, Morgan Stanley Research

Exhibit 13
IDC Paid Consumer Security Software Market Share



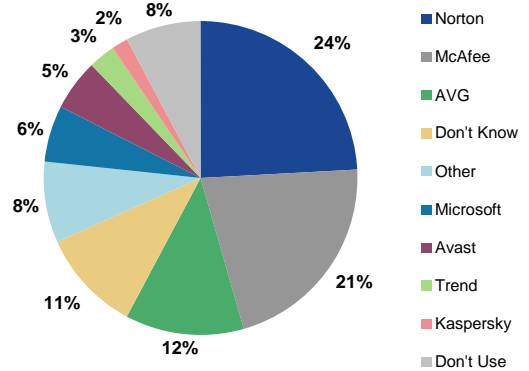
Source: IDC, Morgan Stanley Research

Consumer security is a saturated market

Our survey shows that 92% of respondents currently use some security software today, illustrating little room remaining for green field expansion in the consumer base, particularly within

developed markets. Our estimate of the consumer user bases for the top 15 vendors at ~120% of the total consumer installed PC base further highlights this saturation. With an equal number of consumers intending to turn off security software (8%) and to begin using security software (8%) with the purchase of their next PC, further penetration of the base appears limited.

Exhibit 14
92% of Respondents Report Using Consumer Security Software



Source: Morgan Stanley Research, Alphawise

Exhibit 15
Consumer Security Seems to Be Oversaturated

| | Users (millions) | Est. Corporate Endpoints | Est. Consumer Endpoints |
|---------------------------------|------------------|--------------------------|-------------------------|
| Symantec | 101 | 45 | 56 |
| McAfee | 57 | 30 | 27 |
| Trend Micro | 80 | 38 | 42 |
| Kaspersky | 300 | 111 | 189 |
| Sophos | 100 | 100 | 0 |
| AVG | 110 | 11 | 99 |
| F-Secure Corp. | 16 | 6 | 10 |
| BitDefender | 69 | 12 | 57 |
| Panda Software | 15 | 8 | 7 |
| ESET | 14 | 6 | 8 |
| Webroot | 7 | 2 | 5 |
| Avast | 110 | 11 | 99 |
| CA | 10 | 8 | 2 |
| AVIRA | 100 | 10 | 90 |
| Microsoft | 12 | 0 | 12 |
| Total Endpoints | 1100 | 397 | 703 |
| 2009 Est. PC Installed Base (M) | | 633 | 588 |
| Endpoint Penetration | | 63% | 120% |

Source: Company data, Morgan Stanley Research. PC data from IDC, May 2009. Does not include smaller endpoint vendors and therefore is underestimating penetration.

Exhibit 16

Consumer Security Landscape

| | Products | Anti-Virus | Spyware | Anti-Spam | Firewall | Rootkit Detection | Identity Protection | Secure Backup | List Price | PC World 2010 Review |
|------------------------------|-----------------------------------|------------|---------|-----------|----------|-------------------|---------------------|---------------|----------------|----------------------|
| Example Free Offerings | AVG Anti-Virus Free Edition | ✓ | ✓ | | | | | | Free | Not Rated |
| | avast! Free Home Edition | ✓ | ✓ | | | ✓ | | | Free | Not Rated |
| | FortiClient Standard | ✓ | ✓ | ✓ | ✓ | ✓ | | | Free | Not Rated |
| | Microsoft Security Essentials | ✓ | ✓ | | | | | | Free | Not Rated |
| Example Paid Security Suites | PC Tools Internet Security 2010 | ✓ | ✓ | ✓ | ✓ | ✓ | | | \$49.95- 3 PCs | 4 stars |
| | AVG Internet Security 9.0 | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | | \$54.99- 1 PC | 4 stars |
| | Webroot Internet Security | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | \$59.95- 3 PCs | 3.5 stars |
| | BitDefender Internet Security | ✓ | ✓ | ✓ | ✓ | ✓ | | | \$49.95- 3 PCs | 3.5 stars |
| | F-Secure Internet Security 2010 | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | | \$59.99- 3 PCs | 3 stars |
| | Norton Internet Security 2010 | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | | \$69.99- 3 PCs | 4.5 stars |
| | McAfee Internet Security 2010 | ✓ | ✓ | ✓ | ✓ | ✓ | | ✓ | \$34.99- 3 PCs | 3.5 stars |
| | Trend Micro Internet Security Pro | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | \$69.95- 1 PC | 3.5 stars |
| | Kaspersky Internet Security 2010 | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | | \$79.95- 3 PCs | 4.5 stars |

Source: Company data, PCWorld.com

Increasingly competitive distribution deals + rising penetration of free = declining economics

When asked what is their most likely consumer security purchase when they acquire their next computer, 27% of respondents reported they will use the software which ships on the new machine and 48% will continue to use their current vendor. With essentially a quarter of their user base up for grabs as consumers refresh their PCs, competition for OEM distribution deals will remain competitive. At the same time, free offerings continue to shrink the paid opportunity within this heavily saturated market. Bottom-line in our view, economics in the consumer security business are likely to continue deteriorating. McAfee and Symantec's consumer businesses make up ~37% and ~30% of total revenue, respectively and between 35-40% of operating income for both vendors. While the current PC cycle represents a near-term tailwind for both vendors, in the medium to longer-term, the deteriorating economics likely pressures both businesses and, in our view, suppresses potential multiple expansion for both stocks.

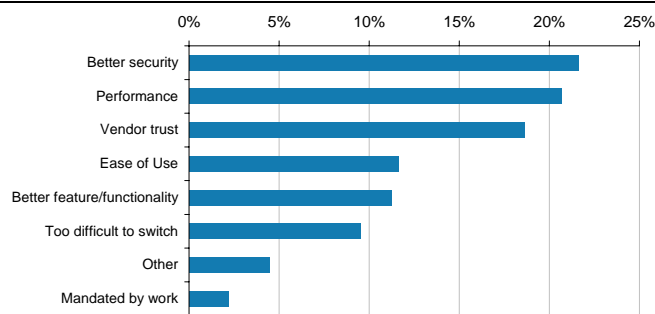
How do the traditional AV vendors win?

Forge relationships that go beyond the PC. The most often cited reasons for staying with a paid vendor were "better security" and "performance". However, these rationales are not particularly well supported by independent lab tests which

show limited differentiation in terms of the effectiveness of anti-virus solutions from most of the major vendors (free or paid) and actually report better performance from some free solutions (Microsoft and avast!) than McAfee or Symantec. In our view, traditional AV vendors must aggressively transition their customer bases towards product suites which extend beyond security and move their relationship from vendor-to-PC more fully toward vendor-to-user.

Exhibit 17

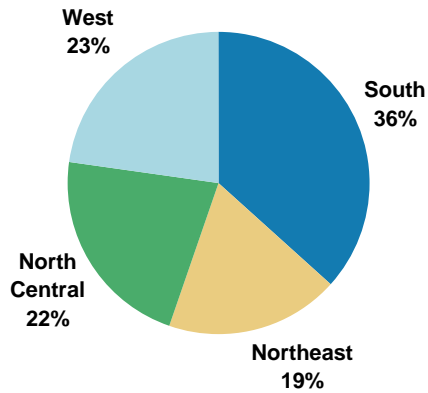
Two Most Often Cited Reasons for Staying With Paid Security Software Are Security and Performance...



Source: Morgan Stanley Research, Alphawise

Exhibit 21

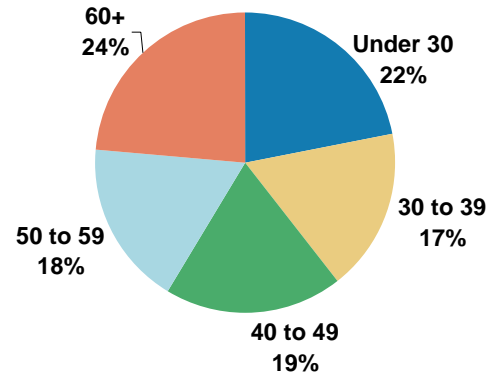
Survey Demographics: Geographic Distribution



Source: Morgan Stanley Research, Alphawise

Exhibit 23

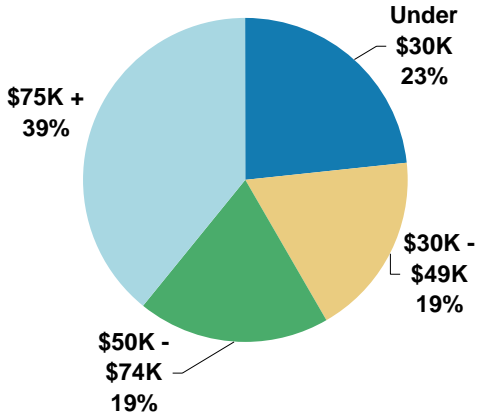
Survey Demographics: Age Distribution



Source: Morgan Stanley Research, Alphawise

Exhibit 22

Survey Demographics: Income Distribution



Source: Morgan Stanley Research, Alphawise

Morgan Stanley AlphaWiseSM

Research for this report was conducted with Morgan Stanley's AlphaWise, which conducts proprietary evidence-based investment research.

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(as of April 30, 2010)

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May 17, 2010
Software

| Stock Rating Category | Coverage Universe | | Investment Banking Clients (IBC) | | |
|--------------------------|-------------------|------------|----------------------------------|----------------|----------------------|
| | Count | % of Total | Count | % of Total IBC | % of Rating Category |
| Overweight/Buy | 1065 | 42% | 328 | 42% | 31% |
| Equal-weight/Hold | 1118 | 44% | 357 | 46% | 32% |
| Not-Rated/Hold | 14 | 1% | 4 | 1% | 29% |
| Underweight/Sell | 366 | 14% | 88 | 11% | 24% |
| Total | 2,563 | | 777 | | |

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Cautious (C): The analyst views the performance of his or her industry coverage universe over the next 12-18 months with caution vs. the relevant broad market benchmark, as indicated below.

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May 17, 2010

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Industry Coverage:Software

| Company (Ticker) | Rating (as of) | Price* (05/14/2010) |
|---|----------------|---------------------|
| Adam Holt | | |
| Adobe Systems (ADBE.O) | O (10/29/2009) | \$33.72 |
| Citrix Systems Inc (CTXS.O) | U (09/08/2009) | \$46.51 |
| Fortinet Inc. (FTNT.O) | O (01/06/2010) | \$16.14 |
| Guidance Software Inc. (GUID.O) | U (10/02/2008) | \$5.8 |
| Intuit (INTU.O) | O (05/03/2010) | \$35.53 |
| McAfee (MFE.N) | E (05/17/2010) | \$33.68 |
| Microsoft (MSFT.O) | O (04/24/2009) | \$28.93 |
| NetSuite (N.N) | E (01/14/2010) | \$15.41 |
| Oracle Corporation (ORCL.O) | O (06/23/2008) | \$23.78 |
| Red Hat, Inc. (RHT.N) | E (12/19/2008) | \$30.4 |
| Salesforce.com (CRM.N) | E (08/12/2009) | \$84.72 |
| SolarWinds, Inc. (SWI.N) | O (06/29/2009) | \$20.09 |
| Sourcefire (FIRE.O) | E (01/14/2010) | \$19.39 |
| SuccessFactors (SFSF.O) | E (12/16/2008) | \$22.04 |
| Symantec (SYMC.O) | E (05/07/2009) | \$16.12 |
| Taleo Corporation (TLEO.O) | O (01/14/2010) | \$25.53 |
| VMware Inc (VMW.N) | E (06/23/2008) | \$60.2 |
| Keith Weiss, CFA | | |
| ArcSight Inc (ARST.O) | O (03/26/2008) | \$23.48 |
| Autodesk (ADSK.O) | U (09/08/2009) | \$30.77 |
| Check Point Software Technologies Ltd. (CHKP.O) | E (04/15/2010) | \$32.63 |
| DemandTec (DMAN.O) | U (01/08/2010) | \$6.11 |
| RightNow Technologies, Inc. (RNOW.O) | E (04/06/2006) | \$15.05 |
| Websense Inc. (WBSN.O) | O (01/29/2010) | \$22.2 |

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