

THE WALL STREET TRANSCRIPT

Connecting Market Leaders with Investors

Internap Network Services Corporation (INAP)



PAUL CARMODY is a Senior Vice President of Internap Network Services Corporation, and he leads the product management and business development functions across the complete portfolio of Internap solutions, including data center services and IP services. He is a seasoned executive with extensive product management, development and strategy experience spanning key technology sectors, including IT hosting, software as a service and enterprise software. Mr. Carmody leads his teams in the creation, evaluation and execution of business plans that support Internap's long-term profitable growth strategy. He was previously at The Broadlane Group, one of the leading cost-management companies in the health care industry, where he served as SVP of Marketing, Product & Strategy. At Broadlane, he led the conception and implementation of corporate strategy, contributing to the successful sale of the company in November

2010. Prior to Broadlane, Mr. Carmody spent four years in key positions at Rackspace US, Inc., including Vice President of Product Development. At Rackspace, he was a central player in developing product strategy, building the product team and overseeing dozens of product launches as the company grew from less than \$100 million to more than \$600 million in annual revenue. Mr. Carmody began his career as a Consultant at McKinsey & Company and has also held positions at Closedloop Solutions, Inc.; Lawson and Zenith Electronics. He holds an MBA from Stanford University and an A.B. from Princeton University.

SECTOR — COMPUTERS

TWST: Please start with a brief history of Internap and bring us to where the company is today.

Mr. Carmody: Internap was founded in 1996 under the premise that the Internet could be made better for how we live and work. We developed a proprietary Internet routing technology called Managed Internet Route Optimizer, MIRO, that analyzes Internet traffic in real time and leverages numerous network service providers worldwide to deliver customers' content and applications over the best-performing route. Over time, we added colocation as an offering because we found that customers increasingly wanted a secure, scalable environment to host their IT infrastructure — and of course connect it to our IP service. In 2007, we added a content delivery network, CDN, through the acquisition of VitalStream, and we have continued to develop and upgrade those capabilities. In 2009, we began to focus on building our managed hosting offering, which is a rapidly growing segment of our business. And this year, we're adding a complete private and public cloud services portfolio.

Based on our broad set of offerings, we differentiate ourselves in two key areas. First is best performance to the end user — that's with

our optimized enterprise IP services and CDN. Second, because of the scope of the portfolio, we provide the maximum IT platform flexibility. Depending on their needs, customers can deploy in colocation, managed hosting, a private or public cloud — or any combination of these.

TWST: So those are the key services and products you offer customers today. Would you like to expand on any of them?

Mr. Carmody: Absolutely. From the standpoint of best performance to the end user, there are really three major services that we offer. The first is our enterprise IP service, which I talked about previously. We call it Performance IP. We sell Performance IP standalone to many businesses, as well as in conjunction with our other IT infrastructure services. By optimally routing packets over multiple carrier options, our IP network wins from a performance perspective. Moreover, the reliability of our global Performance IP network allows us to offer customers a proactive 100% uptime service level agreement, which is really unparalleled in the industry.

We also provide Accelerated IP, XIP, a TCP acceleration service. TCP is the protocol that rides on top of Internet routing, and we are able to optimize that in such a way that companies can deliver content about 1.5 to four times faster over the Internet. That's actually quite an

impressive improvement. Thirdly, we have our content delivery network, CDN, which stores and accelerates delivery of content from a location close to the end user. These three services taken together enable Internap to provide best performance to the end user.

TWST: The company is scheduled to launch comprehensive enterprise cloud service in the third quarter. Please tell us more about this and why it's important for your customers.

Mr. Carmody: We chose to enter the cloud market with a broader set of cloud offerings than you can find from competitors in the marketplace. For example, some providers have a cloud offering that's based on VMware, or they might have a cloud offering that's based on some sort of public, open source hypervisor. Many providers today show a clear affinity toward either VMware or open source. What we've chosen to do is to offer both, so we believe we will be one of the only — if not the only — company in the marketplace with a public cloud offering that lets customers choose either VMware or open source, based on the OpenStack management system. We also offer a private cloud spectrum where customers can choose a fully dedicated environment or a virtual data center using VMware. So we actually have two choices on the public side and two choices on the private side, which again supports our strategy of building an IT infrastructure services platform with maximum flexibility and choice for our customers.

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TWST: Meanwhile, I believe you have some data center expansions planned in a few markets for next year. Where are those exactly and what's driving those expansions?

Mr. Carmody: The markets are Dallas, which we have stated will be online during the first quarter of 2012; Los Angeles in the second quarter of 2012; and an expansion of our current data center in Atlanta in the third quarter of 2012. So we have three major data centers under construction at this point in time. Our investment in data center expansions is driven not only by our belief in the local market demand for colocation services, but also our belief in the value of the integrated IT platform. Internap's unique ability to fill these data center expansions with customers seeking any combination of colocation, managed hosting and/or cloud IT services is a compelling customer benefit and competitive differentiator for the company. Thus, we've increased our company-controlled data center footprint by 70% in just over three years. This strategy improves our margins and provides the foundation for us to continue to build out our IT platform flexibility.

TWST: Does the company have any particular initiatives around green buildings? One in California recently received a certification.

Mr. Carmody: Yes, absolutely. At Internap, we're focused on being responsible from an environmental standpoint. Our Santa Clara data center, which came online in the summer of 2010, is a great example of our commitment to the environment. The facility was just recently Green Globes certified — a designation that is issued by the Green Buildings Initiative — making it the first public data center in the United States and the first nongovernmental building in California to achieve this designation. In the facility, we use reclaimed water for cooling. We

have a separate line that comes in from the city that delivers gray water that we condition and use for chilling so that we don't have to use regular tap water. We wind up saving about 27 million gallons of drinking water per year at full load by doing that. We are also very conscious about building materials. We chose to use recycled materials wherever we could. We're also working toward Green Globes as well as LEED and Energy Star certifications at our other Internap-owned data centers.

TWST: In addition to being environmentally responsible, are there cost savings that the company realizes?

Mr. Carmody: There are in some cases, for sure. The example I gave, using reclaimed water for our cooling facilities, winds up saving us money. Moreover, we try to engineer facilities to be energy efficient, saving money on electricity as well. So there are oftentimes savings from being green and environmentally responsible. And I would also say that in markets like California — and more and more across the board — the buying public is very sensitive to the environmental responsibility of the companies that they purchase services from.

TWST: Who are the company's typical customers?

Mr. Carmody: We segment our customers into two main categories, based on role or job function rather than industry. One group is the chief technology officers. CTOs tend to be at companies that are optimizing large-scale Internet applications. They have engineering

staffs that tailor their application to a particular IT platform, and naturally they're very conscious of application performance since it forms the basis of their business. Historically these companies have tended to be in industries such as gaming, software as a service, and media and entertainment where you have, say, an ad-supported Web site — basically, the types of companies that rely heavily on Internet performance. So that's one type of customer, and it constitutes a fairly large user group for us. These customers value Internap's performance message and our ability to allow them to implement applications on the data center services most appropriate for their scale — from colocation to the cloud.

The second category is the chief information officers. CIOs manage a portfolio of applications. The typical CIO is worried about the ERP system, the e-mail system, the corporate Web site, the e-commerce application that was just rolled out and so forth. They aren't going to tune each application to a particular IT deployment platform. They want an infrastructure provider who can meet the needs of any of their applications, whether they belong in colocation, managed hosting or the cloud. We are that provider for the CIO segment as well.

TWST: How are your customers' needs trending, and how do you meet their needs?

Mr. Carmody: I'd say there are two different trends that we see. If you take the CIO group, what we find is they are generally getting more comfortable with IT infrastructure outsourcing, particularly at the midsize company level — at about the \$200 million to \$2 billion in sales level. They are becoming very interested in outsourcing as a way to increase flexibility and reduce costs. And what we see is, once they begin, they will often start with a colocation or a managed hosting type of platform, then they'll experiment with moving into private cloud and

eventually into public cloud. They start off at the dedicated end of the spectrum and then migrate over time toward cloud services as they become more comfortable.

We find the other trend in the CTO market or the Internet company market I spoke to earlier. Here, startups may begin by using the public cloud because it allows for very low costs and scales very easily, but as they get bigger and more successful, they actually migrate to a private cloud and then on to managed hosting/colocation for the performance and security benefits offered with dedicated infrastructure. So we see both of those trends occurring, and the good news is that we satisfy both of those requirement sets.

TWST: I would imagine that helps minimize customer churn since you're able to meet their needs as they evolve.

Mr. Carmody: We call that future-proofing your IT infrastructure strategy. Yes, customers may need colocation today but managed hosting tomorrow. On the CTO side, we might say, "Okay, you want public cloud today, but you know you're going to need dedicated infrastructure tomorrow. So choose a single vendor that grows with you over the life cycle of your application."

Another thing that keeps churn very low is that we place strong emphasis on having a world-class customer-support organization. Calls into our network operation center are answered within 10 seconds on average, and our caller abandon rate is amazingly low at just 0.01%. And about 95% of the time, the person who answers that call actually solves the problem right there. Those are things that are difficult to find in this industry, and customers really appreciate it, and there's no doubt that it is a primary contributor to our low churn rate.

TWST: Are any of your business segments most profitable for the company right now, and what's the outlook going forward?

Mr. Carmody: I would break it into the two different external business segments that we report on — data center services and IP services. In our data center services segment, our strategy has been to convert from selling low-margin, third-party partner colocation to selling colocation services within facilities that Internap designs, builds and operates. We've also been rapidly growing our managed hosting business, which is reported as part of our data center services business segment.

The move away from third-party data center resale and the investment in Internap's own data centers is that our data center services segment margins are going up over time, and that is easily visible in our financial results. Our IP services segment remains uniquely positioned in the market and highly profitable. With gross margins consistently in the low 60% range, we obviously benefit from this segment's ability to generate cash flow.

TWST: There must be more upfront costs and capital investment in that move toward owned buildings.

Mr. Carmody: That's right. We're investing our own capital, but we wind up getting higher returns by holding business in our own data centers. As I mentioned, the data center is the foundation for all of the services that we offer. When we effectively own the data center, we can put colocation in it, as well as managed hosting, CDN and cloud, and

so on. So controlling the underlying data center outright affords us the flexibility to add and continue to build out all of these services.

TWST: Looking ahead over the next year or two, what should both customers and investors look for when analyzing the company?

Mr. Carmody: Customers and investors should expect to see us accelerate the deployment of IT infrastructure services that meet customers' needs and also drive long-term profitable growth for our business. As I mentioned earlier, we've got multiple data center openings coming up over the next several quarters. In addition, we're excited about the upcoming introduction of our cloud offering, and customers are showing a lot of interest in that. I think that the breadth of our data center services offering, soon to include public cloud services, along with our increased data center footprint through more geographical locations, are the key developments for 2012.

TWST: Is the company mostly focused on the U.S.?

Mr. Carmody: While the vast majority of our revenue currently comes from services sold in the United States, we do sell internationally. We sell colocation services via partners in markets like London and Frankfurt, as well as Hong Kong. We also offer managed hosting in London and Hong Kong. We talked about IT platform flexibility in terms of allowing people to grow with us over time, changing from managed hosting to cloud or from managed hosting to colocation, for example, but another important aspect of growing with our customer base is that geographic footprint. We have many customers that start off with colocation domestically, and then they want to expand to Europe and into Asia Pacific, and so on. We're in a position where we can grow with those customers, which is important.

TWST: Is there anything else you'd like to add?

Mr. Carmody: I would end with saying I've been at Internap for about eight months now, and my perspective is that it's an exciting place to be. We're getting a lot of resonance around our best performance and IT platform flexibility message. I think we're at a point where, from a product portfolio standpoint, we're fulfilling both of those messages, and we look forward to getting that message across to more potential customers and continuing to grow the company.

TWST: Thank you. (MN)

PAUL CARMODY
Senior Vice President
Internap Network Services Corporation
250 Williams St.
Atlanta, GA 30303
(404) 302-9700
(877) 843-7627 — TOLL FREE
www.internap.com
e-mail: gen_info@internap.com