UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

x **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the quarterly period ended November 30, 2011

OR

o **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the transition period from to

Commission file number: 001-33634

DemandTec, Inc.

(Exact name of registrant as specified in its charter)

Delaware	**94-3344761**
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification Number)

One Franklin Parkway, Building 910

San Mateo, California 94403

(Address of Principal Executive Offices including Zip Code)

(650) 645-7100

(Registrant s Telephone Number, Including Area Code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x No o

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate website, if any, every interactive data file required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer o	Accelerated filer x
Non-accelerated filer o (Do not check if a smaller reporting company)	Smaller reporting company o

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes o No x

The number of shares of the registrant s common stock, par value $0.001, outstanding as of December 30, 2011 was: 33,815,217.

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DEMANDTEC, INC.

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

DemandTec, Inc.

Condensed Consolidated Balance Sheets

(In thousands, except par value data)

	November 30, 2011 (Unaudited)	February 28, 2011
ASSETS		
Current assets:		
Cash and cash equivalents	$ 18,821	$ 26,583
Marketable securities	40,716	40,834
Accounts receivable, net of allowances of $118 and $130 as of November 30, 2011 and February 28, 2011, respectively	14,652	9,357
Deferred commissions	1,158	1,073
Prepaid expenses and other current assets	2,707	2,475
Total current assets	78,054	80,322
Marketable securities, non-current	6,864	5,563
Property, equipment and leasehold improvements, net	7,266	6,556
Intangible assets, net	4,272	2,714
Goodwill	26,074	18,828
Other assets, net	1,530	1,112
Total assets	$ 124,060	$ 115,095
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Accounts payable and accrued expenses	$ 18,483	$ 13,084
Deferred revenue	48,048	41,121
Total current liabilities	66,531	54,205
Deferred revenue, non-current	1,238	304
Other long-term liabilities	1,610	1,783
Commitments and contingencies (see Note 5)		
Stockholders equity:		
Common stock, $0.001 par value 175,000 shares authorized; 33,482 and 31,782 shares issued and outstanding, respectively, as of November 30, 2011 and February 28, 2011	33	32
Additional paid-in capital	173,880	161,505
Accumulated other comprehensive income	95	147
Accumulated deficit	(119,327)	(102,881)
Total stockholders equity	54,681	58,803
Total liabilities and stockholders equity	$ 124,060	$ 115,095

See Notes to Condensed Consolidated Financial Statements.

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DemandTec, Inc.

Condensed Consolidated Statements of Operations

(In thousands, except per share data)

(Unaudited)

	Three Months Ended November 30, 2011	Three Months Ended November 30, 2010	Nine Months Ended November 30, 2011	Nine Months Ended November 30, 2010
Revenue	$ 22,313	$ 21,670	$ 66,795	$ 60,103
Cost of revenue (1)	8,012	7,468	25,627	21,664
Gross profit	14,301	14,202	41,168	38,439
Operating expenses:				
Research and development	8,464	8,011	26,722	23,557
Sales and marketing	5,787	5,629	19,412	17,616
General and administrative	2,336	2,433	7,665	7,273
Acquisition-related costs (see Note 13)	2,222		2,222	
Amortization of purchased intangible assets	210	217	632	800
Restructuring charges			604	
Total operating expenses	19,019	16,290	57,257	49,246
Loss from operations	(4,718)	(2,088)	(16,089)	(10,807)
Other income (expense), net				
Interest income	38	62	108	190
Interest expense	(14)	(26)	(37)	(70)
Other expense	(145)	(4)	(110)	(10)
Other income (expense), net	(121)	32	(39)	110
Loss before provision for income taxes	(4,839)	(2,056)	(16,128)	(10,697)
Provision for income taxes	148	29	318	105
Net loss	$ (4,987)	$ (2,085)	$ (16,446)	$ (10,802)
Net loss per common share, basic and diluted	$ (0.15)	$ (0.07)	$ (0.50)	$ (0.36)
Shares used in computing net loss per common share, basic and diluted	33,376	30,751	32,808	30,244

(1) Includes amortization of purchased intangible assets	$ 358	$ 466	$ 1,801	$ 1,397

See Notes to Condensed Consolidated Financial Statements.

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DemandTec, Inc

Condensed Consolidated Statements of Cash Flows

(In thousands)

(Unaudited)

	Nine Months Ended November 30, 2011	Nine Months Ended November 30, 2010
Operating activities:		
Net loss	$ (16,446)	$ (10,802)
Adjustment to reconcile net loss to net cash provided by operating activities:		
Depreciation	2,830	2,434
Stock-based compensation expense	8,563	7,665
Amortization of purchased intangible assets	2,433	2,197
Provision for doubtful accounts		485
Other	(32)	47
Changes in operating assets and liabilities:		
Accounts receivable	(4,744)	(4,005)
Prepaid expenses and other current assets	170	(506)
Other assets	(365)	(310)
Accounts payable and accrued liabilities	5,519	(639)
Accrued compensation	(2,365)	(2,004)
Deferred revenue	6,236	11,116
Net cash provided by operating activities	1,799	5,678
Investing activities:		
Purchases of property, equipment and leasehold improvements	(3,384)	(3,605)
Purchases of marketable securities	(42,132)	(52,297)
Maturities of marketable securities	40,949	43,523
Business acquisitions, net of cash acquired	(8,687)	(1,326)
Net cash used in investing activities	(13,254)	(13,705)
Financing activities:		
Proceeds from issuance of common stock	3,814	4,006
Payment of employee withholding tax in lieu of issuing common stock		(937)
Net cash provided by financing activities	3,814	3,069
Effect of exchange rate changes on cash and cash equivalents	(121)	2
Net decrease in cash and cash equivalents	(7,762)	(4,956)
Cash and cash equivalents at beginning of period	26,583	21,335
Cash and cash equivalents at end of period	$ 18,821	$ 16,379

See Notes to Condensed Consolidated Financial Statements.

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DemandTec, Inc.

Notes to Condensed Consolidated Financial Statements

1. Business Summary and Significant Accounting Policies

Description of Business

DemandTec, Inc. (the Company or We) was incorporated in Delaware on November 1, 1999. We provide a collaborative optimization network of software services connecting retail and consumer products, or CP, companies, enabling them to define category, brand, and shopper marketing strategies based on a scientific understanding of consumer behavior and make actionable pricing, promotion, assortment, space, and other merchandising and marketing decisions to achieve their revenue, profitability, sales volume, and customer loyalty objectives. We provide our applications by means of a software-as-a-service, or SaaS, model, which allows us to capture and analyze the most recent retailer and market-level data, enhance our software services rapidly to address our customers ever-changing merchandising and marketing needs, and connect retailers and CP companies online to enable improved, more collaborative business processes between trading partners. We are headquartered in San Mateo, California, with additional sales presence in North America, Europe, and South America, and research and development personnel in India, China, and Russia.

On December 7, 2011, we entered into a definitive agreement and plan of merger (the Merger Agreement) with International Business Machines Corporation (IBM) and Cudgee Acquisition Corp. (Sub), a wholly-owned subsidiary of IBM. Subject to the terms of the Merger Agreement and subject to the conditions thereof, Sub will merge with and into DemandTec, and DemandTec will become a wholly owned subsidiary of IBM (the Merger). If the Merger is completed, DemandTec s stockholders will be entitled to receive $13.20 in cash (the Merger Consideration) for each share of DemandTec s common stock owned by them as of the date of the Merger. See Note 13-Subsequent Event.

Basis of Presentation

Our condensed consolidated financial statements include our accounts and those of our wholly-owned subsidiaries. All significant intercompany balances and transactions have been eliminated in consolidation. Our fiscal year ends on the last day in February. References to fiscal 2012, for example, refer to our fiscal year ending February 29, 2012. The accompanying condensed consolidated balance sheet as of November 30, 2011, the condensed consolidated statements of operations for the three and nine months ended November 30, 2011 and 2010, and the condensed consolidated statements of cash flows for the nine months ended November 30, 2011 and 2010 are unaudited. The consolidated balance sheet data as of February 28, 2011 was derived from the audited consolidated financial statements included in our Annual Report on Form 10-K for the fiscal year ended February 28, 2011 (the Form 10-K) filed with the Securities and Exchange Commission, or SEC, on April 21, 2011. The accompanying statements should be read in conjunction with the audited consolidated financial statements and related notes contained in the Form 10-K, as well as subsequent filings with the SEC.

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States, or GAAP, for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, certain information and footnote disclosures normally included in consolidated financial statements prepared in accordance with GAAP have been condensed or omitted pursuant to such rules and regulations. The unaudited condensed consolidated financial statements have been prepared on the same basis as the audited consolidated financial statements and, in the opinion of our management, include all adjustments necessary, all of which are of a normal recurring nature, for the fair presentation of our statements of financial position and our results of operations for the periods included in this Quarterly Report on Form 10-Q. The results for the three and nine months ended November 30, 2011 are not necessarily indicative of the results to be expected for any subsequent quarter or for the fiscal year ending February 29, 2012.

Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the condensed consolidated financial statements, as well as the reported amounts of revenue and expenses during the periods presented. Significant estimates and assumptions made by management include the determination of the fair value of share-based payments, the fair value and estimated useful lives of purchased intangible assets, the recoverability of long-lived assets, the allowance for doubtful accounts, and the provision for income taxes. We believe that the estimates and judgments upon which we rely are reasonable, based upon information available to us at the time that these estimates and judgments are made. To the extent there are material differences between these estimates and actual results, our condensed consolidated financial statements will be affected.

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Revenue Recognition

We generate our revenue from providing access to hosted software and delivering related services to retailers and CP companies. Our customers generally do not have the contractual right to take possession of the software we host. Our agreements typically have initial contractual terms of one to three years and contain multiple elements, which include the use of our software, SaaS delivery services, professional services, maintenance, and customer support. Professional services consist of implementation, training, data modeling, and analytical services related to our customers use of our software. We have determined that the elements within our agreements generally do not qualify for treatment as separate units of accounting because our elements do not have stand-alone value. Software subscription, SaaS delivery services, maintenance, and customer support do not have stand-alone value because we do not sell these elements separately or without professional services due to their nature and complexity. Our professional services do not have stand-alone value because we do not sell these services separately and no third party vendors provide the complete set of professional services required to support our customers. Therefore, we account for all fees received under our agreements as a single unit of accounting and recognize them ratably over the term of the related agreement, commencing upon the later of the agreement start date or the date access to the application is provided to the customers, and when all of the following conditions are also met:

- there is persuasive evidence of an arrangement;
- the service has been provided to the customer;
- the collection of the fees is probable; and
- the amount of fees to be paid by the customer is fixed or determinable.

Deferred Revenue

Deferred revenue consists of amounts billed or payments received in advance of revenue recognition. Contracts under which we advance bill customers have generally been non-cancellable. For agreements with terms over one year, we generally invoice our customers in annual installments. Accordingly, the deferred revenue balance associated with such multi-year, non-cancellable agreements does not represent the total contract value. Deferred revenue to be recognized in the succeeding twelve-month period is included in current deferred revenue on our consolidated balance sheets, with the remaining amounts included in non-current deferred revenue.

Concentrations of Credit Risk, Significant Customers and Suppliers and Geographic Information

Our financial instruments that are exposed to concentrations of credit risk consist primarily of cash and cash equivalents, marketable securities, accounts receivable, and a line of credit. Although we deposit our cash with multiple financial institutions, our deposits, at times, may exceed federally insured limits. Collateral is not required for accounts receivable.

As of November 30, 2011 and February 28, 2011, long-lived assets located outside the United States were not significant. As of November 30, 2011, two customers accounted for 25% and 17%, respectively, of our accounts receivable balance. As of February 28, 2011, two customers accounted for 22% and 13%, respectively, of our accounts receivable balance.

In each of the three and nine months ended November 30, 2011, one customer accounted for 22% of total revenue. In the three months ended November 30, 2010, two customers accounted for 23% and 12%, respectively, of total revenue. In the nine months ended November 30, 2010, two customers accounted for 20% and 11%, respectively, of total revenue.

Revenue by geographic region, based on the billing address of the customer, was as follows (in thousands):

	Three Months Ended November 30,		Nine Months Ended November 30,	
	2011	**2010**	**2011**	**2010**
United States	$ 18,793	$ 18,756	$ 57,017	$ 51,962
International	3,520	2,914	9,778	8,141
Total revenue	$ 22,313	$ 21,670	$ 66,795	$ 60,103

The equipment hosting our software is in three third-party data center facilities located in San Jose and Sacramento, California, and Mesa, Arizona. We do not control the operation of these facilities, and our operations are vulnerable to damage or interruption in the event any one of these third-party data center facilities fails.

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Marketable Securities

We consider all highly liquid investments purchased with original maturities of three months or less to be cash equivalents. Cash and cash equivalents, which primarily consist of cash on deposit with banks and money market funds, are recorded at cost, which approximates fair value.

Our primary objectives when investing excess cash, in order of priority, are capital preservation, short-term liquidity, and achieving a reasonable rate of return. A significant portion of our marketable securities mature within one year and we limit the amount of credit exposure to any one issuer. We invest excess cash primarily in the securities of high credit quality issuers, such as highly liquid debt instruments of government-sponsored enterprises, commercial paper, corporate bonds, certificate of deposit, and money market instruments.

We classify our investments as held-to-maturity at the time of purchase and reevaluate the classification at each balance sheet date. We further classify them as current or non-current based on the maturity dates of the individual debt securities at each reporting date.

We monitor our investments in marketable securities for impairment on a periodic basis. For the purpose of impairment evaluation, we determine fair value based on the quoted market rate for the instrument or similar instruments. In the event that the carrying value of an investment exceeds its fair value and the decline in value is determined to be other-than-temporary, we record an impairment charge and establish a new cost basis for the investment. In order to determine whether a decline in value is other-than-temporary, we evaluate, among other things, the duration and extent to which the fair value has been less than the carrying value, current market conditions, and our intent and ability to retain the investment for a period of time sufficient to allow for any anticipated recovery in fair market value. We did not record any impairment adjustments in the current and prior year periods.

Business Combinations

We allocate the total cost of an acquisition to the underlying net assets based on their respective estimated fair values and recognize the identifiable assets acquired and liabilities assumed in accordance with business combination accounting standards. As part of the allocation process, we identify and attribute values and estimated useful lives to the intangible assets acquired. These determinations involve significant estimates and assumptions regarding multiple, highly subjective variables, including those with respect to future cash flows, discount rates, asset lives, and the use of different valuation models. We base our fair value estimates on assumptions we believe to be reasonable but are inherently uncertain. Depending on the purchase price of a particular acquisition as well as the mix of intangible assets acquired, our financial results could be materially impacted by the application of a different set of assumptions and estimates.

Impairment of Long-Lived Assets

Long-lived assets are reviewed for possible impairment whenever events or circumstances indicate that the carrying amount of these assets may not be recoverable. We evaluate the recoverability of each of our long-lived assets, including purchased intangible assets and property, equipment, and leasehold improvements, by comparison of its carrying amount to the future undiscounted cash flows we expect the asset to generate. If we consider the asset to be impaired, we measure the amount of any impairment as the difference between the carrying amount and the fair value of the impaired asset. We observed no impairment indicators through the filing of this Quarterly Report on Form 10-Q.

Stock-Based Compensation

We account for and recognize all share-based payments as an expense in our statements of operations. Grants of stock options to employees generally vest over four years. We measure the value of stock options based on the grant date fair value using the Black-Scholes pricing model. Performance-based stock units, or PSUs, vest pursuant to certain performance and time-based vesting criteria set by our Compensation Committee. We evaluate the probability of meeting the performance criteria at the end of each reporting period to determine how much compensation expense to record. Because the actual number of shares to be issued is not known until the end of the performance period, the actual compensation expense related to these awards could differ from our current expectations. We also have time-based restricted stock units, or RSUs, outstanding that entitle the recipient to receive shares of our common stock upon vesting and settlement of the awards pursuant to time-based vesting criteria set by our Compensation Committee. Stock-based compensation expense for PSUs and RSUs is based on the closing price of our common stock on the grant date. We amortize the fair value of those awards, net of estimated forfeitures, as stock-based compensation expense over the vesting period of the awards.

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Net Loss per Common Share

Basic net loss per share is computed using the weighted average number of common shares outstanding during the period. Potential common shares consist of the incremental common shares issuable upon the exercise of stock options or upon the settlement of PSUs and RSUs, and shares subject to issuance under our 2007 Employee Stock Purchase Program, or ESPP. The dilutive effect of such potential common shares is reflected in diluted loss per share by application of the treasury stock method and on an if-converted basis from the date of issuance. In the three months ended November 30, 2011 and 2010, weighted average outstanding shares subject to options to purchase common stock, PSUs and RSUs, and shares subject to issuance under our ESPP were approximately 1,776,000 shares and 3,828,000 shares, respectively. In the nine months ended November 30, 2011 and 2010, weighted average outstanding shares subject to options to purchase common stock, PSUs and RSUs, and shares subject to issuance under our ESPP were approximately 2,757,000 shares and 3,189,000 shares, respectively. Because the Company has been in a loss position in all periods shown, shares used in computing basic and diluted net loss per common share were the same for all periods presented, as the impact of all potentially dilutive securities outstanding was anti-dilutive.

Recent Accounting Pronouncements

In September 2011, the Financial Accounting Standards Board (the FASB) issued revised guidance regarding testing goodwill for impairment. The revised guidance is intended to reduce the cost and complexity of the annual goodwill impairment test by providing entities an option to perform a qualitative assessment to determine whether further impairment testing is necessary. An entity has the option to first assess qualitative factors to determine whether it is necessary to perform the current two-step test. If an entity believes, as a result of its qualitative assessment, that it is more likely than not that the fair value of a reporting unit is less than its carrying amount, the quantitative impairment test is required. Otherwise, no further testing is required. The guidance is effective for annual and interim goodwill impairment tests performed for fiscal years beginning after December 15, 2011. Early adoption is permitted. We expect to adopt the revised guidance in our first quarter ending May 31, 2012 and do not expect the adoption of this guidance to have an impact on our consolidated operating results or financial condition.

In June and December 2011, the FASB issued new guidance regarding the presentation of comprehensive income. The new guidance requires the presentation of the total of comprehensive income, the components of net income and the components of other comprehensive income either in a single continuous statement of comprehensive income or in two separate but consecutive statements, eliminating the option to present other comprehensive income as part of the statement of stockholder s equity. The guidance is effective prospectively for fiscal years beginning after December 15, 2011 and interim periods within those years. Early adoption is permitted. We expect to adopt the new presentation guidance in our first fiscal quarter ending May 31, 2012.

In May 2011, the FASB issued additional guidance on fair value measurements. The updated guidance provides a consistent definition of fair value and aligns the fair value measurement and disclosure requirements between U.S. GAAP and International Financial Reporting Standards (IFRS), amends certain guidance primarily related to fair value measurements for financial instruments, and enhances disclosure requirements particularly for level 3 fair value measurements. The guidance is effective prospectively for fiscal years beginning after December 15, 2011 and interim periods within those years. Early adoption is permitted. We do not expect the adoption of this guidance to have a significant impact on our consolidated operating results or financial condition.

In December 2010, the FASB issued guidance to amend the disclosure requirements for supplementary pro forma information for business combinations. The guidance improves consistency in how pro forma revenue and earnings are calculated. The amendments also expand the supplemental pro forma disclosures to include a description of the nature and amount of material, nonrecurring pro forma adjustments directly attributable to the business combination included in the reported pro forma revenue and earnings. The amendments are effective prospectively for business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2010. We adopted this new standard in the quarter ended May 31, 2011 and disclosed the required supplementary pro forma information in our condensed consolidated financial statements associated with the M-Factor acquisition. See Note 2-Acquisitions.

In October 2009, the FASB issued a new accounting standard for revenue recognition for arrangements with multiple deliverables. The new standard impacts the determination of when the individual deliverables included in a multiple-element arrangement may be treated as separate units of accounting. Additionally, the new standard modifies the manner in which the transaction consideration is allocated across the separately identified deliverables by no longer permitting the residual method of allocating arrangement consideration. The new standard is effective for fiscal years beginning on or after June 15, 2010. We adopted this new standard in the quarter ended May 31, 2011 and there was no impact on our condensed consolidated operating results or financial condition.

In October 2009, the FASB issued a new accounting standard for the accounting for certain revenue arrangements that include software elements. The new standard amends the scope of pre-existing software revenue guidance by removing from the guidance

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non-software components of tangible products and certain software components of tangible products. The new standard is effective for fiscal years beginning on or after June 15, 2010. We adopted this new standard in the quarter ended May 31, 2011 and there was no impact on our condensed consolidated operating results or financial condition.

2. Acquisitions

M-Factor, Inc.

On March 11, 2011, we acquired all of the outstanding equity interests of privately-held M-Factor, Inc. (M-Factor) for $9.5 million in cash. M-Factor is a software-as-service company that enables consumer products companies to continuously analyze, forecast, and optimize marketing investments and trade spending. We paid $9.0 million of the purchase consideration in the nine months ended November 30, 2011. The remaining $500,000, less any amounts used to satisfy any claims for indemnification obligations, will be distributed to the former M-Factor investors within sixteen months of the consummation of the acquisition.

Purchase Price Accounting

We accounted for the M-Factor acquisition as a business combination. We allocated the purchase price to the tangible and identifiable intangible assets acquired and liabilities assumed based on their estimated fair values as of the date of acquisition. We engaged an independent third-party valuation firm to assist us in the determination of the value of the purchased intangible assets. The excess of the purchase price over the fair value of net tangible and identifiable intangible assets acquired was recorded as goodwill. Although we believe the purchase price allocation is substantially complete, the finalization of certain liabilities, or the settlement of tax-related issues, among other things, could result in a future adjustment to the purchase price allocation.

The following table summarizes the estimated fair values of the assets acquired and liabilities assumed at the acquisition date (in thousands):

Cash	$	313
Current assets		716
Deferred tax assets, current		383
Property and equipment		182
Intangible assets		3,991
Goodwill		7,246
Deferred revenue		(1,625)
Other current liabilities		(1,323)
Deferred tax liabilities, non-current		(383)
Total purchase price	$	9,500

Goodwill will not be amortized and is not deductible for tax purposes. As part of the purchase accounting, we recorded $1.6 million of non-current deferred tax liabilities to reflect the tax effect of the temporary difference between the $4.0 million in fair value assigned to intangible assets acquired and their tax bases. We also recorded $1.6 million of deferred tax assets (approximately $383,000 in current assets and $1.2 million in non-current assets) to reflect the tax effect of the temporary differences on certain liabilities assumed and future tax deductible expenses, as well as a portion of M-Factor s pre-acquisition cumulative net operating loss. Approximately $1.2 million of the total $1.6 million of non-current deferred tax liabilities were offset by the non-current portion of the deferred tax assets.

Purchased Intangible Assets

The following table sets forth the estimated fair value of the purchased intangible assets and their estimated useful lives:

Purchased Intangible Assets		**Estimated Fair Value (In thousands)**	**Estimated Useful Life (In years)**
Developed technology	$	2,100	5
Customer relationships		850	3
Backlog		840	2
Non-compete covenants		190	2
Trade name		11	1
Total	$	3,991	

Intangible assets are being amortized on a straight-line basis over a weighted average period of 4.0 years. In the three months ended November 30, 2011, amortization expense related to the purchased intangible assets was approximately $307,000, of which

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$210,000 was included in cost of revenue and $97,000 was included in operating expenses. In the nine months ended November 30, 2011, amortization expense related to the purchased intangible assets was approximately $922,000, of which $630,000 was included in cost of revenue and $292,000 was included in operating expenses.

Acquisition-Related Costs and M-Factor s Post-Acquisition Operating Results

Acquisition-related costs associated with our acquisition of M-Factor were approximately $324,000, of which $194,000 was recorded in our condensed consolidated statements of operations for the nine months ended November 30, 2011 and the remaining costs were incurred prior to fiscal 2012. Acquisition-related costs, including legal fees and personnel costs for transitional and certain other employees and integration-related professional services, were recorded as operating expenses in accordance with the accounting guidance for business combinations. M-Factor s operating results have been included in our condensed consolidated financial statements from the date of the acquisition. In the three and nine months ended November 30, 2011, we derived approximately $514,000 and $2.4 million, respectively, of our revenue from acquired M-Factor customer contracts. The incremental operating loss from M-Factor was not separately identifiable due to our integration.

Unaudited Pro Forma Financial Information

The unaudited pro forma financial information in the table below presents the combined results of operations of the Company and M-Factor, as if the acquisition had occurred on March 1, 2010. The unaudited pro forma results presented include amortization expense for purchased intangible assets, elimination of intercompany transactions, and nonrecurring adjustments such as acquisition-related and restructuring costs. The unaudited pro forma financial information for the three and nine months ended November 30, 2010 combines our historical operating results for the three and nine months ended November 30, 2010 and M-Factor s historical operating results for the three and nine months ended September 30, 2010 (due to differences in reporting periods). The unaudited pro forma financial information for the nine months ended November 30, 2011 reflects the operating results of the combined company for the nine months ended November 30, 2011.

	Three Months Ended November 30,	Nine Months Ended November 30,	
	2010	2011	2010
	(in thousands, except per share data)		
Pro forma total revenue	$ 22,728	$ 66,981	$ 62,876
Pro forma net loss attributable to common stockholders	$ (4,797)	$ (15,734)	$ (19,542)
Pro forma basic and diluted net loss per common share	$ (0.16)	$ (0.48)	$ (0.65)

The unaudited pro forma financial information is presented for informational purposes only and is not indicative of the consolidated results of operations or financial condition of the combined company that would have been reported had the acquisition been completed as of the dates presented and should not be taken as representative of our future consolidated results of operations or financial condition.

Applied Intelligence Solutions, LLC

In December 2010, we acquired substantially all of the assets of Applied Intelligence Solutions, LLC (AIS), a provider of intelligent software solutions for retail enterprises, for approximately $3.2 million in cash. We accounted for the transaction as a business combination and recorded approximately $2.2 million of goodwill and $950,000 of identifiable intangible assets. Intangible assets are being amortized on a straight-line basis over a period of two to four years. Because this was an asset acquisition, the goodwill is tax deductible. Pro forma results of the acquired business have not been presented as it was not material to our consolidated financial statements for all periods presented.

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3. Balance Sheet Components

Marketable Securities

Marketable securities consisted of the following as of the dates indicated (in thousands):

	November 30, 2011				February 28, 2011			
		Unrecognized		Fair		Unrecognized		Fair
	Cost	Gain	Loss	Value	Cost	Gain	Loss	Value
Commercial paper	$ 5,298	$	$	$ 5,298	$ 1,800	$	$	$ 1,800
Certificates of deposit	1,567		(1)	1,566				
Corporate bonds	17,228	8	(17)	17,219	13,904	30	(2)	13,932
Obligations of government-sponsored enterprises	23,487	18	(2)	23,503	30,693	13	(2)	30,704
	$ 47,580	$ 26	$ (20)	$ 47,586	$ 46,397	$ 43	$ (4)	$ 46,436

The following table summarizes the book value of our investments in marketable debt securities classified by the contractual maturity date of the security as of the dates indicated (in thousands):

	November 30, 2011	February 28, 2011
Due within one year	$ 40,716	$ 40,834
Due within one to two years	6,864	5,563
	$ 47,580	$ 46,397

We classify all investments as held-to-maturity and, accordingly, record them on our balance sheet at amortized cost. We monitor our investments for impairment on a periodic basis and record an impairment charge if the carrying value of an investment exceeds its fair value and the decline in value is determined to be other-than-temporary. For the purposes of this impairment evaluation, we determine fair value based on the quoted market rate for the instrument or similar instruments. We have the ability and intent to hold our marketable securities to maturity and do not believe any of the marketable securities were impaired based on our evaluation of available evidence at the current balance sheet date and through the time of filing of this quarterly report on Form 10-Q. We expect to receive all principal and interest on all of our investment securities.

Accounts Payable and Accrued Expenses

Accounts payable and accrued expenses consisted of the following as of the dates indicated (in thousands):

	November 30, 2011	February 28, 2011
Accounts payable	$ 6,689	$ 3,528
Accrued acquisition-related costs (see Note 13)	2,222	
Accrued professional services	737	824
Income taxes payable	153	45
Accrued bonuses	1,593	3,054
Accrued vacation	2,183	1,726
Other accrued compensation	1,316	2,177
Merger consideration payable	975	
Other accrued liabilities	2,615	1,730
Total accounts payable and accrued expenses	$ 18,483	$ 13,084

4. Goodwill and Purchased Intangible Assets

We record as goodwill the excess of the acquisition purchase price over the fair value of the tangible and identifiable intangible assets acquired. We do not amortize goodwill, but perform an annual impairment review of our goodwill during our third fiscal quarter, or more frequently if indicators of potential impairment arise. We have a single operating segment and consequently evaluate goodwill for impairment based on an evaluation of the fair value of our company as a whole. As of February 28, 2011, we had approximately $18.8 million of goodwill from our acquisition of AIS in December 2010 and our pre-fiscal 2010 acquisitions of Connect3 and TradePoint. In the nine months ended November 30, 2011, we recorded approximately $7.2 million of goodwill associated with our acquisition of M-Factor in March 2011.

We record purchased intangible assets at their respective estimated fair values at the date of acquisition. Purchased intangible assets are being amortized using the straight-line method over their estimated useful lives of approximately one to seven years, with a remaining weighted average useful life of 2.9 years at November 30, 2011. We evaluate the remaining useful lives of intangible assets on a periodic basis to determine whether events or circumstances warrant a revision to the remaining estimated amortization period. Amortization expense related to the purchased intangible assets was approximately $568,000 and $683,000 in the three months ended

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November 30, 2011 and 2010, respectively, and was approximately $2.4 million and $2.2 million in the nine months ended November 30, 2011 and 2010, respectively.

We recognized no impairment charges as a result of our most recent impairment review. Additionally, we observed no impairment indicators for goodwill or intangible assets through the filing of this Quarterly Report on Form 10-Q.

5. Commitments and Contingencies

Commitments

We lease office space in various locations throughout the United States, Europe, and India. In September 2009, we entered into a lease agreement for office space in San Mateo, California, under which the total lease term is eight years with an initial non-cancellable lease term of five years commencing December 1, 2009. We use the office space as our corporate headquarters. The aggregate minimum lease commitment was approximately $10.1 million at the inception of the lease and $7.3 million as of November 30, 2011. To secure our obligations under the lease, we have provided the lessor a $223,000 cash security deposit and a $917,000 letter of credit, secured by using our existing revolving line of credit as described in Note 6. Additionally, the lessor provided us with a tenant improvement allowance of $265,000 and assumed our payment obligations (equal to approximately $200,000) under the previous sublease for our then-existing corporate headquarters in San Carlos, California for the period from December 1, 2009 through February 28, 2010, the expiration date of such sublease. The tenant improvement allowance and the $200,000 of assumed sublease obligations have been deferred and are being recognized on a straight-line basis over the lease term as reductions of rent expense. The leasehold improvements are being amortized on a straight-line basis over the lesser of the lease term or the estimated useful lives of the assets.

In fiscal 2010 and fiscal 2011, we entered into equipment and facility operating leases associated with our new data center in Mesa, Arizona, with minimum lease terms of two years for the equipment lease and three years for the facility lease. The aggregate minimum lease payments were approximately $1.5 million at the inception of the leases.

Legal Proceedings

We are aware of one purported class action lawsuit filed in the Superior Court of the State of California in and for the County of Santa Clara that an alleged DemandTec stockholder has filed against us, each member of our board of directors, IBM and Cudgee Acquisition Corp. in connection with the Merger. The complaint asserts claims for breach of fiduciary duty and aiding and abetting breach of fiduciary duty and seeks equitable relief, including an injunction preventing the consummation of the Merger, rescission in the event the Merger is consummated, and an award of damages. The outcome of any such litigation is uncertain. If a dismissal is not granted or a settlement is not reached, this lawsuit could prevent or delay completion of the Merger and result in substantial costs to us, including any costs associated with the indemnification of our directors and officers. Other DemandTec shareholders may also file additional lawsuits against us, IBM, and/or our directors and officers in connection with the Merger.

In addition, we have from time to time become involved in legal matters that arise in the normal course of business and otherwise. For example, we are currently involved in arbitration proceedings with an M-Factor customer associated with that customer s failure to pay amounts due under, and purported termination of, their agreement with M-Factor relating to certain services which is in the second year of a three year committed term. Beginning in our quarter ended November 30, 2011, that customer began withholding quarterly amounts, currently $573,000, due under the agreement. We are continuing to assess the impact of this dispute. There can be no assurance that this matter or other third party claims and litigation that may arise in the future will not have a material adverse effect on our business, financial position, results of operations, or cash flows, including a loss of customers, or subject us to significant financial or other remedies.

6. Debt

In May 2009, we amended our revolving line of credit that we had entered in April 2008 to, among other things, extend the maturity date of the loan agreement and to increase the revolving line of credit from $15.0 million to $20.0 million. The amended revolving line of credit can be used to (a) borrow revolving loans, (b) issue letters of credit, and (c) enter into foreign exchange contracts. Revolving loans may be borrowed, repaid, and reborrowed until May 2012. Amounts borrowed will bear interest, at our option, at either (1) a floating per annum rate equal to the financial institution s prime rate, or (2) the greater of (A) the LIBOR rate plus 250 basis points or (B) a per annum rate equal to 4.0%. A default interest rate shall apply during an event of default at a rate per annum equal to 500 basis points above the otherwise applicable interest rate. The line of credit is collateralized by substantially all of our assets and requires us to comply with working capital, net worth, and other non-financial covenants, including limitations on indebtedness and restrictions on dividend distributions, among others. In September 2009, the available balance was reduced by approximately $917,000 to $19.1 million to secure a new operating lease commitment. There were no outstanding amounts under the line of credit at November 30, 2011. Through the filing of this Quarterly Report on Form 10-Q, we were in compliance with all loan covenants.

7. Stock-Based Compensation

Equity Incentive Plans

1999 Equity Incentive Plan

In December 1999, our Board of Directors adopted the 1999 Equity Incentive Plan (the 1999 Plan). The 1999 Plan provided for incentive or nonstatutory stock options, stock bonuses, and rights to acquire restricted stock to be granted to employees, outside directors, and consultants. We ceased issuing awards under the 1999 Plan upon the completion of our Initial Public Offering (IPO) in August 2007. As of November 30, 2011, options to purchase 2,893,222 shares were outstanding under the 1999 Plan. Such options

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are exercisable as specified in each option agreement, generally vest over four years, and expire no more than ten years from the date of grant. If options awarded under the 1999 Plan are forfeited or repurchased, then shares underlying those options will no longer be available for awards.

2007 Equity Incentive Plan

In May 2007, our Board of Directors adopted, and in July 2007 our stockholders approved, the 2007 Equity Incentive Plan (the 2007 Plan). The 2007 Plan became effective upon our IPO. The 2007 Plan, which is administered by the Compensation Committee of our Board of Directors, provides for stock options, stock units, restricted shares, and stock appreciation rights to be granted to employees, outside directors and consultants. We initially reserved 3.0 million shares of our common stock for issuance under the 2007 Plan. In addition, on the first day of each fiscal year commencing with fiscal year 2009, the aggregate number of shares reserved for issuance under the 2007 Plan is automatically increased by a number equal to the lowest of a) 5% of the total number of shares of common stock then outstanding, b) 3,750,000 shares, or c) a number determined by our Board of Directors. As of November 30, 2011, 8,791,510 shares were reserved for issuance under the 2007 Plan.

Stock Options

Options granted under the 2007 Plan may be either incentive stock options or nonstatutory stock options and are exercisable as determined by the Compensation Committee and as specified in each option agreement. Options vest over a period of time as determined by the Compensation Committee, generally four years, and generally expire seven years (but in any event no more than ten years) from the date of grant. The exercise price of any stock option granted under the 2007 Plan may not be less than the fair market value of our common stock on the date of grant. The term of the 2007 Plan is ten years. As of November 30, 2011, options to purchase 3,266,666 shares were outstanding under the 2007 Plan.

Performance Stock Units (PSUs)

PSUs are awards under our 2007 Plan that entitle the recipient to receive shares of our common stock upon vesting and settlement of the awards pursuant to certain performance and time-based vesting criteria set by our Compensation Committee.

In May 2010, our Compensation Committee granted 314,250 PSUs to our executive officers, which related to fiscal 2011 company performance objectives and subsequent individual service requirements over a period of approximately 17 months, subject to each grantee s continued service. In April 2011, our Compensation Committee granted 159,375 PSUs to certain of our executive officers, which relate to fiscal 2012 company performance objectives and subsequent service requirements over a period of approximately 17 months. Those PSUs were granted in lieu of all or a portion of the annual variable cash compensation opportunity for certain executives. In September 2011, the Compensation Committee waived the performance objectives with respect to 12,500 of those PSUs that had been granted to one of our officers, such that those units will vest solely based on the officer s time-based service requirement (subject to certain change-in-control acceleration provisions). The modification had an immaterial impact on the stock-based compensation expense for the three months ended November 30, 2011.

As part of our annual equity incentive program, our Compensation Committee granted 839,800 PSUs to certain of our executive officers and other employees in April 2011, which relate to fiscal 2012 company performance objectives and subsequent individual service requirements over a period of approximately 33 months. The performance objectives associated with those PSUs were subsequently modified in June 2011 for all optionees, except with respect to our executive officers and certain other employees, as approved by our Compensation Committee. Had the performance objectives associated with those PSUs not been modified, stock-based compensation costs would have been approximately $633,000 lower in the nine months ended November 30, 2011. In addition, in September 2011, the Compensation Committee waived the performance objectives with respect to 20,000 of those PSUs that had been granted to one of our officers, such that those units will vest solely based on the officer s time-based service requirement (subject to certain change-in-control acceleration provisions). This modification had an immaterial impact on the stock-based compensation expense for the three months ended November 30, 2011.

As of November 30, 2011, there were approximately 959,150 shares subject to outstanding PSUs from grants in May 2010 and April 2011.

Restricted Stock Units (RSUs)

RSUs are awards under the 2007 Plan that entitle the recipient to receive shares of our common stock upon vesting and settlement of the awards pursuant to time-based vesting criteria set by our Compensation Committee.

In January 2010, our Compensation Committee granted 100,000 RSUs that vest over a period of approximately four years, subject to the grantee s continued services. In fiscal 2011, our Compensation Committee granted 1,322,000 RSUs to certain of our executive officers, other employees, and consultants. Such RSUs will vest over a period of approximately 24 to 27 months, subject to each

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grantee s continued service. In the nine months ended November 30, 2011, our Compensation Committee granted 305,250 RSUs to certain employees. These RSUs will vest over periods of approximately two to three years, subject to each grantee s continued service. Additionally, in August 2011, our Compensation Committee granted a total of 79,093 RSUs to the non-employee members of our board of directors, which will be fully vested on the earlier of a) the date of our 2012 Annual Meeting of Stockholders, or b) one year from the date of grant. As of November 30, 2011, there were approximately 1,053,122 shares subject to outstanding RSUs from these grants.

A summary of equity award activity during fiscal 2011 and the nine months ended November 30, 2011 follows (shares in thousands):

	Shares Available for Grant	**Shares Subject to Options Outstanding**	**Weighted Average Option Exercise Price per Share**
Balance at February 28, 2010	1,359	7,248	$ 5.72
Additional shares authorized	1,475		
Options granted	(1,570)	1,570	8.34
PSUs granted	(314)		
RSUs granted	(1,401)		
Options exercised		(1,515)	3.32
1999 Plan options cancelled/forfeited (1)		(54)	9.37
2007 Plan options cancelled/forfeited	598	(598)	8.96
PSUs and RSUs cancelled/forfeited	166		
Balance at February 28, 2011	313	6,651	$ 6.56
Additional shares authorized	1,589		
Options granted	(483)	483	9.91
PSUs granted	(999)		
RSUs granted	(384)		
Options exercised		(428)	3.40
1999 Plan options cancelled/forfeited (1)		(5)	9.04
2007 Plan options cancelled/forfeited	541	(541)	8.48
PSUs and RSUs cancelled/forfeited	266		
Balance at November 30, 2011	843	6,160	$ 6.87

(1) Under the terms of the 1999 Plan, shares underlying cancelled or forfeited options are no longer available for awards.

A summary of PSU activity during fiscal 2011 and the nine months ended November 30, 2011 follows (in thousands):

	Shares Subject to PSUs Outstanding
Balance at February 28, 2010	387
Granted	314
Released	(188)
Cancelled/forfeited	(30)
Balance at February 28, 2011	483
Granted	999

Released	(367)
Cancelled/forfeited	(156)
Balance at November 30, 2011	959

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A summary of RSU activity during fiscal 2011 and the nine months ended November 30, 2011 follows (in thousands):

	Shares Subject to RSUs Outstanding
Balance at February 28, 2010	560
Granted	1,401
Released	(459)
Cancelled/forfeited	(136)
Balance at February 28, 2011	1,366
Granted	384
Released	(587)
Cancelled/forfeited	(110)
Balance at November 30, 2011	1,053

Employee Stock Purchase Plan (ESPP)

In May 2007 our Board of Directors adopted, and in July 2007 our stockholders approved, the 2007 Employee Stock Purchase Plan. We subsequently amended the ESPP in March 2010. Under the ESPP, eligible employees may purchase shares of common stock at a price per share equal to 85% of the lesser of the fair market values of our common stock at the beginning or end of the applicable offering period. Each offering period lasts for six months. We initially reserved 500,000 shares of our common stock for issuance under the ESPP. In addition, on the first day of each fiscal year commencing with fiscal year 2009, the aggregate number of shares reserved for issuance under the ESPP is automatically increased by a number equal to the lowest of a) 1% of the total number of shares of common stock then outstanding, b) 375,000 shares, or c) a number determined by our Board of Directors. In the nine months ended November 30, 2011, employees purchased 316,859 shares under the ESPP, and the weighted average per share fair value of the options to purchase those shares was approximately $2.43. As of November 30, 2011, a total of 740,912 shares were available for issuance under the ESPP.

Stock-Based Compensation Expense Associated with Awards to Employees

We have issued employee stock-based awards in the form of stock options, PSUs, RSUs, and shares subject to the ESPP. We measure the value of stock options and shares subject to the ESPP based on their grant date fair value using the Black-Scholes pricing model. Stock-based compensation expense for PSUs and RSUs granted to employees is based on the closing price of our common stock on the grant date.

The determination of the fair value of stock options and shares subject to the ESPP on the date of grant is affected by our stock price, as well as by assumptions regarding a number of complex and subjective variables. These variables include our expected stock price volatility over the term of the options and awards, actual and projected employee stock option exercise behaviors, risk-free interest rates, and expected dividends, which are set forth in the table below:

Weighted Average	Expected Stock	Risk-free Interest	Expected Dividend	Weighted Average per Share Fair Value of

	Expected Term (in years)	Price Volatility	Rate	Yield	Awards Granted (per share)
Three months ended November 30, 2011					
Stock options	4.4	61%	0.7%	0%	$ 3.38
ESPP	0.5	57%	0.1%	0%	$ 2.20
Three months ended November 30, 2010					
Stock options	4.5	65%	2.4%	0%	$ 5.07
ESPP	0.5	47%	0.2%	0%	$ 3.06
Nine months ended November 30, 2011					
Stock options	4.4	62%	1.2%	0%	$ 4.92
ESPP	0.5	51%	0.1%	0%	$ 2.64
Nine months ended November 30, 2010					
Stock options	4.6	67%	2.3%	0%	$ 3.78
ESPP	0.5	44%	0.2%	0%	$ 2.30

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We amortize the fair value of the awards granted, net of estimated forfeitures, as stock-based compensation expense on a straight-line basis over the vesting period. We estimate forfeitures for our stock options, PSUs, and RSUs at the time of grant. At the end of each reporting period, we evaluate the probability of the service condition being met and revise those estimates based on actual results, taking into account cancellations related to terminations, as applicable to each award. In addition, for PSUs granted, we evaluate the probability of meeting the performance criteria at the end of each reporting period to determine how much compensation expense to record. The estimation of whether the performance targets and service periods will be achieved requires judgment. To the extent actual results or updated estimates differ from our current estimates, either (a) the cumulative effect on current and prior periods of those changes will be recorded in the period those estimates are revised or (b) the change in estimate will be applied prospectively, depending on whether the change affects the estimate of total stock-based compensation expense to be recognized or merely affects the period over which such expense will be recognized. The cumulative adjustments in the three and nine months ended November 30, 2011 decreased stock-based compensation expense by approximately $247,000 and $534,000, respectively. The cumulative adjustments in the three and nine months ended November 30, 2010 were not material.

Stock-Based Compensation for Non-Employees

Stock-based compensation expense related to stock awards granted to non-employees is recognized as the awards vest. We believe that the fair value of the stock-based awards granted is more reliably measurable than the fair value of the services received. The fair value of the stock options granted is calculated using the Black-Scholes option pricing model. The fair value of RSUs granted is based on the closing price of our common stock on each reporting date. The fair value of the award is remeasured at each reporting date until the earlier of (a) the performance commitment date or (b) the date the services required under the arrangement have been completed. Stock-based compensation expense related to awards granted to non-employees for the three and nine months ended November 30, 2011 was approximately $141,000 and $262,000, respectively, and was not material for the three and nine months ended November 30, 2010.

The fair values of unvested options granted to non-employees were calculated using the following assumptions for the periods presented:

	Three Months Ended November 30,		**Nine Months Ended November 30,**	
	2011	**2010**	**2011**	**2010**
Weighted average expected term (in years)	6.2	4.7	6.4	6.2
Expected stock price volatility	61%	65%	61%	67%
Risk-free interest rate	1.6%	1.9%	2.0%	3.1%
Expected dividend yield	0%	0%	0%	0%

Stock-Based Compensation Expense Summary

The following table sets forth the stock-based compensation expense for equity awards recorded in the condensed consolidated statements of operations for the periods presented (in thousands):

	Three Months Ended November 30,		**Nine Months Ended November 30,**	
	2011	**2010**	**2011**	**2010**
Cost of revenue	$ 465	$ 484	$ 1,679	$ 1,312

Research and development	917	894	3,055	2,443
Sales and marketing	748	625	2,237	2,032
General and administrative	402	582	1,592	1,878
Total stock-based compensation expense	$ 2,532	$ 2,585	$ 8,563	$ 7,665

The following table summarizes gross unrecognized stock-based compensation expense as of November 30, 2011, excluding estimated forfeitures:

	Unrecognized Stock-Based Compensation Expense (in thousands)	Remaining Weighted Average Recognition Period (in years)
Stock options granted after March 1, 2006	$ 8,759	2.6
PSUs	3,820	1.5
RSUs	5,494	1.1
ESPP	293	0.4
	$ 18,366	1.9

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8. Income Taxes

In the three and nine months ended November 30, 2011, we recorded income tax expense of approximately $148,000 and $318,000, respectively, compared to income tax expense of $29,000 and $105,000, respectively, in the corresponding periods of the prior year. The effective tax rate for the three and nine months ended November 30, 2011 was approximately 3% and 2%, respectively, based on our estimated taxable income for the year. We recorded tax expense primarily for foreign taxes and state minimum taxes.

There were no material changes to our unrecognized tax benefits in the three months ended November 30, 2011 and we do not expect to have any significant changes to unrecognized tax benefits over the next twelve months. Because of our history of operating losses, all years remain open to audit.

9. Derivative Financial Instruments

We maintain a foreign currency risk management strategy that includes the use of derivative financial instruments designed to protect our economic value from the possible adverse effects of currency fluctuations. We do not enter into derivative financial instruments for speculative or trading purposes. Our hedging relationships are formally documented at the inception of the hedge, and hedges must be highly effective in offsetting changes to future cash flows on hedged transactions both at the inception of a hedge and on an ongoing basis. We record the ineffective portion of hedging instruments, if any, to other income (expense) in the consolidated statements of operations.

As of November 30, 2011, we had three outstanding forward contracts with an aggregate notional principal of approximately $2.8 million, which are summarized as follows (in thousands):

	Notional Principal (Local Currency)	Notional Principal (USD)	Fair Value (USD)	Accumulated Amortized Implicit Interest (USD)
Euro maturing in December 2012 (1)	925	$ 1,251	$ 3	$
Euro maturing in September 2012 and 2013 (1)	1,083	1,544	81	9
	2,008	$ 2,795	$ 84	$ 9

(1) Related to multi-year customer arrangements, under which we separately hedge each equal annual billing amount.

We designated these forward contracts as cash flow hedges of foreign currency denominated firm commitments. Our objective in purchasing these forward contracts was to negate the impact of currency exchange rate movements on our operating results. We record effective spot-to-spot changes in these cash flow hedges in accumulated other comprehensive income until the hedged transaction takes place. Combined implied interest on all forward contracts was excluded from effectiveness testing and is being recorded using the straight-line method over the terms of the forward contracts to interest expense and accumulated other comprehensive income. We did not incur any hedge ineffectiveness in the three and nine months ended November 30, 2011 and 2010.

		Amount of Gain Recognized In Income			
		Three Months Ended November 30,		Nine Months Ended November 30,	
Derivatives Designated as Hedging Instruments	**Location**	**2011**	**2010**	**2011**	**2010**
Forward contracts	Revenue	$ 11	$ 106	$ 140	$ 246

We expect to ratably reclassify an approximately $5,000 net gain associated with the forward contracts that matured in December 2010, February and November 2011 from accumulated other comprehensive income into revenue over the twelve-month period ending November 30, 2012.

10. Fair Value Measurements

The accounting standards for fair value measurements clarify that fair value is an exit price, representing the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants. As such, fair value is a market-based measurement that should be determined based on assumptions that market participants would use in pricing an asset or a

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liability. As a basis for considering such assumptions, the accounting standards establish a three-tier value hierarchy, which prioritizes the inputs used in the valuation methodologies in measuring fair value:

Level 1 Observable inputs that reflect quoted prices (unadjusted) for identical assets or liabilities in active markets.

Level 2 Include other inputs that are directly or indirectly observable in the marketplace.

Level 3 Unobservable inputs which are supported by little or no market activity.

The fair value hierarchy requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value.

We measure our foreign currency forward contracts at fair value using Level 2 inputs, as the valuation inputs are based on quoted prices of similar instruments in active markets and do not involve management judgment.

The following table summarizes the amounts measured at fair value (in thousands):

	Total	Significant Other Observable Inputs (Level 2)
November 30, 2011		
Assets:		
Foreign currency forward contracts (1)	$ 84	$ 84
February 28, 2011		
Liabilities:		
Foreign currency forward contracts (1)	$ 33	$ 33

(1) At November 30, 2011, $46 was included in other current assets and $38 was included in other assets on our condensed consolidated balance sheet. At February 28, 2011, $24 was included in other current liabilities and $9 was included in other long-term liabilities on our condensed consolidated balance sheet.

11. Comprehensive Loss

The following table summarizes the calculation and components of comprehensive loss, net of taxes (in thousands):

	Three Months Ended November 30, 2011	Three Months Ended November 30, 2010	Nine Months Ended November 30, 2011	Nine Months Ended November 30, 2010
Net loss	$ (4,987)	$ (2,085)	$ (16,446)	$ (10,802)
Gain reclassified from accumulated other comprehensive income into revenue	(11)	(106)	(140)	(246)
Change in net unrealized gain (loss) and cumulative implied interest on cash flow hedges	208	(124)	88	277
Total comprehensive loss	$ (4,790)	$ (2,315)	$ (16,498)	$ (10,771)

12. Restructuring Charges

In the nine months ended November 30, 2011, we recorded approximately $604,000 of expenses associated with the reduction of our workforce as part of our M-Factor post-acquisition integration process to achieve cost savings and operating efficiencies. Expenses associated with these actions were primarily for severance payments and remaining operating lease obligations as a result of office consolidation. All expenses have been paid at November 30, 2011, except approximately $80,000 of a remaining operating lease obligation.

13. Subsequent Event

On December 7, 2011, we entered into a definitive agreement and plan of merger (the Merger Agreement) with International Business Machines Corporation (IBM) and Cudgee Acquisition Corp. (Sub), a wholly-owned subsidiary of IBM. Subject to the terms of the Merger Agreement and subject to the conditions thereof, Sub will merge with and into DemandTec, and DemandTec will become a wholly owned subsidiary of IBM (the Merger). If the Merger is completed, DemandTec s stockholders will be entitled to

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receive $13.20 in cash (the Merger Consideration) for each share of DemandTec s common stock owned by them as of the date of the Merger. The consummation of the merger is subject to certain conditions, including adoption of the Merger Agreement by DemandTec s stockholders, the continuing accuracy of DemandTec and IBM s respective representations and warranties, the expiration or termination of any waiting period under the Hart-Scott-Rodino Act of 1976, as amended (which waiting period terminated on January 3, 2012), as well as any similar filings that need to be made in any foreign jurisdictions. The dates for closing the Merger and for DemandTec s stockholder meeting to vote on adoption of the Merger Agreement have not yet been determined. The Merger Agreement contains certain termination rights of IBM and DemandTec and provides that, under specified circumstances, upon termination of the Merger Agreeement, DemandTec will be required to pay IBM a termination fee of $14.0 million. A description of the Merger Agreement is contained in DemandTec s Current Report on Form 8-K filed with the SEC on December 7, 2011, and a copy of the Merger Agreement is attached thereto as Exhibit 2.1. In the three months ended November 30, 2011, we recognized and accrued approximately $2.2 million for non-contingent legal and investment banking advisory service fees incurred as a result of the Merger Agreement.

Item 2. Management s Discussion and Analysis of Financial Condition and Results of Operations

This quarterly report on Form 10-Q contains forward-looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended. In addition, we may make other written and oral communications from time to time that contain such statements. Forward-looking statements include statements as to industry trends *and future expectations of ours and other matters that do not relate strictly to historical facts. These statements are often identified by the use of words such as may, will, expect, believe, anticipate, intend, could, estimate, or continue, and similar expressions or variations. These statements are based on the beliefs and assumptions of our management based on information currently available to management. Such forward-looking statements are subject to risks, uncertainties and other factors that could cause actual results and the timing of certain events to differ materially from future results expressed or implied by such forward-looking statements. These forward-looking statements include statements in this Item 2, Management s Discussion and Analysis of Financial Condition and Results of Operations. Factors that could cause or contribute to such differences include, but are not limited to, those identified below, and those discussed in the section titled Risk Factors included elsewhere in this Form 10-Q and in our other Securities and Exchange Commission filings, including our Annual Report on Form 10-K for the fiscal year ended February 28, 2011. Furthermore, such forward-looking statements speak only as of the date of this report. We undertake no obligation to update any forward-looking statements to reflect events or circumstances after the date of such statements.*

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with the condensed consolidated financial statements and related notes thereto appearing elsewhere *in this Form 10-Q and with the consolidated financial statements and notes thereto and management s discussion and analysis of financial condition and results of operation appearing in our Annual Report on Form 10-K for the fiscal year ended February 28, 2011.*

Overview

We provide a collaborative optimization network of software services connecting retail and CP companies, enabling them to define category, brand, and shopper marketing strategies based on a scientific understanding of consumer behavior and make actionable pricing, promotion, assortment, space and other merchandising and marketing recommendations to achieve their revenue, profitability, sales volume, and customer loyalty objectives. We provide our applications by means of a software-as-a-service, or SaaS, model, which allows us to capture and analyze the most recent retailer and market-level data and enhance our software services rapidly to address our customers ever-changing merchandising and marketing needs, and connect retailers and CP companies online to enable improved, more collaborative business processes between trading partners.

Our solutions consist of software services and complementary analytical services and analytical insights derived from the same platform that supports our software services. We offer our solutions individually or as a suite of integrated software services. Our solutions for the retail and CP industries include DemandTec Lifecycle Price Optimization , DemandTec End-to-End Promotion Management , DemandTec Assortment & Space , DemandTec Shopper Insights , DemandTec Targeted Marketing , DemandTec Marketing Plan Optimization , DemandTec Total Trade Optimization , DemandTec Shopper Marketing Optimization , and DemandTec Connect . The DemandTec network connects our solutions for the retail and CP industries. We sell our solutions through our direct sales force and receive a number of customer prospect introductions through third parties, such as systems integrators, strategic consulting firms, and a data syndication company.

We were incorporated in November 1999 and began selling our software in fiscal 2001. Our revenue has grown from $43.5 million in fiscal 2007 to $82.4 million in fiscal 2011, and was $66.8 million in the nine months ended November 30, 2011. Our operating expenses have also increased significantly during these same periods. We have incurred losses to date and had an accumulated deficit of approximately $119.3 million as of November 30, 2011. We generate our revenue from delivery of our hosted software and related services to retailers and CP companies. Our customers generally do not have the contractual right to take possession of the software we host. Our software service agreements with retailers and CP companies are often large contracts. The

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annual contract value for each retail and CP company customer agreement is largely related to the size of the customer. Our agreements with retail customers are typically one to three years in length and billable annually upfront. Our advanced deal management agreements with CP companies that leverage the DemandTec network are principally one year in length and much smaller in annual and aggregate contract value than our other CP company customer software services contracts and our retail customer contracts. Generally, the agreements we have signed in the first fiscal quarter of a fiscal year have had an aggregate annual contract value less than that of the agreements signed in the preceding fiscal fourth quarter. In addition, the aggregate contract value of agreements signed can fluctuate significantly on a quarterly basis within any given fiscal year. A significant percentage of our new and existing customer add-on agreements are entered into during the last month, weeks, or even days of each quarter. We generally recognize the revenue from each agreement ratably over the term of the agreement. Our ability to maintain or increase revenues depends on our attracting new customers, renewing agreements with our existing customers at comparable prices, and selling add-on software services to existing customers as well as successfully incorporating shopper segmentation and analytics into our offerings. Historically, some customers or potential customers have elected not to enter into new or renewal contracts and some other customers have renewed at lower prices or for shorter terms. Further, our revenue will be directly affected by the continued acceptance of our software solutions in the marketplace, as well as the timing, size and term length of our customer agreements. If we are unable to successfully develop or acquire new software and enhance our existing applications, we may not be able to attract and retain customers or increase or maintain our revenue.

We are headquartered in San Mateo, California. We have sales and marketing offices in North America and Europe, and conduct research and development operations in India, Russia, and China. In the quarters ended November 30, 2011 and 2010, approximately 84% and 87%, respectively, of our revenue was attributable to sales of our software to companies located in the United States. In the nine months ended November 30, 2011 and 2010, approximately 85% and 86%, respectively, of our revenue was attributable to sales of our software to companies located in the United States. Our ability to achieve profitability will be affected by our revenue as well as by the level of our operating expenses associated with growing our business. Our largest category of operating expenses is research and development expenses, and the largest component of our operating expenses is personnel costs.

In March 2011, we acquired M-Factor, Inc. (M-Factor), a provider of predictive analytics software for CP companies that optimizes marketing mix and trade investment spending. M-Factor is a software-as-a-service company that enables consumer products companies to continuously analyze, forecast, and optimize marketing investments and trade spending. The services deliver optimized action plans, reliable forecasts for plans and what-if scenarios, and reports that decompose the drivers of sales volume to explain why results came out as they did. The aggregate purchase price was $9.5 million in cash, of which $9.0 million was paid to M-Factor investors upon closing. The remaining $500,000 is being held by the Company to secure potential indemnification obligations of M-Factor investors and will be released approximately sixteen months after the closing, to the extent not used to satisfy the indemnity obligations. We accounted for the M-Factor acquisition as a business combination. See Note 2 of the Notes to Condensed Consolidated Financial Statements. After the M-Factor acquisition, we reduced our workforce and consolidated facilities to achieve cost savings and operating efficiencies, and consequently recorded approximately $604,000 of restructuring charges in the nine months ended November 30, 2011. In addition, we incurred approximately $1.0 million of non-recurring personnel-related costs for transitional employees, redundant facility costs, and integration related professional services fees in the three months ended May 31, 2011 which would not have otherwise been incurred in the period presented as a part of our continuing operations.

As of December 30, 2011, we had approximately 33.8 million shares of common stock outstanding, excluding approximately 8.2 million shares subject to outstanding options, performance stock units, restricted stock units, and rights under our employee stock purchase program. The issuance of shares upon the exercise of these options and settlement of these units, as well as the grant of additional options and units pursuant to our equity compensation plans, would result in additional dilution and may adversely impact our earnings per share. See Note 7 of Notes to Condensed Consolidated Financial Statements.

Recent Development

On December 7, 2011, we entered into a definitive agreement and plan of merger (the Merger Agreement) with International Business Machines Corporation (IBM) and Cudgee Acquisition Corp. (Sub), a wholly-owned subsidiary of IBM. Subject to the terms of the Merger Agreement and subject to the conditions thereof, Sub will merge with and into DemandTec, and DemandTec will become a wholly owned subsidiary of IBM (the Merger). If the Merger is completed, DemandTec s stockholders will be entitled to receive $13.20 in cash (the Merger Consideration) for each share of DemandTec s common stock owned by them as of the date of the Merger. The consummation of the merger is subject to certain conditions, including adoption of the Merger Agreement by DemandTec s stockholders, the continuing accuracy of DemandTec and IBM s respective representations and warranties, the expiration or termination of any waiting period under the Hart-Scott-Rodino Act of 1976, as amended (which waiting period terminated on January 3, 2012), as well as any similar filings that need to be made in any foreign jurisdictions. The dates for closing the Merger and for DemandTec s stockholder meeting to vote on adoption of the Merger Agreement have not yet been determined. The Merger Agreement contains certain termination rights of IBM and DemandTec and provides that, under specified circumstances, upon termination of the Merger Agreeement, DemandTec will be required to pay IBM a termination fee of $14.0 million. A description of the Merger Agreement is contained in DemandTec s

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Current Report on Form 8-K filed with the SEC on December 7, 2011, and a copy of the Merger Agreement is attached thereto as Exhibit 2.1. In the three months ended November 30, 2011, we recognized and accrued approximately $2.2 million for non-contingent legal and investment banking advisory service fees incurred as a result of the Merger Agreement. We expect to incur additional non-contingent legal and other acquisition-related costs in the fiscal quarter ending February 29, 2012. In addition, fees that are contingent upon the consummation of the merger include approximately $4.4 million for investment banking transaction fees.

Critical Accounting Policies and Estimates

We prepare our consolidated financial statements in accordance with accounting principles generally accepted in the United States. These accounting principles require us to make certain estimates and judgments that can affect the reported amounts of assets and liabilities as of the date of our consolidated financial statements, as well as the reported amounts of revenue and expenses during the periods presented. We believe that our estimates and judgments were reasonable based upon information available to us at the time that these estimates and judgments were made. We evaluate our estimates and judgments on an ongoing basis. To the extent that there are material differences between these estimates and actual results, our consolidated financial statements could be adversely affected. The accounting policies that we believe reflect our more significant estimates, judgments and assumptions and which we believe are the most critical to aid in fully understanding and evaluating our reported financial results include the following:

- Revenue Recognition
- Stock-Based Compensation
- Goodwill and Intangible Assets
- Impairment of Long-Lived Assets

In many cases, the accounting treatment of a particular transaction is specifically dictated by GAAP and does not require management s judgment in its application. There are also areas in which management s judgment in selecting among available accounting policy alternatives would not produce a materially different result.

During the nine months ended November 30, 2011, there were no significant changes in our critical accounting policies. Please refer to Management s Discussion and Analysis of Financial Condition and Results of Operations contained in our Annual Report on Form 10-K for the fiscal year ended February 28, 2011 and Note 1 of Notes to Condensed Consolidated Financial Statements included herein for a more complete discussion of our critical accounting policies and estimates.

Results of Operations

Revenue

We derive our revenue from delivery of hosted software and related services to retailers and CP companies. Our customers generally do not have the contractual right to take possession of the software we host. We generally recognize all revenue ratably over the term of the agreement. Our agreements have generally been non-cancellable, but customers typically have the right to terminate their agreement for cause if we materially breach our obligations under the agreement and, in certain situations, may have the ability to extend the duration of their agreement on pre-negotiated terms. We invoice our customers in accordance with contractual terms, which generally have provided that our customers are invoiced in advance for annual use of our software services. We have provided certain implementation services on a fixed fee basis and have generally invoiced our customers in advance. In addition, we have provided implementation and training services on a time and materials basis and have invoiced our customers monthly in arrears. Our payment terms typically require our customers to pay us within 30 days of the invoice date.

	Three Months Ended November 30,		Nine Months Ended November 30,	
	2011	2010	2011	2010
	(in thousands)			
Revenue	$ 22,313	$ 21,670	$ 66,795	$ 60,103

Three and Nine Months Ended November 30, 2011 Compared to the Three and Nine Months Ended November 30, 2010. Revenue for the three months ended November 30, 2011 increased approximately $643,000, or 3%, compared to the corresponding period of the prior year, primarily due to $2.0 million of revenue from new customers, of which approximately $514,000 was derived from acquired M-Factor customer contracts, offset by a $1.4 million decrease in revenue from existing customers. Revenue for the nine months ended November 30, 2011 increased approximately $6.7 million, or 11%, compared to the corresponding period of the prior year, primarily due to $5.0 million of revenue from new customers, of which approximately $2.4 million was derived from acquired M-Factor customer contracts, and a $1.7 million increase in revenue from existing customers. New customers are those that did not

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contribute any revenue in the three and nine months ended November 30, 2010. Existing customers are those that contributed revenue in each of the periods presented.

In each of the three and nine months ended November 30, 2011, one customer accounted for 22% of total revenue. In the three months ended November 30, 2010, two customers accounted for 23% and 12%, respectively, of total revenue. In the nine months ended November 30, 2010, two customers accounted for 20% and 11%, respectively, of total revenue.

Percentages of total revenue by customer type and geographic region for the periods presented were as follows:

	Three Months Ended November 30,		Nine Months Ended November 30,	
	2011	**2010**	**2011**	**2010**
By customer type:				
Retail	77%	82%	77%	81%
CP	23	18	23	19
Total revenue	100%	100%	100%	100%
By location:				
United States	84%	87%	85%	86%
International	16	13	15	14
Total revenue	100%	100%	100%	100%

Revenue from CP companies and from customers located outside the United States continued to increase as a percentage of total revenue in the three and nine months ended November 30, 2011 compared to the corresponding periods of the prior year, largely as a result of incremental revenue from former M-Factor customers, all of which are CP companies. Over the long term, we expect that revenue from CP companies and international customers will increase as a percentage of total revenue on an annual basis.

Our revenue growth depends on our ability to attract new customers and to retain the existing revenues from our current customers over time. In addition, revenue from new customers in any given period can fluctuate depending upon when the contract is signed during the period, the number of new customer contracts, and the size of the new retailer or CP customer. With the existing uncertainties in the global economic environment, we believe our revenue growth is difficult to predict.

Cost of Revenue

Cost of revenue includes expenses related to data centers, depreciation expenses associated with computer equipment and software, compensation and related expenses of operations, technical customer support, production operations and professional services personnel, amortization of purchased intangible assets, and allocated overhead expenses. We have contracts with three third parties for the use of their data center facilities, and our data center costs principally consist of the amounts we pay to these third parties for rack space, power and similar items. We amortize purchased intangible assets, principally for developed technology. We allocate overhead costs, such as rent and occupancy costs, employee benefits, information management costs, and legal and other costs, to all departments predominantly based on headcount. As a result, we include allocated overhead expenses in cost of revenue and each operating expense category.

	Three Months Ended November 30, 2011	Three Months Ended November 30, 2010	Nine Months Ended November 30, 2011	Nine Months Ended November 30, 2010
	(dollars in thousands)			
Revenue	$ 22,313	$ 21,670	$ 66,795	$ 60,103
Cost of revenue	8,012	7,468	25,627	21,664
Gross profit	14,301	14,202	41,168	38,439
Gross margin	64%	66%	62%	64%

Three and Nine Months Ended November 30, 2011 Compared to the Three and Nine Months Ended November 30, 2010. Cost of revenue in the three and nine months ended November 30, 2011 increased approximately $544,000, or 7%, and $4.0 million, or 18%, respectively, from the corresponding periods of the prior year, primarily due to increased personnel-related costs, data center costs, allocated overhead costs, and amortization of purchased intangible assets associated with the AIS and M-Factor acquisitions.

Personnel-related costs in the three and nine months ended November 30, 2011 increased $259,000 and $1.9 million, respectively, compared to the corresponding periods of the prior year. Average headcount increased by approximately 12 and 20, respectively, in the three and nine months ended November 30, 2011 compared to the corresponding periods of the prior year, primarily due to the M-Factor acquisition. In addition, stock-based compensation expense, which is a component of personnel-related costs, increased $367,000 in the nine months ended November 30, 2011 compared to the corresponding period of the prior year as we granted

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additional PSUs and RSUs in April 2011. Expenses associated with our data center in Mesa, Arizona in the three and nine months ended November 30, 2011 increased $145,000 and $824,000, respectively, compared to the corresponding periods of the prior year, as we expanded our infrastructure to handle the increased level of customer data processed and analyzed to embed shopper segments and insights in our service offerings and replaced old equipment. Allocated overhead costs in the three and nine months ended November 30, 2011 increased $198,000 and $607,000, respectively, compared to the corresponding periods of the prior year, largely due to increased headcount and facility-related and IT costs allocated to cost of revenue, which included some non-recurring charges related to our office consolidation. Amortization of purchased intangible assets decreased $107,000 in the three months ended November 30, 2011 but increased $405,000 in the nine months ended November 30, 2011, compared to the corresponding periods of the prior year, due to the increased amortization expenses from the purchased developed technologies associated with the AIS and M-Factor acquisitions that were partially offset by decreased amortization expenses from intangible assets associated with the TradePoint and Connect3 acquisitions that became fully amortized in October and August 2011, respectively.

Our gross margin decreased to 64% and 62%, respectively, in each of the three and nine months ended November 30, 2011 compared to 66% and 64% in the corresponding periods of the prior year, primarily due to increased personnel-related costs associated with the AIS and M-Factor acquisitions and the expansion of the infrastructure of our data centers. We anticipate that, in the short term, our gross margin will remain flat or increase slightly.

Research and Development Expenses

Research and development expenses include personnel costs for our research, product management and software development personnel, and allocated overhead expenses. We devote substantial resources to extending our existing software applications as well as to developing new software.

	Three Months Ended November 30, 2011	Three Months Ended November 30, 2010	Nine Months Ended November 30, 2011	Nine Months Ended November 30, 2010
	(dollars in thousands)			
Research and development	$ 8,464	$ 8,011	$ 26,722	$ 23,557
Percent of revenue	38%	37%	40%	39%

Three and Nine Months Ended November 30, 2011 Compared to the Three and Nine Months Ended November 30, 2010. Research and development expenses in the three and nine months ended November 30, 2011 increased approximately $453,000, or 6%, and $3.2 million, or 13%, respectively, from the corresponding periods of the prior year, primarily due to increased personnel-related costs and consulting expenses.

Personnel-related costs in the three and nine months ended November 30, 2011 increased $182,000 and $1.9 million, respectively, compared to the corresponding periods of the prior year. Average headcount increased by approximately 13 and 18, respectively, in the three and nine months ended November 30, 2011, primarily due to our recently established development presence in India and employees retained from our M-Factor acquisition. Stock-based compensation expense, which is a component of personnel-related costs, increased approximately $612,000 in the nine months ended November 30, 2011 compared to the corresponding period of the prior year, primarily due to additional PSUs and RSUs granted in April 2011. Consulting expenses increased $248,000 and $977,000, respectively, in the three and nine months ended November 30, 2011 from the corresponding periods of the prior year, as we expanded our outsourced research and development services in China, retained third-party consulting services in Russia as part of the AIS acquisition, and supplemented our development efforts related to apparel retailing by using outside consultants.

We intend to continue to invest significantly in our research and development efforts because we believe these efforts are essential to maintaining our competitive position over the long-term. In the short term, we expect that research and development costs will increase in absolute dollars. Over time, we expect that our research and development costs will decrease as a percentage of revenue.

Sales and Marketing Expenses

Sales and marketing expenses include personnel costs for our sales and marketing personnel, including commissions and incentives, travel and entertainment expenses, marketing programs such as product marketing, events, corporate communications and other brand building expenses, and allocated overhead expenses.

	Three Months Ended November 30,		Nine Months Ended November 30,	
	2011	2010	2011	2010
	(dollars in thousands)			
Sales and marketing	$ 5,787	$ 5,629	$ 19,412	$ 17,616
Percent of revenue	26%	26%	29%	29%

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Three and Nine Months Ended November 30, 2011 Compared to the Three and Nine Months Ended November 30, 2010. Sales and marketing expenses in the three and nine months ended November 30, 2011 increased approximately $158,000, or 3%, and $1.8 million, or 10%, respectively, from the corresponding periods of the prior year. The increase in the three months ended November 30, 2011 was primarily due to increased personnel-related costs, partially offset by decreased outside consulting costs. The increase in the nine months ended November 30, 2011 was primarily due to increased personnel-related costs, outside consulting, and travel-related expense, partially offset by decreased bad debt expense.

Personnel-related costs in the three and nine months ended November 30, 2011 increased $247,000 and $1.8 million, respectively, compared to the corresponding periods of the prior year, primarily attributable to increases in stock-based compensation expense, severance expense and employer payroll tax in both the three and nine month periods, and commission and salary expenses in the nine-month period only. Stock-based compensation expense, a component of personnel-related costs, increased $122,000 and $205,000 in the three and nine months ended November 30, 2011 as a result of the grant of PSUs and RSUs in April 2011. Severance expense in the three and nine months ended November 30, 2011 was associated with the termination of sales employees. Increased employer payroll tax, associated with settlement of stock awards and increased commission payments to non-U.S. employees, also contributed to the increased personnel-related costs. Average sales and marketing headcount decreased by approximately four in the three months ended November 30, 2011, but increased by approximately three in the nine months ended November 30, 2011, compared to the corresponding periods of the prior year. Commission expense increased in the nine months ended November 30, 2011 compared to the corresponding period of the prior year as a result of increased sales.

Consulting and marketing-related expenses decreased $187,000 during the three months ended November 30, 2011, but increased $217,000 in nine months ended November 30, 2011, compared to the corresponding periods of the prior year. The decrease in the three months ended November 30, 2011 was largely the result of a reduction in marketing-related initiative spending, including tradeshow and advertising spending. The increase in the nine months ended November 30, 2011 was primarily attributable to consulting services associated with developing our collaborative optimization network, as well as increased spending on our annual DemandBetter user conference and other marketing initiatives in the first fiscal quarter ended May 31, 2011.

Travel-related expense in the nine months ended November 30, 2011 increased $197,000 from the corresponding period of the prior year, as a result of user conferences and other marketing events as well as increased international travel.

Partially offsetting the increases in sales and marketing expense in the nine months ended November 30, 2011 was a $485,000 decrease in bad debt expense, as we fully reserved for a customer invoice that was in dispute in the nine months ended November 30, 2010 and had no similar charges in the nine months ended November 30, 2011.

We expect that, in the short term, sales and marketing expenses may increase slightly or remain flat in absolute dollars.

General and Administrative Expenses

General and administrative expenses include personnel costs for our executive, finance and accounting, human resources, legal and information management personnel, third-party professional services, travel and entertainment expenses, other corporate expenses and overhead not allocated to cost of revenue, research and development expenses, or sales and marketing expenses. Third-party professional services primarily include outside legal, audit and tax-related consulting costs.

	Three Months Ended November 30, 2011	2010	Nine Months Ended November 30, 2011	2010
	(dollars in thousands)			
General and administrative	$ 2,336	$ 2,433	$ 7,665	$ 7,273
Percent of revenue	10%	11%	11%	12%

Three and Nine Months Ended November 30, 2011 Compared to the Three and Nine Months Ended November 30, 2010. General and administrative expenses in the three months ended November 30, 2011 decreased $97,000, or 4%, primarily due to a decrease in stock-based compensation expense, but increased $392,000, or 5%, in the nine months ended November 30, 2011 compared to the corresponding periods of the prior year, primarily due to an increase in personnel-related costs and professional services expense.

The decrease in general and administrative expenses in the three months ended November 30, 2011 compared to the corresponding period of the prior year was primarily due to a decrease of $180,000 in stock-based compensation expense as the PSUs granted to executives based on our fiscal 2011 performance metrics became fully vested and we revised the number of PSUs associated with fiscal 2012 performance metrics that we expect to vest. The increase in general and administrative expenses in the nine months ended November 30, 2011 compared to the corresponding period of the prior year was primarily attributable to an increase of $304,000 in accounting and legal services costs, including costs associated with the M-Factor acquisition and a litigation matter with an M-Factor customer. In addition, payroll-related expense increased $132,000 as the average headcount increased by approximately three. The increases were partially offset by a decrease of $286,000 in stock-based compensation expense for PSUs.

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In the short term, we expect that general and administrative expenses may increase slightly or remain flat in absolute dollars.

Amortization of Purchased Intangible Assets

	Three Months Ended November 30, 2011	Three Months Ended November 30, 2010	Nine Months Ended November 30, 2011	Nine Months Ended November 30, 2010
	(dollars in thousands)			
Amortization of purchased intangible assets	$ 210	$ 217	$ 632	$ 800
Percent of revenue	1%	1%	1%	1%

Three and Nine Months Ended November 30, 2011 Compared to the Three and Nine Months Ended November 30, 2010. Expenses associated with amortization of purchased intangible assets (recognized as a component of operating expenses) decreased $7,000 and $168,000, respectively, in the three and nine months ended November 30, 2011 from the corresponding periods of the prior year. The decreases were primarily due to full amortization of intangible assets associated with certain intangible assets from prior acquisitions, partially offset by increased amortization expense from the intangible assets associated with our recent AIS and M-Factor acquisitions. Intangible assets are being amortized using the straight-line method over their estimated useful lives, with an estimated weighted average period of 2.9 years remaining at November 30, 2011.

We expect that, in the short term, amortization expense relating to the existing purchased intangible assets (recognized as a component of operating expenses) will remain flat, absent any impairment loss.

Other Income (Expense), Net

	Three Months Ended November 30, 2011	Three Months Ended November 30, 2010	Nine Months Ended November 30, 2011	Nine Months Ended November 30, 2010
	(in thousands)			
Interest income	$ 38	$ 62	$ 108	$ 190
Interest expense	(14)	(26)	(37)	(70)
Other income (expense)	(145)	(4)	(110)	(10)
Other income (expense), net	$ (121)	$ 32	$ (39)	$ 110

Three and Nine Months Ended November 30, 2011 Compared to the Three and Nine Months Ended November 30, 2010. Other income, net decreased in the three and nine months ended November 30, 2011 compared to the corresponding periods of the prior year, primarily due to foreign currency exchange losses associated with certain unhedged customer receivables and cash balances denominated in Euros as a result of the weakening of the Euro against the U.S. dollar. Also contributing to the decrease in other income, net was the decreased interest income as a result of lower interest rates on invested cash and marketable securities.

Provision for Income Taxes

	Three Months Ended November 30,		Nine Months Ended November 30,	
	2011	2010	2011	2010
	(in thousands)			
Provision for income taxes	$ 148	$ 29	$ 318	$ 105

Three and Nine Months Ended November 30, 2011 Compared to the Three and Nine Months Ended November 30, 2010. In the three and nine months ended November 30, 2011, we recorded income tax expense of approximately $148,000 and $318,000, respectively, compared to $29,000 and $105,000 in the corresponding periods of the prior year. The effective tax rate for the three and nine months ended November 30, 2011 was approximately 3% and 2%, respectively, based on our estimated taxable income for the year. We recorded tax expenses primarily for foreign taxes and state minimum taxes. Foreign taxes increased in the three and nine months ended November 30, 2011 compared to the corresponding periods of the prior year, primarily due to withholding taxes on sales to non-U.S. customers.

Since inception, we have incurred annual operating losses and, accordingly, have recorded a provision for income taxes primarily for federal minimum income taxes, state income taxes principally in states where we have no net operating loss carryforwards, and foreign taxes. At February 28, 2011, we had federal and state net operating loss carryforwards of approximately $87.8 million and $63.6 million, respectively, that may be available to offset future taxable income.

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Stock-Based Compensation Expense

	Three Months Ended November 30, 2011	Three Months Ended November 30, 2010	Nine Months Ended November 30, 2011	Nine Months Ended November 30, 2010
	(in thousands)			
Stock-based compensation expense	$ 2,532	$ 2,585	$ 8,563	$ 7,665

Stock-based compensation expense decreased approximately $53,000 in the three months ended November 30, 2011, but increased approximately $898,000 in the nine months ended November 30, 2011, compared to the corresponding periods of the prior year.

The net decrease in the three-month period was primarily due to lower expenses due to the vesting of PSUs and RSUs granted to certain employees in fiscal 2010 and 2011 and the grant of fewer options relative to prior years. The decrease was largely offset by an increase in expenses associated with RSUs and PSUs granted in fiscal 2012.

The net increase in the nine-month period was primarily attributable to the RSUs granted to employees in fiscal 2011 and 2012, including former M-Factor employees, and PSUs granted in fiscal 2012. The increase was partially offset by lower expenses associated with vesting of PSUs granted to certain employees in fiscal 2010 and 2011 that became vested in the twelve months ended November 30, 2011.

See Note 7 of Notes to Condensed Consolidated Financial Statements for the amount of gross unrecognized stock-based compensation expense at November 30, 2011, and further explanation of how we derive and account for these estimates. We expect that stock-based compensation expense will vary over the long term depending on the timing and magnitude of equity incentive grants and revisions to our estimates of the number of shares expected to vest.

Liquidity and Capital Resources

At November 30, 2011, our principal sources of liquidity consisted of cash, cash equivalents, and marketable securities of $66.4 million, accounts receivable (net of allowance) of $14.7 million, and available borrowing capacity under our credit facility of $19.1 million, after a reduction of approximately $917,000 to secure the operating lease commitment associated with our San Mateo headquarters facility.

Our $20.0 million revolving line of credit may be borrowed, repaid, and reborrowed until May 7, 2012 and includes a number of covenants and restrictions with which we must comply. For example, our ability to incur debt, grant liens, make investments, enter into mergers and acquisitions, pay dividends, repurchase our outstanding common stock, change our business, enter into transactions with affiliates, and dispose of assets is limited. To secure the line of credit, we have granted our lenders a first priority security interest in substantially all of our assets. Through the filing of this Quarterly Report on Form 10-Q, we were in compliance with all loan covenants.

	Nine Months Ended November 30, 2011	2010
	(in thousands)	
Net cash provided by operating activities	$ 1,799	$ 5,678
Net cash used in investing activities	(13,254)	(13,705)
Net cash provided by financing activities	3,814	3,069

Operating Activities

Our cash flows from operating activities in any period are significantly influenced by the number of customers using our software, the number and size of new customer contracts, the timing of renewals of existing customer contracts, and the timing of payments by these customers. Our largest source of operating cash flows is cash collections from our customers, which results in decreases to accounts receivable. Our primary uses of cash in operating activities are for personnel-related expenditures and rent payments. Our cash flows from operating activities in any period will continue to be significantly affected by the extent to which we add new customers, renew existing customers, collect payments from our customers and increase personnel to grow our business. Additionally, certain executives received all or a portion of their fiscal 2011 annual variable compensation in the form of PSUs rather than cash, which had a beneficial impact on cash flows from operating activities in the nine months ended November 30, 2011.

Net cash provided by operating activities in the nine months ended November 30, 2011 was $1.8 million compared to $5.7 million in the corresponding period of the prior year. Cash collections from our customers decreased approximately $1.1 million in the nine months ended November 30, 2011 compared to the corresponding period of the prior year. In addition to the decrease in cash

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collections, operating expenses increased, primarily as a result of increased headcount associated with the M-Factor acquisition in the nine months ended November 30, 2011.

We anticipate that the economic environment may not improve in the near term and, as a result, the signing of customer contracts and the collection of cash will continue to remain challenging and unpredictable, thereby impacting our cash generation. In addition, in the three months ending February 29, 2012, we expect to pay off the $2.2 million of the accrued non-contingent legal and investment banking advisory service fees associated with the merger with IBM. We expect to incur additional non-contingent legal and other acquisition-related costs in the fiscal quarter ending February 29, 2012. Fees that are contingent upon the consummation of the merger include approximately $4.4 million for investment banking transaction fees.

Investing Activities

Our primary investing activities have been capital expenditures on equipment for our data center, investment in marketable securities, and payments for businesses acquisitions.

In the nine months ended November 30, 2011, net cash used in investing activities was $13.3 million compared to $13.7 million in the corresponding period of the prior year. In the nine months ended November 30, 2011, we paid approximately $8.7 million associated with the M-Factor acquisition (net of cash received) and $3.4 million in capital expenditures and used approximately $1.2 million of cash for the net purchase of marketable securities. In the nine months ended November 30, 2010, we had an $8.8 million cash outflow in net purchases of marketable securities, spent $3.6 million in capital expenditures, and paid $900,000 cash to former Connect3 shareholders and $426,000 cash to former TradePoint shareholders related to these prior acquisitions.

Financing Activities

Our primary financing activities have been the exercise of stock options, the sale of shares pursuant to our ESPP, and borrowings and repayments under our credit facilities.

In the nine months ended November 30, 2011, net cash provided by financing activities was approximately $3.8 million, all from the issuance of common stock under our equity incentive plans. In the nine months ended November 30, 2010, net cash from financing activities was approximately $3.1 million. Net proceeds from issuance of common stock was approximately $4.0 million, partially offset by a $937,000 cash payment to fulfill employee federal and state withholding tax obligations in connection with the vesting and settlement of certain outstanding RSUs.

We believe that our cash, cash equivalents, and marketable securities balances at November 30, 2011, along with cash provided by operating activities, if any, will be sufficient to fund our projected operating requirements for at least the next twelve months. We may need to raise additional capital or incur debt to continue to fund our operations over the long term. Our future capital requirements will depend on many factors, including revenues, profits or losses incurred therefrom, any expansion of our workforce, the timing and extent of any expansion into new markets, the timing of introductions of any new functionality and enhancements to our software, the timing and size of any acquisitions of other companies or assets and the continuing market acceptance of our software. We may enter into arrangements for potential acquisitions of complementary businesses, services or technologies, which also could require us to seek additional equity or debt financing. Additional funds may not be available on terms favorable to us or at all.

Contractual Obligations

Our principal commitments consist of obligations under operating leases for office space in the United States, data center facilities and equipment, and merger consideration payable. Our future operating lease obligations will change if we enter into new lease agreements upon the expiration of our existing lease agreements or if we enter into new lease agreements to expand our operations.

At February 28, 2011, the future minimum payments under our lease commitments, contractual commitments, and amounts due for merger consideration were as follows:

	Payments Due by Period				
	Total	Less than 1 Year	1 - 3 Years	3 - 5 Years	More than 5 Years
			(In thousands)		
Operating leases (1)	$ 10,653	$ 3,043	$ 5,232	$ 2,366	$ 12
Contractual commitments (2)	2,187	2,187			
AIS acquisition consideration payable	475		475		
Total contractual obligations	$ 13,315	$ 5,230	$ 5,707	$ 2,366	$ 12

(1) Includes approximately $9.1 million in future minimum lease payments, $8.5 million of which was associated with our

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headquarters facility in San Mateo, California, and approximately $1.5 million in future minimum lease payments for equipment and facility operating leases associated with our data center in Mesa, Arizona, entered into in fiscal 2010 and 2011. See Note 5 of Notes to Condensed Consolidated Financial Statements.

(2) Amounts are associated with agreements for contract engineering services and other purchase commitments that are enforceable and legally binding and that specify all significant terms, including fixed or minimum services to be used; fixed, minimum, or variable price provisions; and the approximate timing of the transactions. Obligations under contracts that we can cancel without a significant penalty are not included.

Off-Balance Sheet Arrangements

We do not have any relationships with unconsolidated entities or financial partnerships, such as entities often referred to as structured finance or special purpose entities, which would have been established for the purposes of facilitating off-balance sheet arrangements or other contractually narrow or limited purposes, nor do we have any undisclosed material transactions or commitments involving related persons or entities.

Recent Accounting Pronouncements

For information with respect to recent accounting pronouncements and the impact of these pronouncements on our condensed consolidated financial statements, see Note 1 of Notes to Condensed Consolidated Financial Statements.

Item 3. Quantitative and Qualitative Disclosures about Market Risk

Foreign Currency Risk

As we operate internationally and fund our international operations, our cash and cash equivalents could be affected by fluctuations in foreign exchange rates. In each of the three and nine months ended November 30, 2011 and 2010, the foreign currency exchange rate effect on our cash and cash equivalents was not significant.

Certain of our international sales agreements are denominated in the country of origin currency, and therefore our revenue and receivables are subject to foreign currency risk. Also, some of our operating expenses and cash flows are denominated in foreign currencies and, thus, are subject to fluctuations due to changes in foreign currency exchange rates, particularly changes in the exchange rates for the British Pound and the Euro. We periodically enter into foreign exchange forward contracts to reduce exposure in non-U.S. dollar denominated receivables. We formally assess, both at a hedge s inception and on an ongoing basis, whether the derivatives used in hedging transactions are highly effective in negating currency risk. At November 30, 2011, we had three outstanding forward foreign exchange contracts to sell Euros for U.S. dollars that mature between September 2012 and September 2013, with an aggregate notional principal of approximately 2.0 million (or approximately $2.8 million). We do not enter into derivative financial instruments for speculative or trading purposes.

With respect to our international operations, which are primarily sales and marketing and research and development support entities, we have remeasured our accounts denominated in non-U.S. currencies using the U.S. dollar as the functional currency and recorded the resulting gains (losses) within other income (expense) for the period. We remeasure all monetary assets and liabilities at the current exchange rate at the end of the period, non-monetary assets and liabilities at historical exchange rates, and revenue and expenses at average exchange rates in effect during the period.

Interest Rate Sensitivity

We had cash and cash equivalents totaling $18.8 million and marketable securities totaling $47.6 million at November 30, 2011. These amounts were invested primarily in government securities and corporate notes and bonds with credit ratings of at least A-1 or better, money market funds registered with the SEC under rule 2a-7 of the Investment Company Act of 1940, and interest-bearing demand deposit accounts. By policy, we limit the amount of credit exposure to any one issuer and we do not enter into investments for trading or speculative purposes. Our cash and cash equivalents and marketable securities are held and invested with capital preservation as the primary objective.

Our cash equivalents and marketable securities are subject to market risk due to changes in interest rates. Fixed-rate interest securities may have their market value adversely impacted due to a rise in interest rates, while floating rate securities may produce less income than expected if interest rates fall. Due in part to these factors, our future investment income may fall short of expectations due to changes in interest rates or we may suffer losses in principal if we are forced to sell securities that decline in market value due to changes in interest rates. However, because we classify our marketable securities as held-to-maturity, no gains or losses are recognized due to changes in interest rates unless such securities are sold prior to maturity or declines in fair value are determined to

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be other-than-temporary. We believe that we do not have any material exposure to changes in the fair value of our investment portfolio as a result of changes in interest rates. Declines in interest rates, however, will reduce future investment income, if any. For instance, a fluctuation in interest rates of 100 basis points at November 30, 2011 would result in a change of approximately $664,000 in annual interest income.

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

We evaluated the effectiveness of the design and operation of our disclosure controls and procedures as of November 30, 2011, the end of the period covered by this Quarterly Report on Form 10-Q. This evaluation (the controls evaluation) was done under the supervision and with the participation of management, including our Chief Executive Officer (CEO) and Chief Financial Officer (CFO). Disclosure controls and procedures means controls and other procedures that are designed to provide reasonable assurance that information required to be disclosed in the reports that we file or submit under the Securities and Exchange Act of 1934, as amended (the Exchange Act), such as this Quarterly Report on Form 10-Q, is recorded, processed, summarized and reported within the time periods specified in the SEC s rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed such that information is accumulated and communicated to our management, including the CEO and CFO, as appropriate to allow timely decisions regarding required disclosure. Based on the controls evaluation, our CEO and CFO have concluded that as of November 30, 2011, our disclosure controls and procedures were effective to provide reasonable assurance that information required to be disclosed in our Exchange Act reports is recorded, processed, summarized and reported within the time periods specified by the SEC and to ensure that material information relating to the Company and our consolidated subsidiaries is made known to management, including the CEO and CFO, particularly during the period when our periodic reports are being prepared.

Our management, including our CEO and CFO, believe that our disclosure controls and procedures are effective at the reasonable assurance level. However, our management, including the CEO and CFO, does not expect that our disclosure controls and procedures will prevent all errors and all fraud. A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Further, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within the company have been detected. These inherent limitations include the realities that judgments in decision-making can be faulty, and that breakdowns can occur because of simple error or mistake. Additionally, controls can be circumvented by the individual acts of some persons, by collusion of two or more people, or by management override of the controls. The design of any system of controls also is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions. Over time, controls may become inadequate because of changes in conditions, or the degree of compliance with the policies or procedures may deteriorate. Because of the inherent limitations in a cost-effective control system, misstatements due to error or fraud may occur and not be detected.

Changes in Internal Control over Financial Reporting

No change in our internal control over financial reporting occurred during the period covered by this Quarterly Report on Form 10-Q that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting. Internal control over financial reporting means a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles.

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PART II. OTHER INFORMATION

Item 1. Legal Proceedings

We are aware of one purported class action lawsuit filed in the Superior Court of the State of California in and for the County of Santa Clara that an alleged DemandTec stockholder has filed against us, each member of our board of directors, IBM and Cudgee Acquisition Corp. in connection with the Merger. The complaint asserts claims for breach of fiduciary duty and aiding and abetting breach of fiduciary duty and seeks equitable relief, including an injunction preventing the consummation of the Merger, rescission in the event the Merger is consummated, and an award of damages. The outcome of any such litigation is uncertain. If a dismissal is not granted or a settlement is not reached, this lawsuit could prevent or delay completion of the Merger and result in substantial costs to us, including any costs associated with the indemnification of our directors and officers. Other DemandTec shareholders may also file additional lawsuits against us, IBM, and/or our directors and officers in connection with the Merger.

In addition, we have from time to time become involved in legal matters that arise in the normal course of business and otherwise. For example, we are currently involved in arbitration proceedings with an M-Factor customer associated with that customer s failure to pay amounts due under, and purported termination of, their agreement with M-Factor relating to certain services which is in the second year of a three year committed term. Beginning in our quarter ended November 30, 2011, that customer began withholding quarterly amounts, currently $573,000, due under the agreement. We are continuing to assess the impact of this dispute. We are currently assessing the potential impact of the dispute, which is at an early stage. There can be no assurance that this matter or other third party claims and litigation that may arise in the future will not have a material adverse effect on our business, financial position, results of operations, or cash flows, including a loss of customers, or subject us to significant financial or other remedies.

Item 1A. Risk Factors

Set forth below and elsewhere in this Quarterly Report on Form 10-Q, and in other documents we file with the Securities and Exchange Commission, or SEC, are risks and uncertainties that could cause actual results to differ materially from the results contemplated by the forward-looking statements contained in this Quarterly Report on Form 10-Q and in other written and oral communications from time to time. Because of the following factors, as well as other variables affecting our operating results, past financial performance should not be considered as a reliable indicator of future performance and investors should not use historical trends to anticipate results or trends in future periods. The risks and uncertainties identified below and elsewhere in this Quarterly Report on Form 10-Q generally relate to our continued operation on a standalone basis and may be impacted by the announcement and pendency of our agreement to be acquired by International Business Machines Corporation discussed below and under Management s Discussion and Analysis of Financial Condition and Results of Operations-Recent Development.

Risks Related to Our Business and Industry

The announcement and pendency of our agreement to be acquired by IBM could adversely affect our business.

On December 7, 2011, we entered into an Agreement and Plan of Merger (the Merger Agreement) with International Business Machines Corporation (IBM), and Cudgee Acquisition Corp. (Sub), a Delaware corporation and wholly-owned subsidiary of IBM, pursuant to which, and subject to the conditions thereof, Sub will merge with and into DemandTec (the Merger), and DemandTec will become a wholly-owned subsidiary of IBM. If the Merger is completed, DemandTec s stockholders will be entitled to receive $13.20 in cash for each share of DemandTec s common stock owned by them as of the date of the Merger. The Merger is conditioned upon, among other things, stockholder approval of the transaction, certain regulatory approvals and other customary closing conditions. Although we will continue to operate as a separate entity until the transaction closes, we have made certain representations and warranties related to our business and operations and have agreed to specified covenants in the Merger Agreement, including covenants relating to the conduct of our business between the date of the Merger Agreement and the closing of the Merger, restrictions on solicitation of proposals for alternative transactions, public disclosures and other matters. The announcement and pendency of the Merger, or any significant delay in the consummation of the Merger, could cause disruptions in our business, including affecting our relationship with our customers, vendors and employees, which could have a material adverse effect on our business, financial results and operations.

The failure to complete the Merger could materially adversely affect our business.

There is no assurance that our acquisition by IBM will occur. If the proposed Merger or a similar transaction is not completed, the share price of our common stock may decline to the extent that the current market price of our common stock reflects an assumption that a transaction will be completed. In addition, as set forth in the Merger Agreement, we may be required to pay IBM a termination fee of $14.0 million (the Termination Fee) if the Merger Agreement is terminated under certain circumstances. The payment of a Termination Fee may have a material adverse impact on our financial condition. Further, a failure to complete the Merger may result in negative publicity and a negative impression of us in the investment community or with customers, potential customers, partners and vendors.

Pending litigation against us could result in an injunction preventing the completion of the Merger or a judgment resulting in the payment of damages in the event the Merger is completed.

We are aware of one purported class action lawsuit filed in the Superior Court of the State of California in and for the County of Santa Clara that an alleged DemandTec stockholder has filed against us, each member of our board of directors, IBM and Cudgee Acquisition Corp. in connection with the Merger. The complaint asserts claims for breach of fiduciary duty and aiding and abetting breach of fiduciary duty and seeks equitable relief, including an injunction preventing the consummation of the Merger, rescission in the event the Merger is consummated, and an award of damages. The outcome of any such litigation is uncertain. If a dismissal is not granted or a settlement is not reached, this lawsuit could prevent or delay completion of the Merger and result in substantial costs to us, including any costs associated with the indemnification of our directors and officers. Other DemandTec shareholders may also file additional lawsuits against us, IBM, and/or our directors and officers in connection with the Merger.

We may experience significant quarterly fluctuations in our operating results due to a number of factors, which makes our future operating results difficult to predict and could cause our operating results to fall below expectations.

Our quarterly operating results may fluctuate significantly due to a variety of factors, many of which are outside of our control. As a result, comparing our operating results on a period-to-period basis may not be meaningful. You should not rely on our past results as an indication of our future performance. If our operating results fall below the expectations of investors or securities analysts or below the guidance, if any, we provide to the market, the price of our common stock could decline substantially.

Factors that may affect our operating results include:

- any impacts of the pendency of our proposed acquisition by IBM;
- our ability to increase sales to existing customers and to renew agreements with our existing customers at comparable prices, particularly larger retail customers;

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- our ability to attract new customers, particularly larger retail and consumer products customers in both domestic and foreign markets;
- changes in our pricing policies or those of our competitors, or pricing pressure on our software services;
- periodic fluctuations in demand for our software and services;
- volatility in the sales of our solutions on a quarterly basis and timing of the execution of new and renewal agreements within such quarterly periods;
- reductions in customers budgets for information technology purchases and/or delays in their purchasing cycles;
- our ability to develop and implement in a timely manner new software and enhancements that meet customer requirements, including our ability to develop certain substantial and customer-specific functionality as required under certain customer engagements;
- our ability to hire, train and retain key personnel;
- our success in broadening the range of our offerings, including our ability to develop and sell solutions to consumer products manufacturers and apparel retailers and to incorporate shopper segmentation and analytics into our offerings;
- the short-term and long-term impacts of acquisitions of businesses or technologies, including the expenses associated with integrating the acquired businesses or technologies into our operations or solutions and our ability to achieve sales growth and margin improvement;
- any significant changes in the competitive dynamics of our market, including new entrants, new product introductions, or substantial discounting of products;
- our ability to control costs, including our operating expenses;
- any significant change in our facilities-related costs;
- the timing of hiring personnel and of large expenses such as those for trade shows and third-party professional services;
- our ability to appropriately resolve any disputes with customers;
- outages and capacity constraints with our hosting partners; and
- the impact of global economic conditions on our business and the retail and CP industries, including any future customer insolvencies or bankruptcies.

We have in the past experienced, and we may continue to experience, significant variations in our level of sales on a quarterly basis. In addition, we have at times failed to meet, and we may in the future fail to meet, our internal periodic bookings plans. In the past, some of our customers have delayed or failed to renew their agreements with us upon expiration, or have renewed at lower prices. For example, during the nine months ended November 30, 2011, a number of retail customers and CP companies either did not renew their agreements, purported to terminate their agreement with us, reduced the scope of their services, renewed at a lower rate, or delayed moving forward from a pilot program to a full-scale implementation. Such variations in our sales, or delays in signing or a failure to sign or renew significant customer agreements, have led to significant fluctuations in our cash flows and deferred revenue on a quarterly and annual basis. For example, we used approximately $6.8 million of net cash in operations in fiscal 2010, while we generated approximately $9.2 million and $13.8 million of net cash from operations in fiscal 2011 and 2009, respectively.

We have a history of losses and we may not achieve or sustain profitability in the future.

We have a history of losses and have not achieved profitability in any fiscal year. We had net losses of $13.7 million, $11.8 million and $5.0 million in fiscal 2011, 2010 and 2009, respectively, and had a net loss of $16.4 million in the nine months ended November 30, 2011. As of November 30, 2011, we had an accumulated deficit of $119.3 million. We expect to continue to incur net losses in fiscal 2012 and perhaps beyond. In addition, our cost of revenue and operating expenses may increase in future periods as we implement initiatives to continue to grow our business, or if we need to procure additional capital equipment, software, or data center

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space to handle increased customer data. If we are unable to increase our revenue to offset these expected increases in our fixed costs and expenses, our losses will increase. Accordingly, we cannot provide assurance that we will be able to achieve or maintain profitability in the future.

We depend on a small number of customers, which are primarily retailers, and, to a lesser extent, consumer products companies, and our growth, if any, depends upon our ability to add new and retain existing customers.

We derive a significant percentage of our revenue from a relatively small number of customers, which are primarily retailers, and, to a lesser extent, consumer products companies. The loss of any one or more of those customers could decrease our revenue and harm our current and future operating results. For example, during the nine months ended November 30, 2011, a number of retail customers and CP companies either did not renew their agreements, purported to terminate their agreement with us, reduced the scope of their services, renewed at a lower rate, or delayed moving forward from a pilot program to a full-scale implementation. In June 2010, we signed a multi-year agreement with Target Corporation (Target) for substantially all of our current and certain potential future software services. In fiscal 2011, revenue from Target represented approximately 21% of our revenue. In the nine months ended November 30, 2011 and 2010, Target accounted for approximately 22% and 20%, respectively, of our revenue and our retail customers accounted for 77% and 81%, respectively, of our revenue. Although our largest customers may vary from period to period, we anticipate that we will continue to depend on revenue from a relatively small number of our large retail customers and, to a lesser extent, CP customers. Further, our ability to grow revenue depends on our ability to increase sales to existing customers, to renew agreements with our existing customers and to attract new customers. If we are unable to add new and retain existing customers, this will adversely affect our revenue and results of operations.

The effects of adverse global economic conditions may adversely impact our business, operating results or financial condition.

Commencing in fiscal 2009, adverse global economic conditions caused a general tightening in the credit markets, lower levels of liquidity, increases in the rates of default and bankruptcy, and economic contraction, and since that time there have continued to be periods of economic volatility and slowdown of economic expansion. The retail and consumer products industries were especially hard hit by these economic conditions, which resulted in some customers or potential customers delaying or not entering into new agreements or renewing their existing agreements with us. If global economic conditions, particularly in light of renewed concerns regarding consumer confidence and a further global economic slowdown, have a material negative impact on our sales or prospects, our business, operating results or financial condition will be adversely impacted.

Our business depends substantially on customers renewing their agreements for our software. Any decline in our customer renewals would harm our operating results.

To maintain and grow our revenue, we must achieve and maintain high levels of customer renewals. We sell our software pursuant to agreements with initial terms that are generally from one to three years in length. Our customers have no obligation to renew their agreements after the expiration of their term. The fees we charge for our solutions vary based on a number of factors, including the software, service and hosting components provided, the size of the customer, and the duration of the agreement term. Our initial agreements with customers may include fees for software, services or hosting components that may not be needed upon renewal. As a consequence, if we renew these agreements, we may receive lower total fees. In addition, if an agreement is renewed for a term longer than the preceding term, we may receive total fees in excess of total fees received in the initial agreement but a smaller average annual fee because we generally charge lower annual fees in connection with agreements with longer terms. In any of these situations, we would need to sell additional software, services or hosting in order to maintain the same level of annual fees from that customer. There can be no assurance that we will be able to renew these agreements in a timely manner, on favorable terms, or at all, or to sell additional software or services or sell to new customers. In the past, certain of our customers have elected not to renew their agreements with us or have renewed on less favorable terms, including during the nine months ended November 30, 2011. Our customer renewal rates may decline or fluctuate as a result of a number of factors, including our customers satisfaction or dissatisfaction with our software, the price of our software, the prices of competing products and services, consolidation within our customer base, customer bankruptcies, or reductions in our customers information technology spending levels. If our customers do not renew their agreements for our software for any reason, or if they renew on less favorable terms, our revenue will decline and our cash flow will be negatively impacted.

Because we generally recognize revenue ratably over the terms of our customer agreements, the lack of renewals or the failure to enter into new agreements may not immediately be reflected in our statement of operations in any significant manner but may negatively affect revenue in future quarters.

We generally recognize revenue ratably over the terms of our customer agreements and invoice our customers in advance for annual use of our software and certain implementation services on a fixed fee basis. As a result, most of our quarterly revenue is generated from agreements entered into during previous quarters. Consequently, a decline in new or renewed agreements in a particular quarter, as well as any renewals at reduced annual dollar amounts, will not be reflected in any significant manner in our revenue for that quarter, but it will negatively affect revenue in future quarters.

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If our security measures are breached and unauthorized access is obtained to our customers data, our operations may be perceived as not being secure, customers may curtail or stop using our software and we may incur significant liabilities.

Our operations involve the storage and transmission of our customers confidential information, and security breaches could expose us to a risk of loss of this information, litigation and possible liability. In recent years cyber attacks and the unauthorized access of confidential data have become much more frequent and have resulted in significant harm to the business of a number of companies. If our security measures are breached as a result of third-party action, employee error, malfeasance or otherwise, and, as a result, someone obtains unauthorized access to our customers data, our reputation will be damaged, our business may suffer and we could incur significant liability. Because techniques used to obtain unauthorized access or to sabotage systems change frequently and generally are not recognized until launched against a target, we may be unable to anticipate these techniques or to implement adequate protective measures. If an actual or perceived breach of our security occurs, the market perception of the effectiveness of our security measures could be harmed and we could lose potential sales and existing customers.

We may expand through acquisitions of and/or partnerships with other companies, which may divert our management s attention and result in unexpected operating and technology integration difficulties, increased costs and dilution to our stockholders.

Our business strategy incorporates the acquisition of complementary software, technologies, or businesses. For instance, we acquired M-Factor, Inc. (M-Factor) in March 2011 and acquired substantially all of the assets of Applied Intelligence Solutions LLC (AIS) in December 2010. Acquisitions may result in unforeseen operating difficulties and expenditures. In particular, we may encounter difficulties in assimilating or integrating the businesses, technologies, services, products, personnel, or operations of the acquired companies, especially if the key personnel of the acquired company choose not to work for us, and we may have difficulty retaining the existing customers or signing new customers of any acquired business or migrating them to a software-as-a-service model. Acquisitions may also disrupt our ongoing business, divert our resources and require significant management attention that would otherwise be available for ongoing development of our current business, or result in disputes with stockholders, employees, customers or vendors of the acquired companies. The successful integration of acquired businesses may be further complicated by our need to simultaneously support ongoing, complicated development efforts, such as our current efforts to integrate shopper segmentation and analytics into our offerings. We also may be required to use a substantial amount of our cash or issue equity securities to complete an acquisition, which could deplete our cash reserves and dilute our existing stockholders and could adversely affect the market price of our common stock. For example, we had cash outflows of approximately $9.0 million and $2.7 million in connection with our acquisitions of M-Factor and AIS. Moreover, we cannot assure you that the anticipated benefits of any acquisition, including our revenue or return on investment assumptions, will be realized or that we will not be exposed to unknown liabilities.

In addition, an acquisition may negatively impact our results of operations because we may incur additional expenses relating to one-time charges, write-downs, amortization of intangible assets, or tax-related expenses, or bringing on additional personnel. For example, our acquisition of Connect3 in February 2009 resulted in approximately $1.8 million and $2.2 million of amortization of purchased intangible assets in fiscal 2011 and 2010, respectively, and a $150,000 of write-off of in-process research and development costs in fiscal 2009. The remaining carrying amount of approximately $626,000 associated with the Connect3 acquisition was fully amortized in the nine months ended November 30, 2011. Our acquisition of M-Factor in March 2011 resulted in approximately $922,000 of amortization of purchased intangible assets in the nine months ended November 30, 2011. We anticipate the aggregate amortization of purchased intangible assets associated with the M-Factor acquisition will be approximately $307,000 in the fourth quarter of fiscal 2012 and $1.2 million and $703,000 in fiscal 2013 and 2014, respectively, and will decline thereafter. In addition, the incremental expenses associated with M-Factor contributed to our increase in operating loss for the three and nine months ended November 30, 2011 compared to the corresponding periods of the prior year. In order to compensate for the dilutive effect of the acquisition, we reduced our workforce, resulting in a $604,000 restructuring charge in the nine months ended November 30, 2011.

We might require additional capital to support our business growth, and this capital might not be available on acceptable terms, or at all.

We intend to continue to make investments to support our business growth and may require additional funds to respond to business challenges and opportunities, including continued economic concerns as well as the need to develop new software or enhance our existing software, enhance our operating infrastructure and acquire complementary businesses and technologies. We have a loan agreement with a financial institution that has a maturity date of May 7, 2012 under which we have a $20.0 million revolving line of credit. However, we may need to engage in equity or debt financings or enter into additional credit agreements to secure additional funds. If we raise additional funds through further issuances of equity or convertible debt securities, our existing stockholders could suffer significant dilution, and any new equity securities we issue could have rights, preferences and privileges superior to those of holders of our common stock. Any debt financing that we secure in the future could involve restrictive covenants relating to our capital-raising activities and other financial and operational matters that make it more difficult for us to obtain additional capital and to pursue business opportunities, including potential acquisitions. In addition, we may not be able to obtain additional financing on terms

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favorable to us, if at all. If we are unable to obtain adequate financing or financing on terms satisfactory to us, when we require it, our ability to continue to support our business growth and to respond to business challenges could be significantly limited.

Our sales cycles are long and unpredictable, and our sales efforts require considerable time and expense.

We market our software to large retailers and CP companies, and sales to these customers are complex efforts that involve educating our customers about the use and benefits of our software, including its technical capabilities. Customers typically undertake a significant evaluation process that can result in a lengthy sales cycle, in some cases over twelve months. We spend substantial time, effort, and money in our sales efforts without any assurance that our efforts will generate long-term agreements or any revenue. In addition, customer sales decisions are frequently influenced by macroeconomic factors, budget constraints, multiple approvals, changes in key customer personnel, and unplanned administrative, processing and other delays. During the nine months ended November 30, 2011, two retail customers completed the initial phases of their projects with us, one of which has not yet moved forward with the next phase pending internal budget approval. If sales expected from a specific customer are not realized, our revenue and, thus, our future operating results could be adversely impacted.

Our business will be adversely affected if the retail and CP industries do not widely adopt technology solutions incorporating scientific techniques to understand and predict consumer demand to make pricing and other merchandising decisions, as well as our related collaborative network strategy.

Our software addresses the new and emerging market of applying econometric modeling and optimization techniques through software to enable retailers and CP companies to understand and predict consumer demand in order to improve their pricing, promotion, and other merchandising and marketing decisions. These decisions are fundamental to retailers and CP companies. Accordingly, our target customers may be hesitant to accept the risk inherent in applying and relying on new technologies or methodologies to supplant traditional methods. Our business model also relies on these retailers and CP companies adopting and embracing the full features and functionality available on our network for inter- and intra- company collaborative interaction, and on us being successful in incorporating shopper segmentation and analytics into our offerings and in achieving market acceptance of our recently acquired M-Factor and AIS solutions. Due to the complexity inherent in the use of our software, some retailers and CP companies, particularly small and medium sized companies, may lack the internal resources and expertise necessary in order to make use of the full capacity of our products. Our business will not be successful if retailers and CP companies do not embrace the use of software to enable more strategic pricing and other merchandising decisions, or otherwise embrace our collaborative network strategy.

If we are unable to continue to enhance our current software, which is becoming increasingly complex, or to develop or acquire new software to address changing business requirements, we may not be able to attract or retain customers.

Our ability to attract new customers, renew agreements with existing customers and maintain or increase revenue from existing customers will depend in large part on our ability to anticipate the changing needs of the retail and CP industries, to enhance our increasingly complex existing software and to introduce new software that meet those needs. Certain of our implementation and integration engagements, particularly with respect to initial deployment with larger customers, have become increasingly complex. Further, certain of our engagements require, and other future engagements may require, us to develop certain substantial and customer-specific functionality. Such engagements can be significantly more time-consuming and complicated than our other customer engagements. Any new software may not be introduced in a timely or cost-effective manner and may not achieve market acceptance, meet customer expectations or contractual commitments, or generate revenue sufficient to recoup the cost of development or acquisition of such software. For example, we have not yet completed development or achieved market acceptance of certain components of our solutions (including the incorporation of shopper segmentation and analytics into our offerings) with respect to which we have made certain development commitments. In addition, we have recently made certain investments in assets and technology related to apparel retailing, and recently acquired M-Factor. If we are unable to successfully develop or acquire new software, enhance our existing applications to meet customer requirements and achieve success with our technology investments and our M-Factor acquisition, we may not be able to attract or retain customers.

Understanding and predicting consumer behavior is dependent upon the continued availability of accurate and relevant data from retailers and third- party data aggregators. If we are unable to obtain access to relevant data, or if we do not enhance our core science and econometric modeling methodologies to adjust for changing consumer behavior, our software may become less competitive or obsolete.

The ability of our econometric models to forecast consumer demand depends upon the assumptions we make in designing the models and in the quality of the data we use to build them. Our models rely on point of sale (POS), transaction log or loyalty program data provided to us directly by our retail customers and by third-party data aggregators. Consumer behavior is affected by many factors, including evolving consumer needs and preferences, new competitive product offerings, more targeted merchandising and marketing, emerging industry standards, and changing technology. Data adequately representing all of these factors may not be readily available in certain geographies or in certain markets. In addition, the relative importance of the variables that influence demand will

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change over time, particularly with the continued growth of the Internet as a viable retail alternative and the emergence of non-traditional marketing channels. If we are unable to obtain POS, transaction log or loyalty program data from our retail customers or from third-party data aggregators, or if we fail to enhance our core science and modeling methodologies to adjust for changes in consumer behavior, customers may delay or decide against purchases or renewals of our software.

We rely on our management team and will need additional personnel to grow our business, and the loss of one or more key employees or our inability to attract and retain qualified personnel could harm our business.

Our success depends to a significant degree on our ability to attract, retain and motivate our management team and our other key personnel. We recently announced the departure and replacement of our senior sales executive. Our professional services organization and other customer-facing groups, in particular, play an instrumental role in ensuring our customers satisfaction. In addition, our science, engineering, and modeling team requires experts in econometrics and advanced mathematics, and there are a limited number of individuals with the education and training necessary to fill these roles should we experience employee departures. All of our employees work for us on an at-will basis, and there is no assurance that any employee will remain with us. Our competitors may be successful in recruiting and hiring members of our executive management team or other key employees, and it may be difficult for us to find suitable replacements on a timely basis. Many of the members of our management team and key employees are substantially vested in their shares of our common stock or options to purchase shares of our common stock, and therefore retention of these employees may be difficult in the highly competitive market and geography in which we operate our business.

We have derived most of our revenue from sales to our retail customers. If our software is not widely accepted by CP companies, and our collaborative network strategy is not fully realized, our ability to grow our revenue and achieve our strategic objectives will be harmed.

To date, we have derived most of our revenue from retail customers. In the nine months ended November 30, 2011, we generated approximately 77% of our revenue from sales to retail customers, while we generated approximately 23% of our revenue from sales to CP companies. In the nine months ended November 30, 2010, we generated approximately 81% of our revenue from sales to retail customers while we generated approximately 19% of our revenue from sales to CP companies. In order to grow our revenue and to achieve our long-term strategic objectives, including growth of our retail and CP customer network, it is important for us to expand our sales to derive a more significant portion of our revenue from new and existing CP customers (including through our recent acquisition of M-Factor), and for those companies to actively participate in our collaborative network strategy. If CP companies do not widely accept our software, our revenue growth and business will be harmed.

We face intense competition that could prevent us from increasing our revenue and prevent us from becoming profitable.

The market for our software is highly competitive and we expect competition to intensify in the future. Competitors vary in size and in the scope and breadth of the products and services they offer. Currently, we face competition from traditional enterprise software application vendors such as Oracle Corporation and SAP AG, niche retail software vendors such as KSS Group (recently acquired by dunnhumby USA) and Revionics, Inc., and statistical tool vendors such as SAS, Inc. To a lesser extent, we also compete or potentially compete with marketing information providers for the CP industry such as The Nielsen Company and Information Resources, Inc., as well as business consulting firms such as McKinsey & Company, Inc., Deloitte & Touche LLP and Accenture LLP, which offer merchandising consulting services and analyses. Because the market for our solutions is relatively new, we expect to face additional competition from other established and emerging companies and, potentially, from internally-developed applications. This competition could result in increased pricing pressure, reduced profit margins, increased sales and marketing expenses and a failure to increase, or the loss of, market share.

Competitive offerings may have better performance, lower prices and broader acceptance than our software. Many of our current or potential competitors have longer operating histories, greater brand recognition, larger customer bases and significantly greater financial, technical, sales, research and development, marketing and other resources than we have. Competitors with greater financial resources may be able to offer lower prices, additional products or services, or other incentives that we cannot match or offer. As a result, our competition may be able to offer more effective software or may opt to include software competitive to our software as part of broader, enterprise software solutions at little or no charge.

We may not be able to maintain or improve our competitive position against our current or future competitors, and our failure to do so could seriously harm our business.

We rely on three third-party service providers to host our software, and any interruptions or delays in services from these third parties could impair the delivery of our software as a service or harm our reputation.

We deliver our software to customers over the Internet. The software is hosted in three third-party data centers located in San Jose and Sacramento, California, and Mesa, Arizona. We do not control the operation of any of these facilities, and we rely on these service providers to provide all power, connectivity and physical security. These facilities could be vulnerable to damage or interruption from

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earthquakes, floods, fires, power loss, telecommunications failures and similar events. They are also subject to break-ins, computer viruses, sabotage, intentional acts of vandalism and other misconduct. The occurrence of a natural disaster or intentional misconduct, a decision to close these facilities without adequate notice or other unanticipated problems could result in lengthy interruptions in our services. Additionally, because we currently rely upon disk and tape bond back-up procedures, but do not operate or maintain a fully-redundant back-up site, there is an increased risk of service interruption.

If we fail to respond to rapidly changing technological developments or evolving industry standards, our software may become less competitive or obsolete.

Because our software is designed to operate on a variety of network, hardware and software platforms using standard Internet tools and protocols, we will need to modify and enhance our software continuously to keep pace with changes in Internet-related hardware, software, communication, browser and database technologies. Furthermore, uncertainties about the timing and nature of new network platforms or technologies, or modifications to existing platforms or technologies, could increase our research and development expenses. If we are unable to respond in a timely manner to these rapid technological developments, our software may become less marketable and less competitive or obsolete.

Our use of open source software and third-party technology could impose limitations on our ability to commercialize our software.

We incorporate open source software into our software. Although we monitor our use of open source software closely, the terms of many open source licenses have not been interpreted by United States courts, and there is a risk that these licenses could be construed in a manner that imposes unanticipated conditions, costs, or restrictions on our ability to commercialize our software. In that event, we could be required to seek licenses from third parties in order to continue offering our software, to re-engineer our technology or to discontinue offering our software in the event re-engineering cannot be accomplished on a timely basis, any of which could adversely affect our business, operating results and financial condition. We also incorporate certain third-party technologies, including software programs and algorithms, into our software and may desire to incorporate additional third-party technologies in the future. Licenses to new third-party technologies may not be available to us on commercially reasonable terms, or at all.

If we are unable to protect our intellectual property rights, our competitive position could be harmed and we could be required to incur significant expenses in order to enforce our rights.

To protect our proprietary technology, including our core statistical and mathematic models and our software, we rely on trade secret, patent, copyright, service mark, trademark and other proprietary rights laws and confidentiality agreements with employees and third parties, all of which offer only limited protection. Despite our efforts, the steps we have taken to protect our proprietary rights may not be adequate to preclude misappropriation of our proprietary information or infringement of our intellectual property rights, and our ability to police that misappropriation or infringement is uncertain, particularly in countries outside of the United States, including China, Russia, and India, where we conduct (or third parties conduct on our behalf) a portion of our development activity. Further, we do not know whether any of our pending patent applications will result in the issuance of patents or whether the examination process will require us to narrow our claims. Our current patents and any future patents that may be issued may be contested, circumvented or invalidated. Moreover, the rights granted under any issued patents may not provide us with proprietary protection or competitive advantages, and, as with any technology, competitors may be able to develop technologies similar or superior to our own now or in the future.

Protecting against the unauthorized use of our trade secrets, patents, copyrights, service marks, trademarks and other proprietary rights is expensive, difficult and not always possible. Litigation may be necessary in the future to enforce or defend our intellectual property rights, to protect our trade secrets or to determine the validity and scope of the proprietary rights of others. This litigation could be costly and divert management resources, either of which could harm our business, operating results and financial condition. Furthermore, many of our current and potential competitors have the ability to dedicate substantially greater resources to enforcing their intellectual property rights than we do. Accordingly, despite our efforts, we may not be able to prevent third parties from infringing upon or misappropriating our intellectual property.

We cannot be certain that the steps we have taken will prevent the unauthorized use or the reverse engineering of our technology. Moreover, others may independently develop technologies that are competitive to ours or infringe our intellectual property. The enforcement of our intellectual property rights also depends on our legal actions against these infringers being successful, but we cannot be sure these actions will be successful, even when our rights have been infringed. Furthermore, effective patent, trademark, service mark, copyright and trade secret protection may not be available in every country in which our services are available or where we have development work performed. In addition, the legal standards relating to the validity, enforceability and scope of protection of intellectual property rights in Internet-related industries are uncertain and still evolving.

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Material defects or errors in our software or any failure to meet service level agreements with our customers could harm our reputation, result in significant expense to us and impair our ability to sell our software.

Our software is inherently complex and may contain material defects or errors that may cause it to fail to perform in accordance with customer expectations. Any defects that cause interruptions to the availability of our software could result in lost or delayed market acceptance and sales, require us to provide sales credits or issue refunds to our customers, cause existing customers not to renew their agreements and prospective customers not to purchase our software, divert development resources, hurt our reputation and expose us to claims for liability. After the release of our software, defects or errors may also be identified from time to time by our internal team and by our customers. In addition, we have entered into service level agreements with some of our customers warranting defined levels of uptime reliability and software performance and permitting those customers to receive service credits or discounted future services, or to terminate their agreements in the event that we fail to meet those levels. The costs incurred in correcting any material defects or errors in our software or in failing to meet any such service levels may be substantial.

Because our long-term success depends, in part, on our ability to operate and to expand sales of our software to customers located outside of the United States, our business may be increasingly susceptible to risks associated with international operations.

Our international operations are not significant. In the nine months ended November 30, 2011 and the twelve months ended February 28, 2011, respectively, approximately 15% and 13% of our revenue was attributable to sales to companies located outside the United States. The limited scope of our international operations to date increases the risk that any international expansion efforts that we may undertake will not be successful. In addition, conducting international operations subjects us to new risks that we have not generally faced in the United States. These include:

- fluctuations in currency exchange rates;
- unexpected changes in foreign regulatory requirements, including with respect to the enforcement of the Foreign Corrupt Practices Act or the recently- adopted U.K. Bribery Act;
- localization of our software, including translation of the interface of our software into foreign languages and creation of localized agreements;
- longer accounts receivable payment cycles and difficulties in collecting accounts receivable;
- tariffs and trade barriers and other regulatory or contractual limitations on our ability to sell or develop our software in certain international markets;

- difficulties in managing and staffing international operations;

- potentially adverse tax consequences, including the complexities of international value added tax systems and restrictions on the repatriation of earnings;

- the burdens of complying with a wide variety of international laws and different legal standards, including local data privacy laws and local consumer protection laws that could regulate retailers permitted pricing and promotion practices;

- potential interruption of internet access by foreign governments;

- political, social and economic instability abroad, terrorist attacks and security concerns in general; and

- reduced or varied protection of intellectual property rights in some countries, in particular China and Russia.

The occurrence of any of these risks could negatively affect our international business and, consequently, our results of operations.

Because portions of our software development, sustaining engineering, quality assurance and testing, operations and customer support are provided internationally, including by third parties in China and Russia, our business is susceptible to risks associated with having substantial operations overseas.

Portions of our software development, sustaining engineering, quality assurance and testing, operations and customer support are provided by Sonata Services Limited, or Sonata, a third party located in Shanghai, China, as well as to a more limited extent by a third party located in Russia and internal development resources in India. As of November 30, 2011, in addition to our 179 employees in our operations, customer support, science, product management and engineering groups located in the United States, an additional 83 Sonata personnel were dedicated to our projects. Remotely coordinating resources in China, Russia, and India requires significant

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management attention and substantial resources, and there can be no assurance that we will be successful in coordinating these activities. Furthermore, if there is a disruption to these operations, it will require that substantial management attention and time be devoted to achieving resolution. If our international third-party contractors were to stop providing these services or if there was widespread departure of their trained personnel, this could cause a disruption in our product development process, quality assurance and product release cycles and customer support organizations and require us to incur additional costs to replace and train new personnel.

Enforcement of intellectual property rights and contractual rights may be more difficult in China and Russia, and their laws and regulations may not be sufficient to cover all aspects of economic activities. In particular, because these laws and regulations are relatively new, and because of the limited volume of published decisions and their non-binding nature, the interpretation and enforcement of these laws and regulations involve uncertainties. Accordingly, the enforcement of our contractual arrangements with our international third- party contractors, our confidentiality agreements with each contractor dedicated to our work, and the interpretation of the laws governing this relationship are subject to uncertainty.

If we fail to maintain proper and effective internal controls, our ability to produce accurate financial statements could be impaired, which could adversely affect our operating results, our ability to operate our business and investors views of us.

Ensuring that we have internal financial and accounting controls and procedures adequate to produce accurate financial statements on a timely basis is a costly and time-consuming effort that needs to be re-evaluated frequently. The Sarbanes-Oxley Act requires, among other things, that we maintain effective internal control over financial reporting and disclosure controls and procedures. In particular, we are required to perform annual system and process evaluation and testing of our internal control over financial reporting to allow management and our independent registered public accounting firm to report on the effectiveness of our internal control over financial reporting, as required by Section 404 of the Sarbanes-Oxley Act. In the future, our testing, or the subsequent testing by our independent registered public accounting firm, may reveal deficiencies in our internal control over financial reporting that are deemed to be material weaknesses. Our compliance with Section 404 requires that we incur substantial accounting expense and expend significant management time on compliance-related issues. Moreover, if we are not able to comply with the requirements of Section 404 in the future, or if we or our independent registered public accounting firm identifies deficiencies in our internal control over financial reporting that are deemed to be material weaknesses, the market price of our common stock could decline and we could be subject to sanctions or investigations by the NASDAQ Stock Market, the Securities and Exchange Commission, or SEC, or other regulatory authorities, which would require additional financial and management resources.

Furthermore, implementing any appropriate future changes to our internal control over financial reporting may entail substantial costs in order to modify our existing accounting systems, may take a significant period of time to complete and may distract our officers, directors and employees from the operation of our business. These changes, however, may not be effective in maintaining the adequacy of our internal control over financial reporting, and any failure to maintain that adequacy, or consequent inability to produce accurate financial statements on a timely basis, could increase our operating costs and could materially impair our ability to operate our business. In addition, investors perceptions that our internal control over financial reporting is inadequate or that we are unable to produce accurate financial statements may adversely affect our stock price. While neither we nor our independent registered public accounting firm has identified deficiencies in our internal control over financial reporting that are deemed to be material weaknesses, there can be no assurance that material weaknesses will not be subsequently identified.

If one or more of our key strategic relationships were to become impaired or if these third parties were to align with our competitors, our business could be harmed.

We have relationships with a number of third parties whose products, technologies and services complement our software. Many of these third parties also compete with us or work with our competitors. If we are unable to maintain our relationships with the key third parties that currently recommend our software or that provide consulting services on our software implementations or if these third parties were to begin to recommend our competitors products and services, our business could be harmed.

Claims by others that we infringe their proprietary technology could harm our business.

Third parties could claim that our software infringes their proprietary rights. In recent years, there has been significant litigation involving patents and other intellectual property rights, and we expect that infringement claims may increase as the number of products and competitors in our market increases and overlaps occur. In addition, to the extent that we gain greater visibility and market exposure as a public company, we will face a higher risk of being the subject of intellectual property infringement claims. Any claims of infringement by a third party, even those without merit, could cause us to incur substantial defense costs and could distract our management from our business. Furthermore, a party making such a claim, if successful, could secure a judgment that requires us to pay substantial damages. A judgment could also include an injunction or other court order that could prevent us from offering our software. In addition, we might be required to seek a license for the use of the infringed intellectual property, which may not be

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available on commercially reasonable terms or at all. Alternatively, we might be required to develop non-infringing technology, which could require significant effort and expense and might ultimately not be successful.

Third parties may also assert infringement claims relating to our software against our customers. Any of these claims might require us to initiate or defend potentially protracted and costly litigation on their behalf, regardless of the merits of these claims, because in certain situations we agree to indemnify our customers from claims of infringement of proprietary rights of third parties. If any of these claims succeeds, we might be forced to pay damages on behalf of our customers, which could materially adversely affect our business.

Changes in financial accounting standards or practices may cause adverse, unexpected financial reporting fluctuations and affect our reported results of operations.

A change in accounting standards or practices could have a significant effect on our reported results and might affect our reporting of transactions completed before the change is effective. New accounting pronouncements and varying interpretations of accounting pronouncements have occurred in the past and may occur in the future. Changes to existing rules or the questioning of current practices may adversely affect our reported financial results or the way we conduct our business.

We have expanded our operations in recent periods. If we fail to manage this expansion effectively, we may be unable to execute our business plan, maintain high levels of customer service or address competitive challenges adequately.

We have expanded our overall business, headcount and operations in recent periods. For instance, our headcount grew from 198 employees at February 28, 2007 to 351 employees at November 30, 2011. Headcount in research and development increased from 99 employees at February 28, 2007 to 136 employees at November 30, 2011. We may need to continue to expand our operations in order to increase our customer base and to develop additional software. Increases in our customer base could create challenges in our ability to implement our software and support our customers. In addition, we will be required to continue to improve our operational, financial and management controls and our reporting procedures. As a result, we may be unable to manage our business effectively in the future, which may negatively impact our operating results.

Evolving regulation of the Internet may affect us adversely.

As Internet commerce continues to evolve, increasing regulation by federal, state or foreign agencies becomes more likely. For example, we believe increased regulation is likely in the area of data privacy, and laws and regulations applying to the solicitation, collection, processing, or use of personal or consumer information could affect our customers ability to use and share data, potentially reducing demand for our software and restricting our ability to store and process data for our customers. In addition, taxation of software provided over the Internet or other charges imposed by government agencies or by private organizations for accessing the Internet may also be imposed. Any regulation imposing greater fees for Internet use or restricting information exchange over the Internet could result in a decline in the use of the Internet and the viability of Internet-based software, which could harm our business, financial condition and operating results.

Third-party claims and litigation could seriously harm our business.

We have from time to time become involved in legal matters that arise in the normal course of business and otherwise. For example, we are currently involved in arbitration proceedings with an M-Factor customer associated with that customer s failure to pay amounts due under, and purported termination of, their agreement with M-Factor relating to certain services. We are continuing to assess the impact of this dispute. There can be no assurance that this matter or other third party claims and litigation that may arise in the future will not have a material adverse effect on our business, financial position, results of operations, or cash flows, including a loss of customers, or subject us to significant financial or other remedies.

We incur significant costs as a result of operating as a public company, and our management is required to devote substantial time to compliance efforts.

As a public company, we incur significant legal, accounting and other expenses. The Sarbanes-Oxley Act and the Dodd-Frank Wall Street Reform and Consumer Protection Act (the Dodd-Frank Act), and rules currently proposed or subsequently implemented by the SEC and the NASDAQ Global Market, impose additional requirements on public companies. The Dodd-Frank Act subjects us to significant additional executive compensation and corporate governance requirements, a number of which have yet to be implemented by the SEC. Our management and other personnel need to devote a substantial amount of time to complying with these requirements. Moreover, these rules and regulations have increased our legal and financial compliance costs and make some activities more time-consuming and costly. These rules and regulations could also make it more difficult for us to attract and retain qualified persons to serve on our board of directors and board committees or as executive officers and more expensive for us to obtain or maintain director and officer liability insurance.

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Risks Related to Ownership of Our Common Stock

The trading price of our common stock has been volatile in the past, may continue to be volatile, and may decline.

The trading price of our common stock has fluctuated widely in the past and may do so in the future. Further, our common stock has limited trading history. Factors affecting the trading price of our common stock, many of which are beyond our control, could include:

- variations in our operating results, including any decline in our revenues or material changes in our cash flows;
- announcements of technological innovations, new products and services, acquisitions, strategic alliances or significant agreements by us or by our competitors;
- recruitment or departure of key personnel;
- the financial projections we may provide to the public, any changes in these projections or our failure to meet these projections;
- changes in the estimates of our operating results or changes in recommendations by any securities analysts that elect to follow our common stock;
- potential dilution caused by future issuances of our stock, including through currently outstanding or future stock options or restricted stock units;
- market conditions in our industry, the retail industry and the economy as a whole;
- price and volume fluctuations in the overall stock market;
- lawsuits threatened or filed against us or other disputes;

- adoption or modification of regulations, policies, procedures or programs applicable to our business; and
- the volume of trading in our common stock, including sales upon exercise of outstanding options.

In addition, if the market for technology stocks or the stock market in general experiences loss of investor confidence as has happened in prior periods, the trading price of our common stock could decline for reasons unrelated to our business, operating results, or financial condition. The trading price of our common stock might also decline in reaction to events that affect other companies in our industry even if these events do not directly affect us. Some companies that have had volatile market prices for their securities have had securities class actions filed against them. A suit filed against us, regardless of its merits or outcome, could cause us to incur substantial costs and could divert management s attention.

Future sales of shares by existing stockholders, or the perception that such sales may occur, could cause our stock price to decline.

If our existing stockholders, particularly our directors and executive officers and other significant stockholders, sell substantial amounts of our common stock in the public market, or are perceived by the public market as intending to sell, the trading price of our common stock could decline.

If securities analysts do not publish research or publish unfavorable research about our business, our stock price and trading volume could decline.

The trading market for our common stock depends in part on the research and reports that securities analysts publish about us or our business. We have limited research coverage by securities analysts. If we do not obtain further securities analyst coverage, or if one or more of the analysts who cover us downgrade our stock or publish unfavorable research about our business, our stock price would likely decline. If one or more of these analysts cease coverage of our company or fail to publish reports on us regularly, demand for our stock could decrease, which could cause our stock price and trading volume to decline.

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Insiders and other significant stockholders have significant influence over us and will be able to influence corporate matters.

At November 30, 2011, our directors, executive officers and holders of ten percent or more of our common stock beneficially owned, in the aggregate, approximately 20.7% of our outstanding common stock. As a result, these stockholders will be able to exercise significant influence over all matters requiring stockholder approval, including the election of directors and approval of significant corporate transactions, such as a merger or other sale of our company or its assets. This concentration of ownership could limit your ability to influence corporate matters and may have the effect of delaying or preventing a third party from acquiring control over us.

Anti-takeover provisions in our charter documents and Delaware law could discourage, delay or prevent a change in control of our company and may affect the trading price of our common stock.

We are a Delaware corporation and the anti-takeover provisions of the Delaware General Corporation Law may discourage, delay or prevent a change in control by prohibiting us from engaging in a business combination with an interested stockholder for a period of three years after the person becomes an interested stockholder, even if a change in control would be beneficial to our existing stockholders. In addition, our restated certificate of incorporation and amended and restated bylaws may discourage, delay or prevent a change in our management or control over us that stockholders may consider favorable. Our restated certificate of incorporation and amended and restated bylaws:

- authorize the issuance of blank check preferred stock that could be issued by our board of directors to thwart a takeover attempt;
- establish a classified board of directors, as a result of which the successors to the directors whose terms have expired will be elected to serve from the time of election and qualification until the third annual meeting following their election;
- require that directors only be removed from office for cause and only upon a majority stockholder vote;
- provide that vacancies on our board of directors, including newly created directorships, may be filled only by a majority vote of directors then in office;
- limit who may call special meetings of stockholders;
- prohibit stockholder action by written consent, thus requiring all actions to be taken at a meeting of the stockholders;

- require supermajority stockholder voting to effect certain amendments to our restated certificate of incorporation and amended and restated bylaws; and

- require advance notification of stockholder nominations and proposals.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

None.

Item 3. Defaults Upon Senior Securities

None.

Item 4. *(Removed and Reserved)*

Not applicable.

Item 5. Other Information

None.

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Item 6. Exhibits

Exhibit No.	Description
2.1	Agreement and Plan of Merger , dated December 7, 2011, by and among International Business Machines Corporation, Cudgee Acquisition Corp., and Registrant (incorporated by reference to Exhibit 2.1 of Registrant s Current Report on Form 8-K (File No. 001-33634), filed with the SEC on December 8, 2011)
3.1	Restated Certificate of Incorporation (incorporated by reference to Exhibit 3.2 of Registrant s Registration Statement on Form S-1 (Registration No. 333-143248))
3.2	Amended and Restated Bylaws of DemandTec, Inc. (incorporated by reference to Exhibit 3.1 of Registrant s Current Report on Form 8-K (File No. 001-33634), filed with the SEC on June 2, 2011
4.1	Form of Common Stock Certificate (incorporated by reference to Exhibit 4.2 of Registrant s Registration Statement on Form S-1 (Registration No. 333-143248))
31.1	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31.2	Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32.1*	Certification of Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
101**	Interactive data files (XBRL) pursuant to Rule 405 of Regulation S-T: (i) the Condensed Consolidated Balance Sheets as of November 30, 2011 and February 28, 2011, (ii) the Condensed Consolidated Statements of Operations for the three and nine months ended November 30, 2011 and 2010, (iii) the Condensed Consolidated Statements of Cash Flows for the nine months ended November 30, 2011 and 2010 and (iv) the Notes to Condensed Consolidated Financial Statements

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* This certification is not deemed filed with the Securities and Exchange Commission and is not to be incorporated by reference into any filing of DemandTec, Inc. under the Securities Act of 1933 or the Securities Exchange Act of 1934, whether made before or after the date of this Quarterly Report on Form 10-Q, irrespective of any general incorporation language contained in such filing.

** XBRL (Extensible Business Reporting Language) information is not deemed filed with the Securities and Exchange Commission and is not to be incorporated by reference into any filing of DemandTec, Inc. under the Securities Act of 1933 or the Securities Exchange Act of 1934, whether made before or after the date of this Quarterly Report on Form 10-Q, irrespective of any general incorporation language contained in such filing.

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SIGNATURES

Pursuant to the requirements of Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

Dated: January 6, 2012

DemandTec, Inc.

By:	/s/ Mark A. Culhane Mark A. Culhane Executive Vice President and Chief Financial Officer (Principal Financial and Accounting Officer)

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4.1	Form of Common Stock Certificate (incorporated by reference to Exhibit 4.2 of Registrant s Registration Statement on Form S-1 (Registration No. 333-143248))
31.1	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31.2	Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32.1*	Certification of Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
101**	Interactive data files (XBRL) pursuant to Rule 405 of Regulation S-T: (i) the Condensed Consolidated Balance Sheets as of November 30, 2011 and February 28, 2011, (ii) the Condensed Consolidated Statements of Operations for the three and nine months ended November 30, 2011 and 2010, (iii) the Condensed Consolidated Statements of Cash Flows for the nine months ended November 30, 2011 and 2010 and (iv) the Notes to Condensed Consolidated Financial Statements

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* This certification is not deemed filed with the Securities and Exchange Commission and is not to be incorporated by reference into any filing of DemandTec, Inc. under the Securities Act of 1933 or the Securities Exchange Act of 1934, whether made before or after the date of this Quarterly Report on Form 10-Q, irrespective of any general incorporation language contained in such filing.

** XBRL (Extensible Business Reporting Language) information is not deemed filed with the Securities and Exchange Commission and is not to be incorporated by reference into any filing of DemandTec, Inc. under the Securities Act of 1933 or the Securities Exchange Act of 1934, whether made before or after the date of this Quarterly Report on Form 10-Q, irrespective of any general incorporation language contained in such filing.