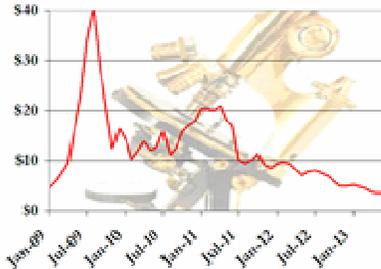


Western Digital to Acquire sTec



OBJECTIVE ANALYSIS SEMICONDUCTOR MARKET RESEARCH



Early Mover to Become Part of HGST

Western Digital Corporation (WDC) and sTec, Incorporated announced on 24 June, 2013, that they have entered into a definitive merger agreement under which sTec will be acquired by WDC's HGST subsidiary for approximately \$340 million in cash, or \$6.85 per share. This compares to sTec's market capitalization, as of the prior trading day's close, of \$168 million.

HGST has committed to continue to support existing sTec products and to collaborate with its customers to understand their future requirements.

The companies' release carefully states that: "HGST remains committed to its highly successful joint development program with Intel Corp. and will continue to deliver current and future SAS-based SSD products with Intel." HGST's current line of SSDs is based upon an Intel controller that has been enhanced to include a SAS interface, end-to-end data protection, and other features key to the enterprise SSD marketplace.

On the news sTec's stock price nearly doubled rising \$3.12 above the prior trading day's \$3.59 closing price to \$6.71, narrowly missing the \$6.85 price of the WDC offer.

sTec Saved from a Bleak Future

sTec was a glorious first mover in the SSD business ever since EMC's early 2008 announcement of a new SSD tier in its Symetrix line of network storage arrays. At the time sTec was the only qualified supplier of Fibre Channel SSDs. Both EMC and sTec anticipated faster customer adoption of these arrays than actually happened, resulting in excess inventory at EMC, which led to cancelled orders at sTec, since the company was over reliant on a single customer.

Although this very obvious fault caused a spectacular rise and fall of sTec stock in 2009 (see chart) the real reason for the stock's current doldrums stem from increased competition in the market, causing sTec to lose a number of enterprise SSD design wins to new entrants.

As of last week sTec stock was selling for less than one tenth of its 2009 peak and a boardroom battle was playing out in which one key investor was demanding the replacement of management and three board members to set a new direction for the company.

WDC's SSD Strategy Coming Into Focus

For a few years it appeared that WDC wasn't giving enough attention to the SSD market. Yes, the company acquired SiliconSystems in 2009, but it never poured enough resources into the effort to make it grow beyond its roots in the military SSD market. With the acquisition of HGST in 2011 WDC gained new strength in the enterprise HDD market along with market dominance in SAS SSDs. This was a big and well-needed change.

Today's announcement further boosts WDC's enterprise SSD strength with design know-how and a number of first-rate products that should further boost its presence in the enterprise SSD market.

It is unclear that any of these moves helps WDC in the client SSD market, but that market is already crowded with over 100 vendors and it has not grown according to many forecasters' expectations. In fact, Objective Analysis was the first to predict that PC end users would continue to choose HDDs over SSDs, and this scenario has consistently played out over the past 8 years.

Synergies and Redundancies

Western Digital is gaining good technology through this acquisition. In a [list of questions](#) posted on the WDC website the companies cite sTec's 55 issued patents and 78 patents pending. sTec has always had excellent NAND flash management technology which should be a good complement to HGST's leadership in SAS interface technology.

From a business standpoint, sTec has far less to offer. WDC distanced itself from the woes of sTec's management stating that founders: "Mark Moshayedi and Manouch Moshayedi will have no ongoing role with the company, but we will work closely with them to ensure a smooth transition." The Moshayedi brothers fell into disfavor with many investors after certain of Manouch Moshayedi's stock trades that later triggered an SEC investigation. Recently Balch Hill Capital Management issued a letter to stockholders reiterating an earlier request to remove Mark Moshayedi from the role of acting CEO and to replace certain board members to turn the firm around.

The company has been working hard to reinvent itself over the past few months, ranging from cosmetic changes (moving from STEC to sTec) to channel revisions and entering flash-based storage appliance market, in competition with some of its customers.

Objective Analysis would expect for sTec's sales efforts to be realigned to match WDC's and for its strategy to be overhauled to fit in with WDC's core competencies. Western Digital is strong in both OEM and direct sales of HDDs, and this strength alone should help the sTec product line to win broader market acceptance.

Impact on the HGST-Intel Relationship

Although we are not privy to the details of the Intel-HGST SSD agreement, our understanding is that Intel will use the Intel controller to make SATA SSDs, HGST will use the same architecture to manufacture SAS SSDs, and the two companies will not overlap on each others' turf. The sTec acquisition brings a number of SATA SSDs directly under HGST's control (unlike the SiliconSystems SATA SSDs) potentially changing the HGST/Intel relationship.

We would not be surprised to hear within the next few months that this

agreement had been modified to adapt to current realities, perhaps with HGST phasing out its use of the Intel SSD architecture.

Overall - A "Win-Win"

This move solidifies WDC's position in SSDs while potentially giving HGST more control over its SSD architecture. Meanwhile, sTec should be able to regain some of its past glory through the help of its new parent. We anticipate an improvement to both companies' businesses as a result of this transaction.

Objective Analysis has published a report: [*The Enterprise SSD: Technologies and Markets*](#), which outlines the enterprise SSD market and profiles its players, forecasting unit shipments and revenues over the following five years. The report can be purchased for immediate download from the Objective Analysis website.

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