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1181
C.A. No. 2:96CV645B

Board of Directors' Report
Finance & Administration

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Q91-1

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Finance
Results of Operations

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RESULTS OF OPERATIONS COMPARED WITH PRIOR YEAR

Consolidated statements of income compared with prior year are presented below for the three months ended September 30, 1990 and 1989 (in millions, except net income per share).

	Q91-1		Q90-1		Growth %
Net revenues	\$369.4	100.0%	\$235.2	100.0%	57
Cost of revenues	<u>76.0</u>	<u>20.6</u>	<u>50.8</u>	<u>21.6</u>	50
Gross profit	<u>293.4</u>	<u>79.4</u>	<u>184.4</u>	<u>78.4</u>	59
Operating expenses:					
Research and development	50.8	13.7	39.7	16.9	28
Sales and marketing	106.7	28.9	67.0	28.5	59
General and administrative	<u>12.9</u>	<u>3.5</u>	<u>8.3</u>	<u>3.5</u>	55
Total operating expenses	<u>170.4</u>	<u>46.1</u>	<u>115.0</u>	<u>48.9</u>	48
Operating income	123.0	33.3	69.4	29.5	77
Non-operating income	5.5	1.5	5.0	2.1	10
Stock option program expense	<u>(1.5)</u>	<u>(0.4)</u>	<u>(1.5)</u>	<u>(0.6)</u>	-
Income before income taxes	127.0	34.4	72.9	31.0	74
Provision for income taxes	<u>39.4</u>	<u>10.7</u>	<u>23.3</u>	<u>9.9</u>	69
Net income	<u>\$ 87.6</u>	<u>23.7%</u>	<u>\$ 49.6</u>	<u>21.1%</u>	77
Average shares outstanding	<u>123.3</u>		<u>114.4</u>		8
Net income per share	<u>\$ 0.71</u>		<u>\$ 0.43</u>		65

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Q91-1 versus Q90-1

Net revenues for Q91-1 increased 57% to \$369.4 million from \$235.2 million for Q90-1. The year-over-year growth was lead by International Finished Goods which increased 106% and accounted for 44.7% of total net revenues. Europe was particularly strong, increasing 132% to \$123.6 million from \$53.3 million in Q90-1, whereas Non-Europe increased 54% to \$41.4 million from \$26.9 million. The following is a breakdown of net revenues by channel of distribution and product group (in millions).

Channel	Q91-1		Q90-1		Growth Percentage
	Revenue	% of Total	Revenue	% of Total	
USSMD	\$128.1	34.7%	\$ 79.5	33.8%	61
International Finished Goods	<u>165.0</u>	<u>44.7</u>	<u>80.2</u>	<u>34.1</u>	106
Worldwide Retail	<u>293.1</u>	<u>79.4</u>	<u>159.7</u>	<u>67.9</u>	84
Domestic OEM	29.7	8.0	35.2	14.9	(16)
International OEM	<u>38.0</u>	<u>10.3</u>	<u>35.2</u>	<u>15.0</u>	8
Worldwide OEM	<u>67.7</u>	<u>18.3</u>	<u>70.4</u>	<u>29.9</u>	(4)
Other	<u>8.6</u>	<u>2.3</u>	<u>5.1</u>	<u>2.2</u>	69
Total	<u>\$369.4</u>	<u>100.0%</u>	<u>\$235.2</u>	<u>100.0%</u>	57
Product Group					
Applications	\$177.9	48.2%	\$106.4	45.3%	67
Systems	116.4	31.5	75.2	32.0	55
SPAG	49.2	13.3	25.3	10.8	94
Languages	14.7	4.0	13.0	5.5	13
Network	4.8	1.3	7.7	3.2	(38)
Other	<u>6.4</u>	<u>1.7</u>	<u>7.6</u>	<u>3.2</u>	(16)
Total	<u>\$369.4</u>	<u>100.0%</u>	<u>\$235.2</u>	<u>100.0%</u>	57

From a product perspective, Win 3, Windows-based applications, and Mice all increased significantly compared with Q90-1. Gross revenue from Win Apps totalled \$80.3 million compared to only \$18.2 million in Q90-1 and \$45.1 million in Q90-4. Revenues from Win 3 (\$28.7 million), Win 3 Updates (\$12.9 million), and Win Apps (\$80.3 million) accounted for approximately 32% of total gross revenues. The Company's leading products for Q91-1 (compared with prior year) are shown in the following table (units in thousands, revenue in millions). Updates are not included in the leading products table. If they were, Win 3 Updates would have been the 9th leading product.

Q91-1 Rank	Q90-1 Rank	Product	Q91-1		Q90-1		Revenue Growth %
			Units	Revenue	Units	Revenue	
1	1	DOS/GW Basic	3,920.5	\$ 60.9	3,519.4	\$ 51.7	18
2	3	Serial/Bus Mouse	491.0	46.3	263.4	24.2	91
3	4	Win Excel	121.6	33.5	84.2	17.6	90
4	-	Win Word	122.5	29.9	-	-	-
5	-	Win 3	335.8	28.7	-	-	-
6	2	PC Word	97.6	28.2	135.6	25.5	11
7	7	PC Works	216.8	15.2	193.9	9.3	63
8	5	Mac Word	75.3	13.4	75.9	12.3	9
9	6	Mac Excel	49.7	10.8	58.0	10.8	-
10	8	Pro C	46.3	6.6	37.9	5.5	20
11	-	Win Project	14.8	6.0	-	-	-
12	15	Mac Office	10.9	5.0	3.1	1.4	257
13	9	PC Multiplan	36.1	4.4	40.4	4.2	5
14	-	Win PowerPoint	15.2	3.9	-	-	-
15	10	Mac Works	27.0	3.8	24.9	3.3	15
			<u>\$296.6</u>			<u>\$165.8</u>	
Percent of net revenues			<u>80%</u>			<u>70%</u>	

Q90-1: #11 Xenix (\$2.3 million); #12 PC Chart (\$1.6 million); #13 Pro Fortran (\$1.6 million); #14 QuickBasic (\$1.6 million)

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Q91-1 versus Q90-1

Cost of revenues for Q91-1 was 20.6% of net revenues compared with 21.6% for Q90-1. The product cost percentage for each channel of distribution and each product group (Q91-1 and Q90-1) is shown in the following table:

Channel	Q91-1			Q90-1		
	Gross Sales Mix	Cost %	Weighted Cost %	Gross Sales Mix	Cost %	Weighted Cost %
USSMD	35.0%	17.9	6.3%	34.5%	21.7	7.5%
Int'l Finished Goods	43.2	18.0	7.8	33.3	22.3	7.4
US OEM	10.1	6.9	0.7	14.0	3.4	0.5
Int'l OEM	9.4	-	-	16.3	-	-
Other	2.3	15.2	0.3	2.0	14.4	0.3
Product cost - gross	<u>100.0%</u>		15.1	<u>100.0%</u>		15.7
Effect of revenue adjustments			x1.045			x1.038
Product cost - net			<u>15.8</u>			<u>16.3</u>
Manufacturing variances			-			(0.4)
Inventory adjustments			1.1			1.8
Freight, shipping and other			2.8			2.5
Royalties			0.9			1.4
Non-product costs			4.8			5.3
Total			<u>20.6%</u>			<u>21.6%</u>

Product Group	Q91-1			Q90-1		
	Gross Sales Mix	Cost %	Weighted Cost %	Gross Sales Mix	Cost %	Weighted Cost %
Applications	47.5%	12.2	5.8%	45.3%	16.6	7.5%
Systems	30.2	11.2	3.4	27.8	7.8	2.2
SPAG	13.1	36.2	4.7	10.7	41.7	4.5
Languages	4.0	18.7	0.7	5.5	21.9	1.2
Other (includes UPB)	5.2	9.6	0.5	10.7	2.8	0.3
Product cost - gross	<u>100.0%</u>		15.1%	<u>100.0%</u>		15.7%

Product costs as a percentage of net revenues were 15.8% for Q91-1 compared with 16.3% for Q90-1. The shift to a greater contribution from worldwide retail was more than offset by significant product cost reductions within several product groups (Applications, SPAG and Languages). As a percentage of net revenues, non-product costs included in cost of revenues were 4.8% for Q91-1 compared with 5.3% for Q90-1.

Operating expenses grew 48% from period-to-period (from \$115.0 million to \$170.4 million). Operating expenses as a percentage of net revenues declined from 48.9% to 46.1%. The operating expense line items with the largest increases were (in millions):

	Q91-1	Q90-1	Increase	%
Payroll	\$ 61.5	\$ 39.4	\$22.1	56
Marketing	23.8	11.6	12.2	105
Marketing accrual	6.4	8.4	(2.0)	(24)
Stlms, lic, ins & taxes	6.3	2.5	3.8	152
Employee fringes	9.5	6.0	3.5	58
Depreciation	9.8	6.3	3.5	56
All other	53.1	40.8	12.3	30
	<u>\$170.4</u>	<u>\$115.0</u>	<u>\$55.4</u>	48

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Q91-1 versus Q90-1

Non-operating income for Q91-1 was \$5.5 million compared with \$5.0 million for Q90-1. Non-operating income (expense) is composed of (in millions):

	<u>Q91-1</u>	<u>Q90-1</u>	<u>Change</u>
Investment income	\$9.1	\$6.5	\$2.6
Allowance for NPLs	(2.9)	--	(2.9)
Interest expense	(0.7)	(0.5)	(0.2)
Foreign currency transactions	0.9	--	0.9
SCO amortization	(0.5)	(0.5)	--
All other	(0.4)	(0.5)	0.1
	<u>\$5.5</u>	<u>\$5.0</u>	<u>\$0.5</u>

Stock option program expense is the result of the Company's program regarding incentive stock options under which employees may receive a cash payment in exchange for taking certain actions that result in a tax benefit to the Company. The Company reports the gross benefit under the program as a contribution to capital, whereas the expense net of directly related taxes is charged against income. Accounting rules require that this expense be recognized ratably over the vesting period of the related options rather than when paid. A reconciliation of the accrual for stock option program payments is as follows (in millions):

Accrual as of June 30, 1990	\$3.7
Stock option program expense	1.5
Payments made upon exercise of converted options	(1.3)
Accrual as of September 30, 1990	<u>\$3.9</u>

The tax rate for Q91-1 was 31.0%, down from 32.0% for Q90-1.

Net income for Q91-1 was \$87.6 million compared with \$49.6 million for Q90-1. Net income as a percentage of net revenues increased from 21.1% to 23.7%. This 2.6% net income margin improvement resulted from gains in gross profit (1.0%), operating expense (2.8%), and stock option program expense (0.2%), offset by a decline in non-operating income (0.6%), and an increase in the provision for income taxes (0.8%).

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RESULTS OF OPERATIONS COMPARED WITH COMPETITION

Consolidated statements of income for Microsoft, Lotus, Oracle, and Novell are presented below (in millions, except net income per share).

	Microsoft		Lotus		Oracle		Novell	
Most recent quarter								
Net revenues	\$369.4	100.0%	\$157.4	100.0%	\$203.8	100.0%	\$131.1	100.0%
Cost of revenues	<u>76.0</u>	<u>20.6</u>	<u>28.4</u>	<u>18.0</u>	<u>57.8</u>	<u>28.4</u>	<u>32.7</u>	<u>24.9</u>
Gross profit	<u>293.4</u>	<u>79.4</u>	<u>129.0</u>	<u>82.0</u>	<u>146.0</u>	<u>71.6</u>	<u>98.4</u>	<u>75.1</u>
Operating expenses:								
Research and development	50.8	13.7	31.5	20.0	20.6	10.1	16.3	12.4
Sales and marketing	106.7	28.9	71.6	45.5	150.1	73.7	37.9	28.9
General and administrative	<u>12.9</u>	<u>3.5</u>	<u>15.5</u>	<u>9.9</u>	<u>22.3</u>	<u>10.9</u>	<u>7.4</u>	<u>5.7</u>
Total operating expenses	<u>170.4</u>	<u>46.1</u>	<u>118.6</u>	<u>75.4</u>	<u>193.0</u>	<u>94.7</u>	<u>61.6</u>	<u>47.0</u>
Operating income	123.0	33.3	10.4	6.6	(47.0)	(23.1)	36.8	28.1
Non-operating income	5.5	1.5	1.5	1.0	(7.5)	(3.7)	4.0	3.0
Stock option program expense	<u>(1.5)</u>	<u>(0.4)</u>	<u>--</u>	<u>--</u>	<u>--</u>	<u>--</u>	<u>--</u>	<u>--</u>
Income before income taxes	127.0	34.4	11.9	7.6	(54.5)	(26.8)	40.8	31.1
Provision for income taxes	<u>39.4</u>	<u>10.7</u>	<u>3.3</u>	<u>2.1</u>	<u>(18.5)</u>	<u>(9.1)</u>	<u>14.7</u>	<u>11.2</u>
Net income	\$ <u>87.6</u>	<u>23.7%</u>	\$ <u>8.6</u>	<u>5.5%</u>	\$ <u>(36.0)</u>	<u>(17.7)%</u>	\$ <u>26.1</u>	<u>19.9%</u>
Average shares outstanding	<u>123.3</u>		<u>43.0</u>		<u>131.4</u>		<u>69.3</u>	
Net income per share	\$ <u>0.71</u>		\$ <u>0.20</u>		\$ <u>(0.27)</u>		\$ <u>0.38</u>	
	Microsoft		Lotus		Oracle		Novell	
Trailing twelve months								
Net revenues	\$1,317.7	100.0%	\$648.0	100.0%	\$999.2	100.0%	\$468.0	100.0%
Cost of revenues	<u>277.9</u>	<u>21.1</u>	<u>112.9</u>	<u>17.4</u>	<u>189.6</u>	<u>19.0</u>	<u>138.1</u>	<u>29.5</u>
Gross profit	<u>1,039.8</u>	<u>78.9</u>	<u>535.1</u>	<u>82.6</u>	<u>809.6</u>	<u>81.0</u>	<u>329.9</u>	<u>70.5</u>
Operating expenses:								
Research and development	191.7	14.6	111.0	17.1	89.3	8.9	55.3	11.8
Sales and marketing	357.3	27.1	260.9	40.3	519.9	52.0	135.1	28.9
General and administrative	<u>43.9</u>	<u>3.3</u>	<u>62.5</u>	<u>9.7</u>	<u>76.7</u>	<u>7.7</u>	<u>28.7</u>	<u>6.1</u>
Total operating expenses	<u>592.9</u>	<u>45.0</u>	<u>434.4</u>	<u>67.1</u>	<u>685.9</u>	<u>68.6</u>	<u>219.1</u>	<u>46.8</u>
Operating income	446.9	33.9	100.7	15.5	123.7	12.4	110.8	23.7
Non-operating income	23.8	1.8	9.1	1.4	(22.7)	(2.3)	8.3	1.7
Stock option program expense	<u>(6.0)</u>	<u>(0.4)</u>	<u>--</u>	<u>--</u>	<u>--</u>	<u>--</u>	<u>--</u>	<u>--</u>
Income before income taxes	464.7	35.3	109.8	16.9	101.0	10.1	119.1	25.4
Provision for income taxes	<u>147.4</u>	<u>11.2</u>	<u>25.5</u>	<u>3.9</u>	<u>31.2</u>	<u>3.1</u>	<u>43.1</u>	<u>9.2</u>
Net income	\$ <u>317.3</u>	<u>24.1</u>	\$ <u>84.3</u>	<u>13.0%</u>	\$ <u>69.8</u>	<u>7.0%</u>	\$ <u>76.0</u>	<u>16.2%</u>
Average shares outstanding	<u>121.6</u>		<u>43.2</u>		<u>135.6</u>		<u>67.7</u>	
Net income per share	\$ <u>2.61</u>		\$ <u>1.95</u>		\$ <u>0.51</u>		\$ <u>1.12</u>	

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Compared with Competition

Consolidated statements of income for Microsoft for each of the four quarters ended September 30, 1990 are presented below (in millions, except net income per share).

	<u>Dec. 31, 1989</u>	<u>Mar. 31, 1990</u>	<u>Jun. 30, 1990</u>	<u>Sep. 30, 1990</u>	<u>Trailing 12 months</u>
Net revenues	\$300.4	\$310.9	\$337.0	\$369.4	\$1,317.7
Cost of revenues	<u>65.8</u>	<u>66.1</u>	<u>70.0</u>	<u>76.0</u>	<u>277.9</u>
Gross profit	234.6	244.8	267.0	293.4	1,039.8
Operating expenses:					
Research and development	41.3	47.1	52.5	50.8	191.7
Sales and marketing	76.3	82.1	92.2	106.7	357.3
General and administrative	<u>10.0</u>	<u>9.2</u>	<u>11.8</u>	<u>12.9</u>	<u>43.9</u>
Total operating expenses	127.6	138.4	156.5	170.4	592.9
Operating income	107.0	106.4	110.5	123.0	446.9
Non-operating income	4.0	5.7	8.6	5.5	23.8
Stock option program expense	<u>(1.5)</u>	<u>(1.5)</u>	<u>(1.5)</u>	<u>(1.5)</u>	<u>(6.0)</u>
Income before income taxes	109.5	110.6	117.6	127.0	464.7
Provision for income taxes	<u>35.0</u>	<u>35.4</u>	<u>37.6</u>	<u>39.4</u>	<u>147.4</u>
Net income	\$ <u>74.5</u>	\$ <u>75.2</u>	\$ <u>80.0</u>	\$ <u>87.6</u>	\$ <u>317.3</u>
Average shares outstanding	<u>118.7</u>	<u>121.1</u>	<u>123.5</u>	<u>123.3</u>	<u>121.6</u>
Net income per share	\$ <u>0.63</u>	\$ <u>0.62</u>	\$ <u>0.65</u>	\$ <u>0.71</u>	\$ <u>2.61</u>
<hr/>					
Net revenues	100.0%	100.0%	100.0%	100.0%	100.0%
Cost of revenues	<u>21.9</u>	<u>21.3</u>	<u>20.8</u>	<u>20.6</u>	<u>21.1</u>
Gross profit	78.1	78.7	79.2	79.4	78.9
Operating expenses:					
Research and development	13.8	15.2	15.6	13.7	14.6
Sales and marketing	25.4	26.4	27.3	28.9	27.1
General and administrative	<u>3.3</u>	<u>2.9</u>	<u>3.5</u>	<u>3.5</u>	<u>3.3</u>
Total operating expenses	42.5	44.5	46.4	46.1	45.0
Operating income	35.6	34.2	32.8	33.3	33.9
Non-operating income	1.3	1.9	2.5	1.5	1.8
Stock option program expense	<u>(0.5)</u>	<u>(0.5)</u>	<u>(0.4)</u>	<u>(0.4)</u>	<u>(0.4)</u>
Income before income taxes	36.5	35.6	34.9	34.4	35.3
Provision for income taxes	<u>11.7</u>	<u>11.4</u>	<u>11.2</u>	<u>10.7</u>	<u>11.2</u>
Net income	<u>24.8%</u>	<u>24.2%</u>	<u>23.7%</u>	<u>23.7%</u>	<u>24.1%</u>

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Compared with Competition

Consolidated statements of income for Lotus for each of the four quarters ended September 30, 1990 are presented below (in millions, except net income per share).

	Dec. 31, 1989	Mar. 31, 1990	Jun. 30, 1990	Sept. 30, 1990	Trailing 12 months
Net revenues	\$149.9	\$165.5	\$175.2	\$157.4	\$648.0
Cost of revenues	<u>24.4</u>	<u>28.9</u>	<u>31.2</u>	<u>28.4</u>	<u>112.9</u>
Gross profit	125.5	136.6	144.0	129.0	535.1
Operating expense:					
Research and development	25.4	25.9	28.2	31.5	111.0
Sales and marketing	58.5	63.1	67.7	71.6	260.9
General and administrative	<u>15.7</u>	<u>16.0</u>	<u>15.3</u>	<u>15.5</u>	<u>62.5</u>
Total operating expenses	<u>99.6</u>	<u>105.0</u>	<u>111.2</u>	<u>118.6</u>	<u>434.4</u>
Operating income	25.9	31.6	32.8	10.4	100.7
Non-operating income	7.7	0.1	(0.2)	1.5	9.1
Stock option program expense	—	—	—	—	—
Income before income taxes	33.6	31.7	32.6	11.9	109.8
Provision for income taxes	<u>4.2</u>	<u>8.9</u>	<u>9.1</u>	<u>3.3</u>	<u>25.5</u>
Net income	\$ <u>29.4</u>	\$ <u>22.8</u>	\$ <u>23.5</u>	\$ <u>8.6</u>	\$ <u>84.3</u>
Average shares outstanding	<u>42.8</u>	<u>43.3</u>	<u>43.8</u>	<u>43.0</u>	<u>43.2</u>
Net income per share	\$ <u>0.69</u>	\$ <u>0.53</u>	\$ <u>0.54</u>	\$ <u>0.20</u>	\$ <u>1.95</u>
Net revenues	100.0%	100.0%	100.0%	100.0%	100.0%
Cost of revenues	<u>16.3</u>	<u>17.5</u>	<u>17.8</u>	<u>18.0</u>	<u>17.4</u>
Gross profit	<u>83.7</u>	<u>82.5</u>	<u>82.2</u>	<u>82.0</u>	<u>82.6</u>
Operating expense:					
Research and development	16.9	15.6	16.1	20.0	17.1
Sales and marketing	39.0	38.1	38.6	45.5	40.3
General and administrative	<u>10.5</u>	<u>9.7</u>	<u>8.8</u>	<u>9.9</u>	<u>9.7</u>
Total operating expenses	<u>66.4</u>	<u>63.4</u>	<u>63.5</u>	<u>75.4</u>	<u>67.1</u>
Operating income	17.3	19.1	18.7	6.6	15.5
Non-operating income	5.1	—	(0.1)	1.0	1.4
Stock option program expense	—	—	—	—	—
Income before income taxes	22.4	19.1	18.6	7.6	16.9
Provision for income taxes	<u>2.8</u>	<u>5.3</u>	<u>5.2</u>	<u>2.1</u>	<u>3.9</u>
Net income	<u>19.6%</u>	<u>13.8%</u>	<u>13.4%</u>	<u>5.5%</u>	<u>13.0%</u>

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Compared with Competition

Consolidated statements of income for Oracle for each of the four quarters ended August 31, 1990 are presented below (in millions, except net income per share).

	Nov. 30, 1989	Feb. 28, 1990	May 31, 1990	Aug. 31, 1990	Trailing 12 months
Net revenues	\$224.6	\$236.4	\$334.4	\$203.8	\$999.2
Cost of revenues	<u>35.7</u>	<u>41.6</u>	<u>54.5</u>	<u>57.8</u>	<u>189.6</u>
Gross profit	<u>188.9</u>	<u>194.8</u>	<u>279.9</u>	<u>146.0</u>	<u>809.6</u>
Operating expense:					
Research and development	21.6	21.7	25.4	20.6	89.3
Sales and marketing	108.7	115.8	145.3	150.1	519.9
General and administrative	<u>13.5</u>	<u>16.3</u>	<u>24.6</u>	<u>22.3</u>	<u>76.7</u>
Total operating expenses	<u>143.8</u>	<u>153.8</u>	<u>195.3</u>	<u>193.0</u>	<u>685.9</u>
Operating income	45.1	41.0	84.6	(47.0)	123.7
Non-operating income	(3.2)	(5.3)	(6.7)	(7.5)	(22.7)
Stock option program expense	--	--	--	--	--
Income before income taxes	41.9	35.7	77.9	(54.5)	101.0
Provision for income taxes	<u>13.4</u>	<u>11.4</u>	<u>24.9</u>	<u>(18.5)</u>	<u>31.2</u>
Net income	<u>\$ 28.5</u>	<u>\$ 24.3</u>	<u>\$ 53.0</u>	<u>\$(36.0)</u>	<u>\$ 69.8</u>
Average shares outstanding	<u>136.7</u>	<u>137.1</u>	<u>137.3</u>	<u>131.4</u>	<u>135.6</u>
Net income per share	<u>\$ 0.21</u>	<u>\$ 0.18</u>	<u>\$ 0.39</u>	<u>\$(0.27)</u>	<u>\$ 0.51</u>
Net revenues	100.0%	100.0%	100.0%	100.0%	100.0%
Cost of revenues	<u>15.9</u>	<u>17.6</u>	<u>16.3</u>	<u>28.4</u>	<u>19.0</u>
Gross profit	<u>84.1</u>	<u>82.4</u>	<u>83.7</u>	<u>71.6</u>	<u>81.0</u>
Operating expense:					
Research and development	9.6	9.2	7.6	10.1	8.9
Sales and marketing	48.4	49.0	43.4	73.7	52.0
General and administrative	<u>6.0</u>	<u>6.9</u>	<u>7.4</u>	<u>10.9</u>	<u>7.7</u>
Total operating expenses	<u>64.0</u>	<u>65.1</u>	<u>58.4</u>	<u>94.7</u>	<u>68.6</u>
Operating income	20.1	17.3	25.3	(23.1)	12.4
Non-operating income	(1.4)	(2.2)	(2.0)	(3.7)	(2.3)
Stock option program expense	--	--	--	--	--
Income before income taxes	18.7	15.1	23.3	(26.8)	10.1
Provision for income taxes	<u>6.0</u>	<u>4.8</u>	<u>7.5</u>	<u>(9.1)</u>	<u>3.1</u>
Net income	<u>12.7%</u>	<u>10.3%</u>	<u>15.8%</u>	<u>(17.7)%</u>	<u>7.0%</u>

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Compared with Competition

Consolidated statements of income for Novell for each of the four quarters ended July 28, 1990 are presented below (in millions, except net income per share).

	Oct. 28, 1989	Jan. 27, 1990	Apr. 28, 1990	Jul. 28, 1990	Trailing 12 months
Net revenues	\$111.0	\$105.9	\$120.0	\$131.1	\$468.0
Cost of revenues	<u>36.6</u>	<u>33.9</u>	<u>34.9</u>	<u>32.7</u>	<u>138.1</u>
Gross profit	<u>74.4</u>	<u>72.0</u>	<u>85.1</u>	<u>98.4</u>	<u>329.9</u>
Operating expense:					
Research and development	12.3	12.6	14.1	16.3	55.3
Sales and marketing	32.2	31.1	33.9	37.9	135.1
General and administrative	<u>7.9</u>	<u>6.4</u>	<u>7.0</u>	<u>7.4</u>	<u>28.7</u>
Total operating expenses	<u>52.4</u>	<u>50.1</u>	<u>55.0</u>	<u>61.6</u>	<u>219.1</u>
Operating income	22.0	21.9	30.1	36.8	110.8
Non-operating income	0.7	1.6	2.0	4.0	8.3
Stock option program expense	—	—	—	—	—
Income before income taxes	22.7	23.5	32.1	40.8	119.1
Provision for income taxes	<u>8.4</u>	<u>8.4</u>	<u>11.6</u>	<u>14.7</u>	<u>43.1</u>
Net income	<u>\$ 14.3</u>	<u>\$ 15.1</u>	<u>\$ 20.5</u>	<u>\$ 26.1</u>	<u>\$ 76.0</u>
Average shares outstanding	<u>67.0</u>	<u>67.2</u>	<u>67.4</u>	<u>69.3</u>	<u>67.7</u>
Net income per share	<u>\$ 0.21</u>	<u>\$ 0.23</u>	<u>\$ 0.30</u>	<u>\$ 0.38</u>	<u>\$ 1.12</u>
Net revenues	100.0%	100.0%	100.0%	100.0%	100.0%
Cost of revenues	<u>33.0</u>	<u>32.0</u>	<u>29.1</u>	<u>24.9</u>	<u>29.5</u>
Gross profit	<u>67.0</u>	<u>68.0</u>	<u>70.9</u>	<u>75.1</u>	<u>70.5</u>
Operating expense:					
Research and development	11.1	11.9	11.8	12.4	11.8
Sales and marketing	29.0	29.4	28.2	28.9	28.9
General and administrative	<u>7.1</u>	<u>6.0</u>	<u>5.8</u>	<u>5.7</u>	<u>6.1</u>
Total operating expenses	<u>47.2</u>	<u>47.3</u>	<u>45.8</u>	<u>47.0</u>	<u>46.8</u>
Operating income	19.8	20.7	25.1	28.1	23.7
Non-operating income	0.7	1.5	1.7	3.0	1.7
Stock option program expense	—	—	—	—	—
Income before income taxes	20.5	22.2	26.8	31.1	25.4
Provision for income taxes	<u>7.6</u>	<u>7.9</u>	<u>9.7</u>	<u>11.2</u>	<u>9.2</u>
Net income	<u>12.9%</u>	<u>14.3%</u>	<u>17.1%</u>	<u>19.9%</u>	<u>16.2%</u>

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Compared with Competition

Consolidated statements of financial position for Microsoft, Lotus, Oracle and Novell are presented below (in millions).

	Microsoft Sept. 30, 1990		Lotus Sept. 30, 1990		Oracle Aug. 31, 1990		Novell Jul. 28, 1990	
Current assets:								
Cash and short-term investments	\$ 495.1	41%	\$298.6	43%	\$ 50.2	6%	\$207.0	46%
Accounts receivable - net	177.6	15	118.5	17	394.7	51	119.1	27
Inventories	58.4	5	22.5	3	-	-	13.5	3
Other	39.7	3	17.4	3	76.4	10	18.5	4
Total current assets	770.8	64	457.0	66	521.3	67	358.1	80
Property, plant and equipment - net	376.8	31	140.0	20	203.9	26	76.3	17
Other assets	55.9	5	97.9	14	53.9	7	15.1	3
TOTAL	\$1,203.5	100%	\$694.9	100%	\$779.1	100%	\$449.5	100%
Current liabilities	\$ 213.1	18%	\$161.7	23%	\$244.4	31%	\$ 80.8	18%
Long-term liabilities	-	-	183.8	27	176.0	23	54.9	12
Stockholders' equity	990.4	82	349.4	50	358.7	46	313.8	70
TOTAL	\$1,203.5	100%	\$694.9	100%	\$779.1	100%	\$449.5	100%

Selected market statistics for Microsoft, Lotus, Oracle, and Novell are presented below.

	Microsoft		Lotus		Oracle		Novell	
	1990	1989	1990	1989	1990	1989	1990	1989
Closing Stock Price (Sept. 30)	\$63.00	\$34.25	\$15.50	\$28.50	\$6.50	\$23.63	\$24.75	\$14.38
Common Shares Outstanding (in millions)	113.7	110.0	42.4	41.0	131.6	127.0	70.3	66.0
Market Value (in millions)	\$7,163	\$3,768	\$657	\$1,169	\$855	\$3,001	\$1,740	\$949
Trailing Twelve Months Revenues (in millions)	\$1,318	\$862	\$648	\$518	\$999	\$669	\$468	\$417
Price/Revenues Ratio	5.4x	4.4x	1.0x	2.3x	0.9x	4.5x	3.7x	2.3x
Trailing Twelve Months EPS	\$2.61	\$1.62	\$1.95	\$1.12	\$0.51	\$0.64	\$1.12	\$0.63
Price/Earnings Ratio	24.1x	21.1x	7.9x	25.4x	12.7x	36.9x	22.1x	22.8x
Cash (in millions)	\$495	\$336	\$299	\$222	\$50	\$42	\$207	\$128
Cash per Share	\$4.35	\$3.05	\$7.05	\$5.41	\$0.38	\$0.33	\$2.94	\$1.94
Price/Cash Ratio	14.5x	11.2x	2.2x	5.3x	17.1x	71.5x	8.4x	7.4x
Book Value (in millions)	\$990	\$625	\$349	\$244	\$359	\$245	\$314	\$219
Book Value per Share	\$8.71	\$5.68	\$8.23	\$5.95	\$2.73	\$1.93	\$4.47	\$3.32
Price/Book Value Ratio	7.2x	6.0x	1.9x	4.8x	2.4x	12.2x	5.5x	4.3x

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RESULTS OF OPERATIONS COMPARED WITH PLAN

Consolidated statements of income compared with plan are presented below for the three months ended September 30, 1990 (in millions, except net income per share).

	Actual Q91-1		Plan Q91-1		Variance Percentage
Net revenues	\$369.4	100.0%	\$304.5	100.0%	21
Cost of revenues	<u>76.0</u>	<u>20.6</u>	<u>62.5</u>	<u>20.5</u>	22
Gross profit	<u>293.4</u>	<u>79.4</u>	<u>242.0</u>	<u>79.5</u>	21
Operating expense:					
Research and development	50.8	13.7	61.1	20.0	(17)
Sales and marketing	106.7	28.9	111.7	36.8	(4)
General and administrative	<u>12.9</u>	<u>3.5</u>	<u>11.4</u>	<u>3.7</u>	13
Total operating expenses	<u>170.4</u>	<u>46.1</u>	<u>184.2</u>	<u>60.5</u>	(7)
Operating income	123.0	33.3	57.8	19.0	113
Non-operating income	5.5	1.5	6.3	2.1	(13)
Stock option program expense	<u>(1.5)</u>	<u>(0.4)</u>	<u>(2.0)</u>	<u>(0.7)</u>	(25)
Income before income taxes	127.0	34.4	62.1	20.4	105
Provision for income taxes	<u>39.4</u>	<u>10.7</u>	<u>19.2</u>	<u>6.3</u>	105
Net Income	\$ <u>87.6</u>	<u>23.7%</u>	\$ <u>42.9</u>	<u>14.1%</u>	104
Average shares outstanding	<u>123.3</u>		<u>124.5</u>		(1)
Net income per share	\$ <u>0.71</u>		\$ <u>0.34</u>		109

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Q91-1 versus Plan

Net revenues for Q91-1 at \$369.4 million were 21% above plan of \$304.5 million. Buoyed by sales of Win 3 and Win Apps, worldwide retail was very strong, whereas conservative reserves brought worldwide OEM in short of plan by \$5.6 million. The OEM shortfall results from a \$7.5 million increase in our reserve for prepaid balances. This reserve totalled \$18.0 million at quarter end. OEM was further adversely affected by a \$1.9 million accrual relating to a pending amendment of our contract with 3Com. The following is a breakdown of net revenues by channel of distribution and product group (in millions).

Channel	Actual Q91-1		Plan Q91-1		Variance %
	Actual	Plan	Actual	Plan	
USSMD	\$128.1	34.7	\$101.7	33.4%	26
International Finished Goods	<u>165.0</u>	<u>44.7</u>	<u>119.1</u>	<u>39.1</u>	39
Worldwide Retail	<u>293.1</u>	<u>79.4</u>	<u>220.8</u>	<u>72.5</u>	33
Domestic OEM	29.7	8.0	35.1	11.5	(15)
International OEM	<u>38.0</u>	<u>10.3</u>	<u>38.2</u>	<u>12.6</u>	(1)
Worldwide OEM	<u>67.7</u>	<u>18.3</u>	<u>73.3</u>	<u>24.1</u>	(8)
Other	8.6	2.3	10.4	3.4	(17)
Total	<u>\$369.4</u>	<u>100.0</u>	<u>\$304.5</u>	<u>100.0%</u>	21
Product Group					
Applications	\$177.9	48.2	\$146.0	48.0%	22
Systems	116.4	31.5	101.2	33.2	15
SPAG	49.2	13.3	27.4	9.0	80
Languages	14.7	4.0	12.0	3.9	23
Network	4.8	1.3	5.0	1.7	(4)
Other	<u>6.4</u>	<u>1.7</u>	<u>12.9</u>	<u>4.2</u>	(50)
Total	<u>\$369.4</u>	<u>100.0%</u>	<u>\$304.5</u>	<u>100.0%</u>	21

The Company's leading products for Q91-1 (compared with plan) were as follows (units in thousands, revenue in millions):

Actual	Plan	Product	Actual Q91-1		Plan Q91-1		Revenue Variance %
			Units	Revenue	Units	Revenue	
1	1	DOS/GW Basic	3,920.5	\$ 60.9	4,256.4	\$59.6	2
2	4	Serial/Bus Mouse	491.0	46.3	342.5	26.4	75
3	2	Win Excel	121.6	33.5	106.9	27.3	23
4	5	Win Word	122.5	29.9	78.1	19.7	52
5	6	Win 3	335.8	28.7	203.2	17.0	69
6	3	PC Word	97.6	28.2	105.3	26.5	6
7	7	PC Works	216.8	15.2	331.1	13.2	15
8	8	Mac Word	75.3	13.4	70.6	12.6	6
9	9	Mac Excel	49.7	10.8	57.5	11.9	(10)
10	11	Pro C	46.3	6.6	20.9	5.1	29
11	-	Win Project	14.8	6.0	7.0	2.6	131
12	10	Mac Office	10.9	5.0	11.9	5.2	(4)
13	15	PC Multiplan	36.1	4.4	16.5	3.1	42
14	-	Win PowerPoint	15.2	3.9	13.8	2.9	34
15	12	Mac Works	27.0	3.8	31.4	4.3	(12)
				<u>\$296.6</u>		<u>\$237.4</u>	

Percent of net revenues

80%

78%

Plan: #13 Win 286 (\$3.7 million); #14 OS/2 (\$3.5 million)

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Q91-1 versus Plan

The five products with the largest Q91-1 revenue shortfalls relative to plan were as follows (units in thousands, revenue in millions):

	Actual Q91-1		Plan Q91-1		Revenue Shortfall
	Units	Revenue	Units	Revenue	
Win 386	79.3	\$ 0.8	150.1	\$ 2.5	\$1.7
OS/2	47.5	1.8	44.4	3.5	1.7
PM Excel	3.8	1.2	7.2	2.3	1.1
Mac Excel	49.7	10.8	57.5	11.9	1.1
PC Flight Simulator	38.0	1.3	68.0	2.3	1.0

Actual cost of revenues for Q91-1 was 20.6% of net revenues compared with a plan of 20.5%. The Q91-1 product cost percentage for each channel of distribution and each product group (actual and plan) is shown in the following table:

Channel	Actual Q91-1			Plan Q91-1		
	Gross Sales Mix	Cost %	Weighted Cost %	Gross Sales Mix	Cost %	Weighted Cost %
USSMD	35.0%	17.9	6.3%	34.6%	17.2	5.9%
Int'l Finished Goods	43.2	18.0	7.8	38.6	17.5	6.7
US OEM	10.1	6.9	0.7	11.2	2.9	0.3
Int'l OEM	9.4	-	-	12.2	-	-
Other	3.2	15.2	0.3	3.4	17.6	0.6
Product cost - gross	<u>100.0%</u>		15.1	<u>100.0%</u>		13.5
Effect of revenue adjustments			x1.045			x1.024
Product cost - net			15.8			13.8
Manufacturing variances			-			0.9
Inventory adjustments			1.1			1.5
Freight, shipping and other			2.8			3.1
Royalties			0.9			1.2
Non-product costs			4.8			6.7
Total			<u>20.6%</u>			<u>20.5%</u>

Product Group	Actual Q91-1			Plan Q91-1		
	Gross Sales Mix	Cost %	Weighted Cost %	Gross Sales Mix	Cost %	Weighted Cost %
Applications	47.5%	12.2	5.8%	48.3%	11.9	5.7%
Systems	30.2	11.2	3.4	32.7	9.6	3.1
SPAG	13.1	36.2	4.7	9.2	37.1	3.4
Languages	4.0	18.7	0.7	4.0	17.3	0.7
Other (includes UPB)	5.2	9.6	0.5	5.8	10.3	0.6
Product cost - gross	<u>100.0%</u>		15.1%	<u>100.0%</u>		13.5%

Product costs as a percentage of net revenues were 15.8% compared with a plan of 13.8%. Relative to plan, both primary sales mix factors (retail vs. OEM and hardware vs. software) pushed the composite product cost percentage higher. Specifically, worldwide retail revenue was 78.2% of gross revenue compared with plan of 73.2%, while hardware revenue was 13.1% of gross revenue compared with plan of 9.2%. On an individual product group basis, SPAG was under plan (36.2% vs. 37.1%), Applications was essentially on plan (12.2% vs. 11.9%), while Systems (11.2% vs. 9.6%) and Languages (18.7% vs. 17.3%) were over plan. The difference in Systems' results from the shift in sales mix from OEM to retail (worldwide retail accounted for 50% of Systems' revenue compared with a plan of only 39%). The difference in Languages occurred in the International Finished Goods channel.

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Q91-1 versus Plan

Non-product costs included in cost of revenues were 4.8% of revenues compared with plan of 6.7%. For Q91-1, actual results were lower than plan in all categories -- 0.9% in manufacturing variance, 0.4% in inventory adjustments, 0.3% in freight, shipping and other, and 0.3% in royalties. It should be noted that the planned manufacturing variance (0.9% of net revenues) was an allowance in International Finished Goods in the event lower than planned MLP sales skewed product costs upward relative to sales.

Operating expenses for Q91-1 at \$170.4 million were 7% below plan of \$184.2 million, and as a percentage of net revenues were 46.1% compared with plan of 60.5%. Operating expenses for Q91-1 include an unbudgeted addition to our litigation reserve of \$2.7 million and an unbudgeted US Windows Computing marketing accrual of \$2.5 million. This marketing accrual is in addition to our normal quarter-end accrual of budgeted, unspent marketing, which totalled \$3.9 million. The operating expense line items with the largest variances were as follows (in millions):

	Actual	Plan	Variance	%
Payroll	\$ 61.5	\$ 65.6	\$ 4.1	6
Marketing	23.8	27.7	3.9	14
Marketing accrual	6.4	--	(6.4)	--
Outside product development	5.6	9.4	3.8	40
Supplies and equipment	7.8	10.9	3.1	28
Travel and entertainment	6.4	9.4	3.0	32
All other	<u>58.9</u>	<u>61.2</u>	<u>2.3</u>	4
	<u>\$170.4</u>	<u>\$184.2</u>	<u>\$13.8</u>	7

Non-operating income for Q91-1 was \$5.5 million compared with a plan of \$6.3 million. The unfavorable variance results from an unbudgeted addition to our allowance for non-performing investments of \$1.7 million (see page 18), partially offset by foreign currency transaction gains of \$0.9 million. Non-operating (expense) is composed of (in millions):

	Actual	Plan	Variance
Investment income	\$9.1	\$9.5	\$(0.4)
Allowance for NPIs	(2.9)	(1.2)	(1.7)
Interest expense	(0.7)	(1.1)	0.4
Foreign currency transactions	0.9	--	0.9
SCO amortization	(0.5)	(0.5)	--
All other	<u>(0.4)</u>	<u>(0.4)</u>	--
	<u>\$5.5</u>	<u>\$6.3</u>	<u>\$(0.8)</u>

Stock option program expense - see discussion on page 4.

The tax rate for Q91-1 was 31.0%, the same as plan.

Net income for Q91-1 was \$87.6 million compared with a plan of \$42.9 million. Net income as a percentage of net revenues was 23.7% compared with a plan of only 14.1%.

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FINANCIAL CONDITION - Q91-1 VERSUS Q90-1

Consolidated balance sheets as of September 30, 1990 and June 30, 1990 and consolidated statements of cash flows for Q91-1 and Q90-1 are presented below (in millions).

	Sept. 30 1990	June 30 1990	Quarter Change	Quarter % Change
Current assets:				
Cash and short-term investments	\$ 495.1	\$ 449.2	\$45.9	10
Accounts receivables - net	177.6	181.0	(3.4)	(2)
Inventories	58.4	55.6	2.8	5
Other	<u>39.7</u>	<u>34.1</u>	<u>5.6</u>	16
Total current assets	770.8	719.9	50.9	7
Property, plant and equipment - net	376.8	325.4	51.4	16
Other assets	<u>55.9</u>	<u>60.0</u>	<u>(4.1)</u>	(7)
Total assets	<u>\$1,203.5</u>	<u>\$1,105.3</u>	<u>\$98.2</u>	9
Current liabilities:				
Accounts payable	\$ 66.5	\$ 51.0	\$15.5	30
Customer deposits	7.1	17.2	(10.1)	(59)
Accrued compensation	27.8	28.8	(1.0)	(3)
Notes payable	10.0	6.5	3.5	54
Income taxes payable	58.2	42.6	15.6	37
Other	<u>43.5</u>	<u>40.7</u>	<u>2.8</u>	7
Total current liabilities	<u>213.1</u>	<u>186.8</u>	<u>26.3</u>	14
Stockholders' equity:				
Common stock and paid-in capital	242.7	219.5	23.2	11
Retained earnings	732.8	688.9	43.9	6
Translation adjustment	<u>14.9</u>	<u>10.1</u>	<u>4.8</u>	48
Total stockholders' equity	<u>990.4</u>	<u>918.5</u>	<u>71.9</u>	8
Total liability & equity	<u>\$1,203.5</u>	<u>\$1,105.3</u>	<u>\$98.2</u>	9
		Q91-1	Q90-1	
Cash flows from operations				
Net income		\$ 87.6	\$ 49.6	
Depreciation and amortization		13.0	9.5	
Current liabilities, excluding notes payable		22.8	23.7	
Accounts receivable		3.4	(19.2)	
Inventories		(2.8)	1.8	
Other current assets		(5.6)	(4.8)	
Translation adjustment		<u>4.8</u>	<u>(2.0)</u>	
Net cash from operations		<u>123.2</u>	<u>58.6</u>	
Cash flows used for financing				
Notes payable		3.5	2.1	
Common stock issued		18.2	10.8	
Common stock repurchased and retired		(45.1)	-	
Income tax benefits related to stock options		<u>6.4</u>	<u>4.4</u>	
Net cash used for financing		<u>(17.0)</u>	<u>17.3</u>	
Cash flows used for investments				
Additions to property, plant and equipment		(61.9)	(40.4)	
Acquisition of intellectual property rights		-	(0.8)	
Other		<u>1.6</u>	<u>1.0</u>	
Net cash used for investments		<u>(60.3)</u>	<u>(40.2)</u>	
Net change in cash and short-term investments		45.9	35.7	
Cash and short-term investments at beginning of period		<u>449.2</u>	<u>300.8</u>	
Cash and short-term investments at end of period		<u>\$495.1</u>	<u>\$336.5</u>	

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Financial Condition

The Company's measures of financial strength and rate of return indicators are shown in the following tables. Each measure established a highwater mark in Q91-1, and each rate of return indicator was very respectable in comparison with prior quarters.

MEASURES OF FINANCIAL STRENGTH (in millions)

	Q91-1	Q90-4	Q90-3	Q90-2
Cash from operations	\$ 123.2	\$ 59.5	\$ 95.1	\$ 71.1
Cash and short-term investments	495.1	449.2	446.6	380.1
Working capital	557.7	533.1	490.4	422.8
Total assets	1,203.5	1,105.3	1,015.3	921.8
Stockholders' equity	990.4	918.5	826.2	731.8

RATE OF RETURN INDICATORS (annualized)

	Q91-1	Q90-4	Q90-3	Q90-2
Return On:				
Equity (average)	36.7%	36.7%	38.6%	43.9%
Assets (average)	30.4%	30.2%	31.0%	34.4%
Non-cash equity (average)	72.7%	75.3%	82.2%	93.1%
Non-cash assets (average)	51.4%	52.2%	54.2%	58.7%
Net revenues	23.7%	23.7%	24.2%	24.8%

As shown in the statement of cash flows on page 15, net income plus non-cash depreciation and amortization (\$100.6 million), plus net changes in operating assets and liabilities (\$22.6 million), resulted in net cash from operations of \$123.2 million. As a frame of reference, net cash from operations for all of FY90 totalled \$278.3 million. And by all accounts, FY90 was a very good year. The exceptional Q91-1 result is attributable to strong earnings, excellent collection of receivables, minimal increase in inventories, and an increase in current liabilities resulting largely from additions to reserves and the absence of a U.S. federal tax payment (\$5 million paid mid October).

In terms of what became of this \$123.2 million cash from operations, \$17.0 million (net) was used for financing, \$60.3 million was used for long-term investments (primarily property, plant, and equipment -- see page 32), and \$45.9 million was retained in cash and short-term investments. Net cash used for financing of \$17.0 million consists of \$45.1 million expended on the stock buyback program, less stock option exercise proceeds and related tax benefits of \$24.6 million and an increase in notes payable of \$3.5 million.

Stock Buyback Program: Under the Company's stock buyback program, repurchases are made during a window that begins three days after we have released earnings and extends through the Friday of the last week in the second month in the quarter. Repurchases are made on our behalf by Goldman Sachs at our direction and their discretion. In our instructions to Goldman we reserve the right to suspend repurchases under the program during the window period. During Q91-1, we repurchased 724,000 shares at an average price of \$62.24 per share for a total of \$45.1 million.

Week	Our Average	Market Average	Number of Shares
7/31-8/3	\$65.71	\$65.63	206,000
8/6-8/10	62.08	62.92	165,000
8/13-8/17	63.61	62.60	135,000
8/20-8/24	56.22	54.50	117,500
8/27-8/31	60.98	61.13	<u>100,500</u>
Total	62.29	62.02	<u>724,000</u>

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Cash and Short-Term Investments

Cash and short-term investments increased \$45.9 million in Q91-1. These liquid assets comprise 64.2% of current assets and 41.1% of total assets, compared with 62.4% and 40.6% at June 30, 1990. At September 30, 1990, the portfolio was in compliance with all investment guidelines, and 87% of the portfolio was in investment-grade securities. As of quarter end, the average maturity of the portfolio was 153 days compared with 138 days at the end of the prior quarter, and the portfolio consisted of the security types listed below (in millions):

	Domestic	International	Total	Percent 9/30/90	Percent 6/30/90
Commercial paper	\$ 1.9	\$ 9.9	\$ 11.8	2.4%	—%
Bank loan participations	5.2	49.8	55.0	11.1	17.6
Floating rate notes (FRNs)	—	11.0	11.0	2.2	1.1
Corporate bonds	11.3	18.5	29.8	6.0	4.9
Increasing rate notes (IRNs)	—	—	—	—	0.4
Auction preferred stock (APSs)	10.0	—	10.0	2.0	6.2
Money market preferred	106.4	—	106.4	21.5	23.5
Fixed adjustable rate preferred (FARPs)	26.1	—	26.1	5.3	6.4
Tax exempt municipals	<u>188.1</u>	—	<u>188.1</u>	<u>38.0</u>	<u>33.5</u>
Investment portfolio	349.0	89.2	438.2	88.5	93.6
Cash and money market funds	<u>4.2</u>	<u>52.7</u>	<u>56.9</u>	<u>11.5</u>	<u>6.4</u>
TOTAL	<u>\$353.2</u>	<u>\$141.9</u>	<u>\$495.1</u>	<u>100.0%</u>	<u>100.0%</u>
Yield*	10.4%	8.8%	10.1%		

* "Yield" represents the weighted average yield to maturity of investments in the portfolio on a pre-tax equivalent basis. The domestic yield is greater than the international yield because the international portfolio cannot invest in U.S. tax-advantaged securities.

Short-term interest rates continued to decline during Q91-1, falling approximately 50 basis points (half of 1%). Yield on the portfolio dropped slightly in tandem with the falling rates. Our diversified investment strategy generates significant incremental yield, particularly from the tax-advantaged securities. The following table estimates pre-tax equivalent investment income during Q91-1 on various security types compared to alternative investment strategies had we invested the portfolio assets in 90-Day LIBOR, 90-Day T-Bills or Overnight Repos (in millions):

	90-Day Libor	90-Day T-Bill	Overnight Repo	Actual
Taxable paper, notes & bonds	\$2.5	\$2.3	\$2.2	\$ 4.1
Money market preferreds	2.8	2.6	2.5	2.7
Municipal securities	<u>3.5</u>	<u>3.3</u>	<u>3.1</u>	<u>4.6</u>
Total estimated income (pre-tax)	<u>\$8.8</u>	<u>\$8.2</u>	<u>\$7.8</u>	11.4
Tax effect				(2.3)
Investment income - net				<u>\$ 9.1</u>

Foreign Cash Balances

At September 30, 1990, the sales subsidiaries held most of the \$52.7 million "cash and money market funds" shown above in offshore locations, up from \$44.7 million at the beginning of the quarter. These balances are invested by the local controllers in overnight paper and other investments in their local jurisdictions pursuant to guidelines provided by the Treasury department. Owing principally to income tax restrictions on repatriation of foreign earnings and our present transfer pricing matrix, our subsidiaries have and will likely continue to build structural cash balances during each year. These balances are minimized as

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much as practical through dividend repatriation strategies and the transfer pricing matrix. To increase yields earned on these balances, MS Treasury plans to centralize excess foreign currency denominated cash balances of European subsidiaries with a single bank to obtain investment economies.

Non-Performing Investments

Changes in the balances of Non-Performing Investments and the related valuation reserve during Q91-1 are summarized below (in millions):

	Non-Performing Investments	Reserve	Reserve %
Beginning balance (6/30/90)	\$10.2	\$3.1	30.4%
Additions/provisions	1.7	2.9	
Collections/write-offs	<u> </u>	<u> </u>	
Ending balance (9/30/90)	<u>\$11.9</u>	<u>\$6.0</u>	50.4%

Uniroyal defaulted on an interest payment due August 1, 1990. During the quarter, we reclassified this \$1.7 million IRN from the IBV portfolio to Non-Performing Investments. This reclassification increased the balance in Non-Performing Investments from \$10.2 million to \$11.9 million. There are no further increasing rate notes in our portfolio.

During Q91-1, the balance in the reserve for Non-Performing Investments was increased by \$2.9 million to a balance of \$6.0 million. Of this \$2.9 million increase, \$1.2 million was budgeted and \$1.7 million was unbudgeted. There were no collections or write-offs during the quarter. MS Treasury considers the reserve adequate.

In addition to Uniroyal, our Non-Performing Investments at September 30, 1990 include the following:

Lomas Financial Floating Rate Notes (\$5 million). Lomas is in Chapter 11, and a reorganization plan is due to be filed. We received a recent quote of 55 cents on the dollar for this issue. There has been limited trading activity at this level. MS Treasury believes there is long-term value in this paper.

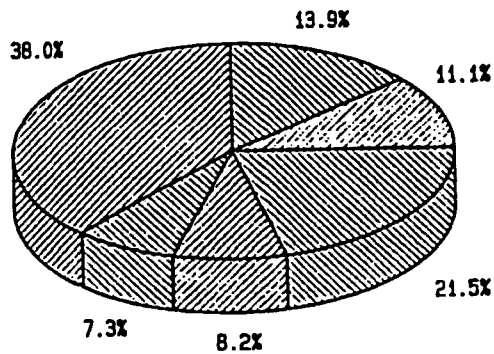
Easco (\$1.2 million). These notes were restructured in May 1990. We received a recent quote in the low 30 cents on the dollar range.

Black Box IRNs (\$2 million). During Q91-1, Black Box was scheduled to come to market with a Restructure/IPO underwritten by Alex. Brown. The issue failed due to the Iraq/Kuwait crisis. We received a recent quote in the range of 28 cents on the dollar.

Heileman Brewing (\$2 million). Heileman continues to experience difficulties. Chapter 11 is rumored. Available quotes are for nominal values.

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**Investment Portfolio
September 30, 1990**



- Cash/
Money Markets/
Repos
- Bank Loan
Participations
- Money Market
Preferreds
- Corporate
Bonds/FRNs
- FARPs/APSs
- Municipal
Securities

**Total Investments
(in Millions)**

Domestic	\$353.2	71.3 %
International	141.9	28.7
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	\$495.1	100.0 %

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As of Date: 09/30/90

QUARTERLY PORTFOLIO SUMMARY EXCLUDING CASH

SECURITY DESCRIPTION	NEXT RED DATE	MATURITY DATE	% PORTFOLIO (AT COST)	COST BASIS	YIELD	PRE-TAX YIELD	MOODY RATING	S & P RATING
Portfolio: Company 10								
Investment Type: Auct Pref Stock								
Bet Plc A Auction Preferred Stock	10/03/90	10/03/90	0.86X	3,000,000	7.78	9.15	A2	A
English China Clays Plc D Auction Pfd	10/17/90	10/17/90	0.86X	3,000,000	8.20	9.65	A3	A
Redland Plc Series D Auction Pfd Stock	10/09/90	10/09/90	1.15X	4,000,000	7.62	8.97	A2	A
			2.87X	10,000,000	7.84	9.23		
Investment Type: Commercl Paper								
Circus Circus Cp	10/01/90	10/01/90	0.57X	1,976,150	8.50	8.50	NR	A-2
			0.57X	1,976,150	8.50	8.50		
Investment Type: Corporate Bond								
Commonwealth Edison 11.75% Corp Bond	09/01/15	09/01/15	1.26X	4,391,120	10.62	10.62	Baa1	BBB
Philadelphia Electric 11.75% 11/15/2014	11/15/90	11/15/14	0.79X	2,763,560	5.43	5.43	NR	A-
South Central Bell Tel 10.375% 12/30/25	12/30/90	12/30/25	0.31X	1,087,500	8.50	8.50	Aaa	AAA
Texas Utilities Elec Co 11.125% 12/1/15	12/01/90	12/01/15	0.62X	2,159,400	8.50	8.50	Baa1	BBB+
US Gypsum Corp 7.375% 12/15/91	12/15/91	12/15/91	0.26X	896,430	8.50	8.50	B3	B+
			3.24X	11,298,010	8.57	8.57		
Investment Type: Fxd Auc Rte Pfd								
Alcoa Int'l B 8.625X (Strap) FARP			0.30X	1,040,000	8.63	11.74	Baa1	A-
Citicorp Pfd Series 8A 8.50%			0.43X	1,500,000	8.50	11.57	A3	A
Citicorp Pfd Series 8B 8.75%			0.57X	2,000,000	8.75	11.91	A3	A
First Interstate Bank Ser C 9.875X FARP			4.28X	14,940,750	9.88	13.44	Baa1	BBB
Mellon Bank Corp Ser G 9.50X FARP			1.81X	6,306,938	9.50	12.93	Baa2	BBB
Talman Finance Corp Series H 7.87%			0.09X	303,000	7.87	10.71	Aaa	AAA
			7.48X	26,090,688	9.55	12.99		
Investment Type: Loan Partic								
Cummins Engine LP	10/01/90	10/01/90	0.63X	2,200,000	8.50	8.50	Ba1	BB+
JR Simplot LP	10/05/90	10/05/90	0.86X	3,000,000	8.43	8.43	NR	NR
			1.49X	5,200,000	8.46	8.46		

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As of Date: 09/30/90

QUARTERLY PORTFOLIO SUMMARY EXCLUDING CASH

SECURITY DESCRIPTION	NEXT RED DATE	MATURITY DATE	% PORTFOLIO (AT COST)	COST BASIS	YIELD	PRE-TAX YIELD	MOODY RATING	S & P RATING
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Portfolio: Company 10

- cont.

Investment Type: Money Mkt Pref

Bankers Trust NY Corp Series H MHP	10/15/90	10/15/90	1.15X	4,000,000	6.51	8.86	A1	A+
Central Power & Light A MHP	10/09/90	10/09/90	1.15X	4,000,000	6.55	8.91	A3	BBB+
Central Power & Light IIB MHP	11/14/90	11/14/90	0.86X	3,000,000	7.47	10.17	A3	BBB+
Citizens & Southern Mtl Bk Series B MHP	11/01/90	11/01/90	0.86X	3,000,000	7.12	9.69	A2	A-
Citicorp Ser 5B Money Market Preferred	11/01/90	11/01/90	0.86X	3,000,000	6.83	9.29	A3	A
Citicorp Ser 6A Money Market Preferred	10/22/90	10/22/90	0.86X	3,000,000	6.55	8.91	A3	A
Citicorp F Remarketed MHP	10/29/90	10/29/90	1.15X	4,000,000	6.58	8.95	A3	A
Connecticut Light & Power MHP	10/24/90	10/24/90	1.15X	4,000,000	6.73	9.15	Baa1	BBB
Duff & Phelps A MHP	10/10/90	10/10/90	1.43X	5,000,000	6.31	8.58	Aaa	AAA
GTE Corp A MHP	11/05/90	11/05/90	0.57X	2,000,000	7.78	10.58	A3	A-
GTE Corp D MHP	10/29/90	10/29/90	0.86X	3,000,000	6.76	9.20	A3	A-
Heller Finance - B Money Market Pfd	11/05/90	11/05/90	0.86X	3,000,000	7.48	10.18	A3	A-
Heller Finance - A Money Market Pfd	10/22/90	10/22/90	0.57X	2,000,000	6.77	9.21	A3	A-
Merrill Lynch RP B Money Market Pfd	10/24/90	10/24/90	0.57X	2,000,000	7.46	10.15	A2	BBB+
Merrill Lynch RP E Money Market Pfd	11/13/90	11/13/90	1.72X	6,000,000	8.29	11.28	A2	BBB+
Morgan Stanley - C MHP	10/24/90	10/24/90	0.57X	2,000,000	6.51	8.86	A1	A-
Morgan Stanley - D Money Market Pfd	10/31/90	10/31/90	1.43X	5,000,000	7.06	9.60	A1	A-
Patriot Select Dividend Trust Ser A MHP	11/14/90	11/14/90	1.29X	4,500,000	6.46	8.79	Aa2	AA
Puget Sound Power & Light Ser A MHP	10/01/90	10/01/90	1.15X	4,000,000	6.10	8.30	Baa1	BBB+
Puget Sound Power & Light Ser B MHP	10/29/90	10/29/90	1.72X	6,000,000	6.60	8.98	Baa1	BBB+
Sara Lee Series F MHP	11/14/90	11/14/90	0.86X	3,000,000	6.75	9.18	A2	A+
Security Pacific MHP	11/13/90	11/13/90	1.43X	5,000,000	7.19	9.79	A1	A+
Smith Kline Beecham MHP	10/22/90	10/22/90	0.86X	3,000,000	6.45	8.78	Aa3	A+
Tucson Electric Power A MHP	10/29/90	10/29/90	2.98X	10,400,000	11.91	16.21	E2	B+
Texas Instruments C-1 Money Market Pfd	11/01/90	11/01/90	0.86X	3,000,000	7.08	9.63	A3	A+
Texas Instruments C-2 Money Market Pfd	11/08/90	11/08/90	0.86X	3,000,000	7.73	10.52	A3	A+
Ultramar Equities Ltd MHP	10/01/90	10/01/90	0.86X	3,000,000	6.10	8.29	Aaa	AAA
Union Bk MHP	10/30/90	10/30/90	1.00X	3,500,000	6.45	8.77	A1	A
			30.48X	106,400,000	7.36	10.02		

Investment Type: Municipal Sec

Alvin Texas GO 4.8X 5/1/92	05/01/92	05/01/92	0.05X	191,780	7.59	11.51	A	A
BayShore NY SchoolDist TAN 6.35 6/27/91	06/27/91	06/27/91	0.57X	2,006,020	5.86	8.89	NR	NR
Beaufort CO HC Tx Gulf PCR 12/1/00 VRDM	12/01/00	12/01/00	0.29X	1,000,000	6.08	9.20	Aaa	NR
Beaverton School Dist TANS 6.25 6/28/91	06/28/91	06/28/91	0.57X	2,005,160	5.80	8.79	MIG1	SP-1+
Berks Cnty PA Rilsan Ser 84 12/1/4 VRDM	12/01/04	12/01/04	0.29X	1,000,000	6.20	9.39	NR	AAA
Cape May Cty NJ Utility Auth 6.1 7/1/15	07/01/91	07/01/15	1.43X	5,000,000	6.08	9.22	Aaa	A-1
Chester City PA RES REC REV 6.25 8/1/21	08/01/91	08/01/21	2.21X	7,698,218	10.75	16.29	NR	SP-1+
Chicago Peoples Gas 5.8X 3/1/15	03/01/91	03/01/15	0.43X	1,484,805	8.26	12.52	Aa3	AA-
Chicago Illinois Ser C 5.75X 10/31/90	10/31/90	10/31/90	0.16X	565,065	8.50	12.88	NR	AAA
Chittanooga KY SchDist BAN 6.62 6/28/91	06/28/91	06/28/91	0.58X	2,007,740	6.00	9.09	A	NR
Clayton Cty GA Sch Dist TAN 12/31/90	12/31/90	12/31/90	1.01X	3,508,470	5.52	8.36	A1	AA-
Colorado Housing Fin Auth 6.15X 3/1/16	03/01/91	03/01/16	0.52X	1,800,000	6.12	9.27	NR	NR
Cypress-Fairbanks TX 5X 2/1/92	02/01/92	02/01/92	0.13X	438,579	7.89	11.96	NR	A
Deer Park TX 5X 2/1/92 Indpt School Dst	02/01/92	02/01/92	0.10X	339,392	7.62	11.55	Aa1	AA

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QUARTERLY PORTFOLIO SUMMARY EXCLUDING CASH

As of Date: 09/30/90

SECURITY DESCRIPTION	NEXT RED DATE	MATURITY DATE	% PORTFOLIO (AT COST)	COST BASIS	YIELD	PRE-TAX YIELD	MOODY RATING	S & P RATING
- cont.								
Portfolio: Company 10								
- cont.								
Investment Type: Municipal Sec								
Delaware Econ Auth 7.25X 11/1/24 IDRB	11/01/90	11/01/24	0.09X	300,000	7.04	10.66	Ba2	NR
Sondolier Farms Metro 7.95X 9/1/91 BAA	09/01/91	09/01/91	0.29X	1,000,000	7.94	12.03	NR	NR
East Central TX GO 5X 5/15/92	05/15/92	05/15/92	0.08X	264,699	7.49	11.34	NR	A
East St Louis MFHSG 6.75X 12/15/20	12/15/90	12/15/20	0.57X	1,977,600	12.02	18.22	NR	SP-1+
East St Louis Port Fac 6.375X 12/15/20	12/15/90	12/15/20	2.25X	7,860,494	9.71	14.71	NR	SP-1+
East St Louis Res Rec 6.375X 12/15/20	12/15/90	12/15/20	0.50X	1,762,493	8.50	12.88	NR	A-1+
Erie Cty NY BAA 6.35X 7/25/91	07/25/91	07/25/91	0.28X	978,110	5.87	8.90	HIG1	NR
Forsythe County Montana 6.2X	01/01/91	01/01/14	0.57X	2,000,000	6.59	9.99	A1	AA
Galveston County TX 5.4X 7/10/1991	07/10/91	07/10/91	0.08X	278,682	8.39	12.70	Baa	NR
Galveston TX Ser B 7.6X 5/1/93	05/01/93	05/01/93	0.28X	985,969	7.11	10.78	Baa	BBB+
Gilford NH GTD TANS 7.4X 12/27/90	12/27/90	12/27/90	0.29X	1,002,530	6.14	9.31	NR	NR
Hampden NH TANS 7.6X 12/27/90	12/27/90	12/27/90	0.57X	2,005,020	6.35	9.62	NR	NR
Motykoe MA BANS 6.78X 11/2/90	11/02/90	11/02/90	1.51X	5,270,752	5.26	7.96	Baa	NR
Idaho School Bd Assn 6.2X 7/11/91	07/11/91	07/11/91	0.57X	2,000,000	6.12	9.27	NR	SP-1+
Independence Cnty AR PCR 9.5X 7/1/12	07/01/91	07/01/12	0.92X	3,200,308	7.46	11.31	Ba3	B
Iowa School Corp 6.55X 12/30/91	12/30/91	12/30/91	1.15X	4,000,000	6.54	9.90	NR	SP-1+
Jacksonville FL 5.1X 4/1/91	04/01/91	04/01/91	0.31X	1,075,459	9.75	14.78	NR	AAA
Jefferson Cnty CO IDR 7.625X 11/1/15	11/01/90	11/01/15	0.17X	601,050	5.41	8.20	NR	A-2
Kentucky HSG Corp 5.9X 7/1/2013	01/01/91	01/01/91	0.15X	533,280	8.50	12.88	NR	AA
Klamath Falls OR Ser B 6.875X 5/1/23	05/01/91	05/01/23	0.86X	3,003,750	6.64	10.06	NR	SP-1+
Klamath Falls OR Ser E 6.875X 5/1/23	05/01/91	05/01/23	0.29X	1,002,000	6.51	9.86	NR	SP-1+
Lancaster CA Willows 85-A 2/1/05 VRDN	02/01/05	02/01/05	0.47X	1,650,000	5.75	8.71	A	AA-
Lapeer MI Econ Dev Corp 6.8X 2/1/91	02/01/91	02/01/91	0.12X	410,000	6.73	10.19	NR	BBB
Lapeer MI Econ Dev Corp 7.0X 2/1/92	02/01/92	02/01/92	0.12X	435,000	6.99	10.59	NR	BBB
Lapeer MI Econ Dev Corp 7.1X 2/1/93	02/01/93	02/01/93	0.10X	365,000	7.09	10.75	NR	BBB
Las Vegas Valley NV 5.6X 9/1/92	09/01/92	09/01/92	0.11X	398,254	7.22	10.94	NR	A-1
Leominster Mass PCR 5.6X 11/1/91	11/01/91	12/01/98	0.36X	1,249,871	8.06	12.21	NR	NR
Lorain OH BANS 6.95X 10/05/90	10/05/90	10/05/90	0.29X	1,001,860	8.50	12.88	Baa	NR
Louisiana State 5X 2/1/93	02/01/93	02/01/93	0.12X	416,311	8.08	12.24	Baa1	BBB+
Louisiana State 5.2X 9/1/91	09/01/91	09/01/91	0.56X	1,955,182	7.76	11.76	Aa1	BBB
Louisiana State Ser A 5.25X 8/1/92	08/01/92	08/01/92	0.26X	923,338	7.51	11.38	Aaa	AAA
Louisiana State Ser C 5.8X 6/1/91	06/01/91	06/01/91	0.28X	989,300	7.45	11.29	Baa1	BBB+
Louisiana Public Fac Auth 7.5X 5/15/12	05/15/92	05/15/12	0.60X	2,095,531	6.39	9.68	NR	AAA
Louisiana State Ser 81-B 9.2X 6/15/91	06/15/91	06/15/91	0.13X	465,017	4.35	6.59	Baa1	BBB+
Louisiana State 9.375X 10/1/90	10/01/90	10/01/90	0.43X	1,494,948	8.50	12.88	Baa1	BBB+
Louisiana State 4.9X 2/1/91	02/01/91	02/01/91	0.07X	242,563	14.06	21.30	Baa1	BBB+
Louisiana State 4.9X 2/1/92	02/01/92	02/01/92	0.06X	225,396	9.86	14.94	Baa1	BBB+
Lubbock Texas Elec Lt & Pwr 5X 4/15/91	04/15/91	04/15/91	0.08X	293,784	9.00	13.63	A1	A+
Maricopa Cnty AZ Ser B 4.45X 7/1/91	07/01/91	07/01/91	0.20X	698,858	14.30	21.66	Aa	AA
Maricopa Cnty AZ IDRB 6.36X 10/1/12	10/01/90	10/01/12	0.24X	832,929	8.50	12.88	A1	NR
Massachusetts Bay Trans Ath 8.75 3/1/93	03/01/93	03/01/93	0.15X	527,525	6.26	9.48	Baa1	BBB
Massachusetts Housing Ser A 6.6X 7/1/91	07/01/91	07/01/91	0.29X	1,000,000	6.58	9.97	Aaa	AAA
Methuen MA 6.75X 10/19/90	10/19/90	10/19/90	0.29X	1,002,310	2.23	3.38	A1	NR
Minneapolis SchoolDist TAN 6.25 1/23/91	01/23/91	01/23/91	0.57X	2,000,980	5.84	8.85	NR	SP-1+
Missouri State Health & Ed Fac Auth	09/03/91	09/03/91	0.86X	3,000,000	6.09	9.23	HIG1	NR
Honroe Fl Sales Tax RANS 6.65X 11/15/91	11/15/91	11/15/91	0.57X	2,000,000	6.49	9.83	HIG1	SP-2
Multnomah County OR TANS 6.25X 6-28-91	06/28/91	06/28/91	0.57X	2,004,420	5.85	8.86	HIG1	NR
North Andover MA BANS 7.15X 10/5/90	10/05/90	10/05/90	0.31X	1,077,010	8.50	12.88	NR	A

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QUARTERLY PORTFOLIO SUMMARY EXCLUDING CASH

SECURITY DESCRIPTION	NEXT RED DATE	MATURITY DATE	% PORTFOLIO (AT COST)	COST BASIS	YIELD	PRE-TAX YIELD	MOODY RATING	S & P RATING
- cont.								
Portfolio: Company 10								
Investment Type: Municipal Sec								
- cont.								
New Hampshire IDA Rev Tmco	11/01/90	11/01/04	0.29%	1,000,000	6.65	10.08	Baa1	BBB
New Mexico Severance Tax 7.9% 7/1/92	07/01/92	07/01/92	0.73%	2,545,475	6.77	10.26	Aa	AA
New Orleans LA 12.0% 12/1/90	12/01/90	12/01/90	0.15%	516,385	8.50	12.88	Baa	A-
North Slope Boro AK Ser C 10% 6/30/93	06/30/93	06/30/93	1.55%	5,417,730	6.56	9.94	Baa1	BBB+
North Slope AK Ser F 8.5% 6/30/91	12/31/90	06/30/91	0.44%	1,533,840	8.50	12.88	Baa1	BBB+
Nassau County NY 3.5% 10/15/92	10/15/92	10/15/92	0.17%	608,005	7.74	11.73	A1	NR
Nassau County NY GO's 5.84% 11/15/90	11/15/90	11/15/90	0.86%	3,000,900	5.53	8.38	A1	NR
New Jersey St Ser A 6.6% 7/1/91	07/01/91	07/01/91	0.11%	399,700	6.69	10.13	Baa	BBB+
New York St Ser 2 GO 4.5% 6/30/05	12/01/90	06/30/05	0.23%	819,810	8.50	12.88	A1	AA-
New York State GO 9.0% 7/15/91	07/15/91	07/15/91	0.88%	3,083,670	5.23	7.93	A	A
New York State TRANS 3/28/91	03/28/91	03/28/91	0.86%	3,010,320	5.77	8.74	MIG2	SP-1
Nassau Cnty FL 7.25% 12/1/20	12/01/90	12/01/20	1.85%	6,462,669	5.94	9.00	Aaa	AAA
Ohio State Highway Ser B 4.25% 5/15/91	05/15/91	05/15/91	0.27%	936,470	8.50	12.88	Aa	AA
Oklahoma City OK 4.6% 10/1/90	10/01/90	10/01/90	0.14%	489,937	8.50	12.88	Aa	AA
Oregon State GO SX 7/1/92	07/01/92	07/01/92	0.53%	1,849,485	7.10	10.76	A1	AA-
Pennsylvania GO 4.35% 7/15/91	07/15/91	07/15/91	0.18%	613,305	7.85	11.90	A1	AA-
Pearland TX 5.1% 2/1/92	02/01/92	02/01/92	0.10%	362,790	7.70	11.67	A	A-
Pensacola FL Health Fac 9.375% 1/1/2011	01/01/92	01/01/11	0.92%	3,208,560	5.13	7.77	NR	AA
Phoenix Airport Rev 3.75% 7/1/92	07/01/92	07/01/92	0.07%	232,252	8.17	12.38	A	A+
Phoenix AZ GO 9.5% 7/1/92	07/01/92	07/01/92	0.30%	1,058,520	5.93	8.98	Aa1	AA+
City of Pittsburgh Urban	08/01/91	10/01/16	0.86%	3,000,000	3.24	4.90	NR	NR
Plainview Texas 4.85% 2/15/92	02/15/92	02/15/92	0.17%	600,013	7.97	12.08	A	A
Platte River Power Auth Colo 6/1/12	06/01/92	06/01/12	0.70%	2,436,840	5.65	8.56	Aaa	AAA
Port Arthur TX SX 5/1/92	05/01/92	05/01/92	0.03%	96,310	7.51	11.37	A	A+
Portland ME Wtr Dist BANS 7.3% 12/14/90	12/14/90	12/14/90	0.29%	1,003,350	5.48	8.30	NR	NR
Portsmouth NH TAN 7.6% 6/28/91	06/28/91	06/28/91	0.57%	2,006,920	7.02	10.64	NR	NR
Puerto Rico Hsg Fin Auth 6.5% 10-1-11	10/01/90	10/01/11	0.57%	2,000,000	8.50	12.88	NR	AA
Redmond WA LID 88-ST-52 6.2% 11/1/90	11/01/90	11/01/90	0.29%	997,460	8.60	13.02	NR	NR
Rhode Island GO TANS 6.5% 12/20/90	12/20/90	12/20/90	0.57%	2,003,380	5.64	8.55	MIG2	NR
Rhode Island Indl Facs Corp 5.75 7/1/92	07/01/92	07/01/92	0.18%	621,117	6.61	10.01	NR	A-2
Richmond Co GA Dev Auth 8.5% 12/1/12	12/01/90	12/01/12	0.29%	1,017,950	8.50	12.88	Baa	NR
Rochester Health Care Fac 5.65 11/15/91	11/15/91	11/15/91	0.28%	960,079	6.12	9.27	NR	AA+
Saline KS Penneys Project 12/1/14 VRDN	12/01/14	12/01/14	0.71%	2,495,000	6.45	9.77	Baa1	BBB
Stevens Cnty Wa Pub Util 7.375% 3/1/92	03/01/92	03/01/92	0.29%	1,000,000	7.37	11.16	NR	NR
Suffolk County NY TAN 6.5% 8/28/91	08/28/91	08/28/91	0.86%	3,004,230	6.30	9.55	NR	SP-1
Tacoma WA Public Util&Lt 4% 7/1/91	07/01/91	07/01/91	0.07%	244,990	14.95	22.65	Aaa	AAA
Tarrant Co Tx Jr College Dist 4% 5/1/91	05/01/91	05/01/91	0.04%	145,206	9.73	14.74	Aa	AA
Toledo OH Special Assessment Bonds	05/15/91	11/15/91	1.22%	4,252,358	5.92	8.96	MIG1	NR
Tulsa OK Hillcrest Ser 83 12/1/08 VRDN	12/01/08	12/01/08	0.29%	1,000,000	6.08	9.20	Aa2	NR
Texas Water Development Muni Bond	08/01/93	08/01/93	0.09%	312,900	7.41	11.23	Aaa	AAA
Utah Housing Auth. 6.9% 1/1/22	07/01/91	01/01/22	0.57%	2,000,000	6.87	10.40	NR	AA
Washington State GO 12% 9/1/99	12/01/91	09/01/99	0.32%	1,117,100	1.83	2.77	Aaa	AAA
Washington State GO 4% 9/1/91	09/01/91	09/01/91	0.14%	482,738	13.60	20.60	A	AA
Westchester County NY GO 6.7% 2/1/92	02/01/92	02/01/92	0.45%	1,563,594	6.00	9.09	Aaa	AAA
Williamsport PA Muni Wtr Au 6.6% 1/1/92	10/01/90	01/01/92	0.86%	3,000,000	8.50	12.88	NR	NR
State of Wisconsin Operating Notes	06/17/91	06/17/91	0.86%	3,005,070	5.94	9.00	MIG1	SP-1+
Wisconsin Hsg & Econ Dev Auth 6.2%	03/01/91	09/01/15	0.57%	1,998,030	6.42	9.72	Aa	A+
Wa Pub Pwr Supply #1 5.0% 7/1/91	07/01/91	07/01/91	0.56%	1,942,922	8.99	13.62	Aa	AA

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As of Date: 09/30/90

QUARTERLY PORTFOLIO SUMMARY EXCLUDING CASH

SECURITY DESCRIPTION	NEXT RED DATE	MATURITY DATE	% PORTFOLIO (AT COST)	COST BASIS	YIELD	PRE-TAX YIELD	MOODY RATING	S & P RATING
Portfolio: Company 10								
Investment Type: Municipal Sec								
- cont.								
Ma Pub Pwr Supply #1 5.4% 7/1/92	07/01/92	07/01/92	0.17%	582,883	7.66	11.61	Aa	AA
Ma Pub Pwr Supply #1 5.6% 7/1/92	07/01/92	07/01/92	0.28%	968,012	7.58	11.48	Aa	AA
Ma Pub Pwr Supply #2 13.875	07/01/92	07/01/12	0.25%	877,828	5.22	7.90	Aa	AA
Ma Pub Pwr Supply #2 14.75%	07/01/92	07/01/12	1.08%	3,763,100	4.70	7.12	Aa	AA
Ma Pub Pwr Supply #2 5.10% 7/1/91	07/01/91	07/01/91	0.06%	205,819	7.86	11.91	Aa	AA
Ma Pub Pwr Supply #3 9.5% 7/1/92	07/01/91	07/01/92	0.08%	263,878	5.79	8.77	Aa	AA
Yonkers NY Series A GO 8/1/92	08/01/92	08/01/92	0.14%	500,000	6.55	9.93	Baa	BBB+
Yonkers NY Series A GO 8/1/93	08/01/93	08/01/93	0.16%	546,678	7.00	10.61	Baa	BBB
				53.88%	188,068,431	6.90	10.66	
Portfolio: Company 10			100.00%	349,033,279	7.35	10.38		

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QUARTERLY PORTFOLIO SUMMARY EXCLUDING CASH

As of Date: 09/30/90

SECURITY DESCRIPTION	NEXT RED DATE	MATURITY DATE	% PORTFOLIO (AT COST)	COST BASIS	YIELD	PRE-TAX YIELD	MOODY RATING	S & P RATING
Portfolio: Company 63								
Investment Type: Commercial Paper								
Condisco Inc CP	10/26/90	10/26/90	8.51X	4,952,342	13.20	13.20	P-2	A-2
			8.51X	4,952,342	13.20	13.20		
Investment Type: Corporate Bond								
Cigna Corp MTN	09/24/92	09/24/92	4.64X	2,700,000	8.56	8.56	Aa2	A+
Paccar Financial Corp MTN 9.0% 9/26/94	09/26/94	09/26/94	5.15X	3,000,000	9.00	9.00	A1	AA-
Philadelphia Electric 11.75% 11/15/2014	11/15/90	11/15/14	7.51X	4,374,562	7.56	7.56	NR	A-
Texas Utilities Elec Co 12% 8/1/15	12/01/90	08/01/15	9.34X	5,440,750	8.50	8.50	Baa2	BBB
US West Financial Svc 8.74% 5/28/91	05/28/91	05/28/91	3.45X	2,008,760	8.03	8.03	A2	A+
Westinghouse Credit 8.7% 7/15/91	07/15/91	07/15/91	1.72X	1,001,390	8.52	8.52	A2	A
			31.82X	18,525,462	8.32	8.32		
Investment Type: Floating Rate								
National Medical Enterprises 4/3/96 FRN	10/17/90	10/17/90	8.59X	5,000,000	9.03	9.03	Baa	BBB
Security Pacific Corp FRN	12/19/90	12/19/90	5.15X	3,000,000	8.28	8.28	A1	AA-
Shearson Lehman Money Market Note	10/09/90	10/09/90	5.15X	3,000,000	8.25	8.25	A3	A-
			18.89X	11,000,000	8.61	8.61		
Investment Type: Loan Partic								
American Stores LP	10/01/90	10/01/90	6.93X	4,035,000	8.55	8.55	P-3	A-3
Armstrong World Industries LP	10/11/90	10/11/90	4.93X	2,870,000	8.23	8.23	P-1	A-1+
Dana Corp LP	10/03/90	10/03/90	4.15X	2,415,000	8.22	8.22	P-2	A-2
Federal Paper Board LP	11/06/90	11/06/90	5.15X	3,000,000	8.26	8.26	NR	NR
HSD Development LP	10/02/90	10/02/90	2.45X	1,425,000	8.99	8.99	NR	NR
Paccar Leasing LP	11/29/90	11/29/90	8.59X	5,000,000	8.08	8.08	NR	NR
Utilicorp LP	10/15/90	10/15/90	8.59X	5,000,000	8.32	8.32	P-2	A-2
			40.78X	23,745,000	8.32	8.32		
Portfolio: Company 63			100.00X	58,222,804	8.79	8.79		

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QUARTERLY PORTFOLIO SUMMARY EXCLUDING CASH

SECURITY DESCRIPTION	NEXT RED DATE	MATURITY DATE	% PORTFOLIO (AT COST)	COST BASIS	YIELD	PRE-TAX YIELD	MOODY RATING	S & P RATING
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Portfolio: Company 65

Investment Type: Commercial Paper

BET Finance Inc LP	10/10/90	10/10/90	16.06%	4,983,375	11.97	11.97	P-1	A-1
			16.06%	4,983,375	11.97	11.97		

Investment Type: Loan Partic

Great Atlantic & Pacific Tea Company LP	10/03/90	10/03/90	16.11%	5,000,000	8.67	8.67	P-2	A-2
ADT Operations LP	10/01/90	10/01/90	9.67%	3,000,000	9.04	9.04	NR	NR
Armstrong World Industries LP	10/11/90	10/11/90	5.41%	1,680,000	8.23	8.23	P-1	A-1+
Dana Corp LP	10/03/90	10/03/90	13.65%	4,235,000	8.22	8.22	P-2	A-2
Huntsman Chemical Loan Participation	10/05/90	10/05/90	16.18%	5,020,000	8.58	8.58	NR	NR
MCI Communications LP	10/15/90	10/15/90	8.12%	2,520,000	8.27	8.27	P-2	A-2
MSD Development LP	10/02/90	10/02/90	5.14%	1,595,000	8.99	8.99	NR	NR
Woolworth Corp LP	10/10/90	10/10/90	9.67%	3,000,000	8.25	8.25	P-1	A-1
			83.94%	26,050,000	8.53	8.53		

Portfolio: Company 65

			100.00%	31,033,375	9.08	9.08		
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GRAND TOTAL

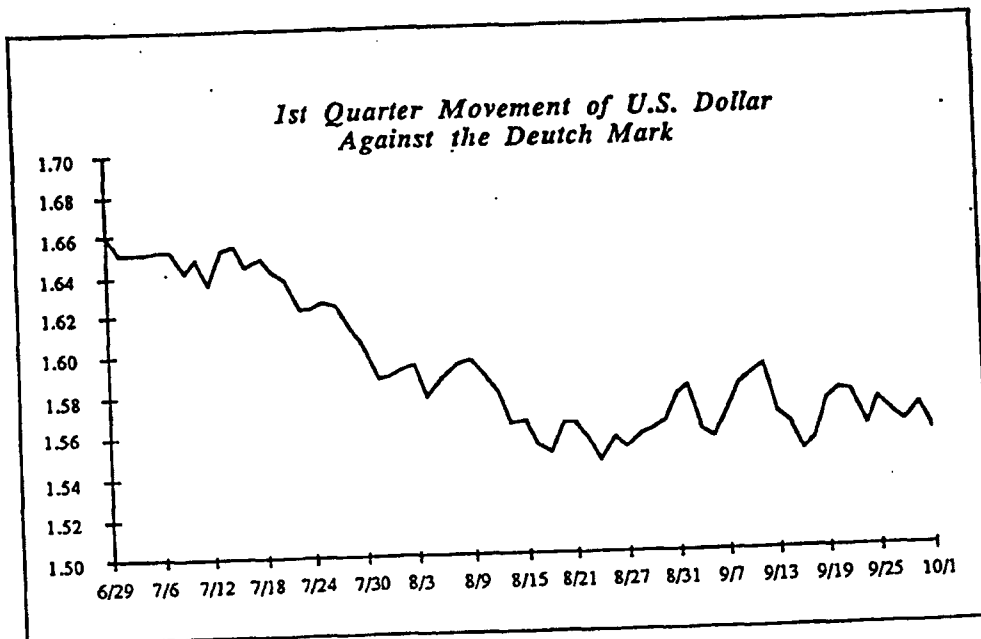
				438,289,458	7.67	10.07		
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Foreign Exchange Hedging Program

During Q91-1, the U.S. Dollar continued an overall weakening trend. Against the Deutch Mark, the Dollar weakened 6.2% during the quarter, after weakening 2.0% in Q90-4. Forward hedge contracts valued at \$76.9 million were executed in Q91-1 versus \$73.6 million in the prior quarter.



Against the ECU (European Currency Unit, which is representative of a basket of European currencies), the dollar weakened 6.7% in Q91-1. Against our original FY91 plan, the dollar was 9.4% weaker than forecasted. All of these factors resulted in a positive European retail sales exchange rate variance from plan in Q91-1 of \$9.2 million on \$123.6 million in sales (see page 42).

We recorded a consolidated foreign currency translation gain of \$850,000 in Q91-1 compared with \$981,000 in Q90-4. This is attributable to the weakening dollar over the course of the quarter and our stop-loss collar hedging methodology that allows these gains to accumulate as the dollar loses strength.

We are accommodating our overseas construction obligations at MS LTD by use of a "natural hedge". By holding and building a reserve of British Pound Sterling that would otherwise be converted to U.S. Dollars, we avoid being forced to purchase Sterling in the currency markets until Q91-3. As payment dates approach, we will lock into favorable currency rates in the event the Dollar should weaken against the Sterling.

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Accounts Receivable

Accounts receivable (net) decreased 2% or \$3.4 million from \$181.0 million at the end of Q90-4 to \$177.6 million at the end of Q91-1. The decrease results from the reclassification of reseller rebates (earned purchase credits which contractually may only be used to offset receivable balances) of \$11.4 million. These were previously shown in current liabilities and now reduce accounts receivable. Consolidated days sales outstanding (DSO), shown below for the past five quarters, increased from 55.6 days at the end of Q90-4 to 56.3 days at the end of Q91-1.

FY Quarter	DSO
Q91-1	56.3
Q90-4	55.6
Q90-3	52.9
Q90-2	55.9
Q90-1	56.0

An analysis of the receivable aging shows that accounts over 60 days comprise 21% of collectible receivables, up from 18% in Q90-4. The increase in the over 60 days balance consists of a \$2.3 million receivable from 3COM, which will be reduced by a pending OEM contract amendment (the impact of which was included in Q91-1's GAAP adjustment), a slowing of USSMD payments, a backlog in returns processing (due to increased volume), and ongoing payment approval delays within some International countries. The \$29.1 million allowance for doubtful accounts represents 62% of all accounts over 60 days, compared with 70% at the end of the Q90-4. The allowance for doubtful accounts remains unchanged at 13% of the total collectible receivables. Mergers within the U.S. computer software reseller industry contributed to a concentration of revenue into fewer accounts, with Ingram MicroD and Merisel representing 37% and 9%, respectively, of the Q91-1 total USSMD accounts receivable balance and 13% of the consolidated accounts receivable-collectible balance.

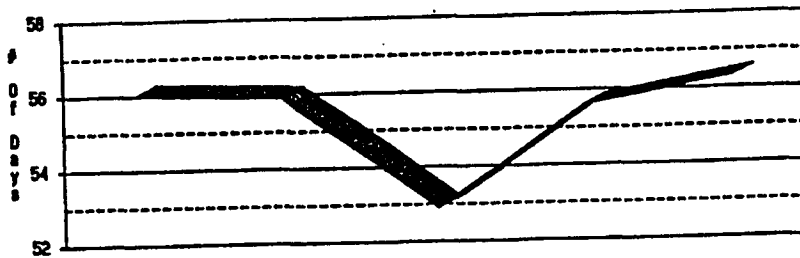
		Aging Summary				
		Total	Current	31-60	61-90	Over 90
<u>Retail</u>	USSMD	\$ 66.1	\$ 45.1	\$17.6	\$ 2.0	\$ 1.4
	International	112.9	68.2	22.2	8.6	13.9
	Worldwide Retail	179.0	113.3	39.8	10.6	15.3
<u>OEM</u>	Domestic	13.3	4.4	1.7	3.9	3.3
	International	31.1	24.1	(2.9)	0.2	9.7
	Worldwide OEM	44.4	28.5	(1.2)	4.1	13.0
<u>Other</u>		7.8	2.1	1.7	1.0	3.0
Accounts Receivables-Collectible		231.2	\$143.9	\$40.3	\$15.7	\$31.3
Aging Percentages			62%	17%	7%	14%
OEM GAAP Adjustment		14.3				
Sales Returns Reserve		(27.4)				
Reseller Rebates		(11.4)				
Allowance		(29.1)				
Accounts Receivables-Net		\$177.6				
Total Quarterly Net Revenues		\$369.4				
Days Sales Outstanding ⁽¹⁾		56.3				

(1) Calculation uses "Accounts Receivable - Collectible" divided by "Total Quarterly Net Revenues" times 90.

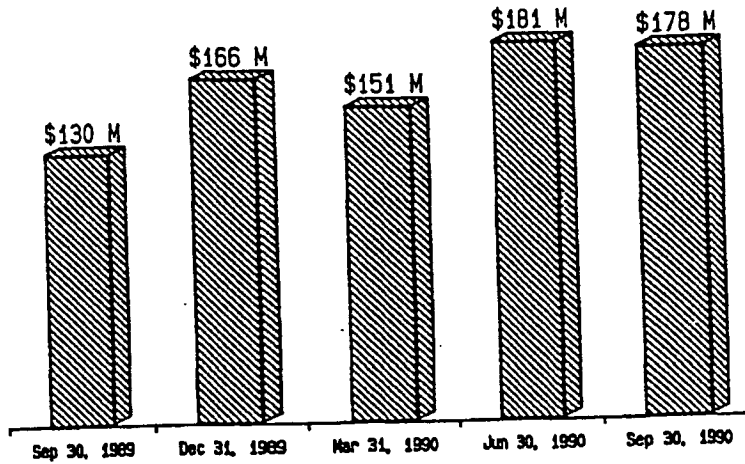
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Days' Sales Outstanding

(Based on Revenues for the Quarter)



Accounts Receivable - Net



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Inventories

Total inventories at the end of Q91-1 were \$58.4 million. This represents a 5% increase from Q90-4. Consolidated days inventory on hand (calculated based on past three months product costs) decreased to 90 days from 99 days at the end of Q90-4. The change represents the fact that revenues increased 10%, while inventory increased only 5%. Inventory by locations was as follows (in millions):

	<u>September 30</u>	<u>June 30</u>	<u>Change</u>
Puerto Rico	\$ 0.6	\$ 0.3	\$ 0.3
Ireland	3.5	2.7	0.8
Campus North	26.2	24.3	1.9
Sub Warehouses	<u>28.1</u>	<u>28.3</u>	<u>(0.2)</u>
	<u>\$58.4</u>	<u>\$55.6</u>	<u>\$2.8</u>

Segregated between raw materials, finished goods and allowances, our inventory was as follows (in millions):

	<u>September 30</u>	<u>June 30</u>	<u>Change</u>
Raw materials	\$19.0	\$18.8	\$0.2
Finished goods	17.1	10.8	6.3
Allowances	<u>(12.4)</u>	<u>(11.4)</u>	<u>(1.0)</u>
Domestic Inventory (CN and PR)	<u>23.7</u>	<u>18.2</u>	<u>5.5</u>
Raw materials	0.7	0.9	(0.2)
Finished goods	3.6	6.2	(2.6)
Allowances	<u>(1.2)</u>	<u>(0.7)</u>	<u>(0.5)</u>
ICON Inventory (CN)	<u>3.1</u>	<u>6.4</u>	<u>(3.3)</u>
Raw materials	6.4	5.6	0.8
Finished goods	30.6	29.8	0.8
Allowances	<u>(5.4)</u>	<u>(4.4)</u>	<u>(1.0)</u>
International Inventory	<u>31.6</u>	<u>31.0</u>	<u>0.6</u>
Consolidated Inventory	<u>\$58.4</u>	<u>\$55.6</u>	<u>\$2.8</u>
Raw materials	26.1	25.3	0.8
Finished goods	51.3	46.8	4.5
Allowances	<u>(19.0)</u>	<u>(16.5)</u>	<u>(2.5)</u>
Consolidated Inventory	<u>\$58.4</u>	<u>\$55.6</u>	<u>\$2.8</u>

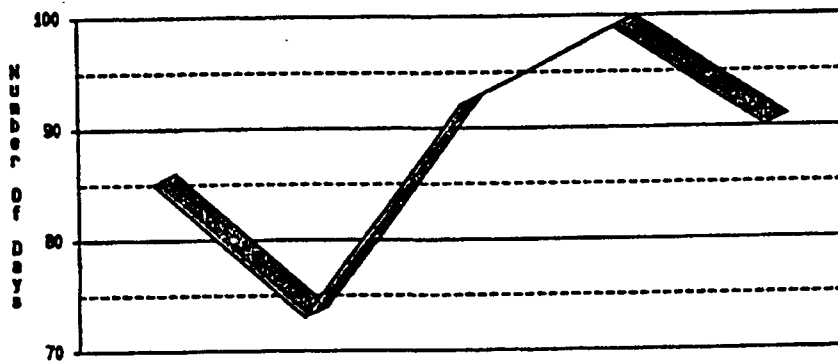
The increase in domestic finished goods is primarily due to the \$4.6 million increase in Mice inventories, as well as significant increases in Windows Excel (\$500,000), PC Works (\$303,000), Windows (\$235,000) and Windows PowerPoint (\$229,000). These increases were partially offset by decreases in Book (\$325,000) and DOS (\$157,000) inventories. Mice inventories continue to build in preparation for the busy holiday season. Windows applications inventory was increased in response to demand. PC Works inventory has also been increased due to a special promotion during Trimester 3. The increase in Windows 3.0 inventory deserves note. At the end of Q90-4, Windows inventory was very low due to the strong demand following its release. The Q91-1 inventory of Windows, although higher than in Q90-4, is significantly lower than it has been throughout the quarter. Due to a pending software modification (version 3.0a) we have stopped building Windows and are clearing out existing inventory. ICON finished goods inventory decreased \$2.5 million due to a concerted effort to reduce inventory levels. The international subsidiaries' local currency inventories are translated into US Dollars using the current exchange rate at quarter end. During Q90-1, subsidiary inventory levels actually decreased from Q90-4. The decrease was, however, offset by the translation effect of the weakening dollar.

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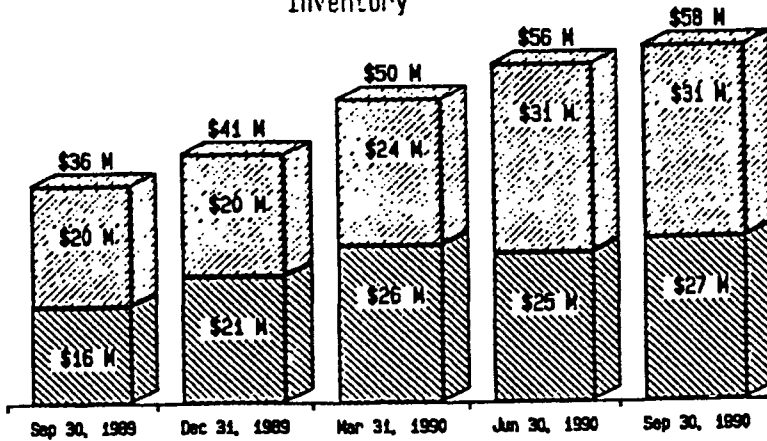
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Days' Supply in Ending Inventory

(Based on Three Month Average Product Costs)



Inventory



☐ International ▨ Domestic

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Property, Plant and Equipment

Net property, plant and equipment increased \$51.4 million in Q91-1 to \$376.8 million from \$325.4 million at June 30, 1990. Property, plant and equipment at September 30, 1990 and June 30, 1990 consists of the following (in millions):

	<u>Sep. 30</u>	<u>Jun. 30</u>	<u>Change</u>
Land	\$ 103.4	\$85.5	\$17.9
Buildings	122.4	109.0	13.4
Leasehold improvements	22.7	17.4	5.3
Furniture and equipment	46.8	41.7	5.1
Computer equipment	<u>165.9</u>	<u>145.7</u>	<u>20.2</u>
	461.2	399.3	61.9
Accumulated depreciation	<u>(84.4)</u>	<u>(73.9)</u>	<u>(10.5)</u>
Net	<u>\$376.8</u>	<u>\$325.4</u>	<u>\$51.4</u>

The increase in land was primarily due to the expansion at Corporate Campus for Phase 9 (\$14.7 million) and Phase 10 (\$1.5 million), and the affect of translation on the London land (\$1.7 million). The increase in buildings primarily results from construction on Corporate Campus buildings 16 and 17 (\$3.0 million each) and construction in Microsoft England (\$4.2 million) and Microsoft Ireland (\$2.5 million). Leasehold improvements increased at Ridgewood (\$1.8 million), Puerto Rico (\$1.1 million), Charlotte (\$1.0 million), Corporate Campus (\$393,000), and the subsidiaries (\$989,000). The increase in furniture and equipment represents telecommunications equipment (\$2.0 million), Puerto Rico (\$826,000), additions in domestic furniture (\$434,000), manufacturing equipment (\$235,000) and the subsidiaries (\$2.2 million). Computer equipment experienced another quarter of growth. The following table and chart summarize the gross and net additions during Q91-1 (dollars in millions):

	<u>Quantity Purchased</u>	<u>Cost</u>
Personal Computers		
Compaq 386 computers	831	\$ 7.1
Northgate computers	182	1.1
Compaq 486 computers	77	1.1
IBM PS/2 computers	97	1.0
Apple computers	129	0.8
Other personal computers	<u>68</u>	<u>0.3</u>
Subtotal	<u>1,384</u>	11.4
Other Computer Equipment		
Subsidiaries		6.5
Corporate networking equipment		1.7
VAX equipment		0.8
Disk drives	171	0.5
Printers	110	0.4
Additional memory		0.3
Other		<u>0.2</u>
Gross additions		21.8
Retirements		<u>(1.6)</u>
Net additions		<u>\$20.2</u>

Computer Additions	Q91-1	Q90-4	Q90-3	Q90-2	Q90-1	\$20.2
	Q91-1	Q90-4	Q90-3	Q90-2	Q90-1	\$19.0
	Q91-1	Q90-4	Q90-3	Q90-2	Q90-1	\$15.5
	Q91-1	Q90-4	Q90-3	Q90-2	Q90-1	\$11.5
	Q91-1	Q90-4	Q90-3	Q90-2	Q90-1	\$10.1

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Other Assets

During Q91-1, other assets decreased \$4.1 million to \$55.9 million from \$60.0 million as of June 30, 1990. Other assets at September 30, 1990 and June 30, 1990 consists of the following (in millions):

	<u>Sep. 30</u>	<u>Jun. 30</u>	<u>Change</u>
Intellectual property rights - net	\$15.4	\$19.9	\$(4.5)
Long-term investments	24.8	26.5	(1.7)
Miscellaneous	<u>15.7</u>	<u>13.6</u>	<u>2.1</u>
	<u>\$55.9</u>	<u>\$60.0</u>	<u>\$(4.1)</u>

The \$4.5 million decrease in intellectual property rights resulted primarily from Q91-1 amortization (\$2.5 million) and purchase price adjustments for Project (\$2.1 million) and SoftPrint (\$149,000). The \$1.7 million decrease in long-term investments was comprised of additional reserves for non-performing investments (\$2.9 million) and amortization of the Company's investment in SCO (\$500,000), offset primarily by the reclassification of a Uniroyal Plastics IRN to non-performing investments (\$1.6 million). Miscellaneous long-term assets increased primarily due to additional funding of the Company's directors and officers trust fund (\$3.8 million), less the reclassification of the Forethought NOL carry forward (\$1.9 million) reducing income taxes payable.

Current Liabilities

During Q91-1, current liabilities increased \$26.3 million to \$213.1 million from \$186.8 million at June 30, 1990. Income taxes payable experienced the largest increase (\$15.6 million), the result of Q91-1 earnings. Accounts payable also grew significantly (\$15.5 million), largely because of increased purchases of raw materials (\$7.8 million) and additional marketing accruals (\$6.4 million). Notes payable increased by \$3.5 million because of borrowings on subsidiaries' credit lines (\$4.9 million), less reductions in hedging activity borrowings (\$1.4 million). The above increases were partially offset by a decrease in customer deposits (\$10.1 million) due primarily to correctly reclassifying reseller rebates to reductions to accounts receivable.

Stockholders' Equity

Stockholder's equity increased \$71.9 million during Q91-1 to \$990.4 million from \$918.5 million at June 30, 1990. Retained earnings increased \$43.9 million, the net result of Company earnings for the quarter of \$87.6 million, less \$43.7 million buy back of 724,000 shares of Company stock. Common stock and paid in capital increased \$23.2 million, the result of stock issued in connection with Company stock option and ESPP programs (\$18.2 million) and the Company's estimated tax benefit relating to NQSO transactions (\$6.4 million), less an additional amount for the stock buy back program (\$1.2 million). Additionally, there was a \$4.8 million favorable foreign currency translation adjustment resulting from the dollar weakening during the quarter against the permanent investments in our subsidiaries.

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SANTA CRUZ OPERATION

Results of Operations

Consolidated statements of income (unaudited) compared with the prior year for the quarter ended June 30, 1990 and 1989 are presented below (in millions).

	1990		1989		Change %
Net revenues	\$27.0	100.0%	\$19.3	100.0%	40
Cost of revenues	<u>11.2</u>	<u>41.5</u>	<u>7.2</u>	<u>40.2</u>	42
Gross profit	15.8	58.5	11.4	59.1	39
Operating expenses	<u>17.7</u>	<u>65.5</u>	<u>13.2</u>	<u>72.1</u>	27
NET LOSS	\$ <u>(1.9)</u>	<u>(7.0)%</u>	\$ <u>(2.5)</u>	<u>(13.0)%</u>	24

Financial Condition

Consolidated balance sheets (unaudited) as of June 30, 1990 and 1989 and a consolidated statement of cash flow for the quarter ended June 30, 1990 are presented below (in millions).

	June 30 1990	June 30 1989	Year Change	Year% Change
Current assets	\$34.8	\$26.9	\$7.9	29
Fixed assets	<u>13.1</u>	<u>16.6</u>	<u>(3.5)</u>	(21)
TOTAL ASSETS	<u>\$47.9</u>	<u>\$43.5</u>	<u>\$4.4</u>	10
Current liabilities	\$30.1	\$17.6	\$12.5	71
Long-term liabilities	4.5	4.4	0.1	2
Stockholders' equity	<u>13.3</u>	<u>21.5</u>	<u>(8.2)</u>	(38)
TOTAL LIABILITIES & EQUITY	<u>\$47.9</u>	<u>\$43.5</u>	<u>\$4.4</u>	10

	Q20-4
Cash from operations	\$ (1.8)
Cash from financing-net	4.3
Cash used for investments	(0.9)
Net change in cash and short term investments	1.6
Cash and short-term investments at beginning of period	<u>6.9</u>
Cash and short-term investments at end of period	<u>\$8.5</u>

SCO indicates that it reported a profit of approximately \$100,000 for the quarter ended September 30, 1990, although this may have involved some "reserve" management.

We are amortizing our investment in SCO at \$500,000 per quarter. At September 30, 1990 our unamortized investment in SCO was \$17.4 million.

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*Finance
Channel Reporting*

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CHANNEL REPORTING

The contribution to net revenues and operating income for Q91-1 on a channel of distribution basis was as follows (in millions):

	Actual		Plan		Variance Percentage
Net Revenues					
USSMD	\$128.1	34.7%	\$101.7	33.4%	26
International Finished Goods	<u>165.0</u>	<u>44.7</u>	<u>119.1</u>	<u>39.1</u>	39
Worldwide Retail	<u>293.1</u>	<u>79.4</u>	<u>220.8</u>	<u>72.5</u>	33
Domestic OEM	29.7	8.0	35.1	11.5	(15)
International OEM	<u>38.0</u>	<u>10.3</u>	<u>38.2</u>	<u>12.6</u>	(1)
Worldwide OEM	<u>67.7</u>	<u>18.3</u>	<u>73.3</u>	<u>24.1</u>	(8)
Other	<u>8.6</u>	<u>2.3</u>	<u>10.4</u>	<u>3.4</u>	(17)
Total	<u>\$369.4</u>	<u>100.0%</u>	<u>\$304.5</u>	<u>100.0%</u>	21

	Actual			Plan			Variance
	Income (Loss)	Percentage Total Revenue		Income (Loss)	Percentage Total Revenue		
Operating Income (Loss)							
USSMD	\$ 40.2	32.7	31.4	\$17.7	30.6	17.4	\$22.5
Int'l Finished Goods	<u>60.4</u>	<u>49.1</u>	36.6	<u>17.4</u>	<u>30.1</u>	14.6	<u>43.0</u>
Worldwide Retail	<u>100.6</u>	<u>81.8</u>	34.3	<u>35.1</u>	<u>60.7</u>	15.9	<u>65.5</u>
Domestic OEM	13.4	10.9	45.1	18.6	32.2	53.0	(5.2)
International OEM	<u>23.9</u>	<u>19.4</u>	62.9	<u>22.2</u>	<u>38.4</u>	58.1	<u>1.7</u>
Worldwide OEM	<u>37.3</u>	<u>30.3</u>	55.1	<u>40.8</u>	<u>70.6</u>	55.7	<u>(3.5)</u>
Other	<u>(14.9)</u>	<u>(12.1)</u>	--	<u>(18.1)</u>	<u>(31.3)</u>	--	<u>3.2</u>
Total	<u>\$123.0</u>	<u>100.0</u>	33.3	<u>\$57.8</u>	<u>100.0</u>	19.0	<u>\$65.2</u>

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Channel Reporting

Quarterly revenue by channel of distribution for the past three plus years is as follows (in millions):

	Q91-1		Q91-2		Q91-3		Q91-4		FY 1991	
	Dollars	Percent	Dollars	Percent	Dollars	Percent	Dollars	Percent	Dollars	Percent
USSMD	128.1	34.7							128.1	34.7
Int'l Finished Goods	165.0	44.7							165.0	44.7
US OEM	29.7	8.0							29.7	8.0
Int'l OEM	38.0	10.3							38.0	10.3
Other	8.6	2.3							8.6	2.3
	<u>369.4</u>	<u>100.0</u>							<u>369.4</u>	<u>100.0</u>

	Q90-1		Q90-2		Q90-3		Q90-4		FY 1990	
	Dollars	Percent	Dollars	Percent	Dollars	Percent	Dollars	Percent	Dollars	Percent
USSMD	79.5	33.8	97.5	32.5	78.3	25.2	103.0	30.6	358.2	30.3
Int'l Finished Goods	80.2	34.1	123.0	40.9	142.5	45.8	146.8	43.6	492.5	41.6
US OEM	35.2	15.0	31.9	10.6	45.0	14.5	39.2	11.6	151.3	12.8
Int'l OEM	35.2	15.0	41.9	13.9	38.4	12.4	40.3	12.0	155.8	13.2
Other	5.1	2.2	6.1	2.0	6.7	2.2	7.7	2.3	25.6	2.2
	<u>235.2</u>	<u>100.0</u>	<u>300.4</u>	<u>100.0</u>	<u>310.9</u>	<u>100.0</u>	<u>337.0</u>	<u>100.0</u>	<u>1,183.4</u>	<u>100.0</u>

	Q89-1		Q89-2		Q89-3		Q89-4		FY 1989	
	Dollars	Percent	Dollars	Percent	Dollars	Percent	Dollars	Percent	Dollars	Percent
USSMD	62.6	35.5	59.8	28.5	43.8	22.2	65.1	29.6	231.3	28.8
Int'l Finished Goods	57.6	32.7	82.4	39.3	79.6	40.4	79.2	35.9	298.7	37.2
US OEM	22.7	12.9	27.4	13.1	32.4	16.4	32.5	14.8	115.0	14.3
Int'l OEM	28.6	16.2	36.2	17.2	36.0	18.3	38.7	17.6	139.6	17.4
Other	4.9	2.8	4.1	2.0	5.2	2.6	4.7	2.1	18.2	2.4
	<u>176.4</u>	<u>100.0</u>	<u>209.9</u>	<u>100.0</u>	<u>197.0</u>	<u>100.0</u>	<u>220.2</u>	<u>100.0</u>	<u>803.5</u>	<u>100.0</u>

	Q88-1		Q88-2		Q88-3		Q88-4		FY 1988	
	Dollars	Percent	Dollars	Percent	Dollars	Percent	Dollars	Percent	Dollars	Percent
USSMD	30.6	29.8	54.1	34.7	53.3	32.9	51.1	30.0	189.0	32.0
Int'l Finished Goods	31.8	31.0	49.0	31.4	55.4	34.2	66.1	38.8	202.3	34.2
US OEM	21.9	21.3	31.5	20.2	26.0	16.1	23.1	13.5	102.5	17.3
Int'l OEM	14.4	14.0	17.9	11.5	22.2	13.7	25.4	14.9	79.9	13.5
Other	3.9	3.8	3.4	2.2	5.0	3.1	4.8	2.8	17.1	2.9
	<u>102.6</u>	<u>100.0</u>	<u>155.9</u>	<u>100.0</u>	<u>161.8</u>	<u>100.0</u>	<u>170.5</u>	<u>100.0</u>	<u>590.8</u>	<u>100.0</u>

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USSMD

The Q91-1 condensed burdened operating income statement for USSMD follows (in millions):

	Actual		Plan		Variance
	\$	%	\$	%	
Net revenues	<u>\$128.1</u>	<u>100.0%</u>	<u>\$101.7</u>	<u>100.0%</u>	\$26.4
Cost of revenues	28.7	22.4	24.5	24.1	(4.2)
Operating expenses	33.8	26.4	32.3	31.8	(1.5)
Allocations - Research and development	14.1	11.0	15.8	15.5	1.7
Allocations - Sales and marketing	9.1	7.1	9.4	9.2	0.3
Allocations - General and administrative	<u>2.2</u>	<u>1.7</u>	<u>2.0</u>	<u>2.0</u>	<u>(0.2)</u>
Burdened operating income	<u>\$ 40.2</u>	<u>31.4%</u>	<u>\$ 17.7</u>	<u>17.4%</u>	<u>\$22.5</u>

USSMD started off the new fiscal year with record setting quarterly net revenues. Net revenues of \$128.1 million were 26% above plan of \$101.7 million. USSMD revenues by product group for Q91-1 were as follows (in millions):

	Actual		Plan		Variance
	\$	%	\$	%	
Applications	\$ 81.2	63.4%	\$ 66.4	65.3%	\$14.8
SPAG	25.7	20.1	14.3	14.1	11.4
Systems	20.9	16.3	21.3	21.0	(0.4)
Languages	7.4	5.8	5.7	5.6	1.7
Adjustments	<u>(7.1)</u>	<u>(5.6)</u>	<u>(6.2)</u>	<u>(6.0)</u>	<u>(0.9)</u>
Net Revenues	<u>\$128.1</u>	<u>100.0%</u>	<u>\$101.5</u>	<u>100.0%</u>	<u>\$26.6</u>

In terms of gross revenue generation, the channel's ten leading products (compared with plan) for the quarter were as follows (units in thousands, dollars in millions):

Actual	Plan	Product	Actual		Plan		Variance
			Units	Revenue	Units	Revenue	
1	1	Mouse	284.6	\$ 25.5	167.5	\$13.8	\$11.7
2	4	Win Word	91.2	16.9	45.1	9.5	7.4
3	2	Win Excel	74.0	15.1	52.0	11.7	3.4
4	5	Windows	150.7	10.3	129.9	9.1	1.2
5	6	Mac Word	53.4	8.2	50.9	7.6	0.6
6	3	Windows Updates	153.6	6.4	260.0	10.4	(4.0)
7	7	Mac Excel	33.4	6.2	38.2	6.9	(0.7)
8	8	PC Word	29.7	5.2	35.2	5.9	(0.7)
9	9	Mac Office	9.6	4.5	10.9	4.8	(0.3)
10	10	PC Works	47.6	4.4	53.6	4.2	0.2
			<u>\$102.7</u>		<u>\$83.9</u>		<u>\$18.8</u>
Percent of USSMD's net revenues			<u>80%</u>		<u>82%</u>		

Following on the heels of Q90-4's Windows 3.0 introduction, Q91-1 kicked off the year of GUI. Exploiting the sockets created by Windows 3.0, Mouse, Win Word and Win Excel all showed incredible growth, combining to represent 85% of USSMD's revenue variance. The Microsoft Mouse was the largest revenue generator with gross revenues of \$25.5 million, 85% above plan, and accounting for 20% of USSMD gross revenues. Win Word revenues of \$16.9 million were 78% above budget. Win Excel revenues were \$15.1 million compared to plan of \$11.7 million. Windows 3.0 continues to show strong demand with sales of \$10.3 million, 13% above plan. Windows 3.0 Update revenue of \$6.4 million missed plan by \$4.0 million. Product marketing attributes this shortfall to higher than planned sales in Q90-4 at the expense of Q91-1.

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USSMD

During Q91-1, sales to Distributors/Franchisors (\$68.5 million) and Contracted Dealers (\$37.1 million) represented 78% of gross revenue. Value Added Resellers represented 5.8% of USSMD revenue. Discounts to Value Added Resellers were negatively impacted by special pricing to IBM for Windows 3.0, Win Word, and Excel in accordance with ACIS pricing. End User revenue of \$6.8 million, accounted for 5.1% of USSMD gross revenue, consisting primarily of Windows 3.0 Updates (\$2.7 million), Pro C 6.0 Updates (\$1.0 million), and Windows 3.0 SDK Updates (\$506,000). Education revenue of \$5.3 million accounted for 3.9% of USSMD gross revenue. This amount represents only our direct sales to educational institutions. Total Education channel revenue (including AED revenue, imbedded in distribution, and IBM ACIS) was \$16.2 million. Revenue from the Government channel was \$3.1 million (\$2.6 million through Government Distributors and \$528,000 in direct sales to state and local governments), compared to \$1.6 million for Q90-4. Our first fiscal quarter is typically the highest Government revenue quarter of the year as agencies attempt to spend budgeted funds prior to the end of their fiscal years. This amount (\$3.1 million) does not include Desktop III (Unisys) revenue which is recognized in the Domestic OEM channel. USSMD gross revenues and average discount by customer type were as follows (in millions):

	Q91-1			Q90-4		
	Sales	%	Discount %	Sales	%	Discount %
Distributors/Franchisors	\$ 68.5	50.6	46.3	\$ 48.1	46.0	46.1
Contracted Dealers (LVRs/ Major Chains)	37.1	27.4	43.2	36.7	35.1	43.1
Value Added Resellers	7.8	5.8	59.0	0.5	0.5	35.8
End User	6.8	5.1	32.2	10.2	9.8	30.7
Corporate Accounts	6.1	4.5	45.5	3.5	3.4	45.1
Education	5.3	3.9	45.7	3.5	3.4	50.4
Government	3.1	2.3	44.2	1.6	1.5	45.6
Other	0.5	0.4	55.5	0.4	0.3	77.3
Gross Revenues	<u>\$135.2</u>	<u>100.0%</u>	45.8	<u>\$104.5</u>	<u>100.0%</u>	44.2

Sales to the top 10 customers, by quarter, for the past five quarters were as follows (in millions):

	Q91-1	Q90-4	Q90-3	Q90-2	Q90-1
Ingram/Micro D	\$ 39.7	\$28.2	\$25.2	\$29.7	\$20.0
Merisel	23.1	14.6	10.0	19.7	12.5
Egghed	12.0	18.1	9.9	13.0	7.3
IBM	7.7	0.4	0.7	8.9	7.0
Software Spectrum	6.7	2.9	2.1	1.9	2.9
Soft Warehouse	4.1	3.1	1.1	--	--
Corporate Software	4.0	2.8	3.2	4.1	1.6
Computerland	3.2	3.8	2.6	3.9	2.6
Softmart	2.7	1.5	1.7	0.9	1.0
Businessland	2.3	2.2	3.6	2.8	2.8
	<u>\$105.5</u>	<u>\$77.6</u>	<u>\$60.1</u>	<u>\$84.9</u>	<u>\$57.7</u>
Percent of Gross Revenue	<u>78%</u>	<u>74%</u>	<u>73%</u>	<u>81%</u>	<u>69%</u>

Rebates were 5.2% of net revenues (\$6.6 million), versus plan of 5.5% (\$5.6 million). The percentage variance is due to the fact that actual sales mix was shifted slightly more towards Distributors, which have lower rebates, than was anticipated in the plan. Distributors and Franchisors may earn rebates by maintaining a 30-day stocking level for 28 key Microsoft products, thus attempting to ensure an adequate supply of Microsoft product in the sales channel. Rebates for LVRs and Major Chains are earned primarily by attaining a predetermined internal market share for specific products based on sell-through (versus

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competitive products) for the individual reseller. This is designed to generate a consistent sell-through of product (not sell-in), striving to prevent excessive inventories.

Cost of revenues, as a percentage of net revenues, was 22.4% compared to plan of 24.1%. Actual cost of revenues consisted of 18.9% product costs, 0.5% royalties and 3.0% allocation of manufacturing and distribution costs; whereas budgeted cost of revenues consisted of 18.2% product costs, 0.7% royalties and 5.2% allocations. The gross margin for Q91-1 was 77.6% compared to plan of 75.9%. USSMD's gross profit margin for the last five quarters follows:

Q91-1	77.6%
Q90-4	76.6%
Q90-3	72.1%
Q90-2	73.9%
Q90-1	70.6%

Product costs were 18.9% versus plan of 18.2%. This unfavorable variance is primarily due to product mix. SPAG, which has the highest product costs, represented 19.0% of USSMD's gross revenue versus plan of 13.3%. In addition, Applications experienced unfavorable product cost variance. As the table below illustrates, Applications had a composite product cost 11.8%, compared to plan of 11.0%.

	Actual			Budget		
	Sales Mix %	Cost %	Weighted Cost %	Sales Mix %	Cost %	Weighted Cost %
Applications	60.1%	11.8%	7.1%	61.6%	11.0%	6.8%
SPAG	19.0	34.7	6.6	13.3	35.6	4.7
Languages	5.5	14.4	0.8	5.3	15.1	0.8
Multimedia	0.0	10.5	0.0	0.1	15.2	0.0
Systems	<u>15.4</u>	22.0	<u>3.4</u>	<u>19.8</u>	24.6	<u>4.9</u>
Product Cost - Gross	<u>100.0%</u>		17.9	<u>100.0%</u>		17.2
Effect of Adjustments			x 105.6			x 106.0
Product Cost - Net			<u>18.9%</u>			<u>18.2%</u>

Applications' product costs were 11.8% of revenue compared to plan of 11.0%. This variance is due to a combination of lower than forecasted revenues for the high margin MLPs, higher than planned revenue from the education channel (including deeply discounted IBM ACIS revenue), and unbudgeted revenue from the relatively lower margin Works/Mouse bundle. SPAG product costs were 34.7% of revenue compared to plan of 35.6%. This favorable variance is primarily due to slightly lower than planned product costs on all Mouse products and sales mix, which favored our established SKUs over the lower margin Naked Mouse. Languages' product costs were 14.4% of revenue compared to plan of 15.1%. This favorable variance is primarily due to higher than planned sales of high margin C Compiler. Systems' product costs were 22.0% of revenue compared to plan of 24.6%. This favorable product cost variance is attributable to Windows 3.0 sales mix. Full product revenues experienced higher than planned sales, while the lower margin update revenue was below plan.

Royalty expense of \$656,000, 0.5% of net revenue, was below plan of \$724,000 and 0.7%. The variance is primarily due to lower than planned sales of Mac Works and Flight Simulator. Allocations of manufacturing and distribution costs of 3.0% (\$3.9 million) of net revenues, were well below plan of 5.2% (\$5.2 million). Lower than planned rework and hardware tooling charges, along with favorable inventory

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variances, were responsible for the majority of the favorable variance. The percentage variance also reflects the fact that Campus North's operating expenses are relatively fixed, while revenue exceeded plan by 26%.

Operating expenses of \$33.8 million, 26.4% of net revenues, were \$1.5 million over a planned \$32.3 million, 31.8% of net revenues. Marketing expenditures were \$9.3 million compared to a plan of \$11.3 million. The variance was primarily due to the slippage of planned marketing programs for Word (\$723,000 all platforms), Mail (\$179,000), Works family (\$122,000), Sinker (\$129,000) and smaller variances for several other products. These variances reflect the inherent difficulty in predicting marketing spending and are expected to turn around in future quarters. In order to cushion the effect of this turnaround, and other planned marketing programs, an accrual of \$4.6 million was made in Q91-1. Due to lower than planned headcount, favorable variances also existed in all employee-related expenses.

Allocations to USSMD were \$25.4 million, 19.8% of net revenues, compared to a plan of \$27.2 million, or 26.7% of net revenues. Every expense allocation was under budget with the exception of Legal (\$173,000) and USSMD Sales and Marketing (\$141,000). The Legal variance represents USSMD's allocation of an increase in the litigation reserve. The USSMD allocation was created this year to properly relieve USSMD of expenses incurred for the benefit of the US Networks channel. The variance reflects the fact that USSMD operating expenses which are subject to allocation, were below plan.

For Q91-1, USSMD set a record with burdened operating income of \$40.2 million (31.4% of net revenues) compared to a planned income of \$17.7 million (17.4% of net revenues). Strong Q91-1 sales, lower than planned cost of revenues, operating expenses and allocated expenses (as a percent of net revenue) combined for an extremely profitable first quarter.

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The Q91-1 condensed burdened operating income statement for International Finished Goods follows (in millions):

	Actual		Plan		Variance
	\$	%	\$	%	
Net revenues	\$165.0	100.0%	\$119.1	100.0%	\$45.9
Cost of revenues	39.2	23.8	31.5	26.4	(7.7)
Operating expenses	38.0	23.0	39.1	32.8	1.1
Allocations - Research and development	23.8	14.5	27.7	23.3	3.9
Allocations - Sales and marketing	2.0	1.2	2.3	1.9	0.3
Allocations - General and administrative	1.6	0.9	1.1	1.0	(0.5)
Burdened operating income	\$ 60.4	36.6%	\$ 17.4	14.6%	\$43.0

International Finished Goods revenues by product group for Q91-1 were as follows (in millions):

	Actual		Plan		Variance
	\$	%	\$	%	
Applications	\$ 99.9	60.5%	\$ 81.4	68.4%	\$ 18.5
Systems	37.1	22.5	18.5	15.5	18.6
SPAG	21.7	13.2	13.6	11.4	8.1
Languages	7.7	4.7	6.6	5.6	1.1
Other	0.4	0.2	0.1	0.1	0.3
Adjustments	(1.8)	(1.1)	(1.1)	(1.0)	(0.7)
	\$165.0	100.0%	\$119.1	100.0%	\$45.9

The International Finished Goods channel's leading product families for the quarter were as follows (in millions):

Actual	Plan		Actual		Plan		Revenue Variance	%
			Units	Revenue	Units	Revenue		
1	1	PC Word	66.1	\$22.8	68.6	\$20.4	12	
2	3	Serial/Bus Mouse	187.3	20.3	133.7	12.0	69	
3	2	Win Excel	45.6	18.3	49.6	15.3	19	
4	5	Win 3	159.6	17.1	73.3	7.9	117	
5	4	WinWord	31.4	12.9	29.2	10.0	29	
6	6	Packaged DOS	163.4	9.9	116.1	7.6	31	
7	7	PC Works	80.7	9.4	64.8	7.4	28	
8	-	Win 3 Updates	95.3	6.6	14.1	0.9	605	
9	8	Mac Word	21.9	5.2	19.7	5.0	4	
10	9	Mac Excel	16.3	4.5	19.3	5.0	(10)	
				\$127.0		\$91.5		
		Percent of net revenues		77%		77%		

Plan: #10 PC Multiplan (\$3.0 million)

International Finished Goods activities are primarily those of wholly-owned subsidiaries. Translation of foreign currency denominated financial statements into U.S. Dollars affects comparisons to plan by increasing actual amounts if the U.S. Dollar is weaker than planned and, conversely, by decreasing actual amounts if the U.S. Dollar is stronger than planned. During Q91-1 the U.S. Dollar was weaker than planned against all currencies except the Korean Won.

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The actual (weekly average) rates versus planned exchange rates and the related percentages of variance for Q91-1 are as follows:

Currency	U.S. Dollars per unit of Foreign Currency		
	Actual Rate	Planned Rate	Variance %
British Pound	1.85974	1.66667	11.6
Swedish Krona	.17147	.16287	5.3
Deutsch Mark	.62777	.58480	7.3
Swiss Franc	.74917	.65789	13.9
French Franc	.18728	.17361	7.9
Dutch Guilder	.55725	.52632	5.9
Italian Lira	.00085	.00079	7.6
Spanish Peseta	.01015	.00911	11.4
Canadian Dollar	.86610	.85470	1.3
Korean Won	.00141	.00143	(1.2)
Australian Dollar	.80606	.73500	9.7
Japanese Yen	.00689	.00640	7.7
Irish Pound	1.68530	1.56250	7.9

International Finished Goods Q91-1 net revenues of \$165.0 million were 38% more than a planned \$119.1 million and comprised 45% of the Company's total Q91-1 net revenues. This \$45.9 million favorable variance was the combined result of a \$34.7 million favorable operation variance and a \$11.2 million favorable exchange rate variance. Actual and planned Q91-1 International Finished Goods net revenues of each consolidating unit are shown in the schedule below.

EUROPE	Actual		Plan		Net Operations		Exchange Rate
					Variance	Variance	Variance
MS LTD (England)	\$ 16.8	10.2%	\$ 11.8	9.9%	\$ 5.0	\$ 3.3	\$ 1.7
MS AB (Nordic Region)	12.2	7.4	7.3	6.1	4.9	4.3	0.6
MS GmbH (Germany)	37.7	22.8	26.8	22.5	10.9	8.3	2.6
MS AG (Switzerland)	4.8	2.9	4.2	3.6	0.6	(0.1)	0.7
MS SARL (France)	38.0	23.1	24.2	20.3	13.8	11.1	2.7
MS BV & NV (Benclux)	7.1	4.3	4.9	4.1	2.2	1.8	0.4
MS SPA (Italy)	5.8	3.5	4.4	3.6	1.4	1.1	0.3
MS SRL (Spain)	1.2	0.7	1.2	1.0	--	(0.2)	0.2
	<u>123.6</u>	<u>74.9</u>	<u>84.8</u>	<u>71.1</u>	<u>38.8</u>	<u>29.6</u>	<u>9.2</u>
ICON							
MS INC (Canada)	10.7	6.5	7.9	6.5	2.8	2.6	0.2
Mexico	1.4	0.8	1.5	1.3	(0.1)	(0.1)	--
Brazil	2.2	1.4	2.7	2.3	(0.5)	(0.5)	--
Venezuela	0.2	0.2	0.2	0.2	--	--	--
AIME (Africa/India/Mid East)	1.6	1.0	1.4	1.2	0.2	0.2	--
	<u>16.1</u>	<u>9.9</u>	<u>13.7</u>	<u>11.5</u>	<u>2.4</u>	<u>2.2</u>	<u>0.2</u>
FAR EAST							
MS CH (Korea)	0.6	0.3	0.6	0.5	--	--	--
MS TC (Taiwan)	0.2	0.1	0.9	0.8	(0.7)	(0.7)	--
Redmond Taiwan	0.9	0.6	0.2	0.2	0.7	0.7	--
Asia Pacific	0.6	0.4	0.5	0.4	0.1	0.1	--
Singapore	1.0	0.6	0.6	0.5	0.4	0.4	--
MS PTY (Australia)	13.1	7.9	9.5	8.0	3.6	2.4	1.2
	<u>16.4</u>	<u>9.9</u>	<u>12.3</u>	<u>10.4</u>	<u>4.1</u>	<u>2.9</u>	<u>1.2</u>
MS KK (Japan)	8.2	4.9	8.1	6.8	0.1	(0.5)	0.6
Other Redmond	0.7	0.4	0.2	0.2	0.5	0.5	--
Total Non-Europe	<u>41.4</u>	<u>25.1</u>	<u>34.3</u>	<u>28.9</u>	<u>7.1</u>	<u>5.1</u>	<u>2.0</u>
Total	<u>\$165.0</u>	<u>100.0%</u>	<u>\$119.1</u>	<u>100.0%</u>	<u>\$45.9</u>	<u>\$34.7</u>	<u>\$11.2</u>

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The channel's total cost of revenues was 23.8% of net revenues for Q91-1, compared with a planned 26.4%. As a percentage of net revenues, product costs were 18.3% versus a planned 17.7%. The actual and planned product cost percentages for Q91-1 of the four principal product groups were:

	Actual			Plan		
	Sales Mix %	Cost %	Weighted Cost %	Sales Mix %	Cost %	Weighted Cost %
Applications	59.5%	12.9	7.7%	67.6%	13.0	8.8%
SPAG	13.1	33.6	4.4	11.3	38.4	4.3
Systems	22.3	21.2	4.7	15.4	20.8	3.2
Languages	4.6	23.1	1.1	5.5	19.5	1.1
Other	0.5	40.7	0.2	0.2	94.8	0.1
Product cost - gross	<u>100.0%</u>		<u>18.1%</u>	<u>100.0%</u>		<u>17.5%</u>
Effect of revenue adjustments			<u>x 1.011</u>			<u>x 1.010</u>
Product cost - net			<u>18.3%</u>			<u>17.7%</u>

The overall sales mix of the various product groups had an unfavorable effect on the composite product cost percentage. Basically, the channel experienced a shift in sales mix from Applications, which has the lowest product cost percentage, to Systems and SPAG. On an individual product group basis, SPAG was considerably under plan (33.6% vs. 38.4%), Applications was essentially on plan (12.9% vs. 13.0%), Systems was slightly over plan (21.2% vs. 20.8%), and Languages was fairly significantly over plan (23.1% vs. 19.5%).

As a percentage of net revenues, non product costs (manufacturing variance, inventory adjustments, freight, shipping and other, royalties and allocations from Ireland and Campus North) were under plan by 3.2% (5.5% compared to 8.7%). The significant component was a pick up of 2.4% in manufacturing variance. The planned manufacturing variance was an allowance in the event lower than planned MLP sales skewed product costs upward relative to sales.

International Finished Goods operating expenses in Q91-1 of \$38.0 million, were \$1.1 million less than the planned \$39.1 million. This variance was the combined result of a \$3.6 million favorable operations variance and a \$2.5 million unfavorable exchange rate variance. The actual and planned operating expenses for Q91-1 charged to the channel by the subsidiaries and Corporate headquarters are as follows (in millions):

	Actual	Plan	Net Variance	Operations Variance	Exchange Rate Variance
EUROPE					
MS LTD (England)	\$ 5.0	\$ 4.5	\$ (0.5)	\$ --	\$ (0.5)
MS AB (Nordic Region)	3.1	3.6	0.5	0.7	(0.2)
MS GmbH (Germany)	8.0	8.2	0.2	0.8	(0.6)
MS AG (Switzerland)	1.1	1.6	0.5	0.6	(0.1)
MS SARL (France)	6.6	7.1	0.5	1.0	(0.5)
MS BV & NV (Benelux)	1.6	1.7	0.1	0.2	(0.1)
MS SpA (Italy)	1.1	1.5	0.4	0.5	(0.1)
MS SRL (Spain)	0.6	0.6	--	--	--
	<u>27.1</u>	<u>28.8</u>	<u>1.7</u>	<u>3.8</u>	<u>(2.1)</u>
ICON					
MS INC (Canada)	2.4	2.3	(0.1)	(0.1)	--
Mexico	0.4	0.5	0.1	0.1	--
Brazil	0.9	0.9	--	--	--
Venezuela	--	0.1	0.1	0.1	--
ADME	0.3	0.5	0.2	0.2	--
	<u>4.0</u>	<u>4.3</u>	<u>0.3</u>	<u>0.3</u>	<u>--</u>

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	Actual	Plan	Net Variance	Operations Variance	Exchange Rate Variance
EAREAST					
MS CH (Korea)	0.2	0.3	0.1	0.1	--
MS TC (Taiwan)	0.1	0.3	0.2	0.2	--
Taiwan Redmond	0.1	--	(0.1)	(0.1)	--
Asia Pacific	0.1	0.2	0.1	0.1	--
Singapore	0.1	0.2	0.1	0.1	--
MS PTY (Australia)	<u>2.6</u>	<u>2.4</u>	<u>(0.2)</u>	<u>--</u>	<u>(0.2)</u>
	<u>3.2</u>	<u>3.4</u>	<u>0.2</u>	<u>0.4</u>	<u>(0.2)</u>
MS KK (Japan)	<u>2.4</u>	<u>2.4</u>	<u>--</u>	<u>0.2</u>	<u>(0.2)</u>
Redmond Operations	<u>1.3</u>	<u>0.2</u>	<u>(1.1)</u>	<u>(1.1)</u>	<u>--</u>
Total	<u>\$38.0</u>	<u>\$39.1</u>	<u>\$ 1.1</u>	<u>\$ 3.6</u>	<u>\$(2.5)</u>

General underspending by the European subsidiaries contributed to the \$3.6 million favorable operations variance, as did a \$1.0 million underspending on marketing campaigns. However, a marketing accrual was made during Q91-1 on the Redmond Operations financials to offset the subsidiaries' marketing underspending. The operating expense line items with the largest variances were as follows (in millions):

	Actual	Plan	Variance	Percent
Payroll	\$10.4	\$11.2	\$0.8	7
Market development	0.3	0.9	0.6	67
Travel and entertainment	1.8	2.4	0.6	25
Marketing	11.1	11.7	0.6	5
Marketing accrual	1.0	--	(1.0)	--
Bad debt	1.0	0.7	(0.3)	(43)
All other	<u>12.4</u>	<u>12.2</u>	<u>(0.2)</u>	<u>(2)</u>
	<u>\$38.0</u>	<u>\$39.1</u>	<u>\$1.1</u>	<u>3</u>

Actual allocated expenses were \$27.4 million compared to a plan of \$31.1 million. The most significant contributions were favorable variances from International R&D (localization) of \$1.9 million (\$7.0 million vs. \$8.9 million), Applications development of \$1.0 million (\$11.4 million vs. \$12.4 million), and Systems development of \$455,000 (\$2.6 million vs. \$3.0 million).

The channel's Q91-1 burdened operating income of \$60.4 million was 246% more than a planned \$17.4 million and was 49% of the Company's total burdened operating income. All elements of International Finished Goods' profit model experienced favorable results during Q91-1. Specifically, net revenues exceeded plan by \$45.9 million, cost of revenues as a percentage of net revenues were 23.8% compared with a plan of 26.4%, and both operating expenses and allocated expenses were less than plan (\$1.1 million and \$3.7 million respectively). As a result, burdened operating income of \$60.4 million exceeded plan.

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Domestic OEM

The Q91-1 condensed burdened operating income statement for Domestic OEM follows (in millions):

	Actual		Plan		Variance
Net revenues	\$29.7	100.0%	\$35.1	100.0%	\$(5.4)
Cost of revenues	3.9	13.1	2.4	6.9	(1.5)
Operating expenses	3.4	11.5	3.5	10.0	0.1
Allocations - Research and development	7.2	24.3	8.9	25.4	1.7
Allocations - Sales and marketing	1.1	3.7	1.3	3.5	0.2
Allocations - General and administrative	0.7	2.3	0.4	1.2	(0.3)
Burdened operating income	\$13.4	45.1%	\$18.6	53.0%	\$(5.2)

Domestic OEM revenues by product group for Q91-1 were as follows (in millions):

	Actual		Plan		Variance
Systems	\$26.3	88.5%	\$25.7	73.2%	\$ 0.6
Networks	3.1	10.5	2.7	7.6	0.4
SPAG	3.1	10.3	0.6	1.8	2.4
UPB	2.4	8.1	1.4	4.0	1.0
Xenix	2.2	7.5	2.4	6.8	(.1)
Applications	1.5	5.2	2.2	6.3	(.7)
Languages	0.2	0.5	0.1	0.3	0.1
Subtotal	38.8	130.6	35.1	100.0	3.7
GAAP adjustment	(4.1)	(13.8)	--	--	(4.1)
Prepays adjustment	(5.0)	(16.8)	--	--	(5.0)
Total	\$29.7	100.0%	\$35.1	100.0%	\$(5.4)
Licensing	\$32.0	82.5%	\$30.3	86.3%	\$ 1.7
Packaged product	6.8	17.5	4.8	13.7	2.0
Total (pre-adjustments)	\$38.8	100.0%	\$35.1	100.0%	\$ 3.7

Significant Domestic OEM customers, by product group, for Q91-1 were (in thousands):

						Actual		Plan	
	Systems	Networks	SPAG	UPB	Other				
3Com	\$ 86	\$ 970	\$ --	\$ 1,873	\$ --	\$ 2,929	7.5%	\$ 1,630	4.6%
Zenith	1,523	--	725	485	23	2,756	7.1	2,300	6.6
Compaq	3,808	--	--	(1,338)	--	2,470	6.4	2,434	6.9
SCO	182	62	--	--	1,584	1,828	4.7	2,075	5.9
American Tel & Tel	1,005	359	322	(221)	198	1,663	4.3	913	2.6
AST	1,408	--	170	--	--	1,578	4.1	968	2.8
Unisys	1,203	18	211	(447)	541	1,526	3.9	1,962	5.6
NCR	1,281	91	21	(24)	--	1,369	3.5	1,284	3.7
Compuadd	741	--	--	423	--	1,164	3.0	1,163	3.3
Phoenix	1,124	--	--	--	6	1,130	2.9	1,000	2.9
Tandon	938	--	98	40	--	1,076	2.8	1,000	2.9
Northgate Comp.	745	--	308	14	--	1,067	2.7	396	1.1
Gateway 2000	--	--	587	472	--	1,059	2.7	834	2.4
Tandy	979	--	44	--	15	1,038	2.7	900	2.6
Commodore	697	--	25	39	195	956	2.5	1,009	2.9
Dell	701	--	19	95	6	821	2.1	790	2.2
Other Customers	9,842	1,632	534	996	1,378	14,382	37.1	14,408	41.0
Total	\$26,263	\$3,132	\$3,064	\$2,407	\$3,946	\$38,812	100.0%	\$35,066	100.0%

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Domestic OEM

Domestic OEM net revenues of \$29.7 million were 15% below the planned \$35.1 million due to the impact of the GAAP adjustment (negative \$4.1 million) and the establishment of a \$5 million reserve for possible contractual adjustments related to prepaid balances. Such adjustments are not budgeted. Absent these adjustments totalling \$9.1 million, revenues of \$38.8 million were 11% above the budgeted \$35.1 million, with licensing revenues 106% of plan and packaged product revenues 141% of plan. The top 10 customers generated 47% of unadjusted revenue for the quarter.

Revenue from the Systems product group (\$26.3 million) accounted for 68% of unadjusted revenue. Licensing and sale of MS-DOS/Shell (\$21.8 million) generated 83% of the Systems revenue, with the remainder resulting from Windows (\$2.7 million), OS/2 (\$1.7 million), and Printer Systems (\$122,000). Network product revenue (\$3.1 million), primarily LAN Manager, gave rise to 8% of unadjusted revenue, and mouse sales (\$3.1 million) generated an additional 8%. The remainder of the revenue resulted primarily from unspecified product billings (\$2.4 million) and royalties from Xenix (\$2.2 million) and Applications (\$1.5 million).

- **3 Com** - Generated revenues of \$2.9 million resulting from a minimum commitment billing. 3 Com reported \$941,000 of LAN Manager against a budget of \$905,000 during Q91-1. However, its prepaid balance continues to build (currently \$8.2 million), a situation that will be remedied when an amendment is signed during Q91-2. This amendment will reduce the Q91-1 minimum commitment by \$2.3 million (see "GAAP adjustment" discussion) and significantly lower future minimum commitments.
- **Zenith** - Had a favorable variance of \$456,000 as a result of strong packaged mouse sales (\$613,000 against a budget of \$150,000).
- **Compaq** - Revenues of \$2.5 million were at plan. MS-DOS royalties continue to ramp steadily each quarter and resulted in revenues of \$3.6 million against a plan of \$2.4 million. However, Compaq was able to recoup its OS/2 prepaid balance against MS-DOS royalties in excess of \$2.5 million for the quarter. The favorable MS-DOS variance was further offset by slow OS/2 sales (\$179,000 against a plan of \$400,000). Compaq's current prepaid balance is \$3.3 million.
- **SCO** - Had a \$247,000 shortfall resulting from below-budget sales of Xenix (\$417,000), partially offset by \$144,000 in unbudgeted applications revenue.
- **American Telephone & Telegraph** - The agreement covering sales of product to the FAA that had been anticipated to be executed this quarter has again been delayed and is expected to be signed in Q91-2. However, strong sales of virtually all products licensed under other agreements resulted in a favorable variance of \$750,000. This includes \$322,000 of unbudgeted mouse sales.
- **AST** - The favorable variance reflects greater than planned royalties for MS-DOS (\$1.3 million versus \$922,000) and unbudgeted sales of mice (\$170,000).
- **Unisys** - Had actual revenues of \$1.5 million against a plan of \$2 million, primarily as a result of its MS Office applications bundle selling 1,200 units against a plan of 3,300 units. Windows royalties of \$468,000 were also below the planned \$600,000.
- **NCR** - Reported MS-DOS royalties of \$1.2 million, \$385,000 over plan. However, as the result of an amendment, \$319,000 of this excess was applied to decrease their OS/2 prepaid balance. Consequently, net revenue for NCR of \$1.4 million approximated plan.
- **Compuadd** - Revenues equalled budget. Compuadd began shipping Windows 3.0 this quarter.
- **Phoenix** - MS-DOS royalties of \$1.1 million caused Phoenix to do slightly better than the budgeted \$1 million. After a downturn in sales resulting from a restructuring and move, Phoenix appears to have regained its marketshare.
- **Northgate Computer** - Generated revenue of \$1.1 million against a budget of \$396,000. Primary components of the variance were unbudgeted sales of Windows (\$363,000) and mice (\$308,000), partially offset by unfavorable variances in OS/2 (\$45,000) and MS-DOS (\$94,000).

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- Gateway 2000 - The \$225,000 favorable variance resulted from unbudgeted revenues from mouse sales (\$587,000) and a minimum commitment (\$601,000) for a new agreement, partially offset by an unfavorable variance for MS-DOS and Windows (\$963,000) due to late royalty reports.
- IBM - Had a budget shortfall of \$332,000 that resulted from late reporting of MS Works (\$279,000), C Compiler (\$57,000), and LAN Manager (\$33,000), partially offset by a \$35,000 favorable variance in OS/2 revenues.
- Supercom - Revenues from Packaged MS-DOS were below budget (\$505,000 versus \$900,000). OEMs selling packaged MS-DOS have been negatively impacted by counterfeit DOS in the marketplace as their customers are opting to obtain DOS from other, less expensive, sources.
- Zeos - An unbudgeted minimum commitment (\$463,000) under a new agreement and unbudgeted sales of packaged mice (\$222,000) caused a favorable variance, despite lower sales of MS-DOS/Shell (\$93,000 versus \$463,000)

The GAAP adjustment is an accrual for royalties earned during the quarter, but not yet reported, net of deferred revenue relating to product that has not yet been accepted by the customer. Our accrual is based upon past experience and current trends. This quarter's adjustment of negative \$4.1 million represents the impact of a \$2.3 million credit tied to the forthcoming 3 Com amendment and Compaq's ability to recoup its OS/2 prepaid balance against MS-DOS royalties. Deferred revenues increased \$100,000.

Unspecified Product Billing (UPB) of \$2.4 million represents due on signing and minimum commitment billings in excess of product-specific revenue. Significant due on signing amounts related to new agreements for the quarter were DAK Industries (\$350,000 - Windows 3.0), Memorex Telex (\$350,000 - MS-DOS/Shell), The Software Toolworks (\$300,000 - Business Consultant, Bookshelf, Stat Pack), Positive Corporation (\$120,000 - Windows 3.0), and Future Domain (\$62,500 - MS-DOS, CD ROM Extension).

When UPB is greater than reported royalties on an agreement, the excess represents prepaid royalties which may be recouped through future royalties. Thus, to the extent that a prepaid balance exists under an agreement, future royalties reported by the customer will not result in additional revenue to Microsoft. This "prepaid" balance does not represent a liability to Microsoft, however, because once product has been delivered and accepted by the customer, Microsoft has fulfilled its obligations under the agreement. At the end of Q91-1, the prepaid balance for Domestic OEM customers was approximately \$48.6 million, unchanged from Q90-4. A \$5 million reserve for potential future concessions related to these prepaid balances was established this quarter. The Domestic OEM net prepaid balance of approximately \$43.6 million therefore declined by approximately \$5 million during the quarter.

The ten largest Domestic OEM prepaid balances at the end of Q91-1 were (in millions):

3Com	\$ 8.2
Zenith	5.1
NCR	4.1
Compaq	3.3
Sun Microsystems	2.4
Headstart Technologies	1.9
Televideo	1.7
Compuadd	1.6
IBM	1.5
Idea Courier	1.1
	<u>\$30.9</u>

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Cost of revenues (\$3.9 million against a plan of \$2.4 million) was unfavorably impacted by packaged mouse sales above plan (137,000 units versus 21,000) and by a shift in sales mix to a higher percentage of packaged product (18% against 14%). Mouse sales have been far stronger than plan due to bundling with Windows 3.0. The unfavorable variance was partially offset by a favorable variance in royalty expense of \$278,000, due to overall lower Xenix and OS/2 volume.

Operating expenses of \$3.4 million approximated budget. There were no significant variances from plan. Allocated expenses were \$1.5 million below plan due to favorable variances in all areas but Legal (\$297,000 resulting from an accrual to the litigation reserve), with the most significant favorable variance coming from the Systems development pool (\$1 million).

In summary, the unfavorable impact of revenue adjustments and increased cost of revenues associated with the higher mix of packaged product revenue outweighed favorable variances in operating expenses and allocations, producing a burdened operating income of \$13.4 million, 28% below the plan of \$18.6 million.

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International OEM

The Q91-1 condensed burdened operating income statement for International OEM follows (in millions):

	Actual		Plan		Variance
Net revenues	\$38.0	100.0%	\$38.2	100.0%	\$ (0.2)
Cost of revenues	0.3	0.7	0.3	0.7	--
Operating expenses	3.8	10.1	3.8	10.1	--
Allocations - Research and development	9.0	23.7	10.9	28.5	1.9
Allocations - Sales and marketing	0.6	1.5	0.7	1.7	0.1
Allocations - General and administrative	0.4	1.1	0.3	0.9	(0.1)
Burdened operating income	<u>\$23.9</u>	<u>62.9%</u>	<u>\$22.2</u>	<u>58.1%</u>	<u>\$1.7</u>

The contribution (actual and plan) to International OEM net revenues by consolidating unit for Q91-1 follows (in thousands):

	Actual		Plan		Variance
EUROPE					
MS LTD (England)	\$ 3,551	9.3%	\$ 1,633	4.3%	\$ 1,918
MS AB (Nordic Region)	3,086	8.1	1,759	4.6	1,327
MS GmbH (Germany)	2,227	5.9	3,936	10.3	(1,709)
MS AG (Switzerland)	3	--	--	--	3
MS SARL (France)	643	1.7	876	2.3	(233)
MS SRL (Spain)	41	0.1	131	0.3	(90)
MS BV (Netherlands)	2,039	5.4	569	1.5	1,470
MS SpA (Italy)	<u>3,164</u>	<u>8.3</u>	<u>3,132</u>	<u>8.2</u>	<u>32</u>
	<u>14,754</u>	<u>38.8</u>	<u>12,036</u>	<u>31.5</u>	<u>2,718</u>
ICON					
MS INC (Canada)	208	0.5	227	0.6	(19)
Mexico	383	1.0	379	1.0	4
Brazil	434	1.2	392	1.0	42
AIME (Africa/India/Mid-East)	<u>226</u>	<u>0.6</u>	<u>145</u>	<u>0.4</u>	<u>81</u>
	<u>1,251</u>	<u>3.3</u>	<u>1,143</u>	<u>3.0</u>	<u>108</u>
FAR EAST					
MS CH (Korea)	5,663	14.8	4,813	12.6	850
MS TC (Taiwan)	4,239	11.2	4,414	11.6	(175)
ASIA Pacific	705	1.9	562	1.5	143
MS PTE (Singapore)	191	0.5	56	0.1	135
MS PTY	<u>45</u>	<u>0.1</u>	<u>111</u>	<u>0.3</u>	<u>(66)</u>
	<u>10,843</u>	<u>28.5</u>	<u>9,956</u>	<u>26.1</u>	<u>887</u>
MS KK (Japan)	<u>8,723</u>	<u>23.0</u>	<u>14,363</u>	<u>37.6</u>	<u>(5,640)</u>
Other Redmond	<u>833</u>	<u>2.2</u>	<u>700</u>	<u>1.8</u>	<u>133</u>
Total Non-Europe	<u>21,650</u>	<u>57.0</u>	<u>26,162</u>	<u>68.5</u>	<u>4,512</u>
Subtotal	36,404	95.8	38,198	100.0	(1,794)
CAAP adjustment	4,100	10.8	--	--	4,100
Prepays adjustment	<u>(2,500)</u>	<u>(6.6)</u>	<u>--</u>	<u>--</u>	<u>(2,500)</u>
Total	<u>\$38,004</u>	<u>100.0%</u>	<u>\$38,198</u>	<u>100.0%</u>	<u>\$ (194)</u>

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International OEM

International OEM revenues by product group for Q91-1 were as follows (in thousands):

	Actual		Plan		Variance
Systems	\$32,204	84.7%	\$36,383	95.3%	\$ (4,179)
UPB	2,029	5.3	540	1.4	1,489
Applications	1,143	3.0	552	1.4	591
Networks	712	1.9	690	1.8	22
Xenix	182	0.5	3	--	179
Multimedia	105	0.3	--	--	105
Languages	29	0.1	22	0.1	7
SPAG	--	--	8	--	(8)
Subtotal	36,404	95.8	38,198	100.0	(1,794)
GAAP adjustment	4,100	10.8	--	--	4,100
Prepays adjustment	(2,500)	(6.6)	--	--	(2,500)
Total	\$38,004	100.0%	\$38,198	100.0%	\$ (194)

Significant International OEM customers, by product group, for Q91-1 were (in thousands):

	Product Group					Actual		Plan	
	Systems	UPB	Apps	Networks	Other				
Nokia Data	\$ --	\$ 3,012	\$ --	\$ --	\$ --	\$ 3,012	8.3%	\$ 1,173	3.5%
Olivetti SpA	3,006	(661)	14	293	--	2,652	7.3	2,600	7.9
Fujiitsu LTD	554	1,774	100	10	61	2,499	6.9	2,501	7.6
Tulip	--	1,950	--	--	--	1,950	5.4	525	1.6
Epson Corp.	1,126	400	24	--	--	1,550	4.3	2,842	8.6
NEC	1,704	(170)	--	2	13	1,549	4.3	2,641	8.0
Samsung Elec.	715	553	--	--	--	1,268	3.5	1,250	3.8
Toshiba Corp.	5,557	(4,322)	--	--	--	1,235	3.4	2,304	7.0
Gold Star	464	731	--	--	--	1,195	3.3	1,125	3.4
Apricot	--	1,012	--	--	--	1,012	2.8	360	1.1
Tatung	532	468	--	--	--	1,000	2.7	1,125	3.4
Hyundai Elec.	851	74	--	--	--	925	2.5	925	2.8
Research Machines	519	140	13	229	--	901	2.5	350	1.1
Siemens AG	1,091	(460)	--	18	174	823	2.3	692	2.1
Datech Enter.	956	(184)	--	--	--	772	2.1	525	1.6
Philips Elec.	--	708	--	--	--	708	1.9	700	2.1
Copam Elec.	1,585	(1,224)	321	--	--	682	1.9	829	2.5
Daewoo Telecom	535	143	--	--	--	678	1.9	650	2.0
Daewoo Elect.	800	(220)	--	--	--	580	1.6	--	--
Viglen Limited	180	377	--	--	--	557	1.5	--	--
Other Customers	12,029	(2,072)	671	160	68	10,856	29.6	15,081	29.9
Total	\$32,204	\$ 2,029	\$1,143	\$712	\$316	\$36,404	100.0%	\$38,198	100.0%

International OEM revenue, with adjustments, of \$38 million for the quarter was essentially at plan. Adjustments of \$1.6 million resulted from a positive GAAP revenue accrual (\$4.1 million) offset by an increase of \$2.5 million in a reserve for potential future contractual concessions related to prepaid balances. The top 10 customers accounted for 49% of unadjusted revenues.

Europe had revenues of \$14.8 million, 23% greater than the budgeted \$12 million, partially as a result of a retroactive billing tied to a new Nokia agreement. ICON (\$1.3 million versus \$1.1 million) and the Far East (\$10.8 million versus \$10 million) each came in just over plan, with MS CH as the primary contributor to the Far East variance. For FY91, MS KK has been separated from the Far East for reporting purposes. Japan's \$5.6 million shortfall (\$8.7 million compared to \$14.4 million) is primarily the result of slower sales of low-end machines by Epson (\$1.3 million) and NEC (\$1.1 million), less new business than was budgeted (\$1.5 million), and an unbudgeted prepaid balance recoupment for Toshiba (\$1.1 million).

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International OEM

Systems products (\$32.2 million) were responsible for 89% of unadjusted revenues. Licensing of MS-DOS/Shell (\$29.3 million) accounted for 91% of Systems revenue, with the remaining Systems revenue resulting from licensing of Windows (\$2.1 million), OS/2 (\$496,000) and Printer Systems (\$258,000). Unspecified Product Billings (UPB) of \$2 million generated another 6% of revenue (down from 17% of revenue in Q90-4), and Applications products accounted for another 3%, primarily from the sale of MS Works. The remaining 2% of revenues stemmed from sale of Networks products, primarily MS Networks. Revenues from the Language, Multimedia, and Xenix product groups were negligible.

- **Nokia** - Became the top customer in Q91-1 due to the signing of a new agreement in September. This retroactive agreement resulted in billing of a due on signing and two minimum commitments of \$1 million each.
- **Olivetti** - Reported royalties of \$3.3 million against a budget of \$2.1 million, primarily for MS-DOS, due to strong shipments of its PCS 286 computer into the home market.
- **Fujitsu** - Revenue of \$2.5 million resulted from a budgeted minimum commitment. Fujitsu's prepaid balance was \$13.9 million at quarter-end.
- **Tulip** - Execution of a retroactive agreement resulted in the billing of three minimum commitment payments for a total of \$2 million. Royalty reports for the related three quarters have not yet been received.
- **Epson** - Contributed \$1.6 million in revenues against a plan of \$2.8 million. The \$1.2 million shortfall resulted from significantly lower royalties relating to MS-DOS and GW BASIC (200,000 units reported for \$1.1 million against a plan of 697,000 units for \$2.9 million), partially offset by an unbudgeted due on signing and minimum commitment for Truelmage (\$400,000). Epson has experienced a sharp decline in its low-end computer market.
- **NFC** - Also reported significantly lower shipments of MS-DOS (141,000 units versus 491,000 units), resulting in a budget shortfall of \$1.1 million.
- **Samsung** - Revenues from this OEM were at plan, resulting from MS-DOS sales slightly below plan (63,000 units for \$697,000 against a plan of 79,000 units for \$864,000) offset by UPB slightly above plan.
- **Toshiba** - Receipt of two quarters of royalty reports during Q91-1 resulted in \$5.6 million in Systems revenues being recognized this quarter (primarily MS-DOS/Shell). However, a Q90-4 amendment added \$2 million to the prepaid balance, resulting in Toshiba's actual revenue, net of recoupment, coming in \$1.1 million below plan. Toshiba's \$4.3 prepaid balance as of Q90-4 was totally recouped by Q91-1 royalties.
- **Apricot** - A retroactive agreement executed this quarter resulted in billing two \$500,000 minimum commitments.
- **Research Machines** - Had a \$551,000 favorable variance due to catch-up billing of three minimum commitments and royalty reports upon execution of a new retroactive agreement.
- **Datatech** - A new agreement resulted in a \$248,000 unbudgeted due on signing.
- **Daewoo Electronics** - Had a \$580,000 variance resulting from an unbudgeted minimum commitment.
- **Violen** - Signed a new agreement that resulted in \$556,800 in unbudgeted minimum commitments.
- **Other Items** - Agreements that had been budgeted but not executed resulted in unfavorable variances for **Datatronix** (\$544,000) and **Schneider Rundfunkwerke** (\$2 million).

The GAAP adjustment is an accrual for royalties earned during the quarter but not yet reported, net of deferred revenue relating to product that has not yet been accepted. This quarter's adjustment of \$4.1 million reflects a decrease in deferred revenue as product was accepted. The accrual for earned but unreported royalties remained unchanged from Q90-4.

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International OEM

Unspecified Product Billings (UPB) of \$2 million reflects due on signing and minimum commitment billings in excess of product-specific revenue. Significant due on signing amounts related to new agreements for the quarter included Nokia (\$1 million - MS-DOS/Windows), Autocomputer (\$270,000 - MS-DOS/MS-DOS ROM) Amstrad (\$250,000 - MS-DOS), Datatech (\$248,000 - Windows), Epson (\$200,000 - True Image), Singapore Technology (\$135,000 - MS-DOS/Shell) Technology Research (\$122,000 - MS-DOS/Shell), Foruno Electric (\$120,000 - MS-DOS) and Kanematsu (\$104,000 - MS-DOS ROM).

When UPB is greater than reported royalties on an agreement, the excess represents prepaid royalties which may be recouped through future royalties. Thus, to the extent that a prepaid balance exists under an agreement, future royalties reported by the customer will not result in additional revenue to Microsoft. This "prepaid" balance does not represent a liability to Microsoft, however, since once product has been delivered to and accepted by the customer, Microsoft has fulfilled its obligations under the agreement. At the end of Q91-1, total prepaid balance for International OEM customers was approximately \$115 million, an increase of \$3 million from Q90-4. A reserve to allow for possible contractual adjustments related to prepaid balances was increased from \$10.5 million to \$13 million. The International OEM net prepaid balance of approximately \$102 million was therefore essentially unchanged quarter over quarter.

The ten largest International OEM prepaid balances at the end of Q91-1 were (in millions):

Fujitsu (Japan)	\$13.9
Acer (Taiwan)	6.8
Hitachi (Japan)	5.3
Sanyo (Japan)	4.7
Samsung Electronics (Korea)	4.3
Tatung (Taiwan)	3.9
Copart (Taiwan)	3.8
Matsushita Electric (Japan)	3.5
Gold Star (Korea)	3.1
Philips Electronics (Netherlands)	3.1
	<u>\$52.4</u>

Total cost of revenues of \$262,000 equalled plan. Actual cost of revenues included an unbudgeted \$61,000 for camera ready copy. However, this was offset by a net savings in royalty expense which stemmed from lower OS/2 volume.

Operating expenses of \$3.8 million were also at plan. Unfavorable variances in most categories (most notably \$174,000 in payroll) were offset by a favorable marketing variance (\$242,000). Allocated expenses were under plan in all areas except Legal (unfavorable \$74,000 resulting from an accrual to the litigation reserve). The most significant favorable variances occurred in Systems and Localization development pools (\$1.3 million and \$394,000, respectively).

In summary, burdened operating income was \$23.9 million (63% of revenues) against a plan of \$22.2 million (58% of revenues) for a favorable \$1.7 million variance. This resulted from the favorable impact of the GAAP accrual and lower allocated expenses.

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Other Channels

Q91-1 condensed burdened operating income statements for "Other" channels follows (in millions):

ACTUAL	US Net	Intl Net	Press	WW PSS	WW MSU	MSI	WW ITIS	Total
Net revenues	\$ 0.6	\$ 0.2	\$4.4	\$ 1.3	\$ 1.8	\$ 0.2	\$ 0.1	\$ 8.6
Cost of revenues	0.6	--	2.1	0.5	0.4	0.2	--	3.8
Operating expenses	3.9	1.2	0.8	1.1	1.6	0.3	0.6	9.5
Allocated expenses	4.9	2.3	1.1	1.6	--	0.2	0.1	10.2
Operating income (loss)	<u>\$ (8.8)</u>	<u>\$ (3.3)</u>	<u>\$ 0.4</u>	<u>\$ (1.9)</u>	<u>\$ (0.2)</u>	<u>\$ (0.5)</u>	<u>\$ (0.6)</u>	<u>\$ (14.9)</u>
PLAN								
Net revenues	\$ 1.4	\$ 0.2	\$5.1	\$ 0.9	\$ 2.1	\$ 0.4	\$ 0.3	\$ 10.4
Cost of revenues	0.5	0.1	2.4	0.3	0.3	0.2	--	3.8
Operating expenses	4.3	2.9	1.0	0.6	2.5	0.2	1.1	12.6
Allocated expenses	6.1	2.1	1.2	2.0	(0.6)	0.2	0.1	12.1
Operating income (loss)	<u>\$ (9.5)</u>	<u>\$ (5.9)</u>	<u>\$ 0.5</u>	<u>\$ (2.0)</u>	<u>\$ (0.1)</u>	<u>\$ (0.2)</u>	<u>\$ (0.9)</u>	<u>\$ (18.1)</u>
VARIANCE								
Net revenues	\$ (0.8)	\$ --	\$ (0.7)	\$ 0.4	\$ (0.3)	\$ (0.2)	\$ (0.2)	\$ (1.8)
Cost of revenues	(0.1)	0.1	0.3	(0.2)	(0.1)	--	--	--
Operating expenses	0.4	1.7	0.2	(0.5)	0.9	(0.1)	0.5	3.1
Allocated expenses	1.2	0.8	0.1	0.4	(0.6)	--	--	1.9
Operating income (loss)	<u>\$ 0.7</u>	<u>\$ 2.6</u>	<u>\$ (0.1)</u>	<u>\$ 0.1</u>	<u>\$ (0.1)</u>	<u>\$ (0.3)</u>	<u>\$ 0.3</u>	<u>\$ 3.2</u>

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US Networks Channel

The Q91-1 condensed burdened operating income statement for US Networks Channel follows (in thousands):

	Actual		Plan		Variance
Net revenues	\$ 581	100.0%	\$ 1,430	100.0%	\$(849)
Cost of revenues	597	102.9	556	38.9	(41)
Operating expenses	3,866	665.8	4,266	298.3	400
Allocations - Research and development	3,830	659.6	4,551	318.2	721
Allocations - Sales and marketing	746	128.5	1,250	87.3	504
Allocations - General and administrative	290	49.7	281	19.7	(9)
Burdened operating income (loss)	<u>\$(8,748)</u>	<u>(1,506.5)%</u>	<u>\$(9,474)</u>	<u>(662.4)%</u>	<u>\$ 726</u>

In terms of gross revenue generation, the channel's revenue by product for the quarter were as follows (dollars in thousands):

	Actual		Plan		Variance
	Units	Revenue	Units	Revenue	
LAN Manager	274	\$284	1,394	\$1,031	\$(747)
SQL Server	261	272	432	474	(202)
SQL Updates	215	42	86	26	16
Other	36	2	--	--	2
Adjustments		(19)		(10)	82
		<u>\$581</u>		<u>\$1,430</u>	<u>\$ 849</u>

Net revenues for Q91-1 at \$581,000 were \$849,000 less than a planned \$1.4 million. US Network revenues were negatively impacted by the delayed announcement and distribution of LAN Manager 2.0. Q91-1 results reflect the initial startup of the U.S Network channel, which has progressed more slowly than anticipated in both revenues and expenses.

Revenue shortfalls resulted in cost of revenues of 102.9% of net revenues compared to a budget of 38.9%. Product costs were 8.5% of net revenues, versus plan of 8.0%. Non-product costs were \$548,000 (94.4% of net revenues) versus plan of \$442,000 (30.9%). The variance is primarily due to unfavorable purchase price variances relating to the initial builds of packaged product and the unbudgeted amortization of license fees, which are included in royalty expense.

Operating expenses of \$3.9 million, were \$400,000 less than a planned \$4.3 million. The expense line items with the largest absolute Q91-1 variances follows (in thousands):

	Actual	Plan	Variance
Marketing expenditures	\$2,165	\$1,819	\$(346)
Travel and entertainment	193	382	189
Employee recruiting	5	136	131
Employee fringes	9	100	91
Payroll	1,086	1,176	90
All other	<u>408</u>	<u>653</u>	<u>245</u>
	<u>\$3,866</u>	<u>\$4,266</u>	<u>\$ 400</u>

Marketing expenditures were \$2.2 million compared to a plan of \$1.8 million. Unfavorable variances in trade shows (\$625,000) and public relations (\$276,000) were partially offset by lower than planned expenditures on marketing materials (\$546,000). Employee-related expenses are less than budget due to slower than planned hiring. Actual headcount at the end of September was 77 versus a planned 92.

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US Networks Channel

Allocated expenses of \$4.9 million were \$1.2 million less than a planned \$6.1 million. Network research and development allocations were \$721,000 below plan. Sales and marketing allocations were also below plan (\$504,000), primarily due to US MSU and USSMD which were below plan by \$424,000 and \$89,000 respectively. The US MSU allocation represents MSU costs being incurred to train both the Microsoft Authorized Network Specialists and our own employees. The lower costs are due to a slower than anticipated ramping of these activities.

For Q91-1, US Networks had a burdened operating loss of \$8.7 million compared to a planned loss of \$9.5 million. Despite the significant revenue shortfall, lower than anticipated allocations and operating expenditures resulted in a burdened operating income loss which was \$700,000 lower than plan.

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Finance
Product Group / Business Unit Reporting

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PRODUCT GROUP/BUSINESS UNIT REPORTING

The contribution to net revenues and operating income for Q91-1 on a product group basis was as follows (amounts in thousands):

	Actual		Plan		Variance Percentage
	Amount	Percentage	Amount	Percentage	
Net Revenues					
Applications	\$177.9	48.2%	\$146.0	48.0%	22
Systems	116.4	31.5	101.2	33.2	15
SPAG	49.2	13.3	27.4	9.0	80
Languages	14.7	4.0	12.0	3.9	23
Networks	4.8	1.3	5.0	1.7	(4)
Other	6.4	1.7	12.9	4.2	(50)
Total	<u>\$369.4</u>	<u>100.0%</u>	<u>\$304.5</u>	<u>100.0%</u>	21

	Actual			Plan			Variance
	Income (Loss)	Percentage		Income (Loss)	Percentage		
		Total	Revenue		Total	Revenue	
Operating Income (Loss)							
Applications	\$ 57.4	46.7	32.3	\$23.3	40.3	16.0	\$34.1
Systems	61.6	50.1	52.9	47.0	81.3	46.5	14.6
SPAG	19.0	15.4	38.7	5.1	8.9	18.6	13.9
Languages	2.8	2.3	19.0	--	--	(0.4)	2.8
Networks	(10.6)	(8.6)	--	(14.8)	(25.6)	(296.8)	4.2
Other	(7.2)	(5.9)	--	(2.8)	(4.8)	(21.0)	(4.4)
Total	<u>\$123.0</u>	<u>100.0</u>	<u>33.3</u>	<u>\$57.8</u>	<u>100.0</u>	<u>19.0</u>	<u>\$65.2</u>

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Product Group / Business Unit Reporting

Quarterly revenue by product group/business unit for the past three plus years is as follows (in millions):

	Q91-1		Q91-2		Q91-3		Q91-4		FY 1991	
	Dollars	Percent	Dollars	Percent	Dollars	Percent	Dollars	Percent	Dollars	Percent
Applications	177.9	48.2							177.9	48.2
Systems	116.4	31.5							116.4	31.5
SPAG	49.2	13.3							49.2	13.3
Languages	14.7	4.0							14.7	4.0
Network	4.8	1.3							4.8	1.3
Other	6.4	1.7							6.4	1.7
	<u>369.4</u>	<u>100.0</u>							<u>369.4</u>	<u>100.0</u>

	Q90-1		Q90-2		Q90-3		Q90-4		FY 1990	
	Dollars	Percent	Dollars	Percent	Dollars	Percent	Dollars	Percent	Dollars	Percent
Applications	106.4	45.3	153.2	51.0	158.1	50.9	145.2	43.1	563.0	47.6
Systems	75.2	32.0	79.3	26.4	87.4	28.1	123.0	36.5	365.0	30.8
SPAG	25.3	10.8	35.7	11.9	33.2	10.7	35.1	10.4	129.4	10.9
Languages	13.0	5.5	13.1	4.4	11.5	3.7	17.0	5.0	54.5	4.6
Network	7.7	3.3	10.0	3.3	11.2	3.6	5.6	1.7	34.5	2.9
Other	7.6	3.2	9.1	3.0	9.4	3.0	11.1	3.3	37.2	3.1
	<u>235.2</u>	<u>100.0</u>	<u>300.4</u>	<u>100.0</u>	<u>310.9</u>	<u>100.0</u>	<u>337.0</u>	<u>100.0</u>	<u>1,183.4</u>	<u>100.0</u>

	Q89-1		Q89-2		Q89-3		Q89-4		FY 1989	
	Dollars	Percent	Dollars	Percent	Dollars	Percent	Dollars	Percent	Dollars	Percent
Applications	72.1	40.8	86.2	41.1	77.3	39.2	105.3	47.8	340.9	42.4
Systems	59.0	33.4	70.9	33.8	73.6	37.3	75.9	34.5	279.3	34.8
SPAG	20.5	11.6	30.1	14.3	22.0	11.2	19.0	8.6	91.5	11.4
Languages	16.0	9.1	13.6	6.5	10.1	5.1	8.7	4.0	48.5	6.0
Network	1.1	0.6	1.6	0.7	3.6	1.8	3.4	1.5	9.6	1.2
Other	7.8	4.4	7.5	3.6	10.5	5.3	7.9	3.6	33.7	4.2
	<u>176.4</u>	<u>100.0</u>	<u>209.9</u>	<u>100.0</u>	<u>197.0</u>	<u>100.0</u>	<u>220.2</u>	<u>100.0</u>	<u>803.5</u>	<u>100.0</u>

	Q88-1		Q88-2		Q88-3		Q88-4		FY 1988	
	Dollars	Percent	Dollars	Percent	Dollars	Percent	Dollars	Percent	Dollars	Percent
Applications	40.3	39.3	61.4	39.4	63.4	39.2	71.2	41.8	236.3	40.0
Systems	37.3	36.3	56.0	35.9	55.8	34.5	56.3	33.0	205.4	34.8
SPAG	9.7	9.4	15.7	10.1	19.2	11.9	19.7	11.5	64.3	10.9
Languages	9.6	9.4	17.6	11.3	15.4	9.5	15.3	9.0	57.9	9.8
Network	0.3	0.3	0.5	0.3	0.7	0.4	0.7	0.4	2.3	0.4
Other	5.4	5.2	4.8	3.1	7.3	4.5	7.2	4.2	24.7	4.2
	<u>102.6</u>	<u>100.0</u>	<u>155.9</u>	<u>100.0</u>	<u>161.8</u>	<u>100.0</u>	<u>170.5</u>	<u>100.0</u>	<u>290.8</u>	<u>100.0</u>

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Applications

The Q91-1 condensed burdened operating income statement for Applications follows (in millions):

	Actual		Plan		Variance
	\$	%	\$	%	
Net revenues	\$177.9	100.0%	\$146.0	100.0%	\$31.9
Cost of revenues	31.5	17.7	28.9	19.8	(2.6)
Operating expenses	36.3	20.4	40.1	27.5	3.8
Allocations - Research and development	5.6	3.1	6.7	4.6	1.1
Allocations - Sales and marketing	45.3	25.5	45.2	31.0	(0.1)
Allocations - General and administrative	1.8	1.0	1.8	1.1	—
Burdened operating income	\$ 57.4	32.3%	\$ 23.3	16.0%	\$34.1

Applications revenues by channel for Q91-1 were as follows (in millions):

	Actual		Plan		Variance
	\$	%	\$	%	
International Finished Goods	\$99.5	55.9%	\$ 81.4	55.8%	\$18.1
USSMD	81.3	45.7	66.4	45.5	14.9
Domestic OEM	1.5	0.9	2.2	1.5	(0.7)
International OEM	1.1	0.6	0.6	0.4	0.5
Adjustments	(5.5)	(3.1)	(4.6)	(3.2)	(0.9)
Net revenues	\$177.9	100.0%	\$146.0	100.0%	\$31.9

In terms of revenue generation, the division's leading products (compared with plan) for the quarter were as follows (units in thousands, dollars in millions):

Actual	Plan		Actual		Plan		Variance
			Units	Revenue	Units	Revenue	
1	1	Win Excel	121.6	\$ 33.5	106.9	\$ 27.3	\$ 6.2
2	3	Win Word	122.5	29.9	78.1	19.7	10.2
3	2	PC Word	97.6	28.2	105.3	26.5	1.7
4	4	PC Works	216.8	15.2	331.1	13.2	2.0
5	5	Mac Word	75.3	13.4	70.6	12.6	0.8
6	6	Mac Excel	49.7	10.8	57.5	11.9	(1.1)
7	—	Win Project	14.8	6.0	7.0	2.6	3.4
8	7	Mac Office	10.9	5.0	11.9	5.2	(0.2)
9	9	PC Multiplan	36.1	4.4	16.5	3.1	1.3
10	10	Win PowerPoint	15.2	3.9	13.8	2.9	1.0
				\$150.3		\$125.0	\$25.3

Percentage of Applications' net revenues 84% 86%

Plan #8 Mac Works (\$4.3 million)

Applications revenue by environment was as follows (in millions):

	Q91-1		Plan		Q90-4		Q90-3	
	\$	%	\$	%	\$	%	\$	%
Windows	\$ 80.3	43.8%	36.7%	\$ 45.1	30.5%	\$ 43.8	27.0%	
DOS	62.7	34.2	35.8	65.1	44.0	74.1	45.7	
Mac	38.7	21.1	25.7	36.8	24.9	42.1	25.9	
Other	1.2	0.9	1.8	1.0	0.6	2.3	1.4	
	183.4	100.0%	100.0%	148.0	100.0%	162.3	100.0%	
Adjustments	(5.5)			2.8		4.2		
Net revenues	\$177.9			\$145.2		\$158.2		

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Applications

A domestic versus international breakdown of Win Apps is as follows (in millions):

	Domestic	Int'l	WW/OEM	Total
Q91-1	\$42.6	\$37.6	\$0.1	\$80.3
Q90-4	16.3	28.7	0.1	45.1
Q90-3	16.9	26.6	0.3	43.8
Q90-2	13.3	13.5	0.3	27.1
Q90-1	8.5	9.1	0.1	17.7

The contribution to Applications net revenues and operating income for Q91-1 on a business unit basis was as follows (in millions):

Net Revenues	Actual		Plan		Variance Percentage
	\$	%	\$	%	
Office	80.6	45.8%	64.4	36.9%	25
Analysis	62.3	32.3	50.8	34.5	23
Entry	24.4	15.9	21.6	14.1	13
Graphics	6.4	3.4	5.1	8.4	25
Data Access	4.2	2.6	4.1	6.1	3
Total	\$177.9	100.0%	\$146.0	100.0%	22

Op. Income (Loss)	Actual			Plan			Variance
	Income (Loss)	Total Percentage	Revenue	Income (Loss)	Total Percentage	Revenue	
Office	\$29.9	52.2	37.2	\$14.4	61.8	22.4	\$15.5
Analysis	25.1	43.7	40.2	12.6	54.3	24.9	12.5
Entry	5.8	10.1	23.7	1.9	8.0	8.6	3.9
Graphics	(0.2)	(0.4)	(3.1)	(1.5)	(6.6)	(29.9)	1.3
Data Access	(3.2)	(5.6)	(75.9)	(4.1)	(17.5)	(100.1)	0.9
Total	\$57.4	100.0	32.3	\$23.3	100.0	16.0	\$34.1

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Office Business Unit (OBU)

The Q91-1 condensed burdened operating income statement for OBU follows (in millions):

	Actual		Plan		Variance
Net revenues	\$80.5	100.0%	\$64.3	100.0%	\$16.2
Cost of revenues	13.9	17.2	12.1	18.8	(1.8)
Operating expenses	11.7	14.5	12.5	19.5	0.8
Allocations - Research and development	3.5	4.4	3.9	6.1	0.4
Allocations - Sales and marketing	21.0	26.1	20.9	32.5	(0.1)
Allocations - General and administrative	0.4	0.6	0.5	0.7	0.1
Burdened operating income	\$30.0	37.2%	\$14.4	22.4%	\$15.6

OBU revenues by channel for Q91-1 were as follows (in millions):

	Actual		Plan		Variance
International Finished Goods	\$47.0	58.3%	\$39.0	60.7%	\$ 8.0
USSMD	32.6	40.5	24.5	38.0	8.1
Domestic OEM	0.2	0.2	0.3	0.5	(0.1)
Adjustments	0.7	1.0	0.5	0.8	0.2
	\$80.5	100.0%	\$64.3	100.0%	\$16.2

Net revenues for Q91-1, at \$80.5 million, were 25% above plan of \$64.3 million. Win Word was the biggest contributor to the favorable variance, generating 37% of net revenues and accounting for 63% of the favorable variance. PC Word slipped from its position as the leading revenue generator, but still contributed 35% of the BU's net revenue. The product group's leading products (compared with plan) for Q91-1 were as follows (units in thousands, dollars in millions):

Actual	Plan		Actual		Plan		Variance
			Units	Revenue	Units	Revenue	
1	2	Win Word	122.5	\$29.9	78.1	\$19.7	\$10.2
2	1	PC Word	97.6	28.2	105.3	26.5	1.7
3	3	Mac Word	75.3	13.4	70.6	12.6	0.8
4	5	Win Word Upgrade	13.2	2.2	8.9	1.4	0.8
5	4	PC Word Update	14.1	2.0	13.3	1.9	0.1
				\$75.7		\$62.1	\$13.6
				94%		97%	

Percentage of OBU's net revenues

Sales through the International Finished Goods channel of \$47.0 million exceeded forecast of \$39.0 million by 20%. Significant favorable variances were recorded by Win Word (\$2.9 million), PC Word (\$2.4 million) and Win Word Upgrade (\$514,000). USSMD revenues of \$32.6 million were 33% above forecast of \$24.5 million. On the strength of Windows Computing momentum, Win Word demand continued to exceed plan, contributing \$7.4 million to the favorable variance. Other contributors to the favorable variance included Mac Word (\$8.2 million versus plan of \$7.6 million) and Win Word Upgrade (\$924,000 versus plan of \$641,000). These favorable variances were partially offset by an unfavorable variance for PC Word of \$664,000. Adjustments to net revenues were \$786,000 compared to plan of \$520,000. The favorable situation may be attributed to a favorable variance in inter-business unit royalty (\$640,000), which was partially offset by an unfavorable variance in rebates of \$524,000. The inter-business unit royalty represents OBU's portion of the revenue generated by the Mac and Win Office. The revenue and product costs for Office, which bundles Word, Excel, PowerPoint and Mail (Mac only), are initially recorded in the Application Business Unit and then transferred to the BUs of the component products. The rebate variance reflects higher than planned revenues.

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Office Business Unit

As a percentage of net revenues, cost of revenues was 17.2% compared to a budget of 18.8%. Product costs were 11.5% of net revenues, versus plan of 10.7%. USSMD's product cost percentage was 12.4% compared to budget of 11.0%. The unfavorable variance is the result of higher than planned revenues from lower margin education sales, particularly IBM ACIS, combined with lower than planned MLP revenue. International Retail's product cost percentage of 11.2% was slightly above the budgeted percentage of 11.0%. Non-product costs of 5.7% of net revenues fell considerably short of the planned 8.1%. The favorable variance was attributable to a lower than planned allocation of both US and international manufacturing and distribution costs (4.2% of net revenues versus plan of 7.0%).

Operating expenses of \$11.7 million, 14.5% of net revenues, were \$814,000 below plan of \$12.5 million, 19.5% of net revenues. The most significant favorable variances occurred in marketing (\$2.0 million) and marketing fund incentive programs (\$277,000). These were partially offset by a marketing accrual (\$1.8 million).

USSMD marketing incurred \$1.9 million in expenses, 47.3% of total marketing expenses, compared to budget of \$3.1 million. All products in OBU showed favorable variances with the exception of Windows Word, which was \$45,000 over plan. The most significant favorable variances occurred in Corporate Programs allocations (\$288,000), PC Word (\$256,000), Mac Word (\$255,000), and PC Mail (\$179,000). International Finished Goods marketing, at \$2.1 million, was \$825,000 below plan. The marketing variance represents timing differences only, and is expected to be absorbed later in the fiscal year. In order to minimize the impact when this occurs, a marketing expense accrual of \$1.8 million was made. Market development costs incurred by the subsidiaries were only \$65,000 compared to plan of \$343,000.

Allocations to OBU were \$24.9 million compared to plan of \$25.3 million. As a percentage of net revenues, allocations were 31.1% of net revenues versus budget of 39.3%. The most significant favorable variances occurred in USSMD (\$487,000) and International Research and Development (\$478,000). The favorable variance in USSMD may be attributed to lower than anticipated spending in headcount-related areas, while International Research and Development was below plan in payroll and outside product development. The favorable variances were partially offset by an unfavorable variance of \$702,000 from International Finished Goods.

The Q91-1 burdened operating income for OBU was \$30.0 million, 37.2% of net revenues, compared to a plan of \$14.4 million, 22.4% of net revenues. The favorable variance may be attributed to revenues generated through both USSMD and International Finished Goods that were significantly above plan, as well as operating expenses and allocated expenses that were markedly below forecasted levels.

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Analysis Business Unit (ABU)

The Q91-1 condensed burdened operating income statement for ABU follows (in millions):

	Actual		Plan		Variance
Net revenues	\$62.3	100.0%	\$50.8	100.0%	\$11.5
Cost of revenues	9.9	15.9	9.5	18.8	(0.4)
Operating expenses	9.7	15.5	10.6	20.9	0.9
Allocations - Research and development	2.1	3.4	2.5	5.0	0.4
Allocations - Sales and marketing	15.2	24.4	15.2	29.8	--
Allocations - General and administrative	0.3	0.6	0.4	0.6	0.1
Burdened operating income	\$25.1	40.2%	\$12.6	24.9%	\$12.5

ABU revenues by channel for Q91-1 were as follows (in millions):

	Actual		Plan		Variance
International Finished Goods	\$33.4	53.6%	\$27.7	54.4%	\$ 5.7
USSMD	27.5	44.2	22.1	43.5	5.4
Domestic OEM	0.4	0.6	0.3	0.6	0.1
International OEM	0.1	0.2	--	--	0.1
Adjustments	0.9	1.4	0.7	1.5	0.2
	\$62.3	100.0%	\$50.8	100.0%	\$11.5

Net revenues for Q91-1, at \$62.3 million, were 23% above plan of \$50.8 million. In terms of revenue generation, the product group's leading products (compared with plan) for Q91-1 were as follows (units in thousands, dollars in millions):

Actual	Plan		Actual		Plan		Variance
			Units	Revenue	Units	Revenue	
1	1	Win Excel	121.6	\$33.5	106.9	\$27.3	\$6.2
2	2	Mac Excel	49.7	10.8	57.5	11.9	(1.1)
3	4	Win Project	14.8	6.0	7.0	2.6	3.4
4	3	PC Multiplan	36.1	4.4	16.5	3.1	1.3
5	5	PM Excel	3.8	1.2	7.2	2.3	(1.1)
				\$55.9		\$47.2	\$8.7

Percentage of ABU net revenues 90% 93%

Sales through the International Finished Goods channel exceeded plan by 20% (\$33.4 million actual versus \$27.7 million budget). The favorable variance was attributed to revenues in excess of plan for Win Excel (\$18.3 million vs. \$15.3 million), Win Project (\$1.9 million vs. \$555,000), and PC Multiplan (\$3.9 million vs. \$3.0 million). Partially offsetting these favorable revenue variances, PM Excel and Mac Excel were below forecasted revenue by \$1.2 million and \$446,000, respectively. USSMD revenues, at \$27.5 million, exceeded forecast by \$5.4 million. Again, the favorable variance can be attributed to above plan revenues for Win Excel (\$15.1 million vs. \$11.7 million) and Win Project (\$4.1 million vs. \$2.0 million). The favorable worldwide results can be attributed to the momentum of Windows Computing, which began in earnest with the May, 1990 introduction of Windows 3.0. Adjustments to net revenues were \$911,000 compared to a plan of \$731,000. The \$180,000 favorable variance was due to higher than anticipated inter-business unit royalties relating to Mac and Win Office (\$475,000 above plan), partially offset by higher than planned rebates (\$395,000 above plan). The inter-business unit royalty represents ABU's portion of the revenues generated by Mac Office and Win Office. The revenues and product costs for the Office bundle of Word, Excel, PowerPoint, and Mail (Mac only) are initially recorded in the Application Business Unit and then transferred to the BUs of the component products.

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Analysis Business Unit

As a percentage of net revenues, cost of revenues was 15.9% compared to a budget of 18.8%. Product costs were 11.2% of net revenues, versus plan of 11.5%. USSMD's product cost percentage was 9.7%, mirroring budget of 9.6%. International Finished Goods' product cost percentage of 12.8% was slightly below the budgeted percentage of 13.5%. As a percentage of net revenues, non-product costs of 4.7% (\$2.9 million), were below plan of 7.3% (\$3.7 million). The variance is due to lower than planned allocations of manufacturing and distribution costs from both the domestic (\$470,000) and international (\$394,000) manufacturing facilities.

Operating expenses of \$9.7 million, 15.5% of net revenues, were \$928,000 under budget of \$10.6 million, 20.9% of net revenues. The most significant favorable variances were incurred in marketing and outside product development (\$939,000 and \$470,000, respectively). These favorable variances were partially offset by a marketing accrual (\$969,000).

International Finished Goods marketing, at \$2.2 million, was \$616,000 below plan of \$2.8 million. USSMD marketing incurred \$1.8 million in expenses, compared to a budget of \$2.1 million. Favorable USSMD marketing variances occurred in Corporate program allocations (\$288,000) and Mac Excel (\$82,000). This underspending was partially mitigated by Windows Project, which was over plan by \$127,000. Additional USSMD Win Computing marketing commitments have been made. In order to minimize the impact when these costs are incurred, a marketing expense accrual of \$969,000 was made. The accrual is expected to be absorbed later in the fiscal year. The favorable outside product development variance was primarily attributable to below plan amortization of purchased code (\$285,000), due to the reduction in the purchase price of Project technology from SofDesign.

Allocations to ABU were \$17.6 million compared to a plan of \$18.1 million. As a percentage of net revenues, actual allocations were 28.4% versus budget of 35.4%. The most significant favorable variances occurred in USSMD (\$375,000) and International Research and Development (\$335,000). The favorable variance in USSMD may be attributed to lighter than anticipated spending in headcount-related areas. International Research and Development was below plan in payroll and product development. Partially offsetting the favorable variances, International Finished Goods experienced an unfavorable variance of \$515,000.

The Q91-1 burdened operating income for ABU was \$25.1 million, 40.2% of net revenues, compared to a plan of \$12.6 million, 24.9% of net revenues. The favorable variance may be attributed to revenues exceeding forecast through both the USSMD and International channel, as well as favorable variances in all other elements of the business unit's profit model.

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Entry Business Unit (EBU)

The Q91-1 condensed burdened operating income statement for EBU follows (in millions):

	Actual		Plan		Variance
	\$	%	\$	%	
Net revenues	\$24.4	100.0%	\$21.6	100.0%	\$2.8
Cost of revenues	5.1	20.7	5.1	23.6	0.0
Operating expenses	6.1	24.9	6.9	31.8	0.0
Allocations - Research and development	1.4	5.6	1.6	7.6	0.2
Allocations - Sales and marketing	5.8	24.0	5.8	27.1	0.0
Allocations - General and administrative	0.2	1.1	0.3	1.3	0.1
Burdened operating income	\$ 5.8	23.7%	\$ 1.9	8.6%	\$3.9

EBU revenues by channel for Q91-1 were as follows (in millions):

	Actual		Plan		Variance
	\$	%	\$	%	
International Finished Goods	\$15.0	61.5%	\$11.0	51.0%	\$4.0
USSMD	8.6	35.4	9.6	44.2	(1.0)
Domestic OEM	0.7	2.9	1.1	5.2	(0.4)
International OEM	0.8	3.3	0.5	2.4	0.3
Adjustments	(0.7)	(3.1)	(0.6)	(2.8)	(0.1)
	\$24.4	100.0%	\$21.6	100.0%	\$2.8

Net revenues for Q91-1, at \$24.4 million, were 13% above plan of \$21.6 million. In terms of revenue generation, the business unit's leading products (compared with plan) for the quarter were as follows (units in thousands, dollars in millions):

Actual	Plan		Actual		Plan		Variance
			Units	Revenue	Units	Revenue	
1	1	PC Works	216.8	\$15.2	331.1	\$13.2	\$2.0
2	2	Mac Works	27.0	3.8	31.1	4.3	(0.5)
3	--	PC Works Update	18.9	1.5	2.5	0.2	1.3
4	4	PC Chart	7.1	1.4	4.6	0.9	0.5
5	3	PC Flight Simulator	38.0	1.3	68.0	2.3	(1.0)
				\$23.2		\$20.9	\$2.3
		Percentage of EBU's net revenues		95%		97%	

Plan #5 Learning DOS (\$0.8 million)

PC Works revenues of \$15.2 million were 15% above plan of \$13.2 million, and represented 62% of the business unit's net revenues. Mac Works revenues of \$3.8 million fell below plan by 12%, primarily due to the continued slowdown in sales of Apple's low-end Mac SEs and Mac Pluses. Led by strong sales in the International Finished Goods channel, PC Works Update revenues of \$1.5 million were \$1.3 million above plan. PC Chart revenues of \$1.4 million were 56% above plan of \$928,000.

As a percentage of net revenues, cost of revenues was 20.7% (\$5.1 million) compared to a planned 23.6% (\$5.1 million). Product costs were 13.9% of net revenue compared with a budget of 14.2%. USSMD product costs were 14.2% of net revenue compared to budget of 12.2%, while International Finished Goods product costs were 14.4% compared to a budget of 17.3%. The USSMD variance is primarily due to the introduction of the Works/Mouse bundles. These unbudgeted bundles have an average product cost of 27.0%. Excluding these from Q91-1 actuals, USSMD product costs would have approximated plan. Non-product costs, as a percentage of revenue, were 6.8% (\$1.7 million) compared to plan of 9.4% (\$2.0 million). A \$120,000 favorable international manufacturing variance and lower than planned royalties, due to depressed sales of Flight Simulator and Mac Works, were responsible for this variance.

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Entry Business Unit

EBU operating expenses for Q91-1 were \$6.1 million, 24.9% of net revenues, compared to a plan of \$6.9 million, 31.8% of net revenues. Favorable variances in marketing (\$832,000) and employee recruiting (\$168,000) were partially offset by a marketing accrual (\$409,000).

The favorable marketing variance was shared by both International Finished Goods (\$447,000) and USSMD (\$389,000). The variance was principally due to underspending by International Finished Goods in public relations, trade shows, and marketing materials, and by delays in domestic Works family and Learning Windows marketing efforts. The domestic variance is expected to turn around in future months. In order to cushion the effect of this turnaround, we accrued \$409,000 in marketing expenses. The favorable employee recruiting variance reflects the fact that headcount has been slightly below plan all quarter.

Allocations to EBU of \$7.4 million were below plan of \$7.7 million by \$300,000. As a percentage of net revenues, actual allocations were 30.7% versus budget of 36.0%. Favorable variances in International R&D (\$179,000) and USSMD (\$149,000) were partially offset by an unfavorable variance in International Finished Goods (\$113,000).

The Q91-1 burdened operating income for EBU was \$5.8 million, 23.7% of net revenues, compared to a plan of \$1.9 million, 8.6% of net revenues. Higher than expected revenues, combined with lower than expected cost of revenues, operating expenses and allocations, all contributed to outstanding operating results.

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Data Access Business Unit (DABU)

The Q91-1 condensed burdened operating income statement for DABU follows (in millions):

	Actual		Plan		Variance
Net revenues	\$4.2	100.0%	\$4.1	100.0%	\$0.1
Cost of revenues	1.3	29.8	1.1	26.7	(0.2)
Operating expenses	3.2	74.9	4.0	97.9	0.8
Allocations - Research and development	1.2	28.2	1.3	32.3	0.1
Allocations - Sales and marketing	1.5	35.9	1.5	36.5	0.0
Allocations - General and administrative	0.2	7.1	0.3	6.7	0.1
Burdened operating income (loss)	<u>\$ (3.2)</u>	<u>(75.9)%</u>	<u>\$ (4.1)</u>	<u>(100.1)%</u>	<u>\$0.9</u>

DABU revenues by channel for Q91-1 were as follows (in millions):

	Actual		Plan		Variance
International Finished Goods	\$2.2	52.7%	\$1.9	47.9%	\$0.3
USSMD	1.7	40.6	1.9	46.8	(0.2)
Domestic OEM	0.2	5.6	0.4	8.6	(0.2)
International OEM	0.2	4.9	0.0	0.0	0.2
Adjustments	(0.1)	(3.8)	(0.1)	(3.3)	0.0
	<u>\$4.2</u>	<u>100.0%</u>	<u>\$4.1</u>	<u>100.0%</u>	<u>\$0.1</u>

Net revenues for Q91-1, at \$4.2 million, were slightly above plan of \$4.1 million. The favorable variance is primarily due to strong sales of Pro Basic Updates, which exceeded plan by \$478,000. Partially offsetting this favorable variance was PC Quick Basic (21% below plan). In terms of revenue generation, the product group's leading products (compared with plan) for Q91-1 were as follows (units in thousands, dollars in millions):

Actual	Plan		Actual		Plan		Variance
			Units	Revenue	Units	Revenue	
1	1	PC Quick Basic	25.4	\$1.5	30.3	\$1.9	\$(0.4)
2	2	Pro Basic	5.0	1.3	5.5	1.4	(0.1)
3	-	Pro Basic Update	5.5	0.5	1.1	0.1	0.4
4	-	Mac Quick Basic	3.5	0.2	2.6	0.2	0.0
5	3	Basic Interpreter	155.3	0.2	200.0	0.2	0.0
				<u>\$3.7</u>		<u>\$3.8</u>	<u>\$(0.1)</u>

Percentage of DABU's net revenues 88% 93%

Plan #4 Mac File (\$0.2 million), Plan #5 MS-Database (\$0.2 million)

International Finished Goods revenues of \$2.2 million were \$270,000 above plan of \$1.9 million. The favorable variance was attributable to Pro Basic Update (\$270,000) and Pro Basic (\$238,000). Partially offsetting the favorable variance, PC Quick Basic experienced a revenue shortfall of \$291,000. USSMD revenues of \$1.7 million were \$197,000 below plan of \$1.9 million. Significant unfavorable variances occurred for Pro Basic (\$351,000) and PC Quick Basic (\$71,000). These unfavorable variances were partially offset by Pro Basic Updates (\$209,000 above plan).

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Data Access Business Unit

As a percentage of net revenues, cost of revenues was 29.8% compared to a budget of 26.7%. Product costs were 21.5% of net revenues, versus plan of 17.5%. USSMD's product costs, as a percentage of net revenue, were 15.8% compared to budget of 17.5%, while International Finished Goods' product costs were 28.7% compared to a budget of 19.4%. The International Finished Goods' product cost variance was due to higher than planned low margin update revenue. Non-product costs, as a percentage of revenues, were 8.3% (\$346,000) compared to a plan of 9.2% (\$376,000). The favorable variance is primarily due to royalties (\$51,000 compared to plan of \$89,000) as a result of lower than planned units shipped for the royalty bearing MS-Database. The product is being licensed specifically for inclusion in the Desktop III bundle.

Operating expenses of \$3.2 million (74.9% of net revenues) were below plan of \$4.0 million (97.9% of net revenues) by \$833,000. The most significant favorable variances occurred in outside product development (\$233,000) and marketing (\$175,000). Less significant favorable variances existed in most employee-related expense line items.

The favorable variance in outside product development was due to lower than planned spending in Japan on localization of Basic Compiler (version 7.0). The favorable marketing variance is primarily due to lower than planned spending on PC Quick Basic and Pro Basic. The favorable variance in employee-related expenses is the result of lower than planned headcount (118 employees versus plan of 131).

Allocations to DABU were \$2.9 million compared to a plan \$3.1 million. As a percentage of net revenues, actual allocations were 71.2% versus budget of 75.5%. The largest favorable variances were in International R&D (\$83,000), and Applications Support (\$48,000). These were partially offset by unfavorable variances in Legal (\$49,000) and International Finished Goods (\$37,000).

In summary, the burdened operating loss for Q91-1 was \$3.2 million compared to a planned loss of \$4.1 million. Lower than expected operating and allocated expenses combined with revenues, which were slightly above plan, resulted in a lower than anticipated burdened operating loss.

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Graphics Business Unit (GBU)

The Q91-1 condensed burdened operating income statement for GBU follows (in thousands):

	<u>Actual</u>		<u>Plan</u>		<u>Variance</u>
Net revenues	\$6,421	100.0%	\$5,146	100.0%	\$1,275
Cost of revenues	1,396	21.7	1,060	20.6	(336)
Operating expenses	2,743	42.7	2,936	57.1	193
Allocations - Research and development	602	9.4	785	15.3	183
Allocations - Sales and marketing	1,753	27.3	1,793	34.7	40
Allocations - General and administrative	128	2.0	110	2.2	(18)
Burdened operating income (loss)	<u>\$(201)</u>	<u>(3.1)%</u>	<u>\$(1,538)</u>	<u>(29.9)%</u>	<u>\$1,337</u>

GBU revenues by channel for Q91-1 were as follows (in thousands):

	<u>Actual</u>		<u>Plan</u>		<u>Variance</u>
USSMD	\$4,529	70.5%	\$3,357	65.2%	\$1,172
International Finished Goods	1,276	19.9	1,351	26.3	(75)
US OEM	66	1.0	108	2.1	(42)
Adjustments	550	8.6	330	6.4	220
Net revenues	<u>\$6,421</u>	<u>100.0%</u>	<u>\$5,146</u>	<u>100.0%</u>	<u>\$1,275</u>

Net revenues for Q91-1, at \$6.4 million, were 25% above plan of \$5.1 million. Win PowerPoint was the revenue leader this quarter with revenues of \$3.9 million versus plan of \$2.9 million. Mac PowerPoint, with revenues of \$1.8 million, approximated plan of \$1.9 million. Sales through the USSMD channel totalled \$4.6 million, or 71% of GBU's revenue, compared to a plan of \$3.3 million, 65%. International Finished Goods fell short of plan, generating \$1.3 million in revenue compared to a plan of \$1.4 million. Revenue adjustments of \$550,000 were \$221,000 greater than a planned \$329,000. This favorable variance is primarily due to inter-business unit royalties which represent GBU's allocation of revenue generated by the Mac and Window Office products. GBU's allocation of Office revenue was \$878,000, \$277,000 above plan. This variance was partially offset by higher than planned rebates. Rebates, which are volume sensitive, were \$304,000 versus plan of \$248,000.

As a percentage of net revenues, cost of revenues was 21.7% compared to a budget of 20.6%. Product costs were 11.5% of net revenues, versus plan of 10.9%. USSMD's product cost percentage, 12.0%, approximated budget of 11.7%. International Finished Goods' product cost percentage was 15.2% compared to budget of 12.6%. Non-product costs were \$656,000 (10.2% of net revenue) versus plan of \$498,000 (9.7%).

Operating expenses for Q91-1 were \$2.7 million (42.7% of net revenue), versus plan of \$2.9 million (57.1%). Favorable variances occurred in outside product development (\$121,000), supplies and equipment (\$91,000), and payroll (\$56,000). An unbudgeted marketing accrual of \$107,000 was made to reflect GBU's portion of certain Windows Computing commitments.

Allocated expenses to the Graphics business unit were \$2.5 million, 38.7% of net revenues, compared to a plan of \$2.7 million, 52.2% of net revenues. Favorable allocations from Applications Support (\$124,000), USSMD (\$73,000) and International R&D (\$59,000) were partially offset by negative variances in International Finished Goods (\$37,000) and Legal (\$25,000).

The Q91-1 burdened operating loss for GBU was \$201,000 compared to a planned loss of \$1.5 million. This \$1.3 million favorable variance was due to higher than expected net revenues combined with lower than expected operating expenses and allocations. If revenues increase as expected in Q91-2 (plan is \$7.6 million), GBU should record its first profitable quarter.

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Systems

The Q91-1 condensed burdened operating income statement for Systems follows (in millions):

	Actual		Plan		Variance
	\$	%	\$	%	
Net revenues	\$116.4	100.0%	\$101.2	100.0%	\$15.2
Cost of revenues	15.6	13.4	12.6	12.5	(3.0)
Operating expenses	22.2	19.1	24.9	24.6	2.7
Allocations - Research and development	1.4	1.2	1.6	1.6	0.2
Allocations - Sales and marketing	13.9	11.9	13.7	13.5	(0.2)
Allocations - General and administrative	1.7	1.5	1.4	1.3	(0.3)
Burdened operating income	\$ 61.6	52.9%	\$ 47.0	46.5%	\$14.6

Systems net revenues by channel for Q91-1 were as follows (in millions):

	Actual		Plan		Variance
	\$	%	\$	%	
International Finished Goods	\$ 37.1	31.9%	\$ 18.5	18.3%	\$18.6
International OEM	32.2	27.7	36.4	36.0	(4.2)
Domestic OEM	26.3	22.5	25.7	25.4	0.6
USSMD	20.9	18.0	21.3	21.1	(0.4)
Adjustments	(0.1)	(0.1)	(0.7)	(0.8)	0.6
Total	\$116.4	100.0%	\$101.2	100.0%	\$15.2

In terms of revenue generation, the Systems product group's leading products (compared with plan) for the quarter were as follows (units in thousands, revenue in millions):

Actual	Plan		Actual		Plan		Variance
			Units	Revenue	Units	Revenue	
1	1	MS-DOS/GW-Basic	3,920.5	\$ 60.9	4,256.4	\$59.6	\$ 1.3
2	2	Win 3.0	335.8	28.7	203.2	17.0	11.7
3	3	Win 3.0 Updates	249.1	12.9	274.1	11.3	1.6
4	--	Win 3.0 SDK	13.7	4.0	5.9	1.5	2.5
5	4	Win 286	284.6	2.8	469.8	3.7	(0.9)
6	5	OS/2	47.5	1.8	44.4	3.5	(1.7)
			\$111.1		\$96.6		\$14.5
Percent of net revenues			95%		95%		

The contribution to Systems net revenues and operating income for Q91-1 on a business unit basis was as follows (in millions):

	Actual			Plan			Variance
	\$	% of Total	% of Revenue	\$	% of Total	% of Revenue	
Net Revenues	\$ 61.0	52.4%		\$ 59.5	58.8%		2
MS-DOS	52.0	44.7		37.0	36.5		41
Windows	3.0	2.6		4.3	4.3		(30)
OS/2	0.4	0.3		0.4	0.4		--
Printer	0.4	0.3		0.4	0.4		15
Total	\$116.4	100.0%		\$101.2	100.0%		

	Actual			Plan			Variance
	Income (Loss)	% of Total	% of Revenue	Income (Loss)	% of Total	% of Revenue	
Operating Income (Loss)	\$46.6	75.7	76.4	\$45.6	97.0	76.7	\$ 1.0
MS-DOS	25.8	41.8	49.6	13.9	29.4	37.4	11.9
Windows	(8.9)	(14.5)	(299.0)	(10.2)	(21.6)	(234.4)	1.3
OS/2	(1.9)	(3.0)	(491.1)	(2.3)	(4.8)	(605.9)	0.4
Printer	0.4	0.3	52.9	0.4	0.4	46.5	\$14.6
Total	\$61.6	100.0	52.9	\$47.0	100.0	46.5	

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MS-DOS

The Q91-1 condensed burdened operating income statement for MS-DOS follows (in millions):

	Actual		Plan		Variance
	\$	%	\$	%	
Net revenues	\$61.0	100.0%	\$59.5	100.0%	\$ 1.5
Cost of revenues	4.1	6.7	3.5	5.8	(0.6)
Operating expenses	3.2	5.2	3.5	5.8	0.3
Allocations - Research and development	0.6	1.0	0.7	1.2	0.1
Allocations - Sales and marketing	6.4	10.5	6.1	10.4	(0.3)
Allocations - General and administrative	0.1	0.2	0.1	0.1	0.0
Burdened operating income	\$46.6	76.4%	\$45.6	76.7%	\$ 1.0

MS-DOS revenues by channel for Q91-1 were as follows (in millions):

	Actual		Plan		Variance
	\$	%	\$	%	
International OEM	\$29.3	48.0%	\$30.6	51.5%	\$(1.3)
Domestic OEM	21.8	35.7	21.3	35.8	0.5
Worldwide OEM	51.1	83.7	51.9	87.3	(0.8)
International Finished Goods	10.2	16.7	7.8	13.0	2.4
USSMD	-	-	-	-	-
Adjustments	(0.3)	(0.4)	(0.2)	(0.3)	(0.1)
Total	\$61.0	100.0%	\$59.5	100.0%	\$ 1.5

Table of significant Domestic and International OEM MS-DOS customers (in thousands):

	Actual	Plan	Variance
Toshiba	\$ 5,430	\$ 2,201	\$ 3,229
Compaq	3,629	2,434	1,195
Olivetti SpA	2,848	1,109	1,739
NEC	1,405	3,295	(1,890)
Copam Electronics	1,318	533	785
AST Research	1,304	922	382
NCR	1,193	808	385
Epson	1,112	2,842	(1,730)
Phoenix	1,111	782	329
Hitachi Ltd	1,036	768	268
DataTech Enter.	956	487	469
American Tel. & Tel.	937	700	237
Memorex	931	475	456
Zenith Data	903	1,232	(329)
Tandy	894	895	(1)
Siemens AG	864	504	360
Hyundai Elec.	851	880	(29)
Other Customers	24,358	31,080	(6,722)
Worldwide OEM	\$51,080	\$51,947	\$ (867)

Revenues for MS-DOS of \$61 million for the quarter were 3% higher than the plan of \$59.5 million. Favorable variances in International Finished Goods (\$2.4 million) and Domestic OEM (\$478,000) were partially offset by an unfavorable variance in International OEM of \$1.3 million.

International OEM revenues were 4% short of the planned \$30.6 million. A significant factor was a decrease in shipments of low-end machines by NEC and Epson, which generated unfavorable variances of \$1.9 million and \$1.7 million, respectively. Other OEMs reporting royalties significantly below plan included Acer (\$679,000), Sanyo (\$349,000), and Tatung (\$264,000). In addition, unfavorable variances were created by a number of OEMs that failed to file timely royalty reports. Among these were

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MS-DOS

Nokia Data (\$439,000), Bull (\$365,000), and Tulip (\$348,000). These shortfalls were only partially offset by the impact of favorable variances generated by Toshiba (\$3.2 million), Olivetti (\$1.7 million), and Copam (\$785,000). Toshiba and Copam reported royalties covering two quarters. Olivetti's variance was due to strong shipments of their PCS 286 computer, a new product targeted to the home market.

Domestic OEM royalty revenue was 7% over plan (\$18.6 million versus \$17.3 million). This more than offset an \$810,000 unfavorable variance in packaged product sales, for a net favorable variance of \$478,000. The royalty variance was led by strong performance from Compaq (\$3.6 million compared to \$2.4 million) and AST (\$1.3 million against \$922,000). Domestic sales of packaged MS-DOS have been negatively impacted by a surge of counterfeit product in the market place. Significant packaged product customers included Supercom (\$505,000), Liwski (\$335,000), Distec (\$294,000) and PC Craft (\$270,000).

International Finished Goods revenues of \$10.2 million were \$2.4 million over the budgeted \$7.8 million. This variance reflects greater sales of the International English (\$1.2 million), Portuguese (\$434,000) and French (\$383,000) versions of MS-DOS. Budgeted sales in the USSMD channel of MS-DOS Retail Upgrade did not occur because of product slippage. Actual USSMD sales will continue to be negligible until the Retail Upgrade ships.

Total cost of revenues were \$614,000 over the budgeted \$3.5 million. Product cost increases were the direct result of a higher volume of packaged product sales by International Finished Goods. Operating expenses of \$3.2 million were under plan by \$313,000. The largest favorable variances were in product development expenses paid to third parties (\$166,000), professional fees (\$93,000) and employee-related expenses (\$57,000). The favorable research and development allocation stemmed from a smaller International R&D (aka localization) pool. The unfavorable sales and marketing allocation was primarily due to a greater amount of non-product specific channel expenses incurred by International OEM (\$191,000).

In summary, the favorable variances in revenue and operating expenses outweighed the higher cost of revenues and larger allocations, resulting in a burdened operating income of \$46.6 million, 2% over a plan of \$45.6 million.

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Windows

The Q91-1 condensed burdened operating income statement for the Windows Business Unit follows (in millions):

	Actual		Plan		Variance
	\$	%	\$	%	
Net revenues	\$52.0	100.0%	\$37.0	100.0%	\$15.0
Cost of revenues	10.8	20.8	8.3	22.4	(2.5)
Operating expenses	7.5	14.5	7.0	19.0	(0.5)
Allocations - Research and development	0.6	1.3	0.7	1.9	0.1
Allocations - Sales and marketing	6.6	12.7	6.8	18.3	0.2
Allocations - General and administrative	0.6	1.1	0.3	1.0	(0.3)
Burdened operating income	\$25.9	49.6%	\$13.9	37.4%	\$12.0

Windows revenues by channel for Q91-1 were as follows (in millions):

	Actual		Plan		Variance
	\$	%	\$	%	
International Finished Goods	\$26.2	50.3%	\$ 9.9	26.7%	\$16.3
USSMD	20.9	40.2	21.3	57.7	(0.4)
Domestic OEM	2.7	5.1	2.6	6.9	0.1
International OEM	2.1	4.1	3.7	10.1	(1.6)
Adjustments	0.1	0.3	(0.5)	(1.4)	0.6
	\$52.0	100.0%	\$37.0	100.0%	\$15.0

Net revenues for the Windows business unit were \$52.0 million for Q91-1, 41% above plan of \$37.0 million. In terms of revenue generation, the products group's leading products (compare with plan) for Q91-1 were as follows (units in thousands, dollars in millions):

Actual	Plan		Actual		Plan		Variance
			Units	Revenue	Units	Revenue	
1	1	Win 3	335.8	\$28.7	203.2	\$17.0	\$11.7
2	2	Win 3 Update	249.1	12.9	274.1	11.3	1.6
3	5	Win 3 SDK	13.7	4.0	5.9	1.5	2.5
4	3	Win 286	284.6	2.8	469.8	3.7	(0.9)
5	4	Win 386	79.3	0.8	150.1	2.5	(1.7)
				\$3.7		\$3.8	\$(0.1)

Percentage of Windows net revenues 95% 97%

International Finished Goods, with revenues which exceeded plan by \$16.3 million, was responsible for the large favorable variance. The strong performance for International Finished Goods may be attributed to the continued success of Windows 3.0. With the exception of French and German localized versions, which were released last quarter, the rollout through most of International occurred during Q91-1, causing the same results seen in USSMD during Q90-4. The favorable variance was partially offset by unfavorable variances in International OEM (\$1.6 million) and USSMD (\$461,000).

Windows 3.0 revenues through International Finished Goods, of \$17.1 million, were 117% above plan of \$7.9 million. Additionally, revenues generated by the Windows 3.0 Update exceeded plan by \$6.0 million. International OEM's revenue shortfall was primarily due to disappointing results for Windows 2.11 for 286 machines, \$1.9 million below plan. The unfavorable results in USSMD were due to update revenue for Windows 3.0 that fell significantly short of plan (\$3.8 million below plan). This was partially offset by the strength of Windows 3.0 full packaged product (\$2.3 million above plan) and Windows SDK (\$1.8 million above plan).

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Windows

Cost of revenues were \$10.8 million (20.8% of net revenues) versus a plan of \$8.3 million (22.4% of net revenues). Product costs were 18.2% of net revenues versus budget of 18.6%. USSMD product costs were 21.8% of net revenues compared to plan of 24.6%. The variance may be attributed to full packaged product revenues that were above plan, while the lower margin updates fell significantly short of plan. International product costs were 18.3% of net revenues compared to forecast of 16.3%. The variance is the result of higher than planned Windows 3.0 update revenues. Non-product costs were \$1.3 million, 2.6% of net revenues, compared to plan of \$1.4 million, 3.8% of net revenues. The variance is primarily due to lower than planned allocations from the international manufacturing facility. The favorable variance was partially offset by \$355,000 in unbudgeted returns of versions 2.x product which were scrapped upon receipt.

Operating expenses were \$7.5 million (14.5% of net revenues) compared to a plan of \$7.0 million (19.0% of net revenues). The overspending primarily occurred in marketing (\$1.2 million) and was partially offset by a favorable variance in outside product development (\$331,000). USSMD marketing incurred \$2.8 million in expenses, 24% above plan. Marketing through the International Finished Goods channel was \$1.2 million versus plan of \$1.1 million. Additionally, USSMD marketing commitments relating to Windows computing have been made. In order to minimize the impact when these expenses are incurred, a marketing expenses accrual of \$881,000 was made.

Allocations to Windows of \$7.8 million (15.1% of net revenues) mirrored plan of \$7.8 million (21.2% of net revenues). The largest unfavorable variances occurred in the allocation of Legal, which was \$297,000 above plan, and International Finished Goods (\$111,000). These were partially offset by lower than planned costs in PSS (\$189,000) and USSMD (\$111,000).

The Q91-1 burdened operating income for Windows was \$25.8 million, 49.6% of net revenues, compared to plan of \$13.9 million, 37.4% of net revenues. The results were due to revenues that exceeded plan, combined with the fact that all other components of the Windows profit model that were below forecast, as a percentage of net revenues.

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OS/2

The Q91-1 condensed burdened operating income statement for OS/2 follows (in thousands):

	<u>Actual</u>		<u>Plan</u>		<u>Variance</u>
Net revenues	\$ 2,986	100.0%	\$ 4,338	100.0%	\$(1,352)
Cost of revenues	743	24.9	893	20.6	150
Operating expenses	8,068	270.1	10,441	240.6	2,373
Allocations - Research and development	1,600	53.6	1,756	40.5	156
Allocations - Sales and marketing	689	23.1	712	16.4	23
Allocations - General and administrative	815	27.3	706	16.3	(109)
Burdened operating (loss)	<u>\$(8,929)</u>	<u>(299.0)%</u>	<u>\$(10,170)</u>	<u>(234.4)%</u>	<u>\$ 1,241</u>

OS/2 revenues by channel for Q91-1 were as follows (in thousands):

	<u>Actual</u>		<u>Plan</u>		<u>Variance</u>
Domestic OEM	\$1,701	56.9%	\$1,841	42.4%	\$ (140)
International OEM	496	16.7	1,627	37.5	(1,131)
Worldwide OEM	2,197	73.6	3,468	79.9	(1,271)
International Finished Goods	792	26.5	876	20.3	(84)
Adjustments	(3)	(0.1)	(6)	(0.2)	3
Total	<u>\$2,986</u>	<u>100.0%</u>	<u>\$4,338</u>	<u>100.0%</u>	<u>\$ (1,352)</u>

Table of significant Domestic and International OEM OS/2 customers (in thousands):

	<u>Actual</u>	<u>Plan</u>	<u>Variance</u>
IBM Corporation	\$ 584	\$ 549	\$ 35
Compaq	179	400	(221)
Fujitsu	112	82	30
Olivetti SpA	105	204	(99)
Unisys	88	46	42
NCR	84	83	1
Toshiba	75	135	(60)
AST Research	68	46	22
Hewlett Packard	58	114	(56)
Nixdorf	61	32	29
Northgate	57	101	(44)
Dell	55	51	4
Accr	52	23	29
Citrix	50	-	50
Other Customers	569	1,602	(1,033)
Worldwide OEM	<u>\$2,197</u>	<u>\$3,468</u>	<u>\$(1,271)</u>

Net revenues for the OS/2 business unit were \$3 million for the quarter, or 31% under the plan of \$4.3 million.

Domestic OEM revenues of \$1.7 million were \$140,000 less than plan. Significant unfavorable variances occurred with Compaq (\$179,000 versus \$400,000) and Zenith Data (\$5,000 versus \$115,000). These were partially offset by favorable variances from several OEMs, including IBM (\$584,000 versus \$549,000), Unisys (\$88,000 versus \$46,000) and Citrix (\$50,000 versus \$0). In addition to royalty revenue, sales of OS/2 Software Development Kits (SDKs) generated \$410,000 in revenues compared to a plan of \$161,000.

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OS/2

International OEM sales of \$496,000 were only 30% of the planned \$1.6 million, due to a lack of product shipments from a number of OEMs and lower volumes reported by those that are shipping. Significant unfavorable variances included Olivetti (\$105,000 versus \$204,000), Hitachi (\$3,000 versus \$123,000), and NEC (\$0 versus \$150,000). In addition, Nokia Data failed to file its royalty report on time (plan was \$230,000).

International Finished Goods reported \$792,000 in sales against a plan of \$876,000. These revenues are for sales of OS/2 SDKs (\$382,000) and fees for support and installation of OS/2 products.

Cost of revenues was \$743,000, compared to the plan of \$893,000. The lower volume from OEMs created a \$238,000 savings in royalty expense. However, this was partially offset by an unfavorable inventory adjustment of \$89,000 tied to a product recost and an obsolete inventory write-off.

Operating expenses of \$8.1 million were \$2.4 million below plan. Significant favorable variances contributing to this savings were outside product development (\$831,000), supplies and equipment (\$419,000), travel & entertainment (\$302,000), and payroll (\$282,000). Allocated expenses were within \$70,000 of budget. The favorable research and development allocation stemmed from a smaller International R&D (localization) pool (\$104,000). The unfavorable general and administrative allocation resulted from higher legal expenses (\$148,000), resulting from an unbudgeted addition to our litigation reserve of \$2.7 million.

In summary, the favorable variances in cost of revenues, operating expenses and allocations outweighed the unfavorable variance in revenues, resulting in a burdened operating loss of \$8.9 million, compared to a planned loss of \$10.2 million.

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Systems, Peripherals and Accessories Group (SPAG)

The Q91-1 condensed burdened operating income statement for SPAG follows (in millions):

	Actual		Plan		Variance
	\$	%	\$	%	
Net revenues	\$49.2	100.0%	\$27.4	100.0%	\$21.8
Cost of revenues	20.8	42.4	13.2	48.0	(7.6)
Operating expenses	3.0	6.1	2.9	10.6	(0.1)
Allocations - Research and development	0.1	0.3	0.2	0.7	0.1
Allocations - Sales and marketing	6.0	12.2	6.0	21.7	(0.0)
Allocations - General and administrative	0.3	0.3	0.0	0.4	(0.3)
Burdened operating income	\$19.0	38.7%	\$ 5.1	18.6%	\$13.9

SPAG revenues by channel for Q91-1 were as follows (in millions):

	Actual		Plan		Variance
	\$	%	\$	%	
USSMD	\$25.7	52.2%	\$14.3	52.3%	\$11.4
International Finished Goods	21.8	44.3	13.6	49.6	8.2
Domestic OEM	3.1	6.2	0.6	2.3	2.5
Adjustments	(1.4)	(2.7)	(1.1)	(4.2)	(0.3)
	\$49.2	100.0%	\$27.4	100.0%	\$21.8

In terms of revenue generation, SPAG's leading products (compared with plan) for Q91-1 were as follows (units in thousands, dollars in millions):

	Actual		Plan		Variance
	Units	Revenue	Units	Revenue	
Serial Mouse	396.0	\$37.2	222.8	\$19.2	\$18.0
Bus Mouse	94.9	9.1	119.7	7.2	1.9
OEM Mouse	172.8	3.4	61.5	1.6	1.8
	663.7	\$49.7	404.0	\$28.0	\$21.7

Percent of SPAG's net revenues 101.0% 102.2%

SPAG net revenues of \$49.2 million were \$21.8 million over plan of \$27.4 million. As the preferred pointing device of the GUI revolution, Mouse sales exceeded plan by a whopping 80%. In terms of revenue generation the Serial Mouse exceeded sales forecast by 94%, the OEM Mouse bettered plan by 114%, and the Bus Mouse was 26% over budget.

USSMD revenues of \$25.7 million were \$11.4 million above plan of \$14.3 million. This huge favorable variance is the result of robust sales of the Serial Mouse/Paintbrush, which exceeded sales forecast by \$8.9 million, and Serial Mouse/Windows 3.0 bundle, which had revenues of \$6.8 million compared to plan of \$3.0 million. These favorable variances were slightly offset by lower than planned sales of the Naked Mouse SKUs. The Naked (or Hardware Only) Mouse generated \$3.0 million in revenue versus plan of \$8.2 million. Customer migration to these new Mice offerings has ramped up much slower than expected. International Finished Goods revenues of \$21.8 million were \$8.2 million above plan of \$13.6 million. This favorable variance is due to incredibly strong Serial Mouse/Paintbrush revenues (\$12.5 million versus plan of \$4.2 million), \$3.0 million in unbudgeted sales of Serial Mouse/Windows 3.0 bundle, and Bus Mouse/Paintbrush revenues which exceeded plan by \$1.0 million. These were partially offset by lower than planned sales of the Hardware Only Mice. Naked Serial Mice were below plan by \$4.5 million while Bus Mice revenue was \$118,000 versus plan of \$1.4 million. Domestic OEM revenues of \$3.1 million were \$2.4 million above plan of \$623,000. This favorable variance is due to \$2.3 million in unbudgeted sales of the OEM Mouse. Domestic OEMs with significant variances included Gateway 2000 (\$587,000), Zenith (\$463,000), AT & T (\$322,000) and Northgate (\$308,000).

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SPAG

Cost of revenues was \$20.8 million, 42.4% of net revenues, versus plan of \$13.2 million, 48.0% of planned net revenues. Product costs, at 37.2% of net revenues, were below plan of 38.6%. SPAG's favorable product cost percentage is due to lower than planned product costs for all Mouse products. Domestically, product costs also benefited from the fact that revenues for the lower margin Naked Mouse were well below plan, while the Serial Mouse/Paintbrush, which had product costs of 33.6% of revenue versus plan of 34.9%, was significantly over budget. As a percentage of net revenues, non-product costs were 5.2% (\$2.5 million) compared to plan of 9.4% (\$2.6 million). Lower than planned allocations of manufacturing and distribution expenses were partially offset by unfavorable inventory adjustments associated with the scrapping of returned old version Mouse products. In addition, inter-business units royalties, which represent a "royalty" to the Windows business unit for the Mouse/Windows 3.0 bundle, was \$1.0 million compared to plan of \$324,000. The large non-product cost variance, as a percentage of net revenues, is due to the fact that the majority of our allocated manufacturing and distribution costs are relatively fixed. Accordingly, while the absolute dollar amount may not fluctuate significantly when a product group exceeds plan by 77%, non-product costs as a percentage of net revenue can be expected to come in well under plan.

SPAG operating expenses for Q91-1 of \$3.0 million approximated plan of \$2.9 million. As a percentage of net revenues, operating expenses were 6.1% versus plan of 10.6%. Favorable variances in marketing (\$407,000) and outside product development (\$225,000) were offset by a marketing accrual of (\$704,000). Actual marketing expenses (\$802,000) were \$407,000 under plan of \$1.2 million. The favorable marketing variance is due to the delayed release of new SPAG products, the Ballpoint Mouse and Font Cartridges. Due to the underspending of marketing expenses this quarter and certain commitments for Window computing marketing programs, we have accrued \$704,000 under the assumption that the underspending will turn around in future quarters.

Allocations to SPAG of \$6.4 million exceeded plan of \$6.2 million. This variance is due to higher than expected allocation from Legal as a result of an accrual to the litigation reserve of \$2.7 million.

Burdened operating income for Q91-1 of \$19.0 million (38.7% of net revenues) exceeded projected operating income of \$5.1 million (18.6% of net revenues) by \$13.9 million. Robust sales of the Mouse/Paintbrush and Mouse/Windows 3.0 bundle combined with lower than anticipated product costs contributed to the superb Q91-1 operating results.

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Languages

The Q91-1 condensed burdened operating income statement for Languages follows (in millions):

	Actual		Plan		Variance
	\$	%	\$	%	
Net revenues	\$14.7	100.0%	\$12.0	100.0%	\$2.7
Cost of revenues	3.9	26.6	3.2	26.6	(0.7)
Operating expenses	4.1	28.0	5.0	41.6	0.9
Allocations - Research and development	0.5	3.3	0.5	4.5	0.1
Allocations - Sales and marketing	3.1	20.9	3.1	25.4	(0.0)
Allocations - General and administrative	0.3	2.2	0.3	2.3	(0.1)
Burdened operating income (loss)	\$ 2.8	19.0%	\$(0.1)	(0.4)%	\$2.9

Language revenues by channel for Q91-1 were as follows (in millions):

	Actual		Plan		Variance
	\$	%	\$	%	
International Finished Goods	\$ 7.7	52.3%	\$ 6.6	55.2%	\$ 1.1
USSMD	7.4	50.2	5.7	47.6	1.7
Domestic OEM	0.2	1.0	0.1	0.9	0.0
International OEM	0.0	0.2	0.0	0.2	0.0
Adjustments	(0.6)	(3.7)	(0.4)	(3.9)	(0.1)
	\$ 14.7	100.0%	\$12.0	100.0%	\$ 2.7

Net revenues for Q91-1, at \$14.7 million, were \$2.7 million above plan of \$12.0 million. In terms of revenue generation, the product group's leading products (compared with plan) for Q91-1 were as follows (units in thousands, dollars in millions):

Actual	Plan		Actual		Plan		Variance
			Units	Revenue	Units	Revenue	
1	1	Pro C	46.3	\$ 6.6	20.9	\$5.1	\$1.5
2	4	Pro C Update	20.0	2.6	10.0	1.1	1.5
3	2	Pro Fortran	5.7	1.5	12.0	1.7	(0.2)
4	3	Quick C	14.7	0.9	18.2	1.1	(0.2)
5	5	Macro Assembler	8.7	0.8	7.1	0.7	0.1
				\$12.4		\$9.7	\$2.7

Percentage of Languages' net revenues

84%

81%

Professional C was once again the leading Language product with sales of \$6.6 million, 45% of Languages' net revenues. Also contributing to the favorable variance were Pro C Update (\$2.6 million vs. \$1.1 million) and Pro Cobol (\$765,000 vs. \$569,000). Quick C and Pro Fortran were below plan \$220,000 and \$181,000, respectively. International Finished Goods, at \$7.7 million, experienced a \$1.1 million favorable variance. Pro C Update had a favorable variance of \$712,000, while Pro C revenues were \$508,000 above plan. Sales through the USSMD channel at \$7.4 million exceeded plan of \$5.7 million by 30%. Pro C and Pro C Update represented \$1.0 million and \$766,000 of the favorable variance.

As a percentage of net revenues, cost of revenues at 26.6% (\$3.9 million) mirrored plan of 26.6% (\$3.2 million). Product costs were 19.4% of net revenue compared with a budget of 17.9%. USSMD's product costs were 14.4% of net revenue compared to a budget of 15.1%. The favorable variance may be attributed to higher than planned sales of high margin Professional C. International Finished Goods product costs, at 23.1%, were above plan of 19.5%. The unfavorable variance in International Finished Goods is partially due to higher than anticipated sales of the lower margin Professional C Update. Non-product costs were

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Languages

7.2% of net revenues (\$1.1 million) compared to plan of 8.7% (\$1.0 million). The absolute dollar variance is due to a slightly unfavorable manufacturing variance, and higher than plan royalties. The royalty variance reflects higher than forecasted sales of Pro Cobol. The percentage variance is due to the fact that revenue exceeded plan by 23% while many of the manufacturing and distribution costs are fixed.

Languages' operating expenses for Q91-1 were \$4.1 million, 28.0% of net revenues, compared to a plan of \$5.0 million, 41.6% of net revenues. The favorable variance was primarily due to marketing (\$427,000), payroll (\$156,000), and building and grounds distribution (\$124,000). USSMD's marketing expenses were \$568,000 versus a planned \$611,000. Underspending on Pro Cobol and Pro Fortran (\$50,000 and \$36,000 respectively) was partially offset by overspending related to Pro C (\$47,000). International Finished Goods' marketing expenditures were \$314,000 versus plan of \$700,000. This variance was well distributed, with GMBH and LTD having the largest variances. The favorable variances in payroll and the building and grounds distribution were the result of below plan headcount (135 vs. 143 at September 30, 1990).

Allocations to Languages of \$3.9 million mirrored plan of \$3.9 million. Unfavorable variances in International Finished Goods (\$60,000), Legal (\$49,000), and PSS (\$35,000) were partially offset by favorable variances in USSMD (\$59,000) and International Research and Development (\$30,000).

The Q91-1 burdened operating income for Languages was \$2.8 million compared to a planned burdened operating loss of \$54,000. Revenues in excess of plan, combined with lower than anticipated operating expenses and allocations, were responsible for the favorable results.

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Networks

The Q91-1 condensed burdened operating income statement for Networks follows (in thousands):

	Actual		Plan		Variance
Net revenues	\$4,839	100.0%	\$4,974	100.0%	\$(135)
Cost of revenues	805	16.6	648	13.0	(157)
Operating expenses	8,567	177.0	9,880	198.6	1,313
Allocations - Research and development	1,375	28.5	1,605	32.3	230
Allocations - Sales and marketing	4,128	85.3	7,136	143.5	3,008
Allocations - General and administrative	515	10.7	467	9.4	(48)
Burdened operating income(loss)	<u>\$(10,551)</u>	<u>(218.1)%</u>	<u>\$(14,762)</u>	<u>(296.8)%</u>	<u>\$4,211</u>

Networks revenues by channel for Q91-1 were as follows (in thousands):

	Actual		Plan		Variance
US OEM	\$3,132	64.7%	\$2,664	53.6%	\$468
Intl OEM	712	14.7	690	13.9	22
US Networks	600	12.4	1,531	30.8	(931)
International Finished Goods	226	4.7	--	--	226
Intl Networks	187	3.9	190	3.8	(3)
Adjustments	(18)	(0.4)	(101)	(2.1)	83
Total	<u>\$4,839</u>	<u>100.0%</u>	<u>\$4,974</u>	<u>100.0%</u>	<u>\$(135)</u>

In terms of gross revenue generation, the channel's leading products (compared with plan) for the quarter were as follows (dollars in thousands):

Actual	Plan	Product	Actual		Plan		Variance
			Units	Revenue	Units	Revenue	
1	1	LAN Manager	37,732	\$3,342	36,793	\$4,065	\$(723)
2	3	MS-Net	40,709	1,047	15,410	317	730
3	2	SQL Server	346	379	432	591	(212)
				<u>\$4,768</u>		<u>\$4,973</u>	<u>\$(205)</u>

Percent of Networks' net revenues

99%

100%

LAN Manager product revenues (\$723,000 below plan) were negatively impacted by the delayed announcement and distribution of LAN Manager 2.0. The unfavorable LAN Manager variance was offset by MS-Net revenues, which were \$730,000 above plan. SQL Server was \$212,000 below plan due to weak retail sales.

Network business unit net revenues of \$4.8 million were \$135,000 below plan of \$5.0 million. US OEM accounted for 65% of the business unit's Q91-1 net revenues. US OEM LAN Manager revenue of \$2.6 million was \$153,000 greater than the budgeted \$2.4 million. Revenue from MS-Net was over forecast by \$339,000 (178%). SQL Server revenue, however, was \$2,000 versus plan of \$25,000. Strong US OEM performers included American Telephone & Telegraph (\$358,000 against a budget of \$83,000), DEC (\$913,000 against a plan of \$825,000), and SCO (unplanned \$62,000).

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Networks

The International OEM channel had revenues of \$712,000 against a planned \$690,000. Lower than planned revenues from LAN Manager and SQL were offset by MS-Net, which was \$391,000 above plan of \$127,000. Strong International OEM performers included Olivetti (\$293,000 against a budget of \$73,000), Research Machines (\$229,000 against a plan of \$73,000), and Bull S.A. (\$100,000 against a budget of \$7,000). Significant shortfalls from budget were reported by Nokia (\$192,000), NEC (\$90,000), and Toshiba (\$53,000).

US Network packaged product revenues of \$600,000 were \$931,000 below planned revenue of \$1.5 million. Actual LAN Manager sales were \$284,000 compared with a planned \$1.0 million. Delays in the announcement and distribution of LAN Manager 2.0, coupled with the initial startup of the US Network channel, adversely impacted Q91-1 revenues. International Finished Goods had unplanned revenues of \$226,000. MS-LTD, MS-SARL and MS-LTDA accounted for \$118,000, \$41,000, and \$31,000 respectively. International Networks had revenues of \$187,000 against a plan of \$190,000. The majority of this revenue was generated by MS-LTD and MS-SPA, \$132,000 and \$39,000.

Cost of revenues was 16.6% of net revenues (\$805,000) compared to a budget of 13.0% (\$648,000). Actual cost of revenues consisted of 2.0% net product costs, 8.7% non-product costs, and 5.9% royalties; whereas the budget consists of 3.1% product costs, 7.2% non-product costs and 2.7% royalties. The product cost variance is due to the fact that the OEM license revenue represented a larger portion of the BU's revenue than anticipated. The non-product cost variance is the result of unfavorable purchase price variances. The unfavorable royalty variance was due to unbudgeted LAN Manager license fee amortization (\$60,000) and LAN Manager X royalties (\$112,000). This was partially offset by lower than planned SQL royalties (\$40,000).

Operating expenses of \$8.6 million, were \$1.3 million less than a planned \$9.9 million. The expense line items with the largest absolute Q91-1 variances follow (in thousands):

	<u>Actual</u>	<u>Plan</u>	<u>Variance</u>
Product development	\$ 471	\$1,231	\$ 760
Supplies and equipment	271	491	220
Employee recruiting	222	428	206
All other	<u>7,603</u>	<u>7,730</u>	<u>127</u>
	<u>\$8,567</u>	<u>\$9,880</u>	<u>\$1,313</u>

Product development expenses were \$471,000 compared to a planned \$1.2 million. This variance is primarily due to lower than planned use of third-party technical consultants relating to Comm Server. In addition, headcount ramped up slower than anticipated. This situation manifests itself in lower than planned computer supplies, recruiting, payroll and other employee driven costs.

Allocated expenses of \$6.0 million were \$3.2 million less than a planned \$9.2 million. The significant favorable variances were in sales and marketing (International Networks \$1.4 million, US Networks \$669,000, US MSU \$565,000 and USSMD \$164,000). These variances reflect the fact that the creation of new packaged product distribution channels has progressed somewhat slower than planned.

For Q91-1 the Network business unit had a burdened operating loss of \$10.6 million compared to a planned loss of \$14.8 million. This \$4.2 million favorable variance is primarily due to lower than planned operating and allocated expenses.

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Other Product Groups / Business Units

Q91-1 condensed burdened operating income statements for "Other" product groups/business units follows (in millions):

ACTUAL	Books	Services	Multimedia	Xenix	MSI	UPR	Elims	Total
Net revenues	\$4.4	\$ 3.3	\$ 0.1	\$2.4	\$ 0.3	\$(3.1)	\$(1.0)	\$ 6.4
Cost of revenues	2.1	1.2	--	0.8	0.2	--	(1.0)	3.3
Operating expenses	1.6	3.6	2.2	0.2	0.5	--	--	8.1
Allocated expenses	<u>0.3</u>	<u>1.6</u>	<u>0.1</u>	<u>0.1</u>	<u>0.1</u>	<u>--</u>	<u>--</u>	<u>2.2</u>
Operating income	<u>\$0.4</u>	<u>\$(3.1)</u>	<u>\$(2.2)</u>	<u>\$1.3</u>	<u>\$(0.5)</u>	<u>\$(3.1)</u>	<u>\$ --</u>	<u>\$(7.2)</u>
PLAN								
Net revenues	\$5.1	\$ 3.3	\$ 0.1	\$2.4	\$ 0.4	\$1.9	\$(0.3)	\$12.9
Cost of revenues	2.4	0.6	--	1.0	0.2	--	(0.3)	3.9
Operating expenses	1.9	4.3	2.8	0.2	0.4	--	--	9.6
Allocated expenses	<u>0.2</u>	<u>1.5</u>	<u>0.3</u>	<u>0.2</u>	<u>--</u>	<u>--</u>	<u>--</u>	<u>2.2</u>
Operating income	<u>\$0.6</u>	<u>\$(3.1)</u>	<u>\$(3.0)</u>	<u>\$1.0</u>	<u>\$(0.2)</u>	<u>\$1.9</u>	<u>\$ --</u>	<u>\$(2.8)</u>
VARIANCE								
Net revenues	\$(0.7)	\$ --	\$ --	\$ --	\$(0.1)	\$(5.0)	\$(0.7)	\$(6.5)
Cost of revenues	0.3	(0.6)	--	0.2	--	--	(0.7)	0.6
Operating expenses	0.3	0.7	0.6	--	(0.1)	--	--	1.5
Allocated expenses	<u>(0.1)</u>	<u>(0.1)</u>	<u>0.2</u>	<u>0.1</u>	<u>(0.1)</u>	<u>--</u>	<u>--</u>	<u>--</u>
Operating income	<u>\$(0.2)</u>	<u>\$ --</u>	<u>\$0.8</u>	<u>\$0.3</u>	<u>\$(0.3)</u>	<u>\$(5.0)</u>	<u>\$ --</u>	<u>\$(4.4)</u>

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Finance
Discussion Draft of the Three-Year Plan

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18-Oct
MICROSOFT CORPORATION
THREE YEAR PLAN IN SEC FORMAT
For The Years Ending June 30, 1993, 1994, 1995, 1996, 1997, 1998, and 1999
(in millions, except net income per share)
** DISCUSSION DRAFT **

	Actual FY 89	Actual FY 90	Plan FY 91	Current Estimate FY 91	Forecast FY 92	Forecast FY 93
Net revenues	5803.5 100.0%	\$1,163.4 100.0%	\$1,516.2 100.0%	\$1,650.0 100.0%	\$2,200.8 100.0%	\$2,878.9 100.0%
Cost of revenues	204.2 23.4%	232.7 21.4%	297.1 19.6%	333.3 20.2%	424.4 19.3%	546.5 19.1%
Gross profit	599.3 74.6%	930.8 78.6%	1,219.1 80.4%	1,316.7 79.8%	1,776.4 80.7%	2,332.4 80.9%
Operating Expenses						
Research and development	110.2 13.7%	160.6 15.3%	222.5 16.7%	232.5 14.1%	321.8 14.6%	400.8 13.9%
Sales and marketing	219.0 27.3%	317.6 26.8%	512.4 33.8%	503.0 30.6%	697.7 31.7%	904.8 31.5%
General and administrative	27.9 3.3%	39.3 3.3%	46.5 3.1%	48.5 2.9%	59.4 2.7%	72.1 2.5%
Total operating expenses	357.1 44.4%	517.5 45.4%	811.4 53.5%	786.0 47.6%	1,079.7 49.0%	1,377.7 47.9%
Operating income	242.2 30.1%	393.2 33.2%	407.6 26.9%	530.7 32.2%	697.7 31.7%	895.7 31.0%
Non-operating income	16.8 2.1%	23.3 2.0%	29.3 1.9%	30.0 1.8%	41.0 1.9%	54.0 1.9%
Stock option program expense	-4.0 -1.0%	-8.0 -0.5%	-4.0 -0.3%	-3.0 -0.2%	0.0 0.0%	0.0 0.0%
Income before income taxes	250.8 31.2%	410.6 34.7%	432.9 28.5%	537.7 33.6%	738.7 33.8%	1,004.7 34.9%
Provision for income taxes	60.3 10.0%	131.4 11.1%	134.2 8.9%	172.9 10.5%	278.0 10.4%	311.5 10.8%
NET INCOME	\$170.5 21.2%	\$279.2 23.6%	\$298.7 19.7%	\$364.8 23.3%	\$460.7 21.3%	\$693.2 24.1%
Average shares outstanding	112.5	119.4	126.0	124.5	137.3	143.7
NET INCOME PER SHARE	\$1.52	\$2.34	\$2.37	\$3.00	\$3.71	\$4.78

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MICROSOFT CORPORATION
THREE YEAR PLANNED GROSS REVENUES
FISCAL YEARS 1991 THRU 1993
(In millions)

	FY89		FY90		FY91		FY92		FY93	
	ACTUAL	%	ACTUAL	%	PLAN	%	FORECAST	%	FORECAST	%
By COUNTRY										
US&ND	250.3	30.4%	375.2	30.8%	680.1	31.0%	669.8	29.7%	783.4	26.6%
INTL FINISHED GOODS	306.7	36.3%	499.9	41.0%	636.3	42.3%	963.2	42.7%	1,290.3	43.7%
US OPM	134.8	13.9%	149.3	12.3%	156.6	10.1%	178.2	7.9%	212.4	7.2%
INTL OPM	138.8	16.9%	169.0	13.9%	167.1	10.8%	181.1	8.0%	216.7	7.3%
US NETWORKS	0.0	0.0%	0.0	0.0%	32.5	2.3%	137.8	7.0%	283.5	9.6%
INTL NETWORKS	0.0	0.0%	0.0	0.0%	13.6	0.9%	41.3	1.8%	78.0	2.6%
PRESS	12.0	1.3%	14.4	1.2%	20.4	1.3%	24.0	1.1%	30.0	1.0%
CD ROM	0.1	0.0%	0.0	0.0%	0.0	0.0%	0.0	0.0%	0.0	0.0%
US PSS	0.9	0.1%	2.2	0.2%	5.0	0.3%	6.5	0.3%	10.0	0.3%
INTL PSS	0.0	0.0%	1.5	0.1%	1.9	0.1%	2.4	0.1%	3.1	0.1%
US MS UNIVERSITY	4.7	0.6%	5.4	0.4%	7.8	0.5%	10.5	0.5%	12.8	0.4%
INTL MS UNIVERSITY	0.0	0.0%	0.1	0.0%	2.2	0.2%	2.7	0.2%	3.1	0.2%
SYSTEMS JOURNAL	1.3	0.2%	1.3	0.1%	3.6	0.2%	9.6	0.4%	16.0	0.5%
US IITS	0.0	0.0%	0.1	0.0%	0.9	0.1%	5.1	0.2%	8.0	0.3%
INTL IITS	0.0	0.0%	0.1	0.0%	0.9	0.1%	5.1	0.2%	8.0	0.3%
GROSS REVENUES	823.7	100.0%	1,218.4	100.0%	1,350.8	100.0%	2,236.3	100.0%	2,950.6	100.0%
% Growth	37.0%		47.9%		27.3%		43.3%		30.7%	
By COMMODITY										
APPLICATIONS	354.2	43.0%	580.0	47.6%	763.7	49.2%	1,073.0	47.6%	1,393.4	47.2%
BOOKS	13.4	1.6%	14.6	1.2%	20.4	1.3%	24.0	1.1%	30.0	1.0%
SPAC	95.4	11.6%	132.5	10.9%	154.9	10.0%	210.2	9.3%	230.3	7.8%
SYSTEMS JOURNAL	1.3	0.2%	1.3	0.1%	2.2	0.1%	2.7	0.1%	2.7	0.1%
LANGUAGES	31.0	6.2%	36.3	4.6%	64.6	4.2%	83.2	3.8%	92.2	3.1%
MULTIMEDIA	1.4	0.2%	1.2	0.1%	0.8	0.1%	9.7	0.4%	21.6	0.7%
NETWORKS	9.6	1.2%	16.2	1.2%	59.8	3.9%	219.0	9.7%	386.3	13.1%
SERVICES	6.9	0.8%	9.9	0.8%	22.4	1.4%	39.1	1.7%	54.4	1.8%
SYSTEMS	233.1	28.3%	336.4	27.6%	439.8	28.4%	603.9	26.8%	756.3	25.6%
UPR	46.0	5.6%	62.1	5.1%	12.9	0.8%	-20.0	-0.9%	-30.0	-1.0%
XENIX	11.3	1.4%	9.9	0.8%	9.3	0.6%	9.5	0.4%	12.4	0.4%
GROSS REVENUES	823.7	100.0%	1,218.4	100.0%	1,350.8	100.0%	2,236.3	100.0%	2,950.6	100.0%

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MICROSOFT CORPORATION
THREE YEAR PLANNED GROSS REVENUES
FISCAL YEARS 1991 THRU 1993
(In millions)

18-Oct-90

	FT89 ACTUAL	FT90 ACTUAL	FT91 PLAN	FT92 FORECAST	FT93 FORECAST
SYSTEMS REVENUE					
WINDOWS		101.5	151.2	234.5	336.8
DOS		221.5	269.2	303.7	351.6
OS/2		12.3	22.2	39.3	61.1
SYSTEMS PRINTER		1.3	3.2	4.5	7.0
GROSS SYSTEMS REVENUE	233.1	336.4	438.8	603.9	756.5
± Growth	50.1%	44.3%	30.7%	37.3%	25.3%
APPLICATIONS REVENUE					
ANALYSIS		184.3	247.2	355.8	473.0
DATA ACCESS		20.4	22.1	47.9	90.2
ENTRY		95.1	108.5	143.4	179.8
GRAPHICS		9.1	28.6	53.1	76.9
OFFICE		239.9	331.7	431.4	503.0
MAC/INT Office Product		11.2	25.6	41.5	30.5
GROSS APPS REVENUE	339.1	580.0	763.7	1,075.0	1,393.4
± Growth	63.2%	63.8%	31.7%	40.5%	29.3%

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MICROSOFT CORPORATION
Then Year Plan - Consolidated Cost of Revenue
Fiscal Years 1991 thru 1993

	FY93 Plan		Weighted	
	Sales Mtr	Cost %	Cost %	Cost %
USSHO	26.8 %	14.7 %	3.9 %	7.7 %
INTL FINISHED GOODS	43.7	17.7	0.3	0.3
US OEM	7.2	4.0	0.0	0.0
INTL OEM	9.8	3.8	0.4	0.4
US NETWORKS	2.6	7.9	0.2	0.2
INTL NETWORKS	1.0	20.2	0.0	0.0
PRESS	0.1	35.0	0.0	0.0
INTL PSS	0.4	0.0	0.0	0.0
US MS UNIVERSITY	0.2	10.1	0.0	0.0
INTL MS UNIVERSITY	0.1	27.8	0.0	0.0
SYSTEMS JOURNAL	0.5	0.0	0.0	0.0
US ITS	0.3	2.2	0.0	0.0
INTL ITS	100.0 %		12.8 %	
Product Cost (Gross)			107.5 %	

	FY92 Plan		Weighted	
	Sales Mtr	Cost %	Cost %	Cost %
USSHO	29.7 %	15.4 %	4.8 %	7.5 %
INTL FINISHED GOODS	42.7	17.8	0.3	0.3
US OEM	7.9	4.1	0.0	0.0
INTL OEM	8.0	0.0	0.3	0.3
US NETWORKS	7.0	3.8	0.1	0.1
INTL NETWORKS	1.8	7.9	0.2	0.2
PRESS	1.1	20.2	0.0	0.0
INTL PSS	0.1	35.0	0.0	0.0
US MS UNIVERSITY	0.3	0.0	0.0	0.0
INTL MS UNIVERSITY	0.2	10.1	0.0	0.0
SYSTEMS JOURNAL	0.1	27.8	0.0	0.0
US ITS	0.4	0.0	0.0	0.0
INTL ITS	0.2	2.2	0.0	0.0
Product Cost (Gross)	100.0 %		11.1 %	
Effect of Revenue Adjustments			102.5 %	

	FY91 Plan		Weighted	
	Sales Mtr	Cost %	Cost %	Cost %
USSHO	31.0 %	16.8 %	5.2 %	7.3 %
INTL FINISHED GOODS	42.3	17.2	0.3	0.3
US OEM	10.1	2.9	0.0	0.0
INTL OEM	10.8	0.0	0.0	0.0
US NETWORKS	2.1	5.5	0.1	0.1
INTL NETWORKS	0.9	7.9	0.1	0.1
PRESS	1.3	20.2	0.3	0.3
INTL PSS	0.1	27.5	0.0	0.0
US MS UNIVERSITY	0.5	0.0	0.0	0.0
INTL MS UNIVERSITY	0.2	15.1	0.0	0.0
SYSTEMS JOURNAL	0.1	22.5	0.0	0.0
US ITS	0.2	0.0	0.0	0.0
INTL ITS	0.1	3.4	0.0	0.0
Product Cost (Gross)	100.0 %		11.3 %	
Effect of Revenue Adjustments			102.3 %	

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Product Cost (net)
Manufacturing Variance
Inventory Adjustments
Freight, Shipping, & Other
Royalties
Total Cost of Revenues

	13.1	0.2	1.2	3.1	1.4	19.1 %
	100.0 %					19.3 %

	FY93 Plan		Weighted	
	Sales Mtr	Cost %	Cost %	Cost %
APPLICATIONS	47.2 %	11.8 %	5.8 %	
BOOKS	1.0	20.2	0.2	
SPAG	7.8	28.3	3.1	
SYSTEMS JOURNAL	0.1	27.8	0.0	
LANGUAGES	3.1	17.8	0.6	
MULTIMEDIA	0.7	11.6	0.1	
NETWORKS	4.3	4.2	0.6	
SERVICES	1.8	8.2	0.1	
SYSTEMS	23.8	10.0	2.8	
UPB	-1.0	0.0	0.0	
XENIX	0.4	0.0	0.0	
Product Cost (Gross)	100.0 %		12.8 %	

	FY92 Plan		Weighted	
	Sales Mtr	Cost %	Cost %	Cost %
APPLICATIONS	47.8 %	11.8 %	3.8 %	
BOOKS	1.1	20.2	0.2	
SPAG	9.3	37.3	3.5	
SYSTEMS JOURNAL	0.1	27.8	0.0	
LANGUAGES	3.8	17.6	0.7	
MULTIMEDIA	0.4	11.7	0.0	
NETWORKS	9.7	4.2	0.4	
SERVICES	1.7	8.2	0.1	
SYSTEMS	28.6	9.6	2.8	
UPB	-0.9	0.0	0.0	
XENIX	0.4	0.0	0.0	
Product Cost (Gross)	100.0 %		11.1 %	

	FY91 Plan		Weighted	
	Sales Mtr	Cost %	Cost %	Cost %
APPLICATIONS	49.2 %	12.0 %	5.9 %	
BOOKS	1.3	20.2	0.3	
SPAG	10.0	26.0	3.7	
SYSTEMS JOURNAL	0.1	22.5	0.0	
LANGUAGES	4.2	17.9	0.7	
MULTIMEDIA	0.1	10.7	0.0	
NETWORKS	3.9	4.8	0.2	
SERVICES	1.4	6.5	0.1	
SYSTEMS	28.4	8.5	2.4	
UPB	0.8	0.0	0.0	
XENIX	0.6	0.0	0.0	
Product Cost (Gross)	100.0 %		13.3 %	

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MICROSOFT CORPORATION

THREE YEAR HEADCOUNT SUMMARY

For Years Ending June 30, 1991, 1992 and 1993

<u>DIVISION/SUBSIDIARY</u>	<u>Actual 6/30/89</u>	<u>Actual 6/30/90</u>	<u>Current 9/30/90</u>	<u>Planned 6/30/91</u>	<u>Planned 6/30/92</u>	<u>Planned 6/30/93</u>
USSMD	500	629	714	844	968	1105
US NETWORKS	na	61	77	193	229	263
US OEM & OEM/PSS MANAGEMENT	35	43	45	52	64	70
PRESS/BOOKS	42	56	61	67	78	83
US PSS/INTL PSS	317	523	558	691	1010	1217
US MS UNIVERSITY	33	49	83	85	108	128
US ITIS	na	3	16	40	67	88
CORPCOM & PR/TRADE SHOWS	89	111	113	129	142	156
INT'L MANAGEMENT	38	53	57	69	75	86
APPLICATIONS	589	753	806	958	1124	1303
SPAG	21	27	32	41	44	50
MULTIMEDIA	37	70	82	100	134	157
SYSTEMS	345	444	462	536	594	638
LANGUAGES	119	133	135	142	142	142
NETWORKS	125	194	233	252	281	298
INT'L R&D	178	286	326	529	688	834
EXECUTIVE	4	5	4	4	5	5
FINANCE & ADMINISTRATION	324	418	446	532	629	711
LAW & CORPORATE AFFAIRS	22	29	32	42	52	62
DOMESTIC OPERATING EXPENSE HEADCOUNT	2818	3889	4263	5304	6432	7397
UK-MS LTD	65	89	106	134	165	202
SCANDINAVIA-MS AB	45	56	68	106	117	149
GERMANY-MS GMBH	116	173	163	307	388	489
SWITZERLAND-MS AG	5	6	3	18	30	40
FRANCE-MS SARL	128	163	174	273	313	385
SPAIN-MS SRL	8	13	21	32	40	50
BENELUX-MS BV/MS NV	26	35	37	56	68	80
ITALY-MS SPA	31	46	50	72	98	124
EUROPEAN HEADQUARTERS	1	6	10	17	25	30
CANADA-MS INC	60	83	89	119	150	180
AUSTRALIA-MS PTY	50	89	100	109	141	171
MEXICO	7	10	12	17	21	29
SOUTH AMERICA	5	13	17	25	31	40
ISRAEL	1	2	2	3	4	5
SINGAPORE	na	1	1	4	5	7
JAPAN-MS KK	113	161	180	228	265	300
KOREA-MS CH	29	36	46	46	57	67
TAIWAN-MS TC	na	13	14	16	23	27
TAIWAN PRINTER SYSTEMS	na	27	32	33	37	40
IRELAND IPG	23	59	76	194	215	268
SUBSIDIARIES OPERATING HEADCOUNT	713	1083	1203	1809	2193	2683
TOTAL OPERATING HEADCOUNT	3531	4972	5466	7113	8625	10080
MANUFACTURING	506	663	655	872	1049	1225
TOTAL CORPORATE HEADCOUNT	4037	5635	6121	7985	9674	11305

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MICROSOFT CORPORATION

THREE YEAR HEADCOUNT SUMMARY
For Years Ending June 30, 1991, 1992 and 1993

DIVISION/SUBSIDIARY	Growth Percentage '90/'89	Growth Percentage '91/'90	Growth Percentage '92/'91	Growth Percentage '93/'92
USSMD	25.8%	34.2%	14.4%	14.4%
US NETWORKS	na	216.4%	18.7%	14.8%
US OEM & OEM/PSS MANAGEMENT	22.9%	20.9%	23.1%	9.4%
PRESS/BOOKS	38.1%	15.5%	16.4%	6.4%
US PSS/INT'L PSS	65.0%	32.1%	48.2%	20.5%
US MS UNIVERSITY	48.5%	73.5%	27.1%	19.4%
US ITIS	na	1233.3%	67.5%	31.3%
CORPCOM & PR/TRADE SHOWS	24.7%	16.2%	10.0%	10.0%
INT'L MANAGEMENT	39.5%	30.2%	8.7%	14.7%
APPLICATIONS	27.8%	27.0%	17.6%	15.9%
SPAG	28.6%	51.8%	7.3%	13.6%
MULTIMEDIA	69.2%	42.9%	34.0%	17.2%
SYSTEMS	28.7%	20.7%	10.8%	7.4%
LANGUAGES	11.8%	6.8%	0.0%	0.0%
NETWORKS	55.2%	29.9%	11.5%	6.0%
INT'L R&D	60.7%	85.0%	30.1%	21.2%
EXECUTIVE	25.0%	-20.0%	25.0%	0.0%
FINANCE & ADMINISTRATION	29.0%	27.3%	18.2%	13.0%
LAW & CORPORATE AFFAIRS	31.8%	44.8%	23.8%	19.2%
DOMESTIC OPERATING EXPENSE HEADCOUNT	38.0%	36.4%	21.3%	15.0%
UK-MS LTD	36.9%	50.6%	23.1%	22.4%
SCANDINAVIA-MS AB	24.4%	89.3%	10.4%	27.4%
GERMANY-MS GMBH	49.1%	77.5%	26.4%	26.0%
SWITZERLAND-MS AG	20.0%	200.0%	66.7%	33.3%
FRANCE-MS SARL	27.3%	67.5%	14.7%	23.0%
SPAIN-MS SRL	62.5%	146.2%	25.0%	25.0%
BENELUX-MS BV/MS NV	34.6%	60.0%	21.4%	17.6%
ITALY-MS SPA	48.4%	56.5%	36.1%	26.5%
EUROPEAN HEADQUARTERS	500.0%	183.3%	47.1%	20.0%
CANADA-MS INC	38.3%	43.4%	26.1%	20.0%
AUSTRALIA-MS PTY	78.0%	22.5%	29.4%	21.3%
MEXICO	42.9%	70.0%	23.5%	38.1%
SOUTH AMERICA	160.0%	92.3%	24.0%	29.0%
ISRAEL	100.0%	50.0%	33.3%	25.0%
SINGAPORE	na	300.0%	25.0%	40.0%
JAPAN-MS KK	42.5%	41.6%	16.2%	13.2%
KOREA-MS CH	31.0%	21.1%	23.9%	17.5%
TAIWAN-MS TC	na	21.1%	43.8%	17.4%
TAIWAN PRINTER SYSTEMS	na	22.2%	12.1%	8.1%
IRELAND IPG	156.5%	228.6%	10.8%	24.7%
SUBSIDIARIES OPERATING HEADCOUNT	51.9%	67.0%	21.2%	22.3%
TOTAL OPERATING HEADCOUNT	40.8%	43.1%	21.3%	16.9%
MANUFACTURING	31.0%	31.5%	20.3%	16.8%
TOTAL CORPORATE HEADCOUNT	39.6%	41.7%	21.1%	16.9%

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TAX MATTERS

DOMESTIC

Tax Legislation: While the final outcome of the tax bill is uncertain, two issues are of principal concern to MS: (1) luxury taxes on electronic equipment valued above \$1,000 (including microcomputers) and (2) the possibility of eliminating the research and development tax credit. The discussion of luxury taxes took place early on, but was later abandoned. Hopefully this provision is dead. We are supporting the American Electronics Association's efforts to retain the R&D benefit. It is uncertain whether Member amendments or an accompanying Technical Corrections bill will allow insertion of Microsoft's cure to the Passive Foreign Investment Company (PFIC) issue.

Rate for FY 91: Q91-1 financial statement taxes were provided at 31%. This may change during the year if impacted by tax legislation (discussed above).

"Spread" From Stock Plans: The "spread" from stock option exercises is deductible and reduces both federal and state taxes. The amounts of the spread and approximate tax benefits are (in millions):

	FY 90		FY 91	
	Spread	Tax Benefit	Spread	Tax Benefit
Q1	\$12.9	\$4.4	\$21.9	\$7.4
Q2	28.1	9.6		
Q3	38.8	13.2		
Q4	69.7	23.7		
Total	<u>\$149.6</u>	<u>\$50.9</u>	<u>\$21.9</u>	<u>\$7.4</u>

Expedited Refund Procedure: Expedited refund procedures are underway. A refund of \$3.1 million is anticipated from FY 89 to be carried back to FY 86.

Tax Returns for FY 90: The due date for federal and state income tax returns has been extended from September 15, 1990 to March 15, 1991 (the date for some states varies). US corporate income taxes of approximately \$23.5 million on pretax income of \$279.7 million are anticipated.

R&D: For FYs 86-90, Microsoft generated approximately \$32.8 million in research and development (R&D) tax credits. In May 1989, the IRS issued proposed regulations severely limiting R&D credits in future years. MS Tax is participating in a coalition with seven major microcomputer software development companies seeking modification or withdrawal of these regulations. Substantive meetings are scheduled with the IRS during November, 1990.

Payroll Exam: MS Tax settled favorably the 1988 and 1989 payroll exams for a combined cost of \$52,000.

State Income Tax Exams: An examination for Minnesota Income Tax of FY 87-89 is scheduled to begin in Q91-2. Also scheduled is a Franchise Tax exam by Ohio of FY 87 and 88 to begin in Q91-3. Amounts at issue are minimal and have been previously reserved.

Sales and Use Tax: Currently we are filing returns in 29 states. Arizona, New Mexico, and Colorado were added in Q91-1. Alabama and Pennsylvania will be added in Q91-2. During Q91-1, agreement with the State of Arizona was reached on a tax settlement going back to Q87-2. The final tax due was \$70,500. Penalties exceeding \$17,000 were waived.

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Tax Matters

B&O Tax: Preston, Thorgrimson, Shidler, Gates, & Ellis has been retained to file suit in Q91-2 against the Washington State Department of Revenue to resolve our long standing disagreement over the business and occupation tax treatment of OEM licensing revenues. Reserves have been provided in the event we are unsuccessful.

Taxation of Computer Software: The final recommendations of the committee established by the Washington legislature to clarify the personal property tax treatment of computer software are due in Q91-2. Currently, a favorable resolution to the "golden master" issue is anticipated.

INTERNATIONAL

Software Manufacturing Coalition: Owing largely to coalition efforts, the IRS appears favorably inclined to the notion that software companies manufacture, an issue key to the tax benefits we receive in Ireland and Puerto Rico. A further meeting with the IRS to solidify this is scheduled for October 22, 1990.

Microsoft License Paks (MLPs): Use of MLPs creates tax complications in nearly all significant foreign locations. Virtually all jurisdictions consider this transaction "license" revenue, like OEM revenues, as opposed to "sales of a product". Attending this distinction are foreign withholding, duty, and Irish tax deferral issues, as well as other complications. MS Tax is currently investigating particulars in hope of identifying practical solutions in significant foreign locations.

Transfer Pricing: Legislative and regulatory trends of the last several years, together with recent federal budget pressures, are expected to result in increased IRS pressures on U.S. companies to raise transfer prices to their foreign subsidiaries. A number of recent Microsoft transfer pricing issues, including "white box" sku's, corporate down loading contracts, bundled products, and Win 3.0 pricing in the context of the new IBM contract, have occupied the attention of MS Tax. During FY 91, MS Tax plans to review the defensibility of Microsoft transfer prices as well as the need for adjustments in our pricing appropriate to our evolving business.

New Subsidiaries: Microsoft Portugal has been incorporated. It is expected to begin operations November 1, 1990. Progress continues toward tentatively scheduled incorporation of Microsoft Austria (January 1, 1991) and Microsoft Venezuela (December 1, 1990). Also proceeding is the incorporation of the current Mexican branch into Microsoft Mexico with incorporation scheduled for November 1, 1990.

Subsidiary Operations - Tax planning and compliance continued during the quarter. Issues included:

Microsoft BV - Review of stock option plans continues by the Dutch tax inspector. Exposure should be immaterial. A group settlement for BV employees is being negotiated.

Microsoft Sarl - Resolution of issues associated with the transfer of sales territories in Portugal and Greece to Microsoft Portugal and Microsoft Ltd respectively. This included the determination of the value of the ongoing businesses created in Portugal and Greece, as well as the resultant French tax liability upon their transfer.

Microsoft AB - Dissemination of information to employees of tax consequences associated with a change in Swedish law which requires the employee to recognize stock option grants as income. Also created agency agreements with new subsidiaries in Denmark and Norway. These agreements were crafted to minimize high tax rates in these countries.

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*Administration
Manufacturing*

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MANUFACTURING

Equivalent Units

Domestic manufacturing uses the concept of "equivalent units" to measure production and plan capacity. An equivalent unit represents the time consumed in building a particular product, relative to other products. A comparison of equivalent units (EUs) built for Q91-1 and Q90-4 follows:

	Q91-1		Q90-4	
	Total EU	EU/Build Day	Total EU	EU/Build Day
In-House	1,549,932	24,602	1,180,739	18,449
Off Site	465,631	7,391	223,346	3,490
Total	2,015,563	31,993	1,404,085	21,939

In-house equivalent units represent the production at Campus North, while off-site represents the production by our four off-site vendors. Off-site vendors are contracted to duplicate and/or assemble product in support of elasticity of demand. The EU/Day measures the number of equivalent units produced per build day during each of the respective periods. The increase in in-house EUs/Day is primarily the result of improved efficiencies, resulting from the continual refinement of duplication and assembly processes. Actual EUs produced during Q91-1 were: July (630,675), August (821,865), and September (563,023). The drop in production for September reflects the fact that August had 25 production days compared to 19 in September. The slight drop in daily EUs is due to lower forecast demand, as opposed to regression of previously gained efficiencies.

The current EU approach classifies products into one of five categories based on the relative difficulty of building the product on the production line. This classification process is not only somewhat subjective, but it focuses only on assembly, ignoring other processes which impact plant performance taken as a whole. Having analyzed our manufacturing process, it is apparent that the cost driver of most of our plant costs is the number of processed Component Pieces (CP). A CP is defined as the lowest level of assembly (manual, disk, etc.). We believe this new measurement, which was implemented on October 1, 1990 for product costing as well as capacity planning, will assist us on the path to World Class Manufacturing.

Microsoft Ireland, which provides the majority of the package products sold by our European sales subsidiaries, measures production in terms of the gross number of packages built. Ireland feels that this is a better measurement for their product mix, which includes fewer Mac products and updates than Campus North. Total units produced in Dublin for Q91-1 were 643,000 compared to 797,000 for Q90-4.

Backlog

Domestic manufacturing plans production based on Product Marketing's forecast of demand. Buildable backlogs occur when sales orders exceed forecasted demand or when the plant fails to build to forecasted demand. Non buildable backlog occurs when orders have been placed for software or other component parts that have not yet been released to manufacturing. Total backlog was as follows:

	Q91-1	Q90-4
Buildable Backlog		
Win Project	\$531,000	--
Win Word	519,000	--
Win Excel	224,000	--
Win SDK	205,000	\$1,691,000
Mouse	--	2,262,000
C Compiler	--	348,000
Mac Office	--	267,000
Other	391,000	1,389,000
Total Buildable Backlog	1,870,000	5,957,000
Non Buildable Backlog	1,686,000	494,000
Total Backlog	\$3,556,000	\$6,451,000

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Manufacturing

The majority of the backlog at the end of Q91-1 was a result of unplanned demand for Windows application products and for the Win 3.0 Software Developer's Kit. Included in the non buildable backlog is PC Word 5.5, Mac Word 4.0 and Windows 3.0. The software for Word 5.5 has not yet been released. Mac Word 4.0 and Windows 3.0 are considered unbuildable due to unreleased modifications of current version software (aka, flying updates).

Irish manufacturing demand is created by firm orders placed on the plant by the European sales subsidiaries. The backlog definition is consistent with that used domestically, however, since transactions are valued at transfer price, backlog is tracked in units rather than dollars. Ireland's total backlog in units for Q91-1 and Q90-4 follows:

	<u>Q91-1</u>	<u>Q90-4</u>
Buildable Backlog	26,000	44,000
Non Buildable Backlog	<u>109,000</u>	<u>85,000</u>
Total Backlog	<u>135,000</u>	<u>129,000</u>

Rate Based Distribution

In Q91-1, we have expanded the Rate Based Distribution program. The program expanded the product line from Word, Excel and Works (both the PC and Mac environments), to include Word for Windows, Windows and Mice. Merisel joined Ingram Micro D, Egghead and Computerland this quarter as a participant in the Rate Base Program. The effect of Rate Based Distribution is the creation of stable weekly demand on the plant as well as lower inventories for both parties, while increasing customer satisfaction.

Puerto Rico Operation

Microsoft Puerto Rico sales (duplicated disks) to Campus North during Q91-1 were \$28.6 million at transfer price. The estimated corporate tax saving generated in Q91-1 was \$3.5 million. Final completion of the facility is still pending due to construction delays. The hiring of 30 additional non exempt employees, as well as 11 temporary employees, substantially increased capacity during the quarter.

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Corporate Systems / MIS*

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CORPORATE SYSTEMS / MIS

Networks

Extension of our Campus and International Networks continued during the quarter. Domestically, our Metropolitan Area Network (MAN) was extended into Koll, Ridgewood Plaza and Lincoln Plaza A, and our Wide Area Network (WAN) was extended to our new support facility in Charlotte. Internationally, we upgraded our Euro-Net-1 from Redmond to Redding to 128Kb and installed a new private 68Kb Euro-Net-2 from Redmond to Dublin. Extensions of our WAN to Toronto, Ireland IPG and Puerto Rico were also accomplished.

During the quarter, our Corporate Campus was converted to a new five digit telephone system. The prefix 936 is now used solely by Microsoft, with the result that we can accommodate up to 10,000 phones before needing an additional prefix.

MIS Applications Using Microsoft Products and Technology

Implementation commenced during the quarter of the Peoplesoft Human Resource System, replacing our existing personnel system, including payroll and benefits related data. Development efforts are underway on Executive Workbench, and executive information system to enable browsing of Microsoft business data. This will add to other applications using our products and technology currently in use, including: (1) The Lead Tracking System, used by USSMD outbound telemarketing; (2) PC World Wide Sales, a Win 3.0 based query tool for accessing consolidated sales data currently in use at Corporate by over 70 people; (3) PC Infobase, a product and promotion information tool based on the Win 3.0 help engine and used by USSMD customer service; and (4) Product Managers Workbench, a set of tools to assist product managers in defining bills of material for manufactured products.

International

International MIS is midway through replacing Nixdorf computers with IBM AS/400s running Mac-Pac in our major foreign subsidiaries. Mac-Pac is an integrated set of software modules from Andersen Consulting that handles manufacturing, distribution, and financial reporting. An enhancement project in FY90 tailored the Mac-Pac software to our individual international needs.

The first installation of Mac-Pac went live in April, 1990 in Redmond to handle international sales. It was followed by installations in England, Sweden and Germany in July, September and October, respectively.

Seven sites remain to be installed through December 1991:

Canada	December 1990
France	March 1991
Australia	April 1991
Netherlands	June 1991
Japan	August 1991
Italy	October 1991
Spain	December 1991

The total cost for this project is approximately \$10 million, \$3.7 million for hardware, \$3.0 million for installation, and the balance for software, enhancements and localization costs. Sales and processing volumes in the subsidiaries are exceeding those originally planned and the installation schedule has been accelerated to obtain savings in Andersen Consulting fees. As a result, approximately ten International MIS hires originally budgeted in FY92 will be accelerating into FY91.

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Risk Management*

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RISK MANAGEMENT

Directors and Officers (D&O) Liability Insurance - D&O coverage was bound effective September 1, 1990 with National Union Fire Insurance Company, the leading D&O insurer in this country. The policy limit is \$25 million for an annual premium of \$295,000. There is no D&O deductible, and the Corporate Reimbursement deductible is \$300,000 each claim. Claims arising out of "wrongful acts" committed prior to inception of the coverage (other than the Apple, Grossman, and REFAC matters) are not excluded by the policy.

Workers' Compensation - Negotiations are under way with Chubb covering the appropriate wage base for premiums paid in fiscal years 1988, 1989, and 1990. MS Risk Management is seeking in excess of \$50,000 premium refund for those years.

The feasibility of self insuring Washington State workers' compensation is being evaluated. Assumption of this risk by Microsoft could save as much as 40% of the current projected fiscal 1991 premium of over \$600,000.

Apple Claim - Discussions with Chubb on the *Apple vs. Microsoft* copyright infringement case are stalled. Microsoft may have to litigate its claim for coverage with Chubb.

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*Administration
Facilities Report*

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FACILITIES REPORT

Microsoft currently controls approximately 232 acres of land at Corporate Campus. Coupled with 23 acres of land at Canyon Park, Microsoft controls a total of 255 acres in the greater Eastside area. Land totalling 13.36 acres was purchased during Q91-1, resulting in a 6% increase in controlled land over Q90-4. In Q91-2, we are projected to add 25 acres, resulting in a 10% increase over Q91-1. The combined land purchases to date and future acquisitions are as follows:

Phase	Seller	Purchased Acres	Total Purchase Price	Currently Occupied By
CONTROLLED				
1	TIAA	30.79	\$7,908,529	Buildings 1-4
2	Evergreen Partners	21.84	\$5,033,354	Buildings 5-6
3	Evergreen Partners	56.00	\$22,123,079	Buildings 8-11
4	Evergreen Partners	31.22	\$9,425,214	Buildings 16-18
5	Mony	17.15	\$18,272,290	Buildings 12-15
6	Terra Savant	1.79	\$653,003	Vacant
7	McNae	18.27	\$6,369,920	Vacant
8	Benchmark	29.56	\$6,373,161	Vacant
9	Horbach/Lind Bldg. Co.	19.31	\$14,775,911	Vacant
10a	B. McNae	5.95	\$1,491,639	Vacant
Canyon Park	*corporate controlled*	231.88	\$92,426,099	
	Belanich	23.12	\$4,290,492	M&D
	total controlled	255.00	\$96,716,591	
COMMITTED				
10b	Faust	1.25	\$313,088	Vacant
11	PM Realty	4.06	\$13,150,000	EVA/EVB
12	Tektronix	2.07	\$2,327,000	Tektronix Bldg.
	total future committed	7.38	\$15,790,088	
NEGOTIATING				
13	Cosmos	9.31	\$10,500,000	* Vacant
14	Simpson Timber	8.60	\$4,500,000	* Simpson Timber Bldg
	total in negotiations	17.91	\$15,000,000	
MONITORING				
	Koll Overlake Building	5.45	\$18,750,000	** Koll Overlake Bldg
	Rainier Northwest	4.33	\$1,886,148	* Vacant
	Dr. Hayward	2.15	\$1,675,000	* Medical/Dental Bldg
	Highland Professional Cntr	0.57	\$248,292	* Dental Building
	Odegard	1.00	\$435,600	* Vacant
	total monitored sites	13.50	\$22,995,040	

* price estimate

Land Purchase Closures and Commitments (see attached maps)

The Horbach/Lind Bldg Co land (Phase 9), a 19.31 acre parcel of undeveloped land located to the west of existing Microsoft Phase IV, closed August 15, 1990 for a total purchase price of \$14.8 million. At this time, the intent is to keep this property undeveloped and maintain the natural landscape amenities.

The B. McNae land (Phase 10a), a 5.95 acre parcel located adjacent to the existing Phase I and II properties on Bel-Red Road, closed August 28, 1990 for a total purchase price of \$1.5 million. A remaining 1.25 acres is left for purchase (Phase 10b Faust). However, title problems exist which will cause a delay in closing.

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Facilities Report

The PM Realty Buildings (Phase 11) are scheduled to close October 30, 1990 for a negotiated base purchase price of \$13.15 million. This is inclusive of the EVA (McDonnell Douglas) and EVB (Micronim) buildings. Due diligence activity is currently underway.

The Tektronix Building (Phase 12), located inside of Microsoft Place Office Park, is scheduled to close December 22, 1990 for a negotiated purchase price of \$2.3 million. Due diligence activity is currently underway. This transaction, along with the purchase of both PM Realty buildings, will give Microsoft full control of all land and buildings inside Microsoft Place.

Land Purchase Negotiations

Cosmos Development Company (Phase 13) owns a 9.3 acre parcel of land south of the Horbach land off of 156th Ave NE. Negotiations have been in progress with Cosmos for the purchase of the property. Cosmos has agreed to a \$10.5 million selling price. We plan tentatively for Cosmos to act as construction manager for a fixed fee during the Microsoft build-out. CER approval and drafting of the Purchase and Sale Agreement are in progress. (see attached map Area 'B')

The Simpson Timber land (Phase 14) located adjacent to the Horbach/Mastro property is under purchase consideration. We intend to pursue this transaction during Q91-2. (see attached map Area 'C').

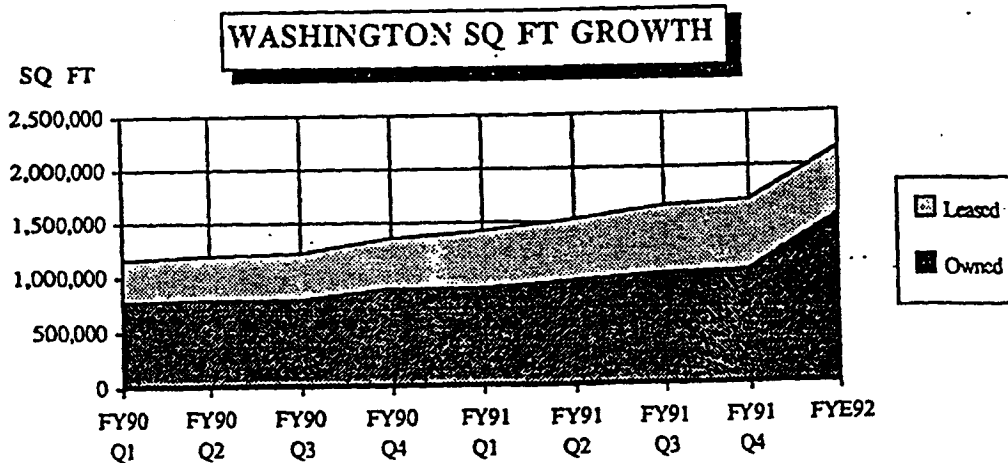
Possible Land Purchase

The Koll Overlake Building, the majority of which is Microsoft leased, is a possible building purchase. This would tie directly with the Cosmos land purchase and give adjacency in that area. (see attached map Area 'A').

Other parcels of land located in the immediate Corporate Campus area are currently being monitored for possible purchase activity (see chart and attached map Area 'D' for actual parcels).

Facilities Within the State of Washington

Anticipated growth in facilities within the state of Washington is shown in the following chart:



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Facilities Report

As of the end of Q91-1, Microsoft owned 900,000 square feet in the State of Washington. Combined with a total of 515,000 square feet leased, total Washington property occupied was 1.4 million square feet. This represents a 5% increase in square footage over Q90-4, equivalent to 70,000 square feet additional during Q91-1. Q91-2 is projected for an additional 96,000 square feet, or a 7% increase over Q91-1. At the end of Q91-4, Microsoft is projected to occupy 1.7 million square feet, a 24% increase in square footage over Q91-1. Of the additional space by the end of Q91-4, 36% will be owned by Microsoft and 64% will be leased. The following is an itemization of the anticipated expansion.

Washington Owned Facilities

Corporate Campus Building 12 is currently occupied by The Ecova Corporation (approximately 31,000 sq ft). Negotiations continue in an effort to reach an agreement with Ecova for them to relocate outside of Microsoft Place.

Corporate Campus Buildings 16 and 17 (320,000 sq ft) are proceeding 2 days ahead of schedule. The slab on grade is currently in progress for the garage area. The pouring of the first raised parking deck has commenced for Building 16. Occupancy is anticipated for Q92-2.

Corporate Campus Building 18 (150,000 sq ft) has been approved by the Design Review Committee for the City of Redmond. Work is continuing on the entire government approval process (Technical Review, Planning and Building Department). Construction is scheduled to commence in late Fall/early Winter 1990.

Washington Leased Facilities

The Koll Overlake Building lease for an additional 72,000 square feet was completed and signed during Q91-1. Several phases of construction and expansion are planned for both Q91-1 and Q91-2, with occupancy by the majority of the IPG group.

EVB (the Microrim Building) is under negotiation with the tenant, Microrim. Microrim is scheduled to vacate their existing building in November 1990.

PSS Lincoln Plaza will house only the Applications side of PSS as of the end of October 1990. Additional footage at Lincoln Plaza totalling 11,000 square feet will be occupied during Q91-2.

Ridgewood Plaza, located in the same complex as Ridgewood F (new home for USSMD Support), will house Product Support Systems groups. The 62,000 square foot building is scheduled for occupancy during October 1990.

Ridgewood Building 'F' is the new home for the USSMD Support division. The building, now referred to as "USSMD F", is located in an existing office park off NE 8th in Bellevue. Occupancy was completed during September 1990.

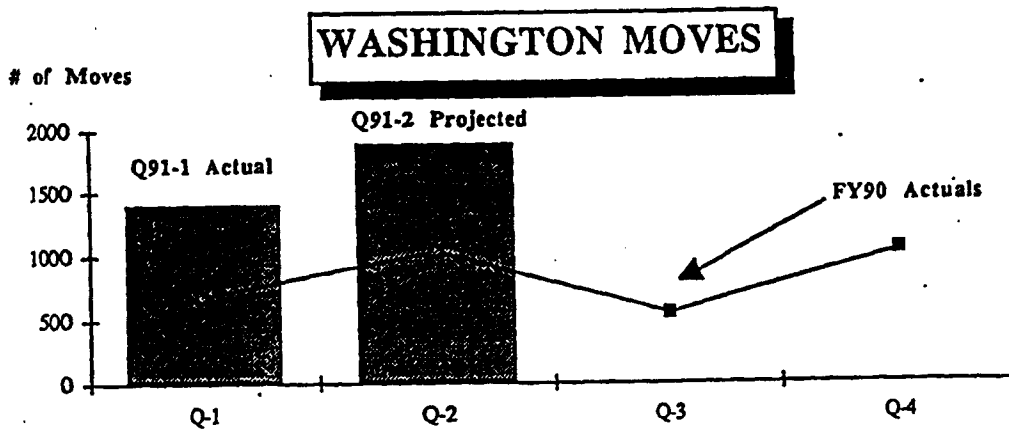
MSU Bellevue will need expansion space for FY91 headcount growth. Several options are being evaluated at this point.

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Facilities Report

Washington Moves and Remodels

In addition to anticipated expansion, the Facilities department is projecting a significant Q91-2 increase in moves and remodels within the state of Washington.



During Q91-1, 1,403 moves were complete. This is a 105% increase in move volume over Q90-1. Q91-2 is projected for 1,873 employee moves; 34% increase over Q91-1 and an 81% increase over Q90-2. The large move volume is primarily the result of IPG to Koll and reshuffles; Systems group reshuffle; USSMD Sales and Support to Ridgewood and reshuffles. Along with the move volume, 47 construction projects were completed during Q91-1, affecting 99,000 square feet of space. This is a 95% increase in square footage remodeled over Q90-1. Q91-1 major moves and remodels:

MOVES:

- The expansion of DOS, Windows and Languages from Building 3 to Buildings 3 and 4 (152 employees).
- The relocation of IPG from Building 9 to Koll Overlake, accompanied by a major reshuffle of IPG in Building 9 (170 employees).
- The relocation of USSMD from Building 8 to Ridgewood F (290 employees).
- OS/2 NT group relocation from Buildings 1 and 2 to Building 4 (85 employees).
- The consolidation of OS/2 in Building 2 from Buildings 1 and 2 and Networking inside of Building 1 (157 employees).

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Facilities Report

REMODELS:

- Construction of the Systems Testing Lab in Building 2 (2,156 square feet).
- Remodel of existing MSU space in Bellevue (3,500 square feet).

Major moves of 150+ employees are scheduled every weekend during Q91-2 excluding holiday weekends. This includes Washington moves only. Field office moves will be occurring at the same time. Projected Q91-2 moves and remodels include:

- During October, IPG will move to Koll Overlake; PSS Systems from Lincoln Plaza to Ridgewood G; MS Press reshuffle in Buildings 12, 13 and expansion of 14; and the OBU relocation to Building 10 from Building 5.
- During November, OS/2, Portable Systems, Dos Windows will reorganize within Buildings 2, 3 and 4 (Systems reshuffle); Finance, Legal and USSMD expansion within Building 8.
- In December, IPG relocation to Koll Overlake; Pac West Sales office relocation to Bellevue Place.
- Remodel projects will include Phase 2 and 3 of the Networking Lab in Building 1.
- Tenant improvement construction of the existing USSMD Open Concept Space in Building 8 into standard offices commencing in September with occupancy in October.
- Construction of the Network Lab (7,500 square feet) in Building 1.

LID/Road Work

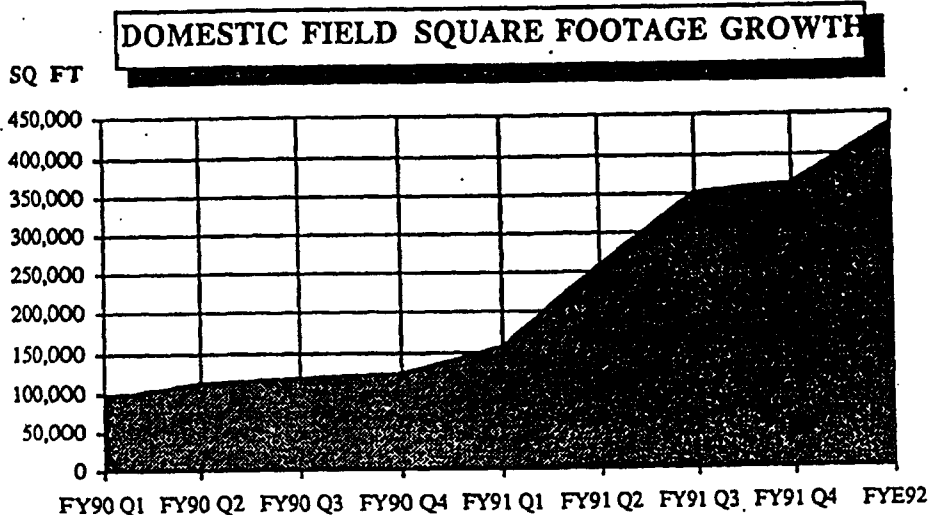
- 156th LID (improvements of 156th avenue from Microsoft's south boundary past the connection with Bel-Red Road) are now complete.
- Bel-Red LID (improvements to Bel-Red from 156th to 40th) is in the final stages of completion. The scope of work involves the widening of Bel-Red Road between 40th and 156th avenue.
- F-line is a planned connecting road from Bel-Red to 156th across the south end of Microsoft property. Discussions with the city are continuing in an attempt to reach agreement on whether or not this public road will be on Microsoft property. Microsoft's goal is not to have a public street dividing the campus. The purchase of the Phase VII (McNae) land further strengthened Microsoft's position in these discussions.

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Facilities Report

Domestic Facilities Outside the State of Washington

Anticipated growth in facilities outside the state of Washington during the next two years is shown in the following chart:



As can be seen by the chart above, Microsoft domestic field locations outside of Washington will increase significantly in square footage during this fiscal year. Current Q90-1 total is at 160,000 square feet. This represents a 28% increase in square footage occupied over Q90-4. Q91-2 is projected for an additional 102,000 square feet, or a 65% increase over Q91-1. At Q91-4 end, the domestic field will total 365,000 square feet of office space, a 128% increase over Q91-1. The majority of the increase will occur in USSMD field locations which currently total 105,000 square feet. The Q91-4 total will be 250,000 square feet, a 140% increase over Q91-1. Outside of USSMD sales locations, a new 54,000 square foot building for PSS Charlone will be the major addition in the field.

USSMD Domestic Locations

Progress of the USSMD field office expansion across the county is proceeding as planned. The majority of moves will occur during Q91-2 and Q91-3. The following is an update on the USSMD projects:

- The Boston office expansion of 8,000 sq ft of office space was completed during July 1990. The office will move to a new floor inside of the existing building during Q91-4 as planned.
- The New York office lease for 29,000 sq ft of new space at Worldwide Center in Midtown Manhattan was completed and signed during Q91-1. Construction drawings are currently underway with occupancy scheduled for January 1991.
- The Philadelphia office will move from executive office suite space in Delaware to a new building in the Philadelphia area. Lease negotiations are underway with occupancy scheduled for January 1991.

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Facilities Report

- The Washington DC office lease for 24,000 sq ft of new office space at Chevy Chase Pavilion in Washington DC proper was completed and signed during Q91-1. Construction drawings are currently underway with occupancy scheduled for December 1990.
- The Chicago office lease for 9,500 sq ft of adjacent expansion space at One Lincoln Centre in Oakbrook Terrace was completed and signed during Q91-1. Construction drawings are currently underway with a phased occupancy scheduled for December and January 1991.
- Dallas expansion of 5,000 sq ft of adjacent expansion space is currently under construction. Occupancy is scheduled for the first week in November 1990.
- The Detroit office lease for 14,000 sq ft of new office space at 1000 Towne Center in Southfield was completed and signed during Q91-1. Construction drawings are complete with occupancy scheduled for December 1990.
- The Minneapolis office lease for 12,000 sq ft of new office space at 8300 Norman Center Drive in Bloomington will be completed during Q91-2. Construction drawings are currently underway with occupancy scheduled for December 1990.
- St. Louis will open a new office during the Winter of 1991. Lease negotiations are underway. Occupancy is tentatively scheduled for February 1991.
- Denver will open a new office during December 1990. The lease for 10,000 sq ft of office space at Regency Plaza in The Tech Center, Denver, was completed during Q91-1. Construction drawings are complete with construction scheduled to commence mid October 1990.
- The Los Angeles office is planned to expand in the latter part of FY91.
- Orange County office opened its doors during Q91-1 with a move into 4,000 sq ft of temporary space in Irvine. Plans for new permanent space are underway with lease negotiations in progress. Occupancy is scheduled for February 1991.
- Phoenix will open a new office during the latter part of FY91.
- The Santa Clara office is planned for a move into 22,000 sq ft of new office space in the San Mateo/Redwood Shores area. Request for Proposals are out to respective buildings. A lease is anticipated to be signed during Q91-2. Occupancy is tentatively scheduled for February 1991.
- The Pac West office lease for 16,000 sq ft of new space at Belleyue Place is currently in the final stages of lease negotiations. Occupancy is scheduled for December 1990.

PSS Domestic Locations

- PSS Charlotte moved into temporary space (17,000 sq ft) during Q91-1. The new facility (54,000 sq ft) is on schedule, with occupancy targeted for December 1990.

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Facilities Report

MSU Remote Locations

- MSU Boston will complete adjacent expansion of 3,500 sq ft during Q91-2. The expansion includes the addition of a training room space.
- MSU Chicago and MSU Dallas are both planned for occupancy January 1991. Both will be located in current USSMD buildings.
- All remaining MSU locations will be co-located with existing USSMD offices (Washington DC, Santa Clara, Los Angeles)

International Facility Development

Facilities development continues to be a major activity for the international offices and subsidiaries. Most of the existing international offices and subsidiaries are in the planning process or are already moved to new locations and offices.

MS AB (MICROSOFT SWEDEN) has finished the review process and the decision has been made to lease new office space at the current location for an additional three years. Concurrently, the search for property and expansion will take place to explore cost and options for future growth.

MS BV (MICROSOFT HOLLAND) is in the process of evaluating future facilities. All signs are pointing toward a 35,000-square-foot lease solution within the existing location. Various options already exist to accommodate space requirements for approximately three to five years.

MS GMBH (MICROSOFT GERMANY) has moved their sales and marketing personnel as an interim solution. Edisonpark - building one (70,000 square feet), is making rapid progress and the completion date of June 1991 should be met. As well, an additional option for building two has been signed. This will guarantee growth over the next three to five years. The search for a solution after that period has begun. The Frankfurt and Berlin sales offices have been occupied.

MS INC (CANADA) Their new 76,000-square-foot facility and warehouse have been slightly delayed. They are confident that they will be able to occupy the facility in January 1991.

MS KK (MICROSOFT JAPAN) will soon require a new facility. A study of our options and costs has begun.

MS LTD (MICROSOFT ENGLAND) has broken ground for the two-phase office building and warehouse. Phase I (65,000 square feet) and the warehouse are targeted for completion by October 1991 and is on schedule. The total project will cover approximately 110,000 square feet of office space.

MS MEXICO is searching for room to expand. Options on cost and space requirements are currently being evaluated.

MS PTY (MICROSOFT AUSTRALIA) The new campus and MSU building are making continuous progress. Occupancy is still targeted for April 1991.

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Facilities Report

MS SARL (MICROSOFT FRANCE) Construction for the new 57,000-square-foot building (Phase I) is on schedule. Given the tremendous growth projections, a decision has been made to start with Phase II immediately. The project is on time and the proposed move is scheduled for March or April 1991.

MS SPA (MICROSOFT ITALY) will outgrow their current space in mid 1991. Negotiations are in progress to expand within the existing building, to last an additional three years. A search has begun, as well, for an alternative purchase of land and building construction, as has been done at other subsidiaries.

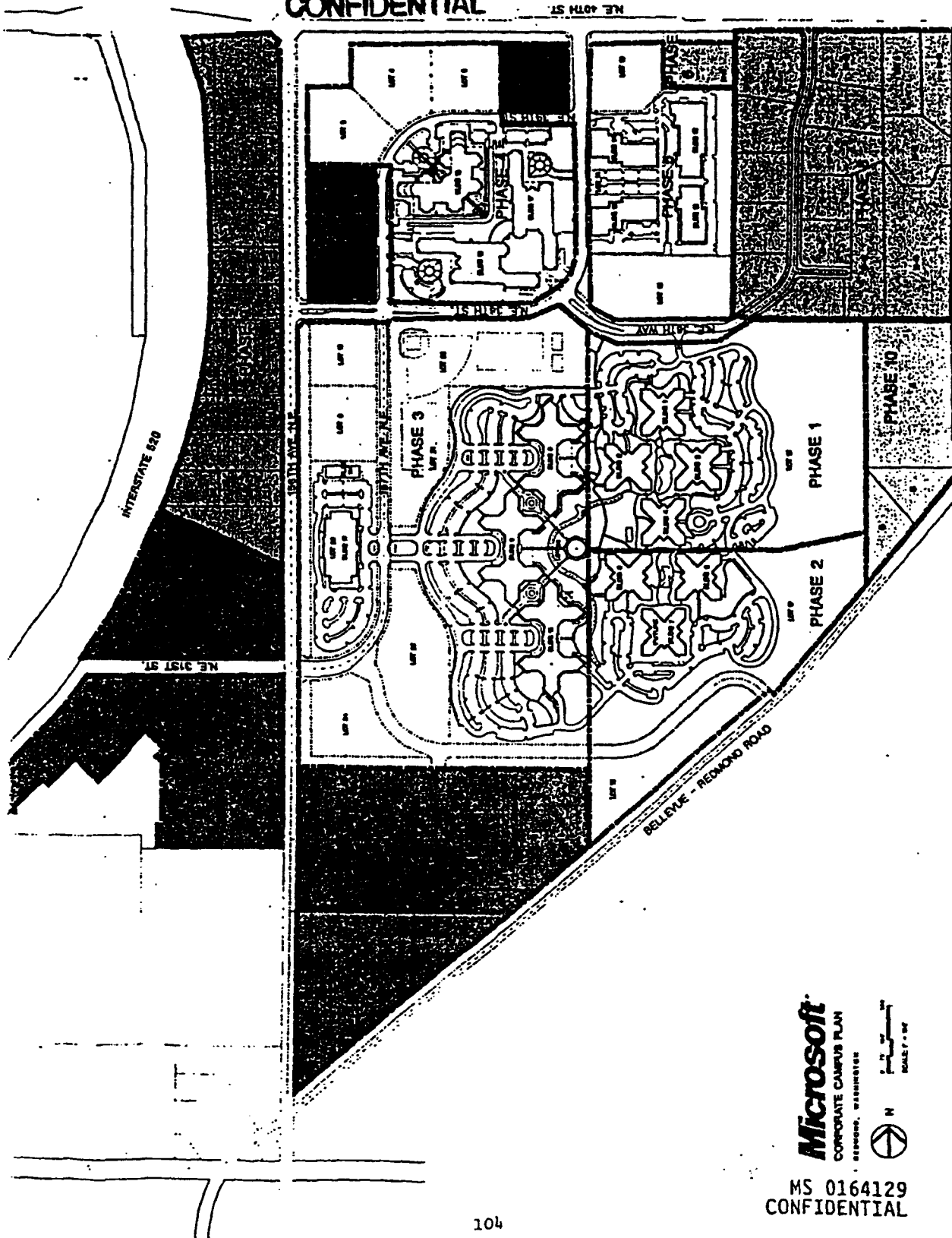
MS SRL (MICROSOFT SPAIN) will finally move into their new office at the end of October 1990. The 12,000-square-foot accommodation will be adequate for two years. The warehouse has been in operation for six months.

MS TC (MICROSOFT TAIWAN) has moved into one additional floor in the existing building. This will give them enough space for two years.

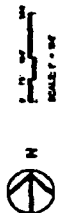
IPG MICROSOFT IRELAND is currently going through the approval process for Phase II of their International Product Group Scandinavian Localization Center.

PUERTO RICO The disk duplication facility has been occupied.

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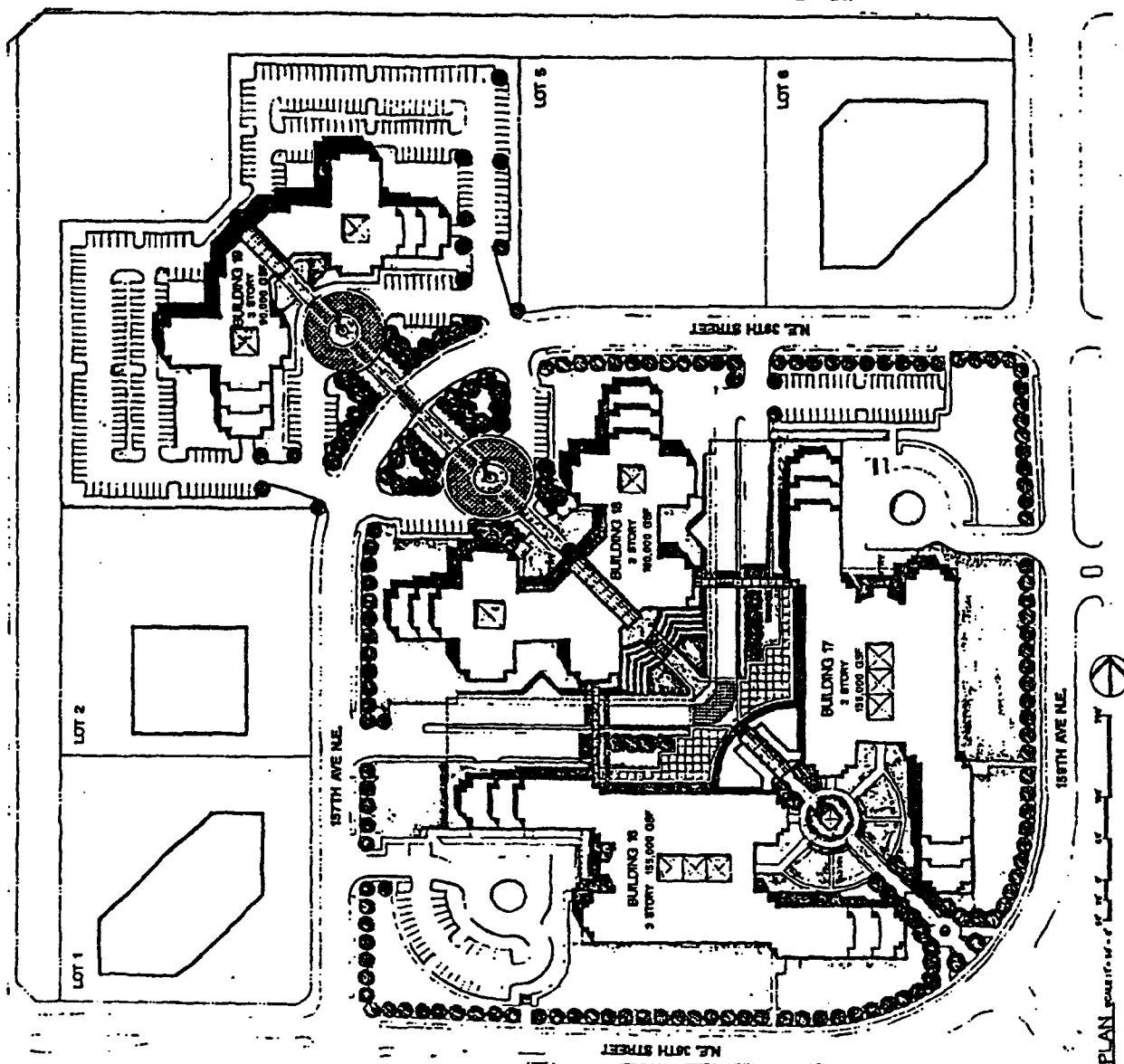
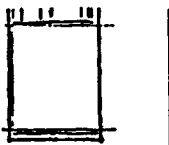
Microsoft
CORPORATE CAMPUS PLAN
REDMOND, WASHINGTON



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Notes:
1. All buildings are 3 stories high.
2. All buildings are 100,000 sq. ft.
3. All buildings are 100,000 sq. ft.

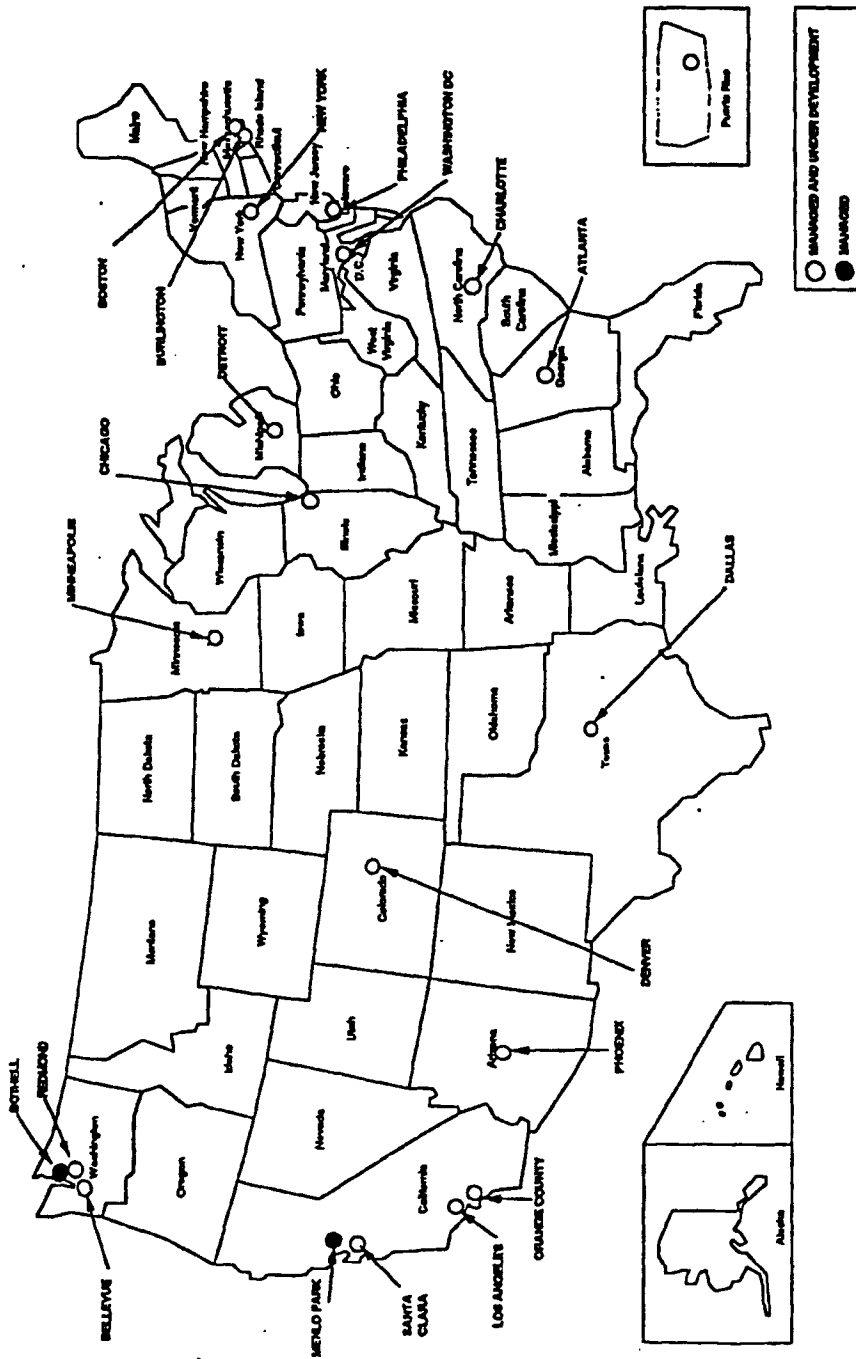


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Microsoft
PHASE IV MASTER SITE PLAN

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MICROSOFT DOMESTIC LOCATIONS

20 CITIES
 12 BUILDINGS OWNED
 40 BUILDINGS WITH LEASED SPACE
 55 TOTAL OCCUPIED BUILDINGS
 1,640,000 Square Feet Managed

SEPTEMBER 1990

FACILITIES - REAL ESTATE/DEVELOPMENT

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**MICROSOFT DOMESTIC SQUARE FOOTAGE
(AS OF THE END OF SEPTEMBER 1990)**

	OCCUPIED MANAGED	DEVELOPMENT
CORPORATE		
buildings 1 - 4	240,000	
buildings 5 - 6	120,000	
buildings 8 - 9	235,000	
building 10	117,500	
building 1111a	83,565	
buildings 16 - 17		320,000
building 18		150,000
buildings 12 - 15	87,185	31,093
tektronix		17,000
koll overlake	26,469	66,822
eva	31,875	13,125
evb		48,000
*corporate subtotal	941,594	646,040
MANUFACTURING/DISTRIBUTION		
canyon park	264,136	
WASHINGTON FIELD		
pss office	95,687	72,893
usmmd ridgewood f	54,000	
corp com warehouse	33,221	
ms university	26,237	10,500
off site storage	7,447	
*washington field	216,592	83,393
USSMD FIELD		
atlanta	6,355	
boston	18,719	24,480
new york	9,668	29,501
wash dc	8,990	24,200
philadelphia	1,360	10,131
*eastern subtotal	45,092	88,312
chicago	7,551	9,531
dallas	14,973	5,203
detroit	2,724	14,100
minneapolis	4,179	11,500
st louis	0	10,920
*central subtotal	29,427	51,254
denver	1,000	9,494
los angeles	11,822	6,448
orange county	4,327	13,920
phoenix	800	5,760
santa clara	7,858	22,500
seattle	3,920	15,828
*western subtotal	29,727	73,950
*USSMD subtotal	104,246	213,516
MISCELLANEOUS FIELD		
msu remotes	3,563	14,935
consulting san francisco		4,500
menlo park (GBU)	31,847	
pss charlotte	17,000	114,632
ny systems journal	3,200	
*miscellaneous field subtotal	55,610	134,067
TOTAL SQUARE FOOTAGE	1,582,178	1,077,016
GRAND TOTAL SQUARE FOOTAGE		2,659,194

10/16/90

Microsoft Domestic Square Footage

Real Estate - Development

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Administration
Investor Relations / Stock Administration

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INVESTOR RELATIONS / STOCK ADMINISTRATION

Q91-1 Earnings Release: On Tuesday, October 16, 1990, at approximately 10:00 am (E.D.T.), the full earnings for the first quarter was released. The conference call with the financial analysts was held at 3:00pm E.D.T.

Selected Earnings Estimates for MSFT for FY91: Below are earnings estimates by selected analysts.

Analyst	Q1E	FY91E
Alex. Brown	\$.70	\$3.10
CJ Lawrence	.70	3.10
Cowen & Co.	.72	3.50
Dean Witter	.70	3.25
DLJ Securities	.60	3.00
Goldman Sachs	.70	3.10
Merrill Lynch	.72	3.00
Montgomery	.70	3.00
Paine Webber	.64	(1.95)*
Piper Jaffray	.66	3.05
Prudential Bache	.63	3.00
Shearson Lehman	.70	3.25

*Loss due to predicted negative result in Apple lawsuit.

Stock Options/Cashless Exercises: In Q91-1, there were 494,891 shares exercised (458 optionees). The 75% decrease in total shares exercised, in comparison to Q90-4, can be related to the high volatility and downward trend of Microsoft's stock price throughout the quarter (high=\$79.25 / low=\$51.75).

Alex. Brown continues to be an integral part of Microsoft's cashless stock option exercise process by facilitating the majority of shares exercised and traded. The confirmed number of accounts for Microsoft employees is currently 1,758. In Q91-1, Alex. Brown performed cashless exercises for 284 optionees (62% of all optionees), which consisted of 80%, or 391,574 shares, of the total 494,891 shares exercised throughout the quarter. As shown in the following table, shares exercised dropped off considerably in Q91-1.

SUMMARY OF SHARES EXERCISED FY90 - FY89

(adjusted for stock split)

	<u>Q90-1</u>	<u>Q90-2</u>	<u>Q90-3</u>	<u>Q90-4</u>	<u>Q91-1</u>
Shares Exercised	747,214	1,296,668	1,276,668	1,909,556	494,891
Price					
High	34.25	44.25	58.25	77.65	79.25
Low	26.00	34.50	43.06	55.75	51.75

Float: Microsoft public float as of September 30, 1990, excluding Officers and Directors, was approximately 40%, or 46,113,479 shares.

Microsoft Ownership Profile

(as of most recent filing)

	<u>Number of Shares</u>	<u>% of Shares Outstanding</u>
Officer, Directors and 10% Shareholders		
William H. Gates	40,350,620	35.5%
Paul Allen	18,350,000	16.1
Steve Ballmer	7,017,004	6.2
Other Officers & Directors	<u>1,854,271</u>	<u>1.6</u>
Total Officers & Directors	67,571,895	59.4
Other Holders	<u>46,113,479</u>	<u>40.6</u>
Total Shares Outstanding	<u>113,685,374</u>	<u>100%</u>

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COMPOSITE INDEX ASSIGNED INDEX (INDUSTRIAL)

HIGH	385.19	412.47
LOW	325.06	352.06
CLOSE	324.24	368.46
PREVIOUS CLOSE	381.21	408.94
% CHANGE	-9.62	-9.45
TOTAL NASDAQ VOLUME	7,081,388,800	
TOTAL MMS TRADING	1,655,050,568	
TOTAL MMS SECURITIES	2,650	

1. PRICE RANGE	HIGH	63 1/2	LOW	54 1/2	PERCENT CHANGE	12.44
2. LAST PRIC. (AUG)	(SEP)	63				
3. VOLUME FOR MONTH		17,000,855				
4. TOTAL TRADES		17,717				
5. BLOCKS: NUMBER OF BLOCKS		283	NUMBER OF SHARES	4,397,200		

MSFT
 Common Stock (\$0.001 PAR VALUE)
 113,599,890
 2,038,432 AS OF 09/14/90

Microsoft Corporation
 Mr. Francis J. Gaudetle
 Senior Vice President Finance
 One Microsoft Way
 Redmond WA 980526399

DATE	HIGH	LOW	LAST	NFT CHANGE	SHARE VOLUME	TRADES	MMS VOLUME	NASDAQ VOLUME	COMPOSITE CLOSE
MON 3					659,468	459	58,232,893	78,140,900	381.67
TUE 4	62 1/2	60 3/4	62 1/4	• 3/4	760,070	872	60,081,755	89,049,200	382.44
WED 5	58 1/2	57 1/2	57 1/2	• 1 1/2	1,508,687	544	82,311,339	98,734,000	378.78
THU 6	58	56 1/4	57 3/4	• 3/4	3,772,902	2,559	290,751,518	103,159,000	380.38
WEEK	63	56 1/4	57 3/4	• 3/4				369,083,100	380.38
MON 10	60 3/4	55 3/4	55 3/4	• 2	1,032,300	747	72,322,387	88,258,800	381.73
TUE 11	59 1/2	55 3/4	57 3/8	• 1 1/8	1,095,144	249	74,401,046	100,088,700	379.49
WED 12	58 1/2	55 3/4	57 1/2	• 1 1/8	1,043,017	587	81,432,911	98,467,600	380.32
THU 13	58 1/2	55 3/4	57 1/2	• 1 1/8	932,421	679	79,032,797	103,651,100	378.18
FRI 14	60 1/4	55 3/4	59 3/4	• 3 1/4	4,815,223	3,625	387,952,230	103,494,100	377.42
WEEK	60 1/4	54 1/2	59 3/4	• 3 1/4				505,938,300	377.42
MON 17	61 3/4	59 1/4	60 3/4	• 1	978,981	823	74,998,832	94,017,800	372.11
TUE 18	61 3/4	59 3/4	61 3/4	• 1 1/4	732,732	654	69,057,894	115,072,300	372.21
WED 19	61 3/4	59 3/4	62 1/2	• 1 1/4	729,015	623	90,491,274	120,898,000	364.43
THU 20	62 3/4	59 3/4	62 3/4	• 2 1/4	1,110,235	427	85,405,304	124,237,700	362.54
FRI 21	63 1/4	58 1/2	60 1/2	• 3/4	4,594,288	3,111	433,873,653	562,115,500	362.54
WEEK	63 1/4	58 1/2	60 1/2	• 3/4				144,826,000	352.18
MON 24	60 1/2	57 1/2	58 1/2	• 2 7/8	1,135,070	788	92,282,210	128,211,700	350.03
TUE 25	60 3/4	58 3/4	60 3/4	• 1 1/8	1,241,168	536	90,969,382	128,211,700	341.19
WED 26	61 1/2	59 1/4	59 1/4	• 1 1/8	546,182	445	39,048,431	153,777,400	344.51
THU 27	61 1/2	58 1/4	61 1/2	• 3/4	513,505	639	127,181,448	157,506,700	344.51
FRI 28	63 1/2	57 1/2	63	• 3 1/2	1,262,507	1,077	942,772,977	654,252,100	344.51
WEEK	63 1/2	57 1/2	63	• 3 1/2					

AS OF 09/28/90

482,900 MIDDY & CO INC
 481,515 BALEMAN EICHLER & MILLEZ
 479,700 FURMAN SECURITIES INC
 479,700 RAGEN SECURITIES INC
 439,461 CYRUS J LAVRENCE, INC
 431,888 OLDE DISCOUNT CORPORATION
 399,690 FARMSTEAD & CO, INC
 343,728 WEEBEN AND CO, INC
 266,260 TUCKER ANTHONYS R. L. RAY
 229,900 PRINCETON FINANCIAL GP INC

7,106,372 SAL OMON PROZ, INC
 1,025,200 REAR SYSTEMS & CO.
 1,309,930 MONTGOMERY SECS INC
 1,049,724 MAYER & SCHWETZER INC
 1,984,359 PRUDENTIAL-BUCKIN & JENNETTE
 795,617 DONALDSON, LUKIN & JENNETTE
 882,525 COPENHAGEN SECURITIES CO, INC
 602,600 DEAN WITTE RYMIDOS, INC.
 405,771 DEAN WITTE RYMIDOS, INC.
 410,776 MIDWEST STOCK EXCHANGE

MERRILL LYNCH PIERCE, FENNER
 THE FIRST BOSTON CP
 PATINWEBER INC & CO
 GOLDMAN, SACHS & CO
 HERZOG, SUTHERLAND & GOULD INC
 PETER JAFFRAY & HOPWOOD, INC
 LEHMAN BROTHERS
 LEHMAN STANLEY & CO INC
 MORGAN BARNY/HARRIS UPIAM
 SMITH BARNY/HARRIS UPIAM
 ALEX BROWN & SONS

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MS-PCA 1189162)
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NASDAQ/NMS SYSTEM STATISTICS

COMPOSITE INDEX ASSIGNED INDEX (INDUSTRIAL)

HIGH	438.59	472.72
LOW	370.68	370.68
CLOSE	381.21	406.94
PREVIOUS CLOSE	438.34	472.81
% CHANGE	-13.01	-13.93

TOTAL NASDAQ VOLUME	3,409,610,100
TOTAL NMS VOLUME	2,407,324,158
TOTAL NASDAQ TRADES	1,250,643
TOTAL NMS TRADES	2,671

SUMMARY FOR THIS SECURITY

1. PRICE RANGE	HIGH	67 1/4	LOW	50 3/4
2. LAST PRICE	(JUL)	66 1/2	(AUG)	61 1/2
3. VOLUME THIS MONTH	(AUG)	27,608,497	(JUL)	27,608,497
4. TOTAL TRADES	(AUG)	1,100	(JUL)	1,100
5. HIGHS NUMBER OF HIGHS	(AUG)	1	(JUL)	1
6. NUMBER OF SHARES	(AUG)	7,412,207	(JUL)	7,412,207
7. PERCENT CHANGE	(AUG)	-7.52	(JUL)	-7.52

Microsoft Corporation
One Microsoft Way
Redmond WA 980528399

DATE	HIGH	LOW	LAST	NCT CHANGE	SHARE VOLUME	TRADES	NMS VOLUME	NASDAQ VOLUME	COMPOSITE CLOSE
WED 1	67 1/4	63 3/4	66 3/4	+	1,545,298	1,071	105,695,149	128,877,700	435.91
THU 2	65 3/4	64 1/4	65	+	1,720,290	1,559	117,625,360	146,537,100	429.89
FRI 3	65 3/4	60 3/8	63 1/4	+	1,630,370	1,359	169,880,593	202,173,900	417.48
WEEK	67 1/4	60 3/8	63 1/4	+	4,902,958	3,089	393,249,102	478,688,400	417.48
MON 6	62 1/4	58 1/2	60 1/2	+	1,571,878	1,288	126,364,082	174,819,400	400.04
TUE 7	62 1/4	60	61 1/2	+	1,250,877	1,132	112,321,861	165,473,800	402.08
WED 8	64 3/4	62 1/4	63 1/4	+	1,200,774	1,086	93,959,567	144,848,900	407.73
THU 9	62 3/4	62 1/4	61 1/2	+	1,071,745	886	85,952,889	129,933,100	412.93
FRI 10	62 3/4	62 3/4	61 1/2	+	1,011,785	804	88,789,328	129,933,100	412.93
WEEK	65 3/4	58 1/2	61 1/2	+	6,132,363	5,343	558,743,005	727,091,900	408.03
MON 13	65 1/2	63 1/4	65	+	750,266	525	67,802,789	87,638,300	408.30
TUE 14	65 1/8	63 3/4	64 1/4	+	468,585	431	61,681,078	107,488,700	410.32
WED 15	65 3/4	61 3/4	64 1/4	+	711,893	428	78,188,791	105,235,900	413.27
THU 16	65 3/4	61 3/4	64 1/4	+	742,138	500	78,188,791	105,235,900	413.27
FRI 17	65 3/8	60 1/4	60 1/4	+	1,325,130	804	125,327,633	146,945,700	393.49
WEEK	65 3/8	60 1/4	60 1/4	+	4,000,392	2,853	439,353,033	562,208,100	393.49
MON 20	60 1/2	55 1/2	55 1/2	+	1,590,012	1,155	84,237,112	118,464,200	388.28
TUE 21	65 3/4	53 3/8	55 3/4	+	2,303,879	1,809	125,626,320	149,100,400	374.84
WED 22	65 3/4	53 3/8	55 3/4	+	1,102,130	1,012	148,181,692	202,763,300	360.32
THU 23	57 3/4	51 1/4	51 1/4	+	1,495,803	1,195	118,529,846	161,077,800	367.33
FRI 24	57 3/4	50 3/4	57 1/4	+	7,816,916	6,350	582,711,168	791,899,400	367.33
WEEK	60 1/2	50 3/4	57 1/4	+	15,311,965	11,381	102,702,888	129,401,400	381.27
MON 27	61 1/4	60	60 3/8	+	1,310,407	934	92,038,388	118,068,100	381.27
TUE 28	62 3/4	60	60 1/2	+	1,084,068	808	82,003,855	108,501,700	376.48
WED 29	62 3/4	60	60 1/2	+	592,618	452	61,705,207	78,140,900	381.21
THU 30	62 3/4	60	61 1/2	+	592,618	452	61,705,207	78,140,900	381.21
FRI 31	62 3/4	60	61 1/2	+	592,618	452	61,705,207	78,140,900	381.21
WEEK	62 3/4	60	61 1/2	+	2,921,722	2,261	437,087,860	549,718,300	381.21

NASDAQ MARKET MAKERS IN THIS SECURITY AS OF 08/31/80

GOLDMAN ACHS & CO	551,131	KLEBER AND CO INC	228,087
MERRILL LYNCH, PIERCE, FENNER	579,680	WEDDER AND CO INC	225,600
HERZOG, HEINE, GEDULD INC	565,180	WASH WEIS/DIV OF SHATKIN INV	153,000
THE FIRST FORT LUN CP	558,872	RAGEN MCKENZIE INC	141,302
PROPER TRAVEL & HOPTWOOD, INC	499,145	MIDWEST STOCK EXCHANGE	117,673
SALOMON BROS INC	480,089	CLUBS SCOVILLE INC	100,334
PRUDENTIAL-BACHE SECS INC	402,040	FURMAN SELZ MAGER DITZ	76,150
PRUDENTIAL SECURITIES INC	389,044	FARMERS STOCK & CO INC	72,300
MORGAN STANLEY & CO INC	377,080	PRINCETON FINANCIAL GP INC	3,500
PATHEWAY & CO INC	377,080	PRINCETON FINANCIAL GP INC	3,500
LEHMAN BROTHERS	356,500	SOUNDVIEW FIN GP INC	2,500
MAYER R SCHWELTZER INC	356,500	SOUNDVIEW FIN GP INC	2,500
PRUDENTIAL-BACHE SECS INC	3,092,906		
ALEX BROWN & SON'S	3,276,067		
SMITH BARNEY SEC CP	2,161,939		
MONTGOMERY SECS INC	2,021,146		
DEAN WITTER REYNOLDS, INC.	1,920,038		
COWEN & CO LUKEIN & JEFFRETTE	1,504,337		
DONALDSON LUFKIN & JEFFRETTE	1,054,337		
BEALMAN BEALMAN & CO	906,886		
BATTEMAN BEALMAN & CO	676,358		

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NASD NATIONAL ASSOCIATION OF SECURITIES DEALERS, INC.
1735 K STREET NORTHWEST, WASHINGTON, D.C. 20006

NASDAQ NATIONAL MARKET SYSTEM STATISTICAL REPORT
FOR MONTH ENDING 31 JUL 90
NASDAQ/NMS SYSTEM STATISTICS

COMPOSITE INDEX	ASSIGNED INDEX (INDUSTRIAL)
HIGH 470.30	911.52
LOW 436.76	469.73
CLOSE 472.81	472.81
PREVIOUS CLOSE 467.29	499.01
% CHANGE -5.20	-5.25

TOTAL NASDAQ VOLUME: 2,984,879,000
TOTAL NMS VOLUME: 2,281,521,100
TOTAL NMS TRADES: 1,174,2070
TOTAL NMS SECURITIES: 1,174,2070

SUMMARY FOR THIS SECURITY

1. PRICE RANGE: HIGH 80 3/4 LOW 65 3/4 PERCENT CHANGE: 12.50
2. LAST PRICE: (JUN) 76 (JUL) 66 1/2
3. VOLUME FOR MONTH: 21,563,789
4. TOTAL TRADES 16,584
5. BLOCKS: NUMBER OF BLOCKS 353 NUMBER OF SHARES 5,781,751

Microsoft Corporation
Mr. Francis J. Gaudette
Senior Vice President Finance
One Microsoft Way WA 980526399
Redmond

NASDAQ SYMBOL: MSFT
SECURITY DESCRIPTION: Common Stock (\$0.001 Par Value)
TOTAL SHARES OUTSTANDING: 112,270,888
SHORT INTEREST REPORTED: 2,189,802 AS OF 07/19/90
PLEASE NOTIFY NASDAQ OF ANY CHANGE IN COMPANY CONTACT OR ADDRESS

DATE	HIGH	LOW	LAST	NET CHANGE	SHARE VOLUME	TRADES	NMS VOLUME	NASDAQ VOLUME	COMPOSITE CLOSE
MON 2	75 1/2	73 5/8	73 3/4	- 2 1/4	493,303	310	87,328,862	114,152,900	482.04
TUE 3	107 10/16	71 1/2	72 3/4	- 3 3/4	1,102,125	851	102,273,483	131,015,100	481.76
WED 4	74 1/2	70 3/4	73 1/4	+ 1 1/4	860,247	638	72,392,907	97,760,800	459.19
THU 5	74	70 3/4	73 1/4	+ 1 1/4	860,247	638	72,392,907	101,159,000	460.53
FRI 6	76	70 3/4	73 1/4	+ 2 3/4	3,057,960	2,270	358,504,725	144,327,800	465.27
WEEK									
MON 8	74 3/4	73 1/2	74 1/4	+ 1 1/2	519,113	384	88,382,650	18,571,500	461.68
TUE 9	75 3/4	73 1/2	73 3/4	+ 1 3/4	413,421	326	123,328,331	15,039,500	463.90
WED 10	77 3/4	75 1/4	75 1/2	+ 2 1/2	408,480	756	130,437,951	153,697,000	487.17
THU 11	77 3/4	75 1/4	77 1/2	+ 1 1/4	1,203,256	1,134	135,334,607	150,592,300	488.44
FRI 12	80 1/2	77 1/2	78 3/8	+ 5 1/8	3,877,364	3,010	585,477,323	734,091,400	488.44
WEEK									
MON 16	80 3/4	78 1/2	79 1/4	+ 1 1/2	678,102	727	101,787,084	138,072,500	489.60
TUE 17	79 3/4	77 3/4	77 3/4	- 1 1/2	653,295	508	118,106,948	165,810,500	484.48
WED 18	77 3/4	75 3/4	76 3/4	+ 1 1/4	878,514	688	141,636,877	158,988,500	480.82
THU 19	76 3/4	75 3/4	75 3/4	- 1 1/4	878,514	688	141,636,877	182,582,700	482.17
FRI 20	80 3/4	77 3/4	78 3/4	+ 2 1/2	1,220,225	897	121,991,097	126,864,600	485.27
WEEK									
MON 23	74 1/2	71 1/4	72 1/2	- 2 1/2	1,022,804	973	129,118,515	166,878,900	444.84
TUE 24	72 1/2	68 3/4	69 1/2	- 3 1/2	1,906,804	1,682	228,001,415	160,504,600	442.56
WED 25	71 3/4	68 3/4	68 3/4	- 1 1/4	836,600	851	110,506,829	141,603,500	443.23
THU 26	70	67 3/4	69	+ 1 1/4	4,215,582	2,241	108,358,091	126,864,600	443.99
FRI 27	70	66 3/4	69	+ 1 1/4	8,710,028	6,583	203,354,197	226,864,600	443.59
WEEK									
MON 30	69 5/8	65 3/4	68 1/2	- 1 1/2	1,223,109	961	92,133,012	120,437,100	439.39
TUE 31	68 5/8	65 3/4	68 1/2	- 1 1/2	1,811,573	1,480	108,958,629	135,186,800	438.24
WEEK									

NASDAQ MARKET MAKERS IN THIS SECURITY

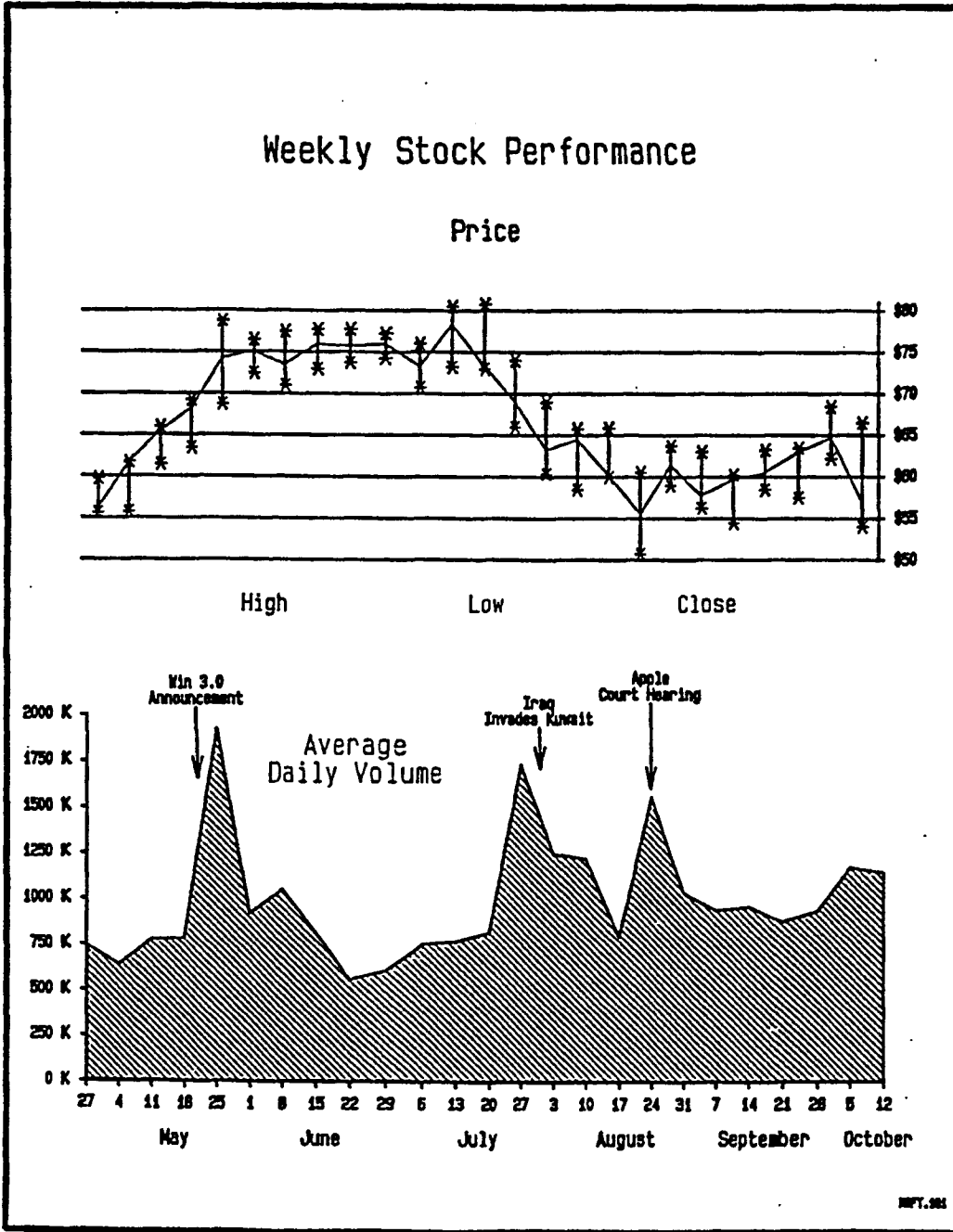
GOLDMAN, SACHS & CO	3,084,780	RONALDSON, LUFKIN & JENNETTE	636,278
THE FIRST BOER GROUP	1,694,130	SMITH, BARNEY/HARRIS UPHAM	587,188
THOFLER SINGER GROUP INC	1,559,230	MAYER & SCHWEITZER INC	510,283
HEBERT, LYNCH, PIERCE, FENNER	1,493,714	COHEN & CO. SECS INC	508,769
PIPER, JAFFRAY & HOWARD, INC	1,381,016	MONTGOMERY SEC CP	448,291
SALONON BROS INC	1,009,455	BRUDENRICH SEC INC	440,206
PALINEWEBER INC	809,350	BEAR STEARNS & CO	393,240
MORGAN STANLIAN & CO INC	764,778	DEAN WITTER REYNOLDS, INC.	363,550
SHEARMAN & STANLEY	645,575	KIDDER, PEABODY & CO INC	287,278
AIFR BROWN & SONS			
JEFFERIES & CO INC			
WEEDEN AND CO INC			
NASH METS OLV GP INC			
ROSENTHAL WICKENITE INC			
OLD DISCOUNT CORPORATION			
MIDWEST STOCK EXCHANGE			
CYRUS J. LAWRENCE, INC.			
FARMESTOCK & CO, INC.			
PRINCETON FINANCIAL GP INC			

AS OF 07/31/90

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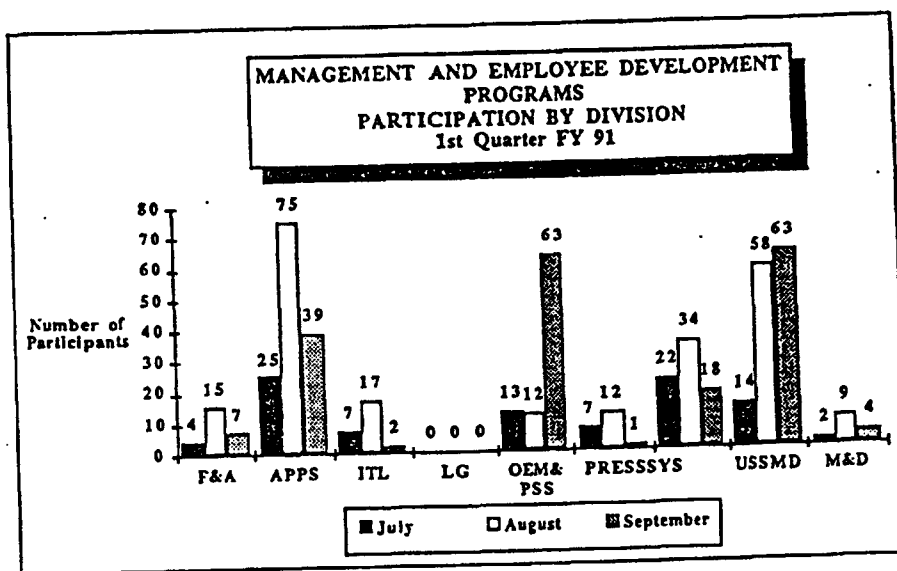
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HUMAN RESOURCES

HR Development and Administration programs grew during the quarter. Our successes in development and training continued with new programs and growing attendance. Total employment was 6,121 at quarter end. Dedicated HR support for the International subsidiaries is making progress. Resident support in the USSMD Regional Sales Offices is in place and moving forward. Our compensation structures are widely accepted. The amount and quality of HR information provided to management appears appropriate. Employee communication initiatives are making a positive impact on employee morale.

Management and Employee Development Programs: During the quarter, 523 managers and employees attended 29 sessions of 15 different seminars. This is a 122.6% increase in number of participants compared to the 235 participants during Q90-1 (see the following chart).



Our curriculum for new technical leads is designed to build foundation skills. We offer advanced management and leadership training for continued development. Emphasis is on communication, motivation, planning, self-management, and creative problem solving. Employee courses help individuals structure their time and develop communication skills to work more effectively with their leads, managers, and peers.

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Two new seminars will be released during Q91-2: Creative Problem Solving and the Technical Leadership Workshop. Forty-five sessions of 22 different seminars are scheduled for the next quarter with 766 projected attendees (see the following chart for courses offered).

COURSES CONDUCTED DURING Q91-1

Course Title	Number of Sessions	Number of Participants
Effective Management Skills	1	13
Interpersonal Review Skills-Managers	2	18
Effective Interviewing Skills	3	38
Time/Business Organization Workshop-Managers	2	36
Selling Your Ideas-Managers	1	10
Conducting Effective Meetings	1	9
Presentation Skills	1	15
Managing Interpersonal Relationships-Managers	1	20
Team Building and Staff Development	1	19
Leading Technical Reviews	1	8
Time/Business Organization Workshop-Employees	6	142
Selling Your Ideas-Employees	2	28
Effective Business Writing-Employees	1	15
Career Planning and Development	3	43
Managing Interpersonal Relationships-Employees	3	109
TOTALS	<u>29</u>	<u>523</u>

COURSES TO BE OFFERED Q91-2

Course Title	Number of Sessions	Number of Participants
Effective Management Skills	2	36
Interpersonal Review Skills-Managers	6	72
Effective Interviewing Skills	1	12
Time/Business Organization Workshop-Managers	1	18
Selling Your Ideas-Managers	1	15
Effective Business Writing-Managers	1	20
Conducting Effective Meetings	1	16
Microsoft Management Styles Seminar	1	18
Presentation Skills	2	32
Managing Interpersonal Relationships-Managers	2	48
Team Building and Staff Development	1	20
Creative Problem Solving	2	30
Software Quality Dynamics	1	18
Technical Leadership Workshop	1	15
Leading Technical Reviews	2	18
Innovation in Design	2	30
Interpersonal Review Skills-Managers	6	90
Time/Business Organization Workshop-Employees	3	90
Selling Your Ideas-Employees	1	15
Effective Business Writing-Employees	1	20
Career Planning and Development	3	45
Managing Interpersonal Relationships-Employees	4	88
TOTALS	<u>45</u>	<u>766</u>

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Employee Relations: The primary goal of our employee relations effort is to assist managers and employees in the resolution of distractions from their work such as: performance problems, internal conflict, career counseling, and personal issues. We have expanded coverage with a Regional HR Manager in each of the Eastern, Central, and Western regions to support the USSMD field groups. A Personnel Administrator at Ridgewood supports the employee relations effort for the sales/services/support groups. At corporate, extended outreach is available in the form of manager orientations, and departmental workshops on interviewing, handling the marginal employee, and performance strategy steps.

Activity for Q91-1 consisted of 185 counseling sessions. Of these, 46% were performance related, resulting in 14 performance improvement plans or probations and 22 terminations or resignations. The remaining were divided with 24% for career counseling and 30% for personal issues. Forty-nine exit interviews were conducted. The two most common concerns cited during exit interviews were poor management skills and low base compensation.

Smoking Policy: In a coordinated effort with Family Services, a variety of smoking cessation programs have been developed and made available to employees and their spouses, free of charge for a six month period, with the majority of the programs scheduled on site. The programs were arranged to coincide with the announcement at the Company Meeting of the Microsoft no smoking policy which became effective October 1, 1990.

Affirmative Action: The EEO job group categories for the comparative analysis statistics for domestic operations are being redefined to coincide with salary ranges. This will streamline record keeping, analysis, and reporting, and strengthen our defense against charges of discrimination. Our percentage of minorities and women has improved slightly.

Employee Communications: The *Micronews*, a popular weekly internal publication, has been expanded to include more in depth background pieces and the publication is now averaging 20 pages per edition.

The July 6 issue carried the second part of a two-part interview with outgoing president, Jon Shirley. Other important stories included coverage of the National Sales Meeting in Hawaii in August, the International Sales Meeting in Rome in September, the Microsoft-Olivetti agreement, WINmail, the PSS site in Charlotte, the Company Store, the new vice president of Microsoft Japan, the annual dealer event at Microsoft France, year end financial figures, new construction at Corporate, the Company Meeting, and the United Way campaign.

A special 15th Anniversary issue was published on the day of the Company Meeting. The issue focused on highlights of Microsoft's history, year by year, and featured interviews with several Microsoft employees who have been with the company since its early days. The issue included a two-page compilation of national magazine covers which featured Bill Gates.

Micronews North is published for the Campus North staff every other week and attached to *Micronews*. In addition, the quarterly edition of the benefits newsletter, *It's To Your Benefit*, was attached to the September 7 issue of *Micronews*. The *Micronews International Edition* began publication on July 20 and is sent every two weeks to the subsidiary offices. The issues consist of *Micronews* articles which are pertinent to the company as a whole and articles from the international correspondents.

Applications Software Training: During Q91-1, Applications Training taught 124 regularly scheduled classes at Corporate Campus and Campus North on Microsoft products and basic computer operation. Students in these classes numbered 914, with 441 on the waiting list for next quarter.

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In addition, over 100 people were trained in a number of special and customized classes held during this period. Over 55 employees of Oglvie & Mather, Microsoft's advertising agency, were trained during July. There were special sessions for CorpCom, Word Processing, MIS, and International. Video training tapes on WINmail and Windows were produced for 250 USSMD Customer Support employees who were moving into a PC environment.

The Brown Bag Seminar for the month of July proved to be a standing-room only success as Tom Corrdry and his staff explored future Microsoft Multimedia products.

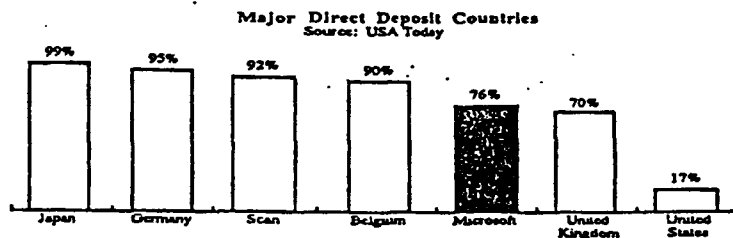
Compensation: During the first quarter, several significant activities occurred in the area of domestic and international compensation and benefits. A career path handbook was developed for Microsoft University employees to create greater awareness of career growth opportunities within MSU and to promote MSU internally. Rollout of a commission plan for MSU Inside Sales met with positive results and the first two month's sales results were strong.

Salary ranges for 1991 are being reviewed based upon market and economic conditions. A market pricing database is now in place to provide immediate analysis capabilities. We are prepared to support the streamlined HR approval process announced by Mike Hallman for employee requisition processing and salary changes.

International Compensation and Benefits: Interpersonal Review Skills training is underway in Europe. Employee and Manager handbook templates are in work and will be ready for distribution in disk format to the subsidiaries in November. These can be customized in each country for specific local guidelines and benefits programs. An automobile policy for the subsidiaries was approved and implemented. Several expatriate and Third Country National (TCN) assignments have been coordinated, with a cost analysis provided to the manager and vice president prior to the assignment being offered.

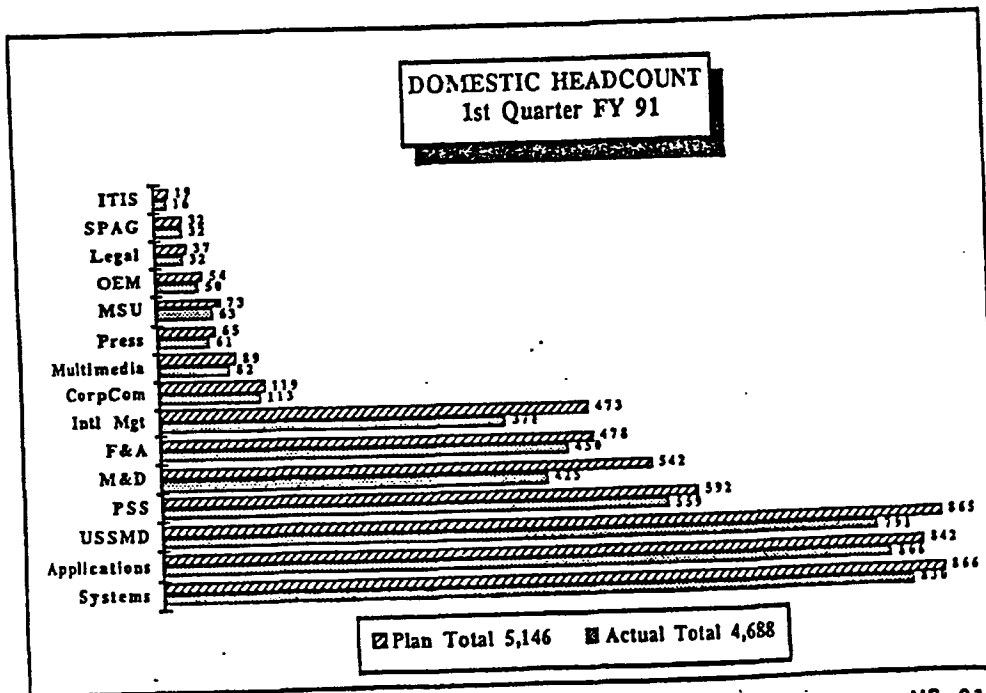
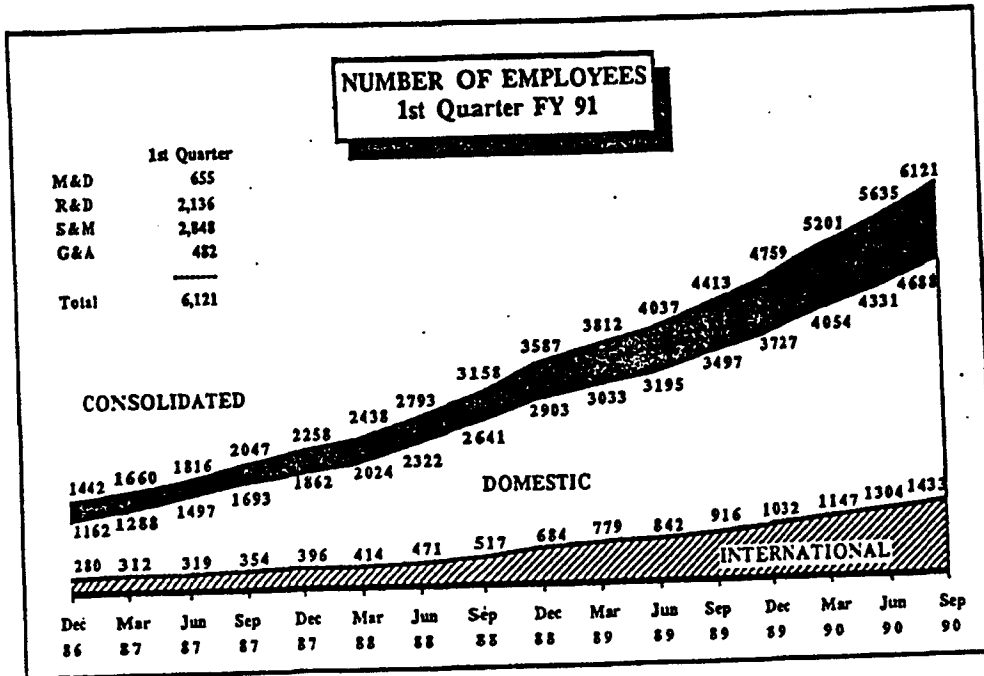
Personnel Systems: As of September 30, the total corporate work force was 6,121 employees, a net increase of 38.7% from one year ago, with 4,688 domestic and 1,433 subsidiary employees including MS Puerto Rico, MS Ireland, and MS Taiwan PBU. Actual headcount for the domestic operations was below planned headcount by 9.8%; subsidiary actual headcount was less than plan by 23.4% (see the following charts, Number of Employees, Domestic Headcount, and Headcount by Location).

Employees continue to expand their use of payroll check direct deposit with over 76% currently participating. As the following chart indicates, Microsoft's participation is several times the national average and closer to practices in Japan and Germany.

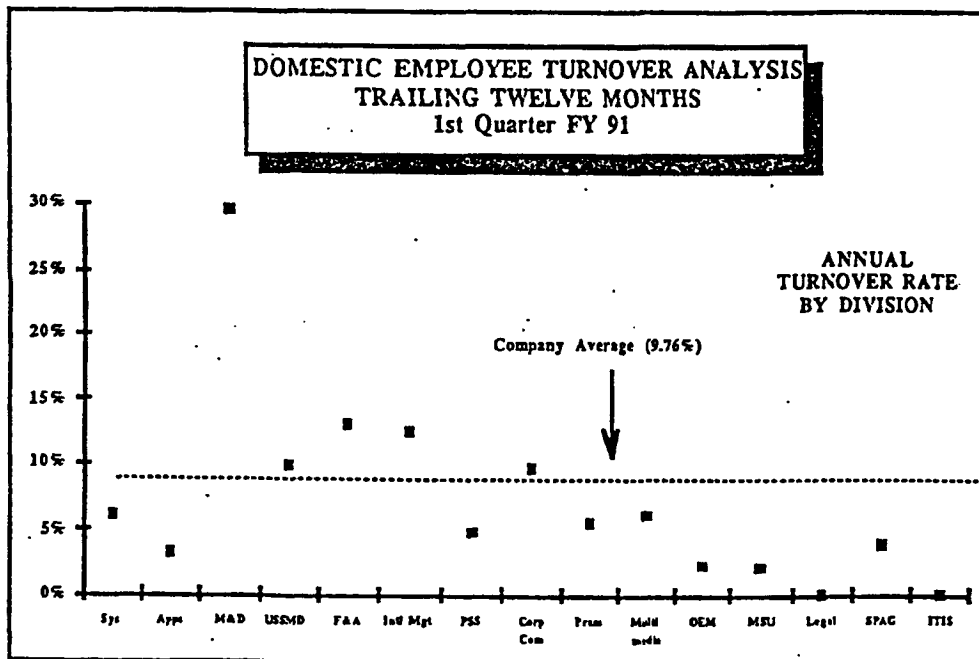
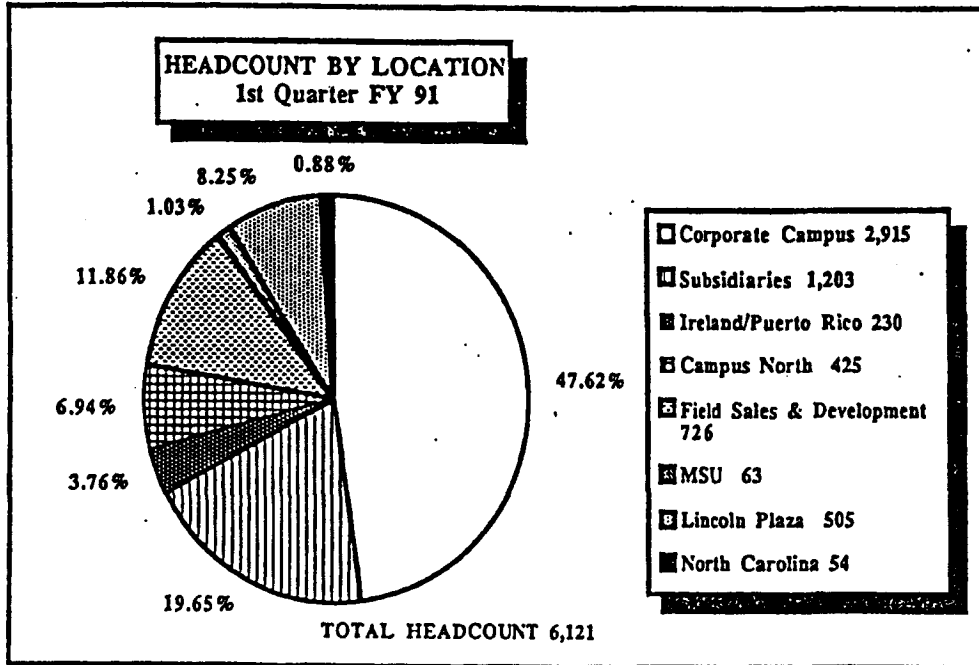


Based on the average headcount and the number of terminations for the last 12 months (not counting product localization associate (AIESEC), co-op, intern, or associate sales positions), the annual domestic turnover rate was 9.8%. This reflects a 0.5% decrease from the Q90-4 turnover rate (see the following chart, Domestic Employee Turnover Analysis).

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Performance Review: An analysis of the August 1990 Review Cycle for domestic operations was completed in September. The distribution of performance ratings, merit increases, actual increases, and bonus awards was charted by division and total corporation. The average overall performance ratings was 3.69 of 5.0 possible; divisions ranged from 3.36 to 3.95. The overall merit increase average was 3.91%; divisions ranged from 2.77% to 5.26%. The overall actual increase was 4.80%; divisions ranged from 4.03% to 7.50%. The average bonus award was 10.03%; divisions ranged from 9.30% to 11.23%. In comparison to the February 1990 Review Cycle, the performance rating average decreased .02 from 3.71, the average merit increase dropped .27% from 4.18% and the bonus award average decreased .14% from 10.17%.

The employee comments made in the August 1990 Review were summarized and distributed to senior management. Approximately 70% of the eligible employee population commented, addressing a broad range of topics and concerns. The comments were summarized under general topic areas addressed most frequently by employees, e.g., Microsoft environment, management, compensation/benefits, resources, workload, career development/training, communication, and review process. Overall the comments were very favorable.

We are investigating ways to streamline the review process in order to increase the employee development aspect of the program while reducing administrative steps. To that end we conducted a survey of managers and employees, and we held focus group meetings to identify the areas in need of improvement. We will begin rolling out the changes with the February 1991 Review Cycle.

Employee Benefits

Savings Plus 401(k) Plan participation continued at 73% for the second consecutive quarter with an average deferral of 7%. We are in the process of reviewing 401(k) fund managers for effectiveness. The reasons for the review are to increase fund performance, increase timeliness of plan reporting, offer employees more flexibility with their portfolios, and provide more detailed accounting of the assets held within each employee's 401(k) account. See charts on pages 120 and 121.

July 2, 1990 marked the 9th semi-annual offering of Microsoft's 1986 Employee Stock Purchase Plan. Automatic enrollment was effectively implemented for the over 4,000 Domestic and International employees currently enrolled. On July 2, 1990, the closing price of the stock was \$73.75 to start the period. The following shows the ESPP has been a very good benefit for its participants:

ESPP PURCHASE PRICE HISTORY

<u>Period Ending</u>	<u>Ending Price*</u>	<u>Purchase Price*</u>
12/31/86	\$ 12.063	\$ 6.03
6/30/87	25.50	10.15
12/31/87	27.125	21.78
6/30/88	33.50	23.80
12/31/88	26.625	22.63
6/30/89	26.50	22.53
12/31/89	43.50	23.06
6/30/90	76.00	37.72

* All prices are adjusted for both the September 1987 and April 1990 stock splits.

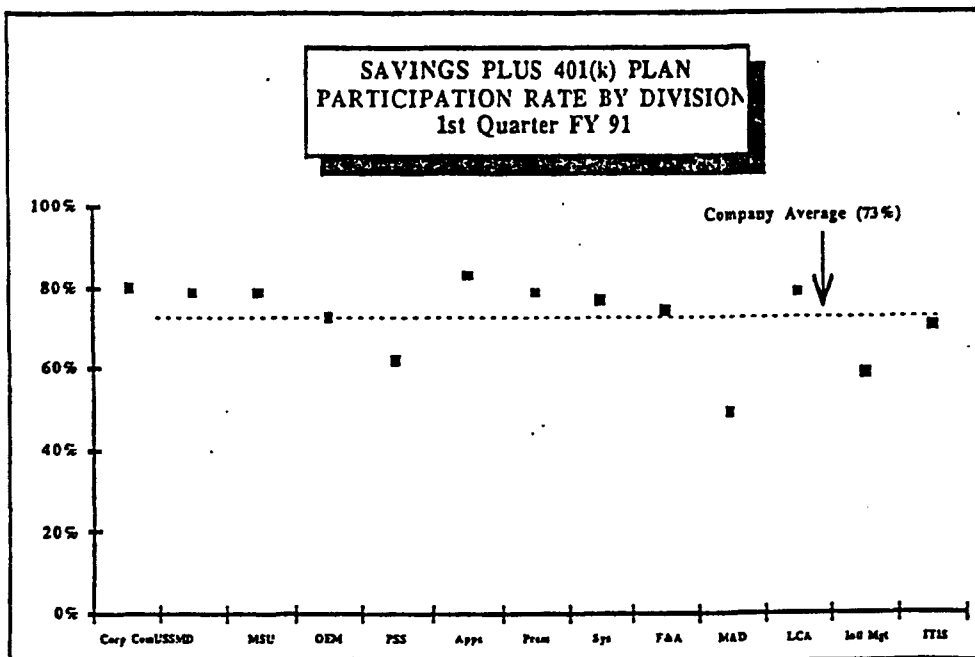
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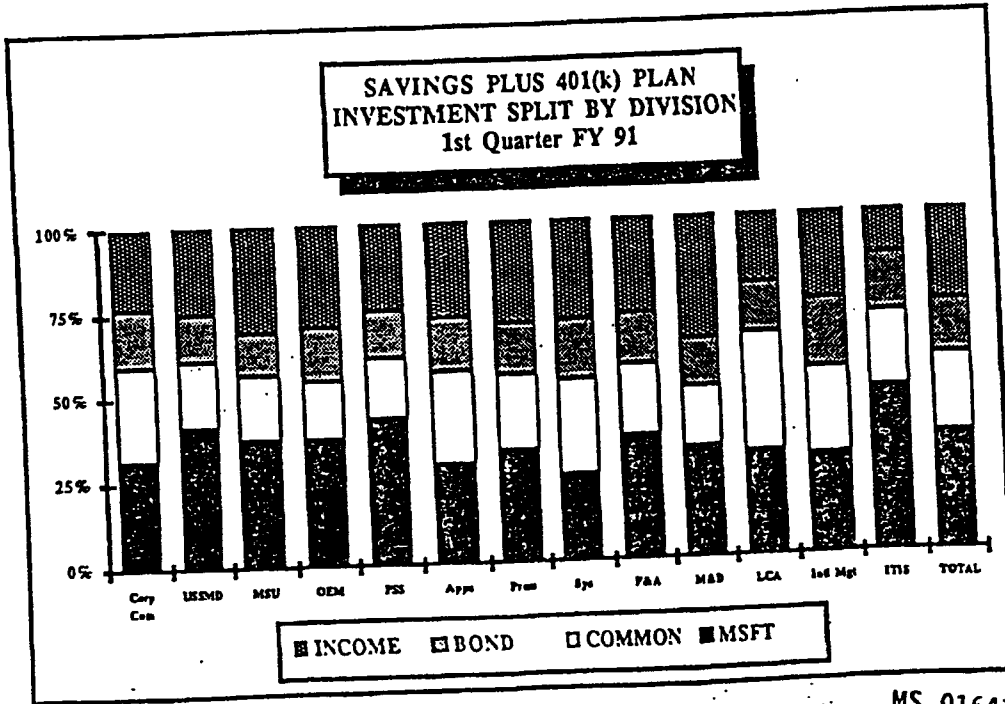
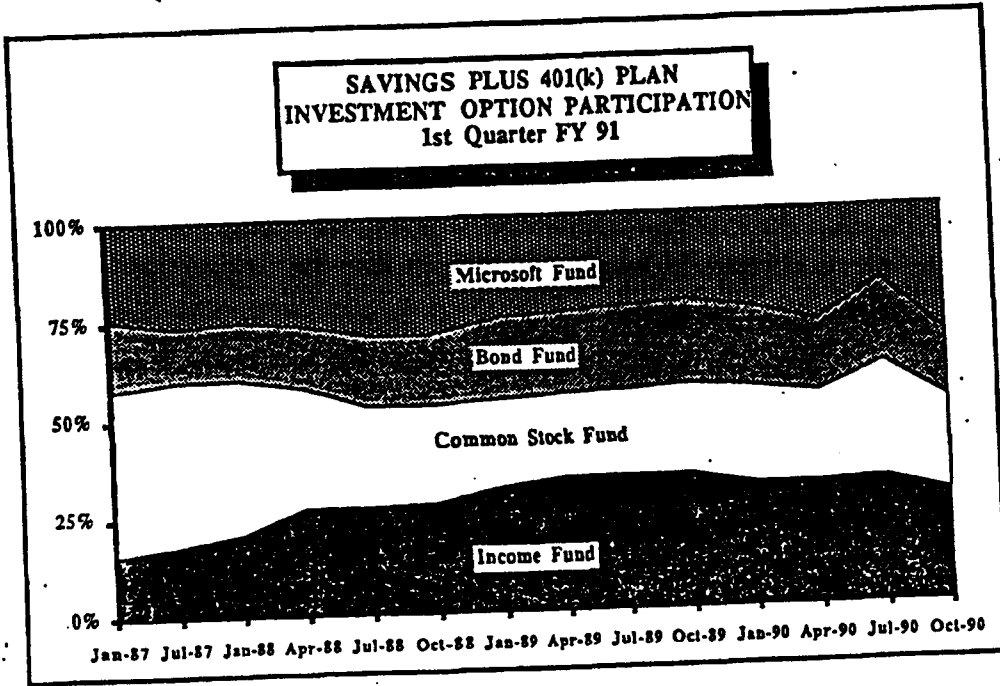
Stock Option Plan: July 31, 1990 marked the lowest closing price (\$66.50) of the 30-day window period for July 1990 review options. A total of 3,179,932 shares were issued to 2,219 employees for the July 1990 Review period.

DIVISION BREAKDOWN

Administration	288,330
Applications	722,610
CorpCom/Trade Shows	72,475
Executive	23,000
International	579,775
Legal	26,850
MSU	32,900
OEM/PSS	252,950
Press	66,530
Systems OS/2	238,665
Systems	543,531
USSMD	<u>332,316</u>
July 1990 Review Grants	3,179,932
New Hire Grants	<u>962,800</u>
TOTAL	<u>4,142,732</u>



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SUMMARY OF STOCK OPTION PLAN ACTIVITY
AS OF SEPTEMBER 30, 1990****Shares Available For Grant**

	Available Beginning Of Period	Additions		Reductions	Available End Of Period
		New Approvals	Forfeited Shares	Net Shares Granted (1)	
Fiscal 1982	0	12,080,000	0	(3,428,000)	8,652,000
Fiscal 1983	8,652,000	0	419,600	(3,717,600)	5,354,000
Fiscal 1984	5,354,000	0	1,561,404	(3,032,460)	3,882,944
Fiscal 1985	3,882,944	0	938,172	(2,626,860)	2,194,256
Fiscal 1986	2,194,256	5,600,000	835,478	(4,938,316)	3,691,418
Fiscal 1987	3,691,418	8,000,000	788,042	(4,812,400)	7,667,060
Fiscal 1988	7,667,060		942,905	(7,772,040)	837,925
Fiscal 1989	837,925	10,000,000	1,175,178	(10,091,860)	1,921,243
Fiscal 1990	1,921,243	12,500,000	991,242	(8,518,890)	6,893,595
Fiscal 1991					
Q91-1	6,893,595		170,405	(4,142,732)	2,921,268
Since Inception	0	48,180,000	7,822,426	(53,081,158)	2,921,268

Outstanding Stock Options

	Outstanding Beginning Of Period	Additions Net Shares Granted (1)	Reductions		Outstanding End Of Period
			Shares Exercised	Forfeited Shares	
Fiscal 1982	0	3,428,000	0	0	3,428,000
Fiscal 1983	3,428,000	3,717,600	(7,600)	(419,600)	6,718,400
Fiscal 1984	6,718,400	3,032,460	(287,168)	(1,561,404)	7,902,288
Fiscal 1985	7,902,288	2,626,860	(859,612)	(938,172)	8,731,364
Fiscal 1986	8,731,364	4,938,316	(2,416,064)	(835,478)	10,418,138
Fiscal 1987	10,418,138	4,812,400	(3,365,664)	(788,042)	11,076,832
Fiscal 1988	11,076,832	7,772,040	(1,852,422)	(942,905)	16,053,545
Fiscal 1989	16,053,545	10,091,860	(2,047,098)	(1,175,178)	22,923,129
Fiscal 1990	22,923,129	8,518,890	(5,230,106)	(991,242)	25,220,671 (2)
Fiscal 1991					
Q91-1	25,220,671	4,142,732	(494,891)	(170,405)	28,698,107
Since Inception	0	53,081,158	(16,560,625)	(7,822,426)	28,698,107

Footnotes:

- (1) Net shares granted is equal to gross shares less ISOs converted to NQSOs.
(2) Due to activity in Q91-1 which affects prior quarters, the number of stock options outstanding as of the end of Q90-4 (25,030,501) has increased by 190,170.