

WIRED ABOUT

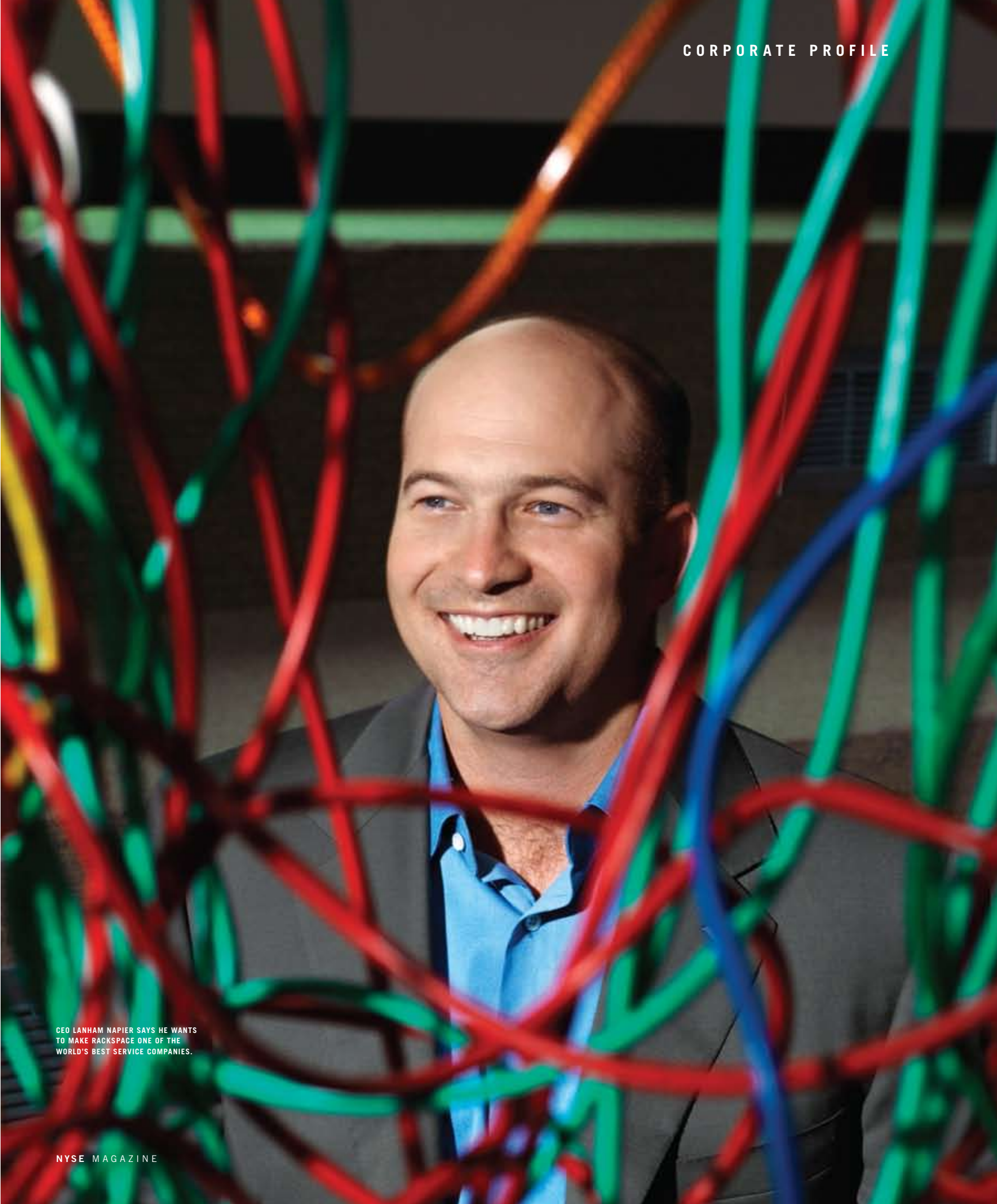
BY CHRISTOPHER WARREN » PHOTOGRAPHS BY RAMONA ROSALES

RACKSPACE HAD ITS STARTUP ROOTS IN TECHNOLOGY, BUT CEO LANHAM NAPIER SAYS ITS BIGGEST FOCUS IS “FANATICAL” CUSTOMER SUPPORT.

Lanham Napier says a crucial moment in the development of **RACKSPACE HOSTING INC.** (RAX) came when it wasn't getting the same amount of funding as its competitors. Napier, president and CEO of the San Antonio-based provider of IT and computing services, which was founded in 1998, says the company missed out on the prodigious amounts of venture capital funding available during the 1990s technology boom. By the time Rackspace was ready to pursue the money, it had largely dried up. “Competitors raised \$400 million, and we raised \$30 million,” notes Napier, 37, who received a BA in economics from Rice University and an MBA from Harvard.

In retrospect, the challenge to find funds was a good thing for Rackspace, Napier explains, because the company didn't have the capital to construct new data centers the way its rivals did. “They had the belief that if you build it, they will come. Then came the technology bust, and demand wasn't there,” he says. Rackspace, which says it is now the world's largest hosting provider based on revenues, offers a number of services, including maintenance of managed Web servers, applications, e-mail and database servers. It also furnishes comprehensive systems-level administrative support, Napier says.

SERVICE



CEO LANHAM NAPIER SAYS HE WANTS TO MAKE RACKSPACE ONE OF THE WORLD'S BEST SERVICE COMPANIES.

Without money to invest in facilities, Rackspace executives say they had to figure out not only which strategies would differentiate the company from others but also how it could become profitable fast. Napier says they wanted customers to associate Rackspace with “Fanatical Support®” — customer support that, in part, focuses on fixing problems when they occur and preventing customers’ Websites from crashing. The CEO insists that hosting is a technology service business and Rackspace’s 33,000-plus global customers want Fanatical Support. “We don’t do trivial things for our customers; we’re taking care of their mission-critical stuff,” he explains.

Napier says focusing on customer support allowed Rackspace to emerge from the technology meltdown in good shape. Rackspace first

THE NEED FOR HOSTING

Rackspace wasn’t always a data hosting company. Originally called Cymitar Technology Group, it was launched in 1998 by Dirk Elmendorf and another founder, former classmates at Trinity University in San Antonio, Texas, who wanted to build Web applications for local businesses, such as doctor’s offices. Pat Condon says he joined the team in the middle of 1998 and quickly realized that they needed to find a new business model if they were going to succeed. That’s when they developed the idea of Rackspace.com, Condon explains. The name refers to the large racks that computers sit on in data centers. Eventually, he says, they changed the name to reflect the focus on this specific part of the business.

Condon recalls how consulting clients, clearly frustrated by the continual crashing of their sites, repeated the same request: Make the Websites work all the time. Condon says he and his partners searched for “the perfect hosting partner.” When they couldn’t find one that was reliable, particularly for complicated, database-driven Websites, the entrepreneurs took over the hosting responsibilities themselves.

“One day we woke up and said hosting looks like a better gig than the Web applications development and IT consulting we’re doing now,” Elmendorf says. The founders spent a long weekend in the fall of 1998 building a Rackspace Website, Elmendorf says. Just 30 days later they had 30 customers, despite a meager advertising campaign — a few online banner ads and search engine impressions. “That told us there was a lot of demand out there,” Elmendorf notes. “We didn’t have to convince people that managed hosting is something they need.”

Still, the founders realized that hosting is an infrastructure business with needs much like those of the telecommunications industry, requiring lots of capital to help spur fast growth (for example, a mobile-phone company must construct a \$1 billion network before it can sell its products). Because the company required capital to build data centers and other technology, Condon explains, Rackspace approached a local San Antonio

entrepreneur, Graham Weston, who owned a tax assessment and real estate company.

Weston recalls that he met the Rackspace founders when his company hired them to wire a building for the Internet. He remembers a meeting at which the trio was asked if they had any other business ideas, and they gave a presentation about their fledgling hosting company. Weston, who is now Rackspace’s chairman, says he was impressed enough with what he heard to make an investment in late 1998. “After a few months, Rackspace burned through the initial investment, but in a good way,” he says. “They had to purchase the hardware the company needed, and Rackspace was growing. When they came back to me for more help, I saw the great growth potential.” Ultimately, it was decided that

THE WEB HOSTING MARKET IN ASIA “IS NOT AS MATURE AS IN THE STATES OR EUROPE. IT’S GROWING A LOT FASTER. THAT’S OUR KIND OF GIG,” SAYS CEO LANHAM NAPIER.

became profitable in early 2001 and has remained so ever since, the CEO says. The company indicates that it has grown net revenues from \$56.6 million in 2003 to \$362 million in 2007, representing an annual growth rate of 59 percent. Today it has more than 3,000 employees, customers in more than 100 countries, and eight data centers: four in the U.S., three in the U.K., and its newest one, in Hong Kong. “Most every company in every country today needs the power of the Internet,” Napier explains. “We provide enterprise computing capability at a fraction of the cost of doing it yourself,” he adds. Europe has been an important element in Rackspace’s overall growth, and Napier expects Asia to be valuable as well. “The Web hosting market in Asia is not as mature as in the States or Europe,” he says. “It’s growing a lot faster. That’s our kind of gig.”

RATHER THAN STRESS TECHNICAL APTITUDE, RACKSPACE WANTS EMPLOYEES WHO ARE CAPABLE OF PROVIDING SUPERIOR CUSTOMER SERVICE.

Weston would become CEO, a position he held until 2006, when Napier, then Rackspace’s CFO, took over the post.

In fact, Weston says, Napier was one of his key hires. Napier, who had worked briefly as an analyst at MERRILL LYNCH & COMPANY INC. (MER), moved to Texas for hands-on work at San Antonio-based investment company Silver Brands Partners. As the firm’s director, Napier says, he learned a great deal about running a successful business during his five years there.

In 2000, just months before the technology downturn, Weston recruited Napier, whom he knew through his work at Silver Brands, as Rackspace’s chief financial officer. Napier says he welcomed the opportunity to join the embryonic yet rapidly growing company. Soon after arriving, Napier introduced financial discipline to lift the company out of what he dubs “cash-

burning mode” and helped set its course toward revenue growth. In January 2001, Napier was named president, and in 2006 he became CEO.

RACKER SERVICE

Once the technology downturn hit, executives say, Napier helped identify Fanatical Support as the way to differentiate Rackspace from its competitors. Napier says he supported Fanatical Support soon after he arrived and has since formalized that idea into Rackspace’s mission to be one of the world’s best service companies.

Napier says that employees — known as Rackers — are compensated based upon “the customer outcome” (measured by customer

responses to a satisfaction survey). Beyond the pay structure, he believes that Rackspace’s customer-focused culture and employee enthusiasm are what makes Fanatical Support possible. “To have a world-class service experience, you must start with a world-class culture,” he says. In 2008, Rackspace reports, it was named No. 32 on the 100 best companies to work for list by *Fortune* magazine and one of the 50 top workplaces in the U.K. by the *Financial Times*.

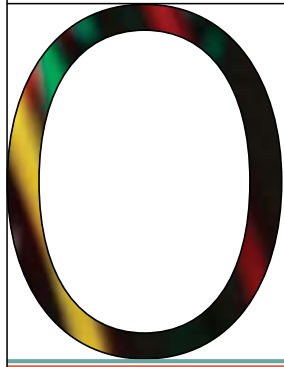
The CEO says creating a workplace culture where people can freely express their ideas begins with hiring the right people. Condon recalls that in the beginning the company made the mistake of exclusively emphasizing a new hire’s technical aptitude rather than whether he or she could provide superior customer service.

As the company refocused around the concept of Fanatical Support, executives say, they modified the employee selection process. “Now we spend a lot of time figuring out if they are naturally wired to deliver great service every day,” Condon explains.

The company says that all new Rackers go through a Rapid Immersion Program, which involves learning the basics of how Rackspace functions. During their first month, the company explains, new employees attend a week-long rookie-orientation program to learn about the Rackspace culture. Executives from departments across the company give presentations. Also, depending on job descriptions, employees may receive technical training at various points throughout their career.



FROM LEFT: PAT CONDON, GRAHAM WESTON, DIRK ELMENDORF AND LANHAM NAPIER ARE ALL CUSTOMER-SERVICE FANATICS.



ORGANIZING RACKERS

INTO TEAMS ACHIEVES
“MANY OF THE BENEFITS
THAT RACKSPACE HAD
WHEN THERE WAS JUST
ONE SMALL TEAM,” CONDON
SAYS. “BUT NOW THERE
ARE MANY SMALL TEAMS.”

Napier says Rackspace also uses the StrengthsFinder, an online questionnaire provided by the research and polling company The Gallup Organization, to determine the set of activities that will help employees excel. The tool asks an employee to choose between a series of activities — for example, would you rather do X or Y — and uses that information to put new hires in jobs where they're most likely to flourish. The CEO says Gallup also measures its employees' engagement — how involved and enthusiastic they are about their work. Those findings show that Rackspace has a stronger, more engaged workforce today than it did five years ago, even though it now has four times as many Rackers.

To underscore Rackspace's culture of support, it assigns teams of 15 to 20 Rackers to a set of customers. What that means, Napier says, is

that customers who call with a question or a problem don't reach a call center but instead talk to a person who knows their business and with whom they've likely had interactions in the past. Napier says he wants clients to see these small support teams as extensions of their own staffs.

Condon adds that organizing the company into small teams recreates the togetherness he and his partners developed when Rackspace was a startup. “They achieve many of the same benefits we had when there was just one small team, but now there are many small teams,” he says.

TECHNOLOGY EDGE

Napier says Rackspace uses best-of-breed technology, but what sets it apart from its competitors are the proprietary systems and processes the company has developed to improve the available technology and tailor it to customer needs. “You can't just walk down the street and purchase the systems we use,” he says.

For example, Rackspace reports that it uses **HEWLETT-PACKARD CO.**'s (HPQ) OpenView software, which monitors servers and facilities to ensure smooth operations. While dubbing OpenView the “gold standard of monitoring,” Napier says Rackspace developed proprietary

code to make the technology even more effective. “The combination and transformation of best-of-breed technology for better usability is a crucial element needed to deliver Fanatical Support,” the CEO says.

According to Rackspace, the global hosting market was worth \$12.3 billion in 2007, and the company expects its growth to far outpace the overall IT market. Napier notes that more companies around the world are expected to turn to hosting to take care of many of their computing needs in much the same way companies now outsource payroll functions. He sees particular promise in “cloud computing,” which allows companies like Rackspace to provide computing services to clients through the Internet. As cloud technology gains acceptance, he adds, it will drive down the overall cost of computing.

Weston believes the company is well situated to flourish, and he likes to compare Rackspace's experiences to the early days of **FORD MOTOR CO.** (F). “Ford revolutionized the auto industry with the mass production of automobiles through the assembly line,” he says. “I see Rackspace revolutionizing the IT industry by delivering IT services such as e-mail and virtualization cloud computing through its hosting services.”

For now, Napier says, the company remains focused on becoming one of the world's great service companies. It's that focus, he says, that led it to become profitable in 2001, then remain profitable on an annual basis beginning in 2003 and ultimately gather enough strength to list on the NYSE. The listing in August was a no-brainer for company strategy, he adds, because it will provide capital for expansion projects, such as the Hong Kong data center that opened in September.

But Napier sees the listing on the NYSE as a milestone, not a destination. “It was an emotional moment for us, but really, we're on a special mission: to build one of the world's great service companies and make technology a pleasure to consume,” he says. “The market stepped up, and people invested a lot of money in us. Now we have to go earn it.” ■

HOSTING BEYOND THE EXPECTED

WHEN WILDFIRES SWEEPED through Southern California last year, Pangea Foundation, a San Diego-based nonprofit that provides other nonprofits around the world with custom enterprise software solutions, faced a big problem. Pangea Foundation received a call from a representative of 2-1-1 San Diego, the premier provider of community information in San Diego County, who was concerned that its Website couldn't keep up with the online traffic generated by residents looking for up-to-date information on road closures, evacuation routes and emergency shelter openings. Ultimately, the Website crashed.

Pangea Foundation's president and CEO, Kraig Kuipers, contacted Rackspace, its hosting provider, with an urgent plea to bring new servers online. Within minutes, Kuipers says, a plan was formulated and less than six hours later two brand-new servers were operating. Pangea Foundation was able to create software that allowed 2-1-1 San Diego to make fresh information available to the public within seconds.

“Rackspace had the servers online in a matter of hours,” says Kristin Kuipers, founder and director of programs for Pangea Foundation. “That's why we were able to accomplish what we did for 2-1-1 San Diego so quickly. We didn't have the hardware capacity or the manpower immediately available to do it ourselves. Rackspace took care of the servers, hosting, bandwidth and network infrastructure around the clock so we could focus our efforts on creating and delivering software for 2-1-1 San Diego.”

“Pangea was in a unique and difficult situation and Fanatical Support rose up to meet their needs,” says Napier. “But the great thing about Fanatical Support is it's not just there when emergencies happen; for customers of all sizes it ensures we'll be there whenever they need us.”