

INVESTOR'S BUSINESS DAILY

MONDAY, AUGUST 23, 2004

INTERNET & TECHNOLOGY

Startup Firm Force10 Looks To Give Cisco A Run For Its Money

Battle For 10-Gigabit Ethernet

Flush with venture capital, Force10 aims to lure away Cisco's dissatisfied users

BY MIKE ANGELL

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Makers of key computer network products called ethernet switches have lagged in the stock market, but a startup in this field closed the second largest venture round of any company last quarter.

Backers say that company, Force10 Networks, is one of the few that can pose a solid threat to the outfit that has long led the network switch market, Cisco Systems^{CSCO}.

"It's true Cisco is the dominant force in the market," said Gary Morgenthaler, a partner at Morgenthaler Ventures and a Force10 investor. "But we've called (Force10's) customers and they're not happy with Cisco."

He says the unhappiness stems from too many network outages. Morgenthaler says Force10's products stand out from Cisco's and other rivals' products because they're more reliable.

"For (Force10 customers), when the network goes down, thousand of comput-

ers go down," Morgenthaler said. "These companies cannot afford outages."

Despite Force10's claims, Cisco's Chief Technology Officer Charlie Giancarlo says Cisco is still a market share leader in this category.

"We lead in both low price and high performance categories" of the ethernet market, Giancarlo said.

Ethernet switches are devices that forward packets of data in the main type of local network. Ethernet switches were a \$10.6 billion market last year.

Cisco, the world's largest maker of networking gear, holds 70% of the market. Despite strong stock market debuts in 1999, ethernet switch makers Foundry Networks^{FDRY} and Extreme Networks^{EXTR} have since floundered. The same goes for Cisco challengers 3Com^{COMS} and Enterasys^{ETS}.

Attracting Funds

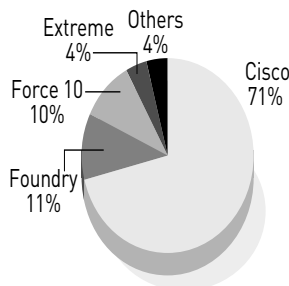
Yet Milpitas, Calif.-based Force10 in June said it had closed a \$75 million venture funding round. That's the second highest for last quarter, says a VentureOne/Ernst & Young survey.

Force10 has raised a hefty \$284 million since its 1999 founding.

Aiming High

Force10 wants to own the high-speed ethernet market. But it has to take share from Cisco

Sales of 10-gigabit ethernet switches



Source: Dell'Oro Group

Other switch makers also promised to be high-performance alternatives to Cisco, says Tim Weingarten, a Force10 board member and a partner at company investor Worldview Technology Partners. The other companies ran short on cash and had to reduce their research and development, he says. Then they lost their technological leads over Cisco.

"They've all tried to be a second source to Cisco," Weingarten said. "All were valid suppliers. But none has been able to innovate fast enough."

Force10 specializes in ethernet switches that transmit data at 1 to 10 gigabits

per second. Those are the highest speeds possible today, equivalent to sending up to 20,000 normal pages of text in one second. Cisco and others also compete in the 10-gigabit switch market.

Universities and labs, rather than companies, are the biggest market for such fast switches, and Force10 claims many such customers.

The schools and labs set the trend for later corporate purchases, a much larger market, says Force10 Marketing Director Andrew Feldman.

Force10 says its 80 customers include NASA, the Homeland Security Department and Dell. Search engine Google also is reportedly a customer, though neither Force10 nor Google would confirm that. These users "view their (network) as a source of competitive advantage," Feldman said. "They could be in the search engine business, manufacturing or a network TV provider."

Prices Dropping

The market for 10-gigabit ethernet is small but growing. Sales amounted to \$85 million last year, according to Dell'Oro Group. It could approach \$360 million this year. (Continued)

Dell'Oro analyst Seamus Crehan says 10-gigabit ethernet prices fell dramatically to just one-fourth what they were last year. "What's happened is that (gigabit ethernet has) gone from way too expensive to a little too expensive," he said.

Much of that price drop stemmed from Cisco pushing down prices in the fourth quarter. As it lowered prices, Cisco gained

market share. As of the first quarter, Cisco had 71% of the 10-gigabit ethernet switch market, which totaled \$50 million in revenue for the quarter, says Dell'Oro. Force10 was No. 3 at 10%, just behind Foundry's 11%.

"10 gigabit is a surprisingly strong market for us," Cisco's Giancarlo said. "The market speaks for itself."

Feldman says Force10's products are in a niche where Cisco and other rivals don't compete. Its switches are connecting larger server computers that run entire networks. He says rival products are used to connect desktop PCs.

"If you are connecting PCs, that is a commodity market," Feldman said. "We are interested in connecting big servers or other switches."

Force10 is still small at just 275 employees. Feldman says the firm is hiring more sales and support staff.

Morgenthaler says sales hit \$25 million last year. Sales are expected to more than double this year and could top \$100 million next year.

"The company is scaling up very nicely," Morgenthaler said. "It's looking like a 2005 IPO."