

Xactly buys closest rival Centive to expand sales performance management presence

Analyst: China Martens, Brenon Daly
Sector: Enterprise Software

Midmarket on-demand sales performance management (SPM) startup **Xactly Corp** has achieved a major competitive coup in its first-ever acquisition by purchasing its software-as-a-service (SaaS) peer and closest rival, **Centive**. As we've discussed in previous reports, the developing SPM applications market is a lively, crowded one. Given its mix of startups and established players, we've been expecting the space to undergo further consolidation following some M&A activity in 2008.

We hadn't necessarily expected such a bold move from one of the younger companies in the sector, but we had earlier voiced concerns about Xactly's ability to hit all of its technology addition targets as well as Centive's ongoing struggle to achieve profitability. This transaction attempts to settle both of those issues, with the Xactly-Centive combination a stronger entity both in terms of customer numbers and range of technologies at its disposal. The longer-term issue is how quickly Xactly can pull together a unified product set drawing on both the strengths of its own software and those of Centive, and how successfully it retains Centive's customers. Xactly's own customer renewal rate in 2008 was 90%.

ACQUIRER

Xactly Corp

TARGET

Centive

SUBSECTOR

Sales performance management

DEAL VALUE

Not disclosed

DATE ANNOUNCED

January 22, 2009

CLOSING DATE

January 22, 2009

ADVISERS

William Blair & Company (Xactly); JMP Securities (Centive)

Deal details

Xactly will pay an undisclosed amount in equity for Centive. The consolidation play will bump up Xactly's revenue by about 50%. We understand that Centive generated about \$10m in revenue in 2008, while Xactly finished last year with sales in the neighborhood of \$25m. Xactly expects the acquisition to be accretive by year-end. **William Blair & Company** advised Xactly, and **JMP Securities** (NYSE: JMP) advised Centive.

Going forward, the combined company will be known as Xactly and will have a total headcount of 130-140 staff, with some layoffs occurring among both Centive and Xactly staff due to overlaps and duplications in job function. Carol Peo, Centive's vice president of engineering and chief technical officer, is joining Xactly to help unify the product lines of the two organizations, but other Centive executives – such as CEO and president Michael

Torto, chief operating officer James Triandiflou and chief marketing officer Bob Conlin – will not come on board. Xactly's headquarters will remain in San Jose, but it intends to retain Centive's Lowell, Massachusetts, headquarters and reposition it as a new East Coast base.

Rationale

This acquisition has been in the works for some time, with the CEOs of the two companies discussing the potential move for the past 12-18 months. Both sides identified plenty of technology and cultural synergies between the two, which are each SaaS SPM pure plays, as well as the opportunity to apply elsewhere the sizable amount of energy both firms were expending on aggressively competing with each other. There's also the sense that in the current tough economy, customers will be less wary of buying applications from the larger combined company rather than the smaller startup that Xactly was prior to the acquisition of Centive.

Xactly and Centive were similar in size in terms of both headcount and customers, and now expect to have a combined user base of well over 200 companies. Centive brings its acquirer major customers like **Adobe** (Nasdaq: ADBE), **McKesson** (NYSE: MCK), **IKON Office Solutions** (NYSE: IKN) and **ZipRealty**, while some of Xactly's largest users include **Dun & Bradstreet** (NYSE: DNB), **Pep Boys** and **Salesforce.com** (NYSE: CRM).

The sweet spot of the market for the combined entity going forward remains the same – 5-5,000 seats, with 300-500 subscribers per organization being the average deal size. Both Centive and Xactly have a strong presence among technology companies, and Xactly sees the addition of Centive as effectively doubling its installed base within other industries such as retail and financial services.

Outlook

Xactly has committed to fully supporting Centive's products for at least the next 18 months as it begins to roll out a unified product roadmap, bringing together some of the best elements from its own and Centive's technologies. The two companies adopted somewhat different packaging approaches, with Xactly building a range of additional modules that cost extra on top of its flagship Incent compensation management application.

By contrast, Centive's Compel offering is an all-in-one SPM suite, with more established functionality than Incent in some areas. For instance, while Xactly is still developing quota and territory management, Compel already provides those capabilities, whereas Xactly offers revamped analytics that it believes may prove interesting to existing Centive users. The idea is to cross-sell such offerings into the Centive or Xactly installed base. Xactly hopes to debut a first take on a unified roadmap fairly quickly, within a six-week time frame. The ultimate goal is to create a hybrid of Incent and Compel that won't require users to engage in any product migration efforts.

Target background

Privately held Centive took on its current form as a SaaS pure play in September 2006 after selling its older on-premises CompCentral enterprise incentive management operation to

Incentive Technology. Centive was originally founded as **Incentive Systems** in 1997, changing its name to Centive in 2002. The company raised more than \$75m over the course of its history, but only \$10m of that investment really relates to its Compel SaaS business, which debuted in May 2005. Investors included **Key Venture Partners, Polaris Venture Partners** and **Venture Strategy Partners**. By contrast, Xactly has raised \$57m since its founding in March 2005, attracting investors like **Cheyenne Ventures** and **Glynn Capital Management**, which led its series D \$30m round in April 2008, as well as earlier backers like **Alloy Ventures, Bay Partners, Outlook Ventures, Rembrandt Ventures** and **Spinner Asset Management**.

Centive had tied a key part of its future fortunes to an OEM partnership it signed in November 2007 with **Automatic Data Processing** (NYSE: ADP) (ADP) that enabled a division of the payroll giant to re-brand, sell and host Compel. While Xactly doesn't consider the continuation of that relationship – which is still largely in its infancy – crucial to the successful incorporation of Centive, it's keen to engage with ADP and hopes to advance that OEM tie-up.

Both Xactly and Centive have already developed products on Salesforce.com's Force.com development platform. In Centive's case, it was an incentive planning and design tool known as Sales Plan Accelerator, while Xactly developed a noncash-rewards module. Xactly intends to continue offering both Incent and Compel via Salesforce.com's AppExchange website.

Competitive landscape

As we previously noted, Xactly and Centive were strong competitors. Teaming up allows the combined entity to more forcefully go after a third player in both the midmarket and enterprise arenas, **Callidus Software** (Nasdaq: CALD). Publicly held Callidus operates in both the SaaS and on-premises worlds and is pushing to retain its enterprise focus while simultaneously appealing to smaller organizations, so it's likely to compete even more frequently with Xactly.

Last year, we saw two new SaaS entrants in the SPM market, **nGenera** and **Merced Systems**, which both bought their way in, with nGenera picking up **Iconixx** and **nCent Software**, while Merced acquired **Practique Associates**. SaaS compensation management startup **Makana Solutions** is also starting to build up a head of steam among smaller organizations. There are also plenty of players at the higher end of the market, including **Oracle** (Nasdaq: ORCL), **SAP** (NYSE: SAP), **Syngy, Varicent** and **Versata**. CRM vendors haven't tended to make a major push into the midmarket SPM space, hence the tight alliances Xactly has with both Salesforce.com and Oracle, and a similar relationship with **Microsoft** (Nasdaq: MSFT) is developing.

Conclusion

If we weren't currently in an economic downturn, acquiring Centive would take Xactly much closer to going public, providing it with more of the necessary heft for an IPO. As it is, the company feels the purchase gives it a year's head start in growth terms. Going forward, Xactly remains focused on the SPM market that has developed out of the incentive compensation arena. But the company is not adverse to the wider take on SPM that Centive

has been voicing, which would embrace players in other sales-focused fields such as sales effectiveness, sales enablement and sales forecasting to create an integrated suite of sales tools. Centive had considered teaming up with companies like **Kadient** and **Right90**. Xactly is open to such partnerships and may even look to make further purchases, once it has fully digested Centive.

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